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## Economic Systems Analysis and Policies

*Also by S. I. Cohen*

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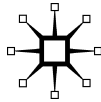
# Economic Systems Analysis and Policies

Explaining Global Differences,  
Transitions and Developments

**S. I. Cohen**

*Professor, Erasmus School of Economics, Erasmus University,  
Rotterdam*

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*To the memory of two teachers and colleagues  
Henk Bos and Jan Tinbergen*

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## List of Abbreviations

BCEE	Baltic, Central and Eastern Europe
BEEPS	WB/EBRD Environment and Enterprise Performance Survey
BRIC	Brazil, Russia, India and China
CPI	Corruption Perception Index
DRC	Real Domestic Resource Cost
DTM	Demographic Transition Model
EAP	East Asia and Pacific
ECB	European Central Bank
EMIS	Emerging Market Information Service at <a href="http://www.securities.com/">http://www.securities.com/</a>
EXSR	Ex-Soviet Republics, except Baltic and Russia
FIG	Financial-Industrial Group
FIM	Firm Intensive System, also referred to as F-system
FMT	Foreign Merchandise Trade
FDI	Foreign Direct Investment
GATT	General Agreement on Tariffs and Trade
GCC	Arab Gulf (Gulf Cooperation Council)
GDP	Gross Domestic Product
HIEF	Heritage Index of Economic Freedom
HIM	Household Intensive System, also referred to as H-system
ICT	Information Communication Technologies
III	Index of Interactive Influence
IMF	International Monetary Fund
KP	Kyoto Protocol
LAC	Latin America and Caribbean
MENA	Middle East and North Africa
MMC	Monopolies and Merger Commission
MPM	Multiple Pole System
NAFTA	North American Free Trade Agreement
ODA	Official Development Assistance
OECD	Organization for Economic Cooperation and Development
PHS	Poverty Headcounts Share in the population
RDM	Relative Distributive Measure in SAM context
RPC	Restrictive Practices Court
ROW	Rest of World
SA	South Asia
SAM	Social Accounting Matrix
SAP	Structural Adjustment Package
SARC	South Asian Regional Council
SIM	State Intensive System, also referred to as S-system
SOE	State Owned and state-holding Enterprises

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SSA	Sub Saharan Africa
TVE	Rural Township and Village Enterprises
VAT	Value Added Tax
WB	World Bank
WBIL	World Bank Index of Liberalization
WTO	World Trade Organization
WVS	World Value Surveys

## Preface

Research, teaching, and advisory work in the two areas of *economic systems* and *development economics* have gone through similar ups and downs in the past three to four decades. In the 1960s and 1970s, both areas attracted the positive attention of many scholars, students, and advisors. The 1980s and 1990s witnessed the empirical documentation of disappointments with the socio-economic performance of centrally planned economies and many developing countries, which are the main clients and subject matters of the two areas, respectively. Justified or unjustified, interest in both areas waned in the 1980s and 1990s, and much of the past academic work on economic systems and economic development was criticized on grounds of being remote from what happens in the real world, inability to foresee the disappointing socio-economic performances, and incompetence in advice on policy matters and reforms.

The period of the downturn has been followed recently by a period of upturn in the twenty-first century. Interest in both areas has again flourished due to, on the one hand, the general success of many transition economies in reforming and redirecting their economic systems towards a more market–state mixed profile despite their past regime failures, and on the other hand, the reappearance of past state-wise rent seeking interests in some major transition countries. Furthermore, the success of some leading and big developing economies like China and India in likely overtaking rich countries in terms of the size of the GDP, industry, trade, and foreign exchange reserves, and the fall back of some other developing regions far behind, have contributed to the upturn in enthusiasm for the sub-disciplines. Moreover, the unexpected global financial meltdown of 2008, which is hurting free market economies more than others and is accompanied by calls for collective actions to stabilize the economic systems, are very likely to further enhance academic and policy interests in economic systems and economic development. The downturn and the upturn caused profound changes in topics and methods pursued by economists dealing with economic systems and economic development. The two areas have become closer to each other than ever before regarding topics and methods, without tarnishing basic differences between transition economies and developing countries. There is now more insight into, and appreciation of the subtleties of these two sets of countries, and how they differ and develop differently from the economic systems of the richer and predominantly Western countries.

It is now again generally appreciated that because of the intrinsic differences in their functioning and future development, economic work on countries manifesting different economic systems need to be framed in distinctive ways.

This book is a meeting point between economic systems and development economics. The scope is the worldwide economic dynamics of national economies that manifests itself in distinct economic systems. The book is directed to scholars

and readers, teachers and students, policy advisors and policy recipients, working on economic systems and development economics.

If each book should state its focal point in one or two sentences, then ours will be the following. The future prospects are not those of a universalistic set of economic behaviours that countries would adopt worldwide some time in the future; instead, our contention is that there are behavioural differentiations of a higher order that separate the interacting agents from integrating and converging towards any one economic system. The behavioural differentiations emanate from different sociological, political, and economic behavioural orientations that characterize major settings (such as household, state and firms settings, respectively), and in which agents interact, and lead ultimately to distinguishable dominant behavioural types.

I sketched in 1978, a model wherein the social and political domains dominated the economic domain and then applied the idea to study the prospects of land reform in India and Chile, in Cohen (1978). The idea of distinguishable dominant behavioural types in different systems/countries was bound to gain strength over time as it became increasingly supported by theoretical foundations and empirical evidence from various distanced sources. In time, and bolstered with this support from theory and empirics, it was possible to elaborate a theoretically founded analytical framework for explaining distinguishable dominant behaviours in economic systems, and demonstrating its validity and applicability to wider issues including the study of emerging systemic problems and subsequent policy responses, as is being done in this book.

The theoretical foundations came with the development of convention theory, starting with David Lewis (1969), who provided the seminal work on common knowledge, and laid the foundations for formal approaches to the study of social conventions and social norms. The formal approaches which at one time consisted of game theory, soon extended to include folk theory, information cascades, evolutionary learning and social network formation, and allowed for the coexistence of multiple behavioural equilibria; thanks to works by Thomas Schelling (1978), Robert Frank (1988), Herbert Simon (1993), and many others. In all these works, typical behavioural patterns that make-up the system anatomies can be described as social conventions in the sense that they result somehow from the interdependency of individual actions subjected to some given initial conditions. While conventions change they tend to follow the down-laid paths of past events and responses, thus resulting in differentiated and sticky systems of joint social, political and economic behaviour. The empirical backing of the persistence of behavioural types and institutional set-ups that associate with such behavioural types in separated societies, whereby intentionally or unintentionally, the institutional set-ups are inclined to benefit specific groups of agents and disfavour others, is the second line of inspiration of the book. Some modern contributors who fit here and who have analysed different economic systems can be quoted as examples: Janos Kornai (1967), Gunnar Myrdal (1968), John Galbriath (1983), Douglas North (2006), and many others.

The book starts with laying in the first two chapters the theoretical foundations for understanding different dominant behaviours in economic systems. The concept of dominant behavioural settings is crucial. I distinguish between household, state, and firm settings that are driven by social, political, and economic motivations, respectively. One motivation tends to dominate over the other motivations, and thus determine the shapes of conduct, structure, and performance. Which motivation prospers where depends on the initial situation, the external environment, and historical events. I introduce a fourth type of setting, calling it persuasive settings, which can play a crucial role in coordinating less integrated multipole social systems. Interactive behaviour of agents in all four types of settings shapes the development path of the economic system. After a motivated classification of world regions to behaviourally dominated prototypes of economic systems, the book examines the real world country counterparts of the prototypes. We devote two chapters for each of the rich industrialized countries, the transition economies, and the world developing regions. The chapters focus on an analysis of conduct, structure, and performance, as well as related policy. Chapters 9 and 10 are devoted to a retrospective comparative analysis between countries belonging to the differing economic systems, and their intercourse in the context of system competition.

The book benefited from interactions in lecture courses on the topics treated to undergraduate and master degree students at Erasmus University Rotterdam and courses and visiting lectures delivered abroad in various countries. The deliberations in these courses convinced me that the ten chapters of the book fit together in a coherent whole that meets four goals: describes world economic systems fairly well; gives theoretically founded explanations to global differences, transitions, and developments; provides convincing grounds for using the developed framework for further fruitful analyses; and highlights policy considerations towards higher growth and more equity. If the book succeeds in contributing to any of the four goals, then it would have achieved its objective.

Indebtedness goes for the forerunners mentioned above, and to Henk Bos and Jan Tinbergen, who introduced me on systems and development, and not least, have paved the way for a sober and humble academic life. Indebtedness goes also to course participants, and colleagues and reviewers who read and commented on isolated parts of the book. I am also thankful for the generous support and editorial work provided by Palgrave Macmillan.

The book has made extensive use of several databanks for which I am gratefully indebted. The majority of computations and tables in the book have relied on these databanks that are generally accessible via the websites that we refer to. The use of these sources are hereby acknowledged, and they are listed below in alphabetic order: Beck's database of political institutions; Centre for Systemic Peace, University of Maryland for its database on war causalities; Economic and Social Research Centre for Islamic Countries for its SESRTCIC Statistical Database; European Bank for Reconstruction and Development for The Business Environment and Enterprise Performance Survey (BEEPS) and for reports of the Bureau of Economic Analysis (BEA); W. Heinsz's dataset on political constraints;

Heritage Foundation for the Index of Economic Freedom; International Monetary Fund for Government Finance Statistics and International Financial Statistics; ISI Emerging markets for the EMIS databank; OECD for Geographical Distribution of Financial Flows to Aid Recipients, and OECD Historical Statistics; Transparency International for the Corruption Perceptions Index, CPI; Unicef-icde for Transmonee database; UN Population Division for its World Urbanization prospects; UN Public Administration Programme for data on the public sector; World Bank for the World Bank Development Indicators Database, development gateway, query, and other related data; World Values Survey Association for World Value Survey; and World Trade Organization for International Trade Statistics.

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A symbolic dedication of this book to the next generation of grand children is in place: to Sophie, Nelson, Yasmine, and Midas. Perhaps some of them some time in the future will pick up from where I have stopped.

(Solomon) Suleiman Ibrahim Cohen