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December 2019

UDC: 338.24:316.334.2(734.112.4:497-15)"1990/2002"
Conference Paper

Social Market Economy as an alternative to the Washington Consensus in the Western Balkans

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Abstract

Nearly three decades after the beginning of transition from communism to democracy and open market economy in Central and Eastern Europe (CEE), the Washington Consensus in general received the mark as a failure. While the experience from the CEE apart from common results showed considerable variations, the package of reforms is questioned even in the long-term perspective, especially for producing high social costs. Recent mass emigrations from the Western Balkans due to poor economic conditions and from the Middle East, have brought to attention the credibility of exporting or imposing the American type of democracy, and with it, the Washington Consensus as a model of economic transformation and development. But is there an alternative? It already existed even before the systemic changes in CEE began, and can be more preferable even now to the countries that have to undergo a considerable economic transformation. That is the social market economy, which still can be applied in some countries that have lagged behind in transition. This paper explored the perspective of introducing and implementing such a model in the Western Balkan countries, with a reference to the role by the state, taxes, income distribution, and business development.

Keywords: Washington Consensus, Social Market Economy, Western Balkans, economic reforms.

1. The promise and the failures of the Washington Consensus

The Washington Consensus was (and still is) a package of economic reforms recommended and offered as a model to the developing countries, mostly to those that emerged after the fall of communism in Central and Eastern Europe (CEE). The policies of these reforms involved three institutions: The International Monetary Fund (IMF), the World Bank, and the U.S. Treasury Department. All these three, two of which international and one of the largest national economy, are based in Washington D.C., the capital city of the U.S. It could not be called differently, regardless that Williamson (1990) can be credited to have coined the term. In principle, the Washington Consensus consisted of the following ten policy reform recommendations for the developing countries:

1) Fiscal policy discipline focused on low fiscal deficit in relation to GDP;
2) Reducing and redirecting public spending towards more pro-growth sectors for the poor such as education, health care and investment in infrastructure;
3) Tax reform by applying moderate marginal rates and broadening the tax base;
4) Positive interest rates that determined by the market, expected to be moderate in real terms;

5) Competitive exchange rates of currencies;
6) Trade liberalization with a reference to imports, including the elimination of quantitative quotas, whereas any trade protectionism should be subject to low and relatively uniform tariffs;
7) Liberalization of foreign direct investment;
8) Privatization of state-owned enterprises;
9) Deregulation, i.e. elimination of the rules impeding new entries in the market or restricting the competition, except those justified on safety, environmental and consumer protection as well as a careful supervision of financial institutions; and
10) Legal protection of property rights.

What impact and outcome has the Washington Consensus produced in CEE countries, will be discussed later. In broad terms, the results during almost the entire decade of the 1990s for much of the countries implementing the package of these reforms was marked by an economic decline, somewhere in greater and elsewhere in lower scale. Was this economic downturn necessary in the road to a longer term pick up, so the reforms could be judged as successful? Not really. It was a surprise which forced many economists to criticize the Washington Consensus as a failed model of transition from centrally planned to a market based economy. Among them, Stiglitz (2002) justified his critique based on his own experience as a chief economist of the World Bank that the model has brought many deliberate or not expected hardships not only in CEE, but also in some African and Asian countries where it was implemented. The same package of reforms for economic transition has been implemented in the Western Balkan countries, which was associated by civil wars, thus making the transition harder. The simultaneous hardships by civil wars that broke up the former Yugoslavia and the fall of communism, made each of the successor states to adopt their own path of economic reforms under the auspices of the Washington Consensus. There was not an elaborated or a detailed strategy as how to proceed and what the expected results of the chosen path might be.

As in the rest of CEE, there were two ideas or proposals for economic transition in the Western Balkans (which is also a part of CEE). The first was known as the fast transition or "shock therapy", and the second as “gradual approach”. The key difference between these two can be summarized as follows: supporters of the first were concerned that the delay in stabilization and liberalization can trigger rent-seeking behavior, and create interest groups that would oppose the reforms with wider benefits reach or cause them to fail. In their justification, they agreed that the institutions were needed but not necessarily before the reforms were undertaken. Proponents of gradual approach feared that rapid moves could be followed by major disorders, and inflict great loss to the economic well-being of citizens. Gradualists, unlike shock therapists, point first to institutions before stabilization and economic liberalization. In general, the “shock therapy” alternative in the view of Havrylyshyn (2007) is witnessed to be more successful. This was implemented by the Baltic States, Poland, the Czech Republic and Slovakia, while Albania, Bulgaria, Macedonia, Kyrgyzstan and Russia had abandoned it. Gradual approach took place in Azerbaijan, Armenia, Georgia, Kazakhstan, Ukraine, Tajikistan, and Romania. Most countries have entered the transition process through “shock therapy” for price liberalization. Inflation was either already present, or a major threat. Beginning with Poland in 1990, the monetary stabilization package was enforced in 25 countries by 1995. The pre-stabilization inflation rates varied greatly: from hyperinflation of 57,000 per cent annually in Georgia to 26 per cent in Hungary. This also clearly distorted the success of reforms. Bulgaria, Estonia, and Lithuania have had the most impressive rates of low inflation performance. Time also mattered as early reformers have been more successful than later ones (Fisher & Sahay, 2000).

The findings that "shock therapy" was more successful in some countries than others who implemented the "gradual approach", should be reminded that the initial conditions were not the same. Poland, the Czech Republic, Slovakia and the Baltic States were geographically close to the developed capitalist countries (Scandinavian countries and Germany), which also affected faster economic relations between them such as greater capital movement towards them, lower trade exchange costs, thus they were at the gates of developed countries. That was one of the main factors affecting the different results in making transition more successful in some countries than in others. The rest have yet to be discussed in the forthcoming section briefly.

2. The failure of Washington Consensus in Central and Eastern Europe

Transition in CEE was unique from many parts of the world as it included systemic changes in both politics and the economy. The one party system was given up in favor of political pluralism or democracy. But what type of democracy? Democracy does not necessarily imply too many political parties. The communist party also might have been considered democratic as it allowed all the voters to decide which candidates to vote. However, the difference was that communism did not allow political opposition, and with it, no alternative or opposition to the reforms in the economy. The party ideology and the state ownership over the means of production were kept as a cornerstone.

Central planning was a doubtful and inefficient system in the long run. The communists in power had their interest in reporting the fulfillment of the plans in greater scale than actually they were carried out. This begun to become clear when the fall of communism commenced and transition emerged where, exaggerated statistics did not correspond to the state on site that faced many shortages, including food items. By the end of communism, production was declining in almost all Soviet type communist regimes, to be accelerated in the first year of transition and continue in forthcoming years. Poland was the first country to reverse this negative economic growth trend, while Ukraine was able to do so only after eight years of decline. Total fall of GDP amounted for 13% from 1989 to 1992 in the Czech Republic, to up to 77% from 1989 to 1994 in Georgia, greater than that during the 1929-33 Great Depression in industrialized countries. The fall of GDP recorded in CEE between 1989 and 1992 averaged 17%. From 1989 to 1997, the fall ranged from 30% in Bulgaria, and Romania, to 40% in former Soviet countries (Aslund, 2000). Five countries (Armenia, Azerbaijan, Georgia, Tajikistan, and to some extent, Moldova) suffered from civil wars and conflicts, but the registered fall of GDP in the rest was unusual for peacetime. It was this unexpected downturn of economic transition that caught most economists by surprise or unprepared about the theories of economic transformation from centrally-planned to an open market-oriented economy.

The decline during transition coincided with the intensity of structural reforms. Hard budget constraints and large scale cuts in subsidies hit many sectors. There were already signs of economic distortions even before transition as the communist countries determined their trade largely from political decisions. The distortions became more evident in the emerging transition, which in turn raised the necessity of adopting structural adjustment programs. At the forefront to these programs for assistance was the IMF providing loans to the countries that were in crisis.

Initially, the programs were focused on fiscal discipline, lowering of inflation, structural reforms, and economic growth (International Monetary Fund, 1997). To what extent these programs (which accounted for much of the Washington Consensus package) were successful, the experience across CEE offered mix results. While there have been and still are critiques towards these IMF programs, one thing was certain: the transition economies were in need of western foreign assistance to implement their economic reforms in order to overcome the crisis in which they entered following the collapse of communism.

2.1. Harder transition and higher social costs of transition: The impact of civil wars

Several causes may be attributed to the communist collapse in CEE as a political and an economic model. In general, it can be argued that the long war of USSR in Afghanistan in support of communism since 1980 to the withdrawal in 1989, has greatly contributed to the downfall of communism. The USSR was no longer able to exercise direct control in satellite states of CEE, as it did earlier in 1956 Hungarian Revolution and in 1968 in former Czechoslovakia. Eventually, the USSR itself had internal problems and disintegrated into 15 new independent states, and agreed that its former satellite states to its west (in CEE) can chose their own separate political and economic course. The choice in many countries was not free of charge from the factors that were beyond their control and hardened economic transition – the civil wars.

The beginning of the 1990s was a period of general turmoil in CEE or in what was known as the "Eastern Block" of communist countries. Transition can be taken to have commenced since the fall of the Berlin Wall in November 1989, which brought the reunification of Germany a year later, then dissolution of the rule by communist parties and the emergence of political pluralism, massive economic reforms with a particular emphasis on transformation and privatization of state ownership. These systemic changes followed a high social cost for many countries, such as the disintegration of two federal states, namely the Soviet and Yugoslav ones, and the establishment of newly independent states, as well as the split of Czechoslovakia. While this latter one broke in two states peacefully into the Czech Republic and Slovakia, in the Soviet Union and Yugoslavia disintegration was associated with costly civil wars. Although the Soviet Union initially followed the Czechoslovak peaceful settlement, further separatist and secessionist movements erupted in many parts of newly independent states. Armenia and Azerbaijan were already in armed conflict over the province of Nagorno Karabah since 1998, which intensified after their independence as both countries were building their armies, and hostilities lasted until 12 may 1994. Next to them or in the Caucasus, there have been armed conflicts in Georgia between her government and the pro-Russian separatists in the provinces of Abkhazia and South Ossetia (1992-1993, and in 1998), then, two wars in Chechnya (first, December 1994-August 1996, and second, August 1999-May 2000), with spillover effects to neighboring provinces and republics. Further to the east of Caucasus or in Central Asia, a civil war in Tajikistan (1992-1997), and the Russian-Ukrainian separatism in Moldova. A far bloodier was the dissolution of former Yugoslavia from 1991 to 1999, involving war crimes and ethnic cleansing. All these wars and ethnic conflicts during the 1990s, apart from material losses, have depleted the human potentials, many of which sought to emigrate in search for better life and perspective. In this scenario, it would be wrong to address the failure or hardship of transition to economic reforms based on the Washington Consensus. A considerable number of people left their countries even after the reconstruction and stabilization took place, and they continue to emigrate even in recent years. Is this because the Washington Consensus recommended reforms did not offer the needed perspective? It is too early to say at this stage of discussion. Let us have e look at the figure of population and Gini coefficient in different periods.

Table 1. Population and Gini coefficient in the Western Balkan countries

	Population (in millions)*			**Gini coefficient**	
Countries	**1990**	**2007**	**2018**	**2002a)**	**Latest estimate b)**
Albania	3.26	2.95	2.87	0.29	0.29 (2012)
Bosnia and Herzegovina	4.36	3.80	3.51	n/a	0.33 (2007)
Croatia	4.78	4.40	4.10	0.35	0.32(2014)
Kosovo	1.96	2.10	1.80	n/a	0.26 (2016)
Northern Macedonia	2.02	2.01	2.07	0.27	0.36 (2015)
Montenegro	0.65	0.70	0.62	0.37	0.32 (2015)
Serbia	7.61	7.50	7.00	0.37	0.29 (2013)

* Includes population census and estimates for different years by the statistical offices of respective countries.
n/a = data not available.
Source:
a) Sukiassyan, G. (2007). Inequality and Growth: what Does the Transition Economy Data Say? *Journal of Comparative Economics, 35*(1), pp. 35-56, Table 3, *op. cit.*
b) World Bank, Gini Index, available at: https://data.worldbank.org/indicator/SI.POV.GINI/, accessed on January 2019.

Since 1990, the number of population appears to have fallen, first as a result of civil wars, and then from 2007 onwards mainly through emigration for economic reasons. The only country to have experienced light population growth from 1990 to 2018, is Northern Macedonia but only by few thousands. The decline in the number of the population is more interesting from 2007 to 2018, because, for a shorter period than from 1990 to 2007, the number of population fell more in peacetime. The last two columns in Table 1 do not provide any sound comparative indicators on income inequality as measured by the Gini coefficient as the data are missing, and what is available, is from time to time. To what extent the policy reforms implemented have contributed to increase or decrease in income inequality, cannot be explained without additional research. Section four of this paper will refer to and explain the governmental source such as tax rates that give rise to income inequalities, while the actual estimates of Gini coefficient across the countries into consideration, that would include other causes of inequality (such as non-governmental policies and causes), remains a topic for future more detailed empirical research.

2.2.Explaining the failures of the Washington Consensus

What would one recommend to a communist economy facing shortages, including food items? That is one of the reasons why an open market economy was preferred by the policy makers when facing the dilemma how to reform or what path should be chosen. The Washington Consensus was an ideal one with an emotional feeling that at some time it probably will result in the freedom, democracy and economic development. But transplanting a system of rules elsewhere does not result in similar phenomenon due to historical, economic, and cultural differences.

The next surprise during transition was the role of the state in economy, and here, those who recommended a gradual approach appear to win in their forecast. Having lived for decades under communist dictatorship, majority of the population felt as if they were immediately freed from someone or the state, to the extent that they neglected its role in the new circumstances of the system that was about to take place. The institutions for a market economy considerably affect performance and this is directly reflected in the citizens' lives. During transition, this role met with reluctance in preparing and implementing the legal framework regarding private sector and regulation of public companies. The policies supporting the establishment of political back up for governance have their impact on other parties that are affected by the reforms, which in turn can hinder the overall conditions in the ease of doing business. An explanation for institutional development is based on bringing the incentives during the transition period. In some countries, the government was actively encouraged to pursue transition of broader participation in establishing the market economy by securing the fundamental property rights and rule of law for all. In some others, the elite was mainly concerned about its own property rights from the state companies to be privatized, by which it could secure an economic and political power to dominate the post-transition period. The governments in the first group countries interacted with potential entrepreneurs in what was called by Frye and Shleifer as the model of "invisible hand", by which the government is well organized, generally not corrupt, and relatively benevolent. In the second group, the government is more or less disorganized and with bureaucrats to act upon their own private interests (Frye & Shleifer, 1997).

Due to these two main types of governance, there were also various experiences in institution building for market economies in transition countries. The initial enthusiasm gradually dropped and turned into disappointment when the reforms failed to materialize expectations. One and a half decade later, transition in general has made the people unhappy for a number of reasons. Guriev & Zhuravskaya (2009) who investigated the life happiness in post-communist economies with various secondary data, found considerable economic benefits after 1995 in terms of increased household consumption, housing, cars, and personal computers at their ownership. Once material concerns were overcoming, unhappiness switched to increased income inequalities as measured by Gini coefficient, deterioration of public goods, increased uncertainty, and human capital depreciation aspiring to emigrate for a better life. Transition in CEE after an initial disorganization and downturn, has resulted in making people with more civil liberties and material gains in longer run. Global economic and technological development would have brought life material gains anyway. What many people in CEE are not so happy with, is not purely related to economics, but rather to unfairness, uncertainty, inequality in incomes, and public goods (especially healthcare and education) for which they have to pay like a consumer to business. This unhappiness is better addressed by the European model or social-market economy.

3. The foundations and performance of social market economy

The social market economy (Soziale Markwirtschaft) originating in West Germany after WWII has been increasingly becoming a European model. Before entering into more details what it entails, it would be useful to discuss the causes of its introduction, as it may help economic policy makers to choose certain paths or models of development in particular circumstances (as opposed to the lack of theories from communism to capitalism). Why did (West) Germany adopted this model and for what purpose? The answer should be traced a little earlier in the chronology of events that occurred in Germany since the end of WWI.

After WWI Germany was on the losing side, not in military fronts but after it signed the armistice. The vast territories it had conquered and still had under control after the war ended in the East (the Treaty of Brest-Litovsk), Belgium and little in France, had to be abandoned, and even lose additional parts to neighboring countries. The armistice followed capitulation and the Treaty of Versailles, with harsh conditions against Germany. There is a general consensus that the Treaty was nothing less than a guarantee for a future war (WWII). The challenges for post WWI Germany were tough. First, the capitulation of Germany was blamed by certain circles within her military on betray by the politicians. Second, harsh conditions against Germany to pay the war reparations and the emergence of anarchists, communists, along with severe economic crisis, created the belief that a strong centralized state must be necessary to counter the threat of Soviet communism, though Germany herself must not be communist but a capitalist dictatorship. Fourth, the Great Depression 1929-33 became an additional evidence for the need of a centralized state. Fifth, the short period within which the Nazis turned Germany from massive unemployment to a shortage of labor, created the belief that this is the model that should be applied against economic crisis, but as it went too far in expansionism beyond the national borders by exploiting the slave labor for war purposes, it ended in catastrophic consequences. Germany lay in ruins after WWII and was occupied by the Allies. How to make Germany economically strong once again when the entire nation was devastated? What model of economic development to follow? Like the one under the Nazi regime? Not any longer. But there was an economic alternative with the same objective like that of the Nazis while distancing from them – social market economy – to make Germany economically great again. How?

Social market economy is a separate capitalist economic model; despite many common features it shares with the American model. In this respect, this model has developed its own approach to almost all economic phenomena, no matter how different or close with the rest, including transition from communism to capitalism which is relevant for this paper. First, let us summarize the main principles of this model in which it is based upon, some 10 of them for comparison with the Washington Consensus (Esderts, 2003; Hase, Hermann & Weigelt, 2008, 2008).

1) A constitutional economic model, whose concept is outlined by the state that makes it compulsory;
2) Active role of the state in the economy to set rules of the game and act as a regulator;
3) Economic planning at national level through government policies and orientation in development;
4) Free choice across economic activities and competition;
5) A role on decision makings at micro level to prevent unlawful exploitation of the workers;

6) Income distribution where the state plays an indirect role in redistribution;
7) Property rights and privatization, where the model is largely based on private property, and privatization of public companies comes into question where competition is secured to avoid monopolies and price discrimination;
8) A liberal international trade in compliance with the rule of law;
9) Social welfare programs (health insurance, education and research) to provide equal opportunities through state funding for all in respective fields of the economy;
10) Higher taxes on businesses to support social welfare programs.

One of the key areas in which the European model differs from the American one, and this proved to be very important when we referred to the experience of post-communist countries, is the role of the state in the economy.[1] It was this feeling of minor or uncoordinated role by the state that gave rise to many failures during transition. The European model had a better view on the role of the state in a market economy, but as we noted earlier, the general public had enough of it under communist dictatorship after which it emotionally switched to uncontrolled freedom. Another key principle differing the two western models with respect to transition economies, is in their approach to privatization. The European model advocates for gradual privatization of state-owned and public companies that would first take into account competition and control for monopolies, while the American one pushes for fast privatization as a gateway to bring about the competition. The next but not least important difference is in the interaction of point 6) and 10) above mentioned, namely in income distribution and taxes. The American model recommends keeping them at relatively low rates to give more opportunities to businesses even if it evolves in monopolies, while the European model wants to tax more profitable businesses and indirectly redistribute incomes to the rest of population. These differences have become a subject of interest, with the objection in the Western Balkans that there is still a better alternative model to the Washington Consensus, and it is available to its doorstep which it wants to join – the European model of social market economy.

3.1. The interaction between politics and economics: The Washington Consensus versus Social Market Economy

The Washington Consensus or the American model is not only about economics; it also impacts politics with the objective of safeguarding and ruling the economy. In this interaction between the economy and politics, we can witness a difference between American and European model, which among others can be noticed by electing the head of the state, President and/or Prime Minister (PM). Traditionally, the U.S. Presidents came from the background of strong business or those who did not have it, were still at the forefront of, or behind, big businesses and billionaires. This is an example how businesses shape politics in the USA.

In Europe this relation between economics and politics is different. Rarely has any PM of an EU country been a powerful businessman. The most notable one was Silvio Berlusconi in Italy, which somehow came to be controversial. The rest were and still are of different background from business, beginning with Angela Merkel (Chancellor of Germany), Emmanuel Macron (France), Theresa May (UK), Giuseppe Conte (Italy), and so on. They neither came from rich background in business nor became so through politics after their mandate expired or got

[1]The term American model should not be confused with the Washington Consensus, despite that the latter derived as a recommendation by the former. The latter is related to the policy recommendations for transition countries, but it is still a good general picture of the former. In any case, both are used as synonymous for the purpose of this paper, like social market economy as the European model which differs and does not apply to all European countries.

retired; they remain "poor" from business perspective. On the contrary, in the Western Balkans, especially in Albania, Bosnia, Kosovo and Northern Macedonia, the politicians after coming into political power try either by themselves or through their friends and relatives in grabbing the opportunities for enrichment through discriminatory and often illegal practices. Some of them even would no longer like to be in political position if it has paid off enough for their wealth obtained, because that would enable them to have their real economic power against the politicians. This is a transition towards the American model, which takes longer time and the results in aggregate terms are uncertain. First of all, the promise of the American model envisages such a scenario or the rule of politics by business that should happen in the future, while the rest of EU has gone to a more advanced stage until the countries concerned in the Balkans are shaping the American model which is causing the population to leave the country in large numbers, primarily to Germany.

The social market economy to maintain social welfare has to rely on charging, on average, higher taxes on businesses, mainly in increased progressive tax rates against large profitable corporations, thus it can meet the demand to provide opportunities for poorer class in different sectors, much of which do not directly support the economic growth (healthcare, education, sport). By this token, businesses in the European model are expected to have less available resources or funds for research and development, investment, growth and expansion as comparably larger proportion of their profit goes to the state which it uses differently. On the contrary, businesses in the American model are expected to have more at their disposal for research and development, thus they can become more innovative and competitive in general. It is this difference why some German economists, such as Seliger & Wrobel (2007) went to recommend that the American model is better for growth and development, from now on. Their claim leaves the impression that the German model (to some extent also of the EU) of social market economy can be preferable to a certain degree or until the beneficiaries of state social welfare become lazy by being accustomed to consume the resources of others or not produced by themselves. Such an assumption about the American model superiority, in particular against the pure German model, should be tested by more detailed empirical studies, among others, to test the hypothesis: If the American model goes faster, becomes more innovative and competitive, then where it will lead in perspective if it does not actively support the rest of population for the labor market as Germany does through vocational training and free education? In Germany, the unproductive or incapable is prepared for the labor market and in the economy through the state programs of social welfare. The American alternative to this question is simpler and it works more efficiently; the USA attracts and imports skilled workers and professionals from across the globe. Why spending the national resources to the proportions of German model for training when we can get them ready from abroad, and leave our businesses with more available profit to further innovation and development, would be the answer of the American model.

At the center of political ideology related to economic development in the USA between democratic and republican party is their rivalry which has always kept a balance in response to economic circumstances. Historically, the two parties, including the President with the power akin to a monarch, have come to and gone from power depending on how the economic situation has evolved and is present. The democrats, who are more or less a left party with similar ideology like in the EU model, follow a similar approach as they are more socially oriented than the republicans. If income differences in the US grow stronger, then it may be the time to favor and vote for a President from the democratic camp. Since the democrats are more socially-oriented like in the German model but to a lesser extent, then when it is observed that the system is taking a toll as a social burden offered to the "parasites" or the system is sliding to the "laziness", then bring back the republicans to resume their agenda of reforms but without changing the system. That is only an ideological principle which in the USA elections not necessarily applies all the time among the two parties – democratic and republican.

4. The Western Balkans is still in transition; social market economy is a better model

The lack of theories on transition from communism to capitalism was one the main reasons of transition surprises. There were theories on transition from capitalism to communism, but not so much in the other way around until communism became seriously weakened, both politically and economically. Ironically, in former Yugoslavia, a popular jargon "Amerika i Engleska biče zemlje proleterska (America and England will become proletarian countries)" was informally invented in the golden days of communism, as if communism was an everlasting system. That was enough for some not to ever think of giving it up to adopt the American or the British system instead. And they were even not eager to embrace any radical economic change until the civil wars broke out, resulting in a more radical change in all aspects of society. Slovenia broke away from Yugoslavia after 10 days of war, and is not part as we define it as the Western Balkans. In Croatia (1991-1995) and Bosnia and Herzegovina (1991-1995) there was greater destruction, loss of population (only in Bosnia over 100 000 killed and over 2 million refugees), and ethnic cleansing. Albania also experienced a kind of civil war in 1997. Her neighboring Kosovo that was part of former Yugoslavia also witnessed war, destruction and massive displacement of the population in 1999. It is beyond the scope of this paper to discuss further on political and economic events of these countries. Perhaps, of greater importance is what economic reforms they have in place, from which we have selected the rate of taxes, with a focus on Value Added Tax (VAT), Personal Income Tax (PIT) and Corporate Income Tax (CIT).

Table 2. Three main tax rates in the Western Balkans (in %) as of 2018

Countries	**VAT***	**PIT****	**CIT**
Albania	20	23	15
Bosnia	17	10	10
Croatia	25	36	18
Kosovo	18	10	10
Macedonia	18	10	10
Montenegro	21	9	9
Serbia	20	10	15
Germany	**19**	**47**	**30**
USA	**0**	**37**	**21**

*Includes only the standard rate for majority of products and services, not the differentiated or lower rates applied to some food items and medicals.
** Ceiling rate, including the breakdown of lower rates by incomes.
Source: Governmental sites summarized at: https://tradingeconomics.com/, accessed on February 2019.

The figures in Table 2 cannot explain the broad picture of the economic model, but they do help a lot in understanding what they aim to and likely results in the economy they will produce. VAT, somewhere known as sales tax, is the main tax and revenue contributor to the state budget of almost all countries in the Western Balkans. It has a relatively higher rate than PIT and CIT, and it is mainly a tax on consumption which the citizens have to pay. Its higher rate along with lower rates in PIT and CIT implies that majority of the population have to pay more to the state on daily basis, while the corporations or the rich have their tax rate lower. This is one of the main sources of income inequality, or the one that is imposed by the state to make the rich richer as the Washington Consensus expects to allow more freedom for businesses to advance their growth at the expense of someone else that pays the VAT. As noted in theoretical consideration comparing the principles of American and German model, we can witness from the figures in Table 2 that Germany charges higher rate of taxes for PIT and CIT, and lower for VAT (even lower than in four out of seven countries in the Western Balkans), than in the USA. CIT in Germany is taxed at a rate 30% compared to 21% in the USA, which is line with the basic concept of the two models regarding taxes. PIT is also higher in Germany than in the USA, 47% versus 37% respectively.

In this way, the difference in concepts between the American and European or German model is also manifested by their legal enforcements in economic policies, the most notable example which is in tax rates. Looking at the tax rates in force in the Western Balkans, it can be argued that these countries are still implementing the reforms fitting the Washington Consensus recommendations, despite their aspiration and the process to join the EU. The result of such economic policy is not a problem of rising income inequalities which in the USA can lead to more economic growth, but to emigration. Once upon a time the people of former Yugoslavia were leaving their country due to security reasons (the civil wars of 1990s) to the Western developed countries, but now many of them leave as their model of economic development does not meet their requirements, or they are unhappy with it.

Conclusion and implications

The post-communist countries in CEE, in the Western Balkans in particular, have gone through a period of systemic political and economic changes. In the latter case, this transition was especially dramatic which coincided with disintegration of the former Yugoslavia and emergence of her successor states. The package of reforms implemented in the rest of CEE known as the Washington Consensus, was also put in operation in this part of Europe. The results as of the second decade of the 21st century are mixed as on one hand they led to economic growth and development, but it caused a number of structural distortions on the other hand. Among others, the reforms enforced by the state for an open market economy are leading to emergence of economic and political class while pushing many others into poverty and causing them to leave their countries in search of better economic life and welfare. They are unhappy with the model in place which favors some at the expense of the rest in this region of the Balkans that is still a potential source of ethnic conflicts.

Some may even maintain that it is already late to embark on yet another model of economic development apart from the one that the Western Balkans has experienced with for more than two decades. However, there are two crucial aspects in which these countries should move in economic reforms, and this amounts to abandoning the American model in favor of the European one. First, as discussion and few figures from this paper suggest, these countries are still implementing the package of reforms from the Washington Consensus, and the results observed so far, are as expected, diverging to some extent from the EU requirements and reality. Second, this part of Europe, except Croatia, is completely surrounded by the EU member states, and in the near future is expected to be part of it. Although it receives a lot of EU support as part of accession and membership, it is running policy reforms that are no so much in the spirit of European model. In order to be more in compliance with the European model, the governments in the Western Balkans should reform their taxes by lowering the VAT and increasing the PIT and CIT. Policy makers would object that such a move by imposing higher taxes constrains both foreign and domestic investment. But these are small and poor countries whose population is gradually shrinking through emigration. They have no time to go through an American path of development, because the USA is a very large and developed country with global impact. The American model does not fit and cannot work in the Western Balkans, or if it does, its performance is arguably poorer in aggregate terms than of social-market economy. Businesses from the Western Balkans will find it hard to become competitive on a global scale like American corporations, even if they are highly encouraged by very low tax rates.

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