# And the Last Shall be First: Party System Institutionalization and Second-Generation Economic Reform in Postcommunist Europe*

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We investigate the conditions under which state reformers in postcommunist Europe can implement radical policies aimed at boosting investment now that the fundamental institutions of a market economy are in place. Surprisingly, such reforms are now being pioneered by those countries considered laggards of the first-generation, market-making reforms in the 1990s. Party system institutionalization offers the best explanation for who adopts second-generation reforms, to what degree, and when. Such institutionalization, which enhances vertical accountability between governments and voters, puts state reformers at a disadvantage in enacting second-generation reforms. By making it difficult to create a coherent and credible opposition against reform, underinstitutionalization insulates state reformers from social and political pressures, allowing them to undertake economic policies hard to envision in a more developed democracy. We test this hypothesis by comparing recent reform attempts in Slovakia, Estonia, Hungary, the Czech Republic, and Romania.

> "As a liberal economist, I view the Slovak economic reforms positively and I prefer them to our [Czech] 'quasi-reforms.' However, the fact that the whole reform process in Slovakia went very smoothly would suggest to me that it progressed without any public support. It is extremely unlikely that such reforms could be undertaken in Germany, France, Italy or the Czech Republic at such a pace without tough debates in society."
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> *Václav Klaus, Czech President and former finance- and prime minister*[1]

In 2004, the World Bank named Slovakia the global economic reformer of the year—a remarkable turnaround for a country that just years earlier had been

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considered the reform laggard of East Central Europe. By the late 1990s, Slovakia had seemed primed for economic meltdown, not accolades from the World Bank. In 1999, Citibank had stood within days of pulling out of the country, citing its weakening currency, high interest rates, and depleted foreign reserves (Barrionuevo, 2005). Slovakia's turnaround was based on a radical set of business-oriented reforms, including sharp reductions in taxes, the institution of a uniform flat tax for individuals and businesses, steep cuts in social programs, weakened labor regulations, and generous incentives to foreign investors (IMF on Slovakia, 2004; EIU on Slovakia, 2004). None of this was popular with the Slovak public. As the finance- and vice prime minister, Ivan Mikloš commented, "This government is among the most unpopular, if not the most unpopular government in the short Slovakian history." Public opinion polls showed that some 70 percent disapproved of the government (Barrionuevo, 2005). Though the reforms were successful in attracting foreign investment, they remained unpopular with the greater part of the public.

Slovakia exemplifies a new generation of reform in postcommunist Europe and highlights a paradox of economic policymaking in the latest stage of transition: What political conditions favor the adoption of radically pro-business policies in new democracies that have already consolidated the basic elements of a market economy? Slovakia's policies typify what we call "second-generation reforms."[2] The first generation of postcommunist reforms aimed to establish the basic conditions for a market economy: dismantling central planning and price controls, stabilizing inflation, establishing currency convertibility, opening up to international trade, privatizing, and establishing a market-based legal framework (Sachs, 1993). During the 1990s, they were initiated and implemented (with varying degrees of success) across the postcommunist region.

If the first-generation reforms were about building a market economy, the second generation reforms are about creating a favorable investment climate once the market is in place—to tap, in particular, investment flows opened up by accession to the European Union. Strengthening business while undercutting organized labor, this deregulatory package suggests the emergence of a very different political economy than the social welfare state of postwar Western Europe (Bohle and Greskovits, 2006). By privileging efficiency over social cohesion, the second-generation agenda runs counter to Western Europe's social market model.[3] Slovakia's flat tax policies, investment incentives, and welfare cuts have been labeled "social dumping" in Western Europe. The French finance minister even suggested limiting European Union (EU) Structural Funds to countries that undercut European social regulations ("Slovensko sa bráni," 2004).

In pushing for greater deregulation than in Western Europe, second-generation policies are, if anything, even more unpopular with the general public than the first-generation reforms were; at least in the first generation, the alternative—the command economy—was perceived as the clearly worse alternative. Moreover, the new policies drastically reduce the state's welfare commitment to those most disadvantaged by the first-generation reforms: the unemployed, elderly, and less educated. In Slovakia, tax cuts and business incentives were funded by cutting unemployment benefits in half and a VAT increase that sharply raised the price of food, energy, and medicine (Bohle and Greskovits, 2006: 21). Meanwhile, the state relinquished its capacity to redress inequality through a progressive income tax. These reforms

led to riots when the government's cuts to the social welfare system took effect. With the cuts, "the basic welfare payment for an individual fell by half to about $200 a month." To quell the riots, more than 2,000 police and army were deployed, Slovakia's largest deployment since the 1989 revolution (Fisher, 2004). Without attempting to assess the fairness of second-generation policies, we begin from the premise, acknowledged by their proponents, that they primarily benefit business and are likely to be opposed by the working classes and poor (Mikloš, 2004).

Second-generation policies exploit investment opportunities opened up by EU accession and, in a kind of competitive deregulation, are heavily influenced by developments in neighboring countries. Slovakia's policies have pressured the Czech Republic, Hungary, and even Austria to lower their taxes as well. After the 2004 EU enlargement, Austria's government lowered the corporate tax from 34 to 25 percent, stating that, "The reduction of the corporate tax rate from 34 to 25 percent is to create vital impetus for the relocation and foundation of new businesses" (Federal Chancellery of Austria, 2004). Though all governments in the region are discussing second-generation reforms, there has been considerable variation in who adopts them, to what degree, and when.[4]

How can we explain this variation? The pattern of policy enactment counters the expectations that derive from much of the literature on economic transition in new democracies, particularly postcommunist ones.[5] An influential strand of that literature argued that, because of its social costs, economic reform is most effectively undertaken by powerful executives insulated from popular pressures (Przeworski, 1991). A rival argument countered that isolated executives were more likely to block reform and suggested that greater popular participation favored reform (Hellman, 1998). Yet a third argument suggested that what really mattered was the degree of elite polarization: polarization undermines government commitment to a given reform and hence its effectiveness (Frye, 2002).

We argue that second-generation reforms do not fit the predictions of any of these models. Contrary to Hellman, they are more likely in weakly consolidated democracies in which underinstitutionalization attenuates the public's voice in policymaking. Contrary to Adam Przeworski, states whose institutions do not concentrate executive power are equally if not more likely to enact second-generation reforms. Finally, counter to Frye's prediction, the second-generation reformers include countries with a high degree of party polarization—nowhere more so than in Slovakia following Mečiar—and that polarization has not undermined the reforms' effectiveness.

What stands out about the second-generation reformers is the following. They have been parliamentary democracies with weak executives. They have chaotic party systems, whose underinstitutionalization weakens vertical accountability between government and voters (O'Donnell, 1999: 29-30). Finally and least surprisingly, they have been initiated by conservative-led governments. By making it difficult to create a coherent and credible opposition, party system underinstitutionalization insulates state reformers from social pressures, allowing them to undertake painful reforms hard to envision in a better institutionalized democracy. We expect that party system institutionalization will offer the best explanation for who adopts second-generation reforms, to what degree, and when.

To assess this hypothesis's plausibility, we compare recent economic reform attempts in Slovakia, Estonia, Hungary, Czech Republic, and Romania. Each has

participated (to varying degrees) in this second generation of policies designed to take advantage of investment opportunities offered by EU expansion. Slovakia, Estonia, and Romania now have flat tax systems that put their taxes among the lowest in Europe. Leaders in the first generation of market-building reform and in party system institutionalization, Hungary and the Czech Republic seem unable to follow the lead of upstarts like Slovakia. Hungarian and Czech policymakers failed to bring similar tax reforms to life—even under conservative governments. The country studies below trace differences in the timing and extent of second-generation reform enactment to the degree of party system institutionalization.

## The Origins and Agents of Second-Generation Reform

Before turning to the essential prerequisite for second-generation reform enactment, an underinstitutionalized party system, we must briefly address where the impulse for such reform comes from. As is typical with transnational policy diffusion, several factors combine to spread the policies' underlying ideas. First, there are changes in the international sphere such as the rise of transnational advocacy networks of academics, international financial institutions, and policy NGOs. None of the second-generation policies were "invented" in postcommunist Europe; they originated among Western policy experts, were nurtured by Western advocacy networks, and only now are taking root in postcommunist Europe.[6] Showing the influence of transnational actors on economic reform, new scholarship on pension policy has shown that the World Bank and USAID have been intervening actively across the world to shift pensions toward a neoliberal model (Orenstein, 2006).[7] The World Bank showered approval on the Dzurinda government's reforms in naming Slovakia the world's leading economic reformer of 2004. Though the advocacy of international financial institutions has not been as intense for policies like the flat tax as it has been for pension reform, the flat tax has received enthusiastic support from conservative organizations like the Heritage Foundation and the Hoover Institution.[8]

Yet, for these ideas to have an effect, they need to find champions within the domestic political elite. As we describe below, the initiative for second-generation reforms tends to come from young technocratic elites without connections to the former regime. Typically, they are trained abroad, usually as economists. Estonia's 32-year-old reform architect Mart Laar is the paradigmatic example, but Slovakia's Ivan Mikloš, and the Justice and Truth Alliance (DA) cabinet in Romania also fit this profile. Inspired and advised by transnational policy networks and working from the institutional base of the Finance Ministry, these technocratic reform teams can bring fully formed, complex policy proposals to parliamentary representatives that often only imperfectly understand them (Mikloš, 2004).

Together, these internal and external factors form the "push" behind the diffusion of second-generation policies. Sorting out their relative weight is beyond the scope of this article. Instead, we accept that each contributes to the pressure for reform enactment and focus on the domestic political factor that determines whether the pressure for policy diffusion is transformed into actual policy—party system institutionalization.

## Theorizing Economic Reform: The First-Generation Perspective

Our argument differs from previous theorizing about economic reform in Eastern Europe's new democracies, which has three dominant strands. Highlighting the tension between economic reform and political stability, Przeworski's (1991) "J-curve" was the starting point for much of this theorizing. He argued that since reforms only produce positive results in the medium- to long-term, after a period of economic pain, reform governments can expect strong opposition, including defeat at the polls, as a reward for their efforts (1991:161). From this logic flowed the precepts (1) that governments undertake reforms early, while still sufficiently popular to withstand their social costs and (2) that reformers insulate themselves from the inevitable antireform coalitions through institutions that concentrate and enhance executive autonomy. In practice, this has meant a preference for presidential systems, which offer stable tenures and reduce the need for coalition building, and against parliamentary systems, in which government tenure depends on maintaining a majority coalition. The bigger the parliamentary coalition, the more vulnerable the reform to transition's losers.[9]

As powerful as the J-curve's logic appears, it has invited two major challenges. First, Joel Hellman (1998) challenged its assumption that the most politically consequential opposition would come from that greater part of the public who lose from reform in the short term. Instead, it is the short-term winners who pose the greatest threat since these are the few, usually politically connected, who benefit from a partially reformed—that is, quasi-privatized, selectively deregulated—economy. Despite the high costs to society, these short-term winners can block completion of the reform process, preserving for themselves the spoils of partial reform.

After Hellman's analytical shift, the institutions recommended by Przeworski appear in a more sinister light. A strong president who is politically insulated from electoral pressures is precisely the situation to be avoided: by capturing this executive, a few short-term winners can block full reform. The best way to restrain such winners and escape the "partial reform trap" is to expand political participation and to open policymaking to the wider public who stand to gain if the reforms are completed (1998: 228, 234).

More recently, Timothy Frye (2002) has shifted the debate away from institutions (Should they emphasize executive dominance or political participation?), focusing instead on elite polarization. Frye argues that economic performance, not reform enactment is the important criterion for transition success, and economic performance depends on the struggle between former communist and anticommunist factions engaged in a war of attrition over economic resources. In sharply polarized political systems, the "electoral calendar" hinders reform: as elections approach, the odds of a change in economic policy increase and growth rates plummet. Not reform enactment, but reform *over*-enactment, or policy reversal, is the problem.

The debate among these three models played out with reference to the market-building phase of the postcommunist economic transition; whatever their relative explanatory power for that period, they are all poorly adapted to explaining second-generation reforms. Once Hellman's partial-reform trap has been overcome, maximizing participation in policymaking is no longer the best strategy if the goal is to attract investment through competitive deregulation. Whereas the general

public stood to gain from escaping the partial reform trap, the same is not true of competitive deregulation that primarily benefits business and eliminates the state's ability to redistribute income. Does this mean a second wind for Przeworski? No, although the governments that have taken second-generation policies the furthest have done so in the absence of a credible opposition, their ability to do so has not generally resulted from strong executive institutions.[10] Instead, the absence of effective opposition resulted from low levels of party system institutionalization, which frustrated the translation of what was considerable social resistance into credible political opposition. Finally, Frye's analysis offers less guidance for this stage of transition than it did for the first because the dichotomy between former communists and anticommunists is fading rapidly. Operationalizing polarization in these terms provides a misleading picture for second-generation reformers like Slovakia and Romania. Slovakia's second-generation reforms were possible only after the toppling of the Mečiar government in 1998, an alternation of government so polarizing it was called Slovakia's second revolution. Furthermore, why have unpolarized political systems like the Czech Republic and Hungary found it so difficult to implement this newer round of reform?

## The Politics of Second-Generation Reform: The Advantages of Underinstitutionalization

Second-generation economic reforms constitute a policy package designed to advantageously position Eastern European countries for the anticipated influx of new investment in an expanded European Union. They share the following core features:

1. Steep tax cuts for business, simplification of the tax code, and a preference for flat-tax systems;
2. Generous incentives to foreign investors, including long tax holidays and land grants;
3. Loosening labor regulations with little consultation from organized labor;
4. Funding tax cuts and incentives through a reduction in the state's commitment to the social welfare system.

Whatever their appeal to economists, such policies are bound to be unpopular with large portions of the voting public. In the short term, they benefit business at the expense of labor and the poor, and in the long term, flat taxes reduce the state's ability to redress inequality. Their advocates portray them as a bitter pill leading to long-term benefits for everyone; but to point this out is to ignore the fact that elected governments need to worry about their policies' short-term consequences. In what kind of political system would the government pursue policies that provoke fierce social opposition in the immediate term? In a system that frustrates the translation of social opposition into credible political opposition.

Second-generation reforms are most likely under the following two conditions. First, and more trivially, it is necessary to have a government led by conservatives. Even though competition for investment puts pressure on all governments to deregulate regardless of their political stripe, a policy package consisting of flat taxes and reduced social spending enforced over the opposition of organized labor is more than most social democratic governments will contemplate. Second, absent a benevolent despot who can force such policies over all opposition, the chances for

sustaining such a reform package are greatly increased in an underinstitutionalized party system. Underinstitutionalization prevents social opposition from finding effective political voice and organized representation.

Especially for new democracies, party system institutionalization is the most important mechanism of vertical accountability, the ability of electorates to discipline governments through the threat to "vote the rascals out." In institutionalized systems, elections present voters with manageable and meaningful choices: there are a limited number of stable parties with familiar coalition-building preferences to choose from (Mainwaring, 1999: 3; Mair, 1997; O'Dwyer, 2006; Toole, 2000: 458; and Kreuzer and Pettai, 2003). Underinstitutionalization means that elections present too many options: voters choose among parties that are often new, unfamiliar, and have uncertain prospects. Government coalitions may be fragile and programmatically heterogeneous, but the opposition is even less organized. Lacking clear constituencies, opposition parties are less resistant to cooptation by the government, and their fragmentation means that the opposition vote is divided among many parties who may not cooperate with each other.

All of this creates considerable maneuvering room for a determined reform team that controls the key ministries and comes prepared with a comprehensive legislative agenda. The lack of an organized opposition allows them to proceed rapidly and radically.[11] As the epigraph by Václav Klaus suggests, such maneuvering would not be possible in an institutionalized party system. In an institutionalized system, concern for their future electoral prospects prevents government parties from allowing their ministry appointees to propose radical policies. In an uninstitutionalized system, innovative governing formulas make possible new partnerships in the next elections, and long-term electoral calculations are difficult anyway. In an institutionalized system, the opposition would be sufficiently organized to credibly threaten a no-confidence vote, and popular resistance to the program would be voiced by at least some of the parliamentary parties.

Insulating policymakers from social opposition through the mechanism of underinstitutionalization is a two-edged sword. It might facilitate reforms, but what is to prevent elites from pursuing rent-seeking policies? In the context examined here, a few factors help prevent the latter. The international and domestic factors outlined earlier—the influence of international policy networks and the sociological profile of the reformers—mitigate against rent-seeking. Moreover, in the EU member- and applicant-states of Eastern Europe, close monitoring by Brussels works against rent-seeking elites (Vachudová, 2005). Finally, to the extent that first-generation, market-making reforms are complete, the biggest rent-seeking opportunities, those from partial reforms, are now closed off. There is, however, no reform guarantee; the success of Slovakia and Estonia notwithstanding, this consideration together with the essentially undemocratic nature of this reform model will hardly recommend it to institutional engineers.

The question of why some party systems fail to institutionalize and establish reliable mechanisms of government accountability has generated considerable research (Mainwaring, 1999; Mair, 1997; Kitschelt et al., 1999). Kitschelt and his collaborators have argued that the presence of multiple social divides in the electorate can have this effect: rather than being structured by the conventional left-right, economic-redistributive divide, party systems are bisected by additional ethnic, sociocultural, or national-cosmopolitan divides. The greater the number of divides,

the more difficult it is for party competition to stabilize and parties to institutionalize (Kitschelt et al., 1999: 62-69). At least one such divide captures the variation in institutionalization in the countries analyzed here: the ethnic divide. In Slovakia, Romania, and Estonia, ethnic politics frustrated the development of a left-right party spectrum structured by a dominant socioeconomic cleavage (Vachudová and Snyder, 1997; Mikkel, 2006: 42). Conversely, Hungary and the Czech Republic both lack significant minority populations, and their party systems are both more institutionalized and structured around socioeconomic cleavages.

Underinstitutionalization—for whatever reason it may occur—is commonly measured using electoral volatility, which captures both the stability of parties' constituencies and their internal organization. We measure volatility by calculating the net change in the vote shares of all parties across elections: the more the vote shifts among parties between elections, the less settled, or institutionalized, the party system (Mainwaring, 1999: 28).[12]

## Country Studies

We test this argument's plausibility by looking at five countries, three of which have poorly institutionalized party competition and two of which stand out as among the most institutionalized in the region. Which elements of the second-generation agenda has each country adopted, when, and how thoroughly? Tables 1-3 summarize the key political and policy differences across countries. The following case studies examine each country in more detail.

**Table 1**
**Electoral Volatility (1990-2006)**

| | Czech Republic | Hungary | Estonia | Slovakia | Romania |
|---|---|---|---|---|---|
| Between 1st and 2nd Election | 67.3% | 21.1% | 70.7% | 51.9% | 76.0% |
| Between 2nd and 3rd Election | 28.7% | 31.5% | 45.5% | 37.3% | 53.4% |
| Between 3rd and 4th Election | 17.5% | 19.3% | 32.4% | 55.1% | 72.7% |
| Between 4th and 5th Election | 22.4% | 6.6% | - | 40.9% | 75.1% |
| Between 5th and 6th Election | 16.0% | - | - | 24.5% | - |

Hungary has a mixed electoral system. To be consistent with the other cases, only the results of the party list elections were used to calculate electoral volatility in Hungary. Table covers all parliamentary elections from 1990 to 2006. These were 1990, 1992, 1996, 1998, 2002, and 2006 for the Czech Republic; 1990, 1994, 1998, 2002, and 2006 for Hungary; 1992, 1995, 1999, and 2003 for Estonia; 1990, 1992, 1994, 1998, 2002, and 2006 for Slovakia; and 1990, 1992, 1996, 2000, and 2004 for Romania. Because its parties have been prone to splits and mergers, Romania's volatility scores are exceptionally high. Even if we relax our criteria and count its postcommunist electoral coalitions—across their various guises—as one party, we still arrive at consistently high levels of volatility in Romania: 78.9 percent by the second elections, 31.0 percent by the third, 49.1 percent by the fourth, and 38.5 percent by the fifth.

*Sources*: University of Essex, Political Transformation and the Electoral Process in Postcommunist Europe <http://www.essex.ac.uk/elections/> and the Centre for the Study of Public Policy, University of Strathclyde, Studies on Societies in Transition <http://www.cspp.strath.ac.uk/index.html>.

**Table 2**
**Top Income- and Corporate Tax Rates in Estonia, Slovakia, Czech Republic, and Hungary**

| Country | Personal Income Tax In… 2004 | Personal Income Tax In… 2005 | Corporate Tax In… 2004 | Corporate Tax In… 2005 |
|---|---|---|---|---|
| Czech Republic | 32 | 32 | 31 | 28 |
| Estonia | 33* | 20 (flat tax) | 35* | 0 |
| Hungary | 40 | 38 | 18 | 16 |
| Slovakia | 38 | 19 (flat tax) | 25 | 19 |
| Romania | 40 | 16 (flat tax) | 25 | 16 |

* This rate for Estonia is from 1993, a year before a flat tax was established.
*Sources*: "Flat tax" (2005); U.S. Department of State, "Estonia Economic Policy and Trade Practices" <http://gopher.state.gov/ERC/economics/trade_reports/1993/estonia.html>; EIU Romania Factsheet 2005 <http://www.economist.com/countries/Romania/profile.cfm?folder=Profile-FactSheet>.

**Table 3**
**Comparison of Second-Generation Reforms by Country**

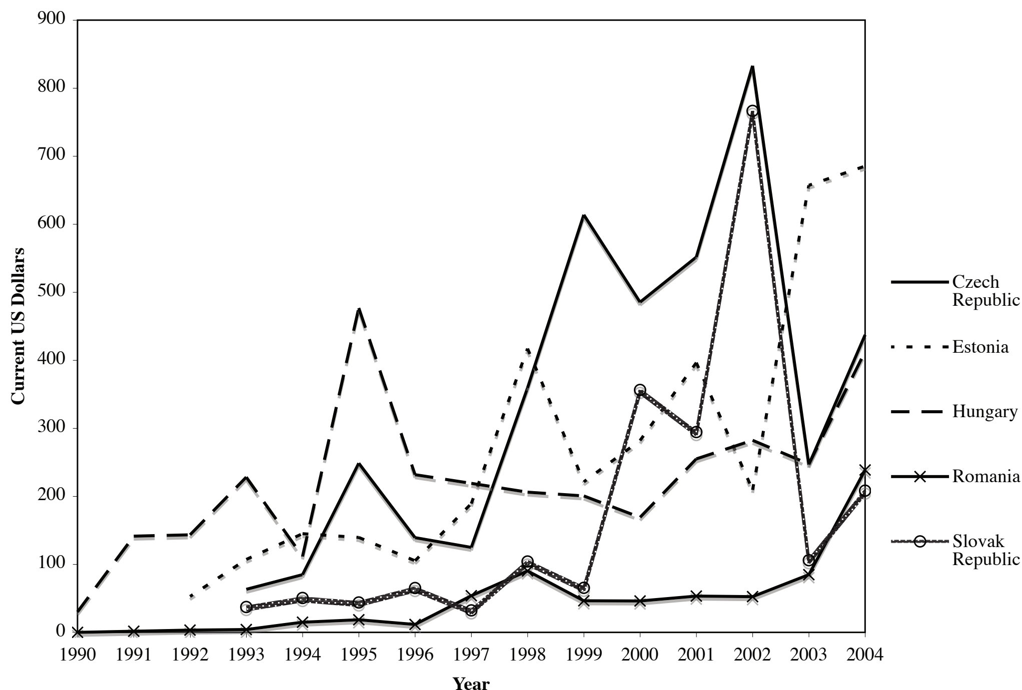
| *Country* | *Tax Cuts* | *Flat Tax* | *Investment Incentives* | *Reductions in State's Welfare Commit-ments* | *Reduction in Power of Organized Labor* | *Overall Character of 2G Reforms* |
|---|---|---|---|---|---|---|
| Estonia | Radical | Yes | Extensive | Yes | Yes | Radical |
| Slovakia | Radical | Yes | Extensive | Yes | Extensive | Radical |
| Hungary | Moderate | No | Neutral | No | Not much | Weak |
| Czech Republic | Moderate | No | Neutral | No | Not much | Weak |
| Romania | Radical | Yes | Yes* | Yes* | Yes* | Radical* |

* Though it is too early to evaluate the record of Romania's new government, its statements and early steps signal a commitment to economic policies consistent with the direction of Estonia and Slovakia.

As Table 1 shows, both Hungary and the Czech Republic have low and declining electoral volatility. Though declining over time, Estonia's volatility is consistently higher than the Czech Republic and Hungary's. At the time of reform enactment, volatility in Slovakia and Romania was stubbornly high. The underinstitutionalized Estonian, Slovak, and Romanian party systems permitted their governments to enact the most radical second-generation reforms. The more institutionalized Hungarian and Czech systems have either prevented or seriously attenuated their governments' ability to follow suit. As Table 2 shows, Estonia, Slovakia, and Romania have enacted more radical tax cuts than the Czech Republic or Hungary.[13] Unlike the Czechs and Hungarians, they have also replaced progressive tax systems with flat ones. Finally, Table 3 summarizes the adoption and implementation of second-generation reforms more generally.

Figure 1 and Table 4 show, first, that the economic context in which second-generation policies are (or are not) adopted differs substantially. Reflecting the low credibility of their first-generation, market-making reforms among international investors, Slovakia and Romania trailed the Czech Republic, Hungary, and Estonia in attracting investment throughout the 1990s. This gap provided the impetus for

**Figure 1**
**Per Capita Net Investment Inflows by Country, 1990-2004**




*Sources*: Authors' own calculations based on World Development Indicators database, <http://devdata.worldbank.org/>.

**Table 4**
**Selected Economic Indicators**

| Country | Average Unemployment Rate, 1993-2003 (%) | Per Capita GDP in 2003 (US$) | Average Real GDP Growth, 1993-2005 (%) | Cumulative FDI, 1990-2004 (Nominal US$ Billions) | Average Per Capita FDI, 1993-2004 (US $) |
|---|---|---|---|---|---|
| Czech Republic | 6.0 | 8,771 | 2.3 | 42.9 | 349 |
| Estonia | 10.2 | 6,720 | 4.3 | 5 | 296 |
| Hungary | 8.2 | 8,278 | 3.4 | 34.1 | 253 |
| Slovakia | 15.9 | 6,045 | 4.0 | 15.9 | 178 |
| Romania | 9.1 | 2,624 | 2.5 | 11.5 | 60 |

*Sources*: Authors' own calculations using EBRD Transition Report 2000, 2005; Eurostat <http://epp.eurostat.cec.eu.int>; World Development Indicators database <http://devdata.worldbank.org/>.

the laggards to embrace the radical second-generation agenda—particularly given the example of Estonia. Estonia's foreign investment takeoff began after 1995, the year in which it enacted a package of radical, pro-business reforms; it has been a regional leader in per capita FDI and economic growth since. Though Slovakia's FDI statistics show an uptick after reforms began in 2003, there are not yet sufficient data to gauge the reforms' results in Slovakia and Romania. According to one comprehensive analysis of Slovakia, the number of large-scale foreign investment projects jumped from 25 in 2002 to 47 in 2004, and included firms such as Kia, Hyundai, Peugeot, and Samsung (Goliaš and Kičina, 2005). Others note that Slovakia's tax policies were key to winning Kia's investment (Bohle and Greskovits, 2006: 21).[14]

Second, Table 4 suggests the further social costs imposed by second-generation policies on those already disadvantaged by the economic transition. Unemployment in Slovakia has averaged 15.9 percent since 1992 and was 17.4 percent in 2003 on the eve of its reforms. By removing job protections and sharply reducing social insurance, while at the same time removing the state's ability to redistribute through taxes, the reforms offered little promise to these most disadvantaged. With its much lower per capita GDP, the consequences of Romania's second-generation policies for the poor are even starker.

*Slovakia*

Criticized for years, Slovakia's economic policies are suddenly viewed as exemplary. Yet the reforms that have so successfully attracted foreign investors reflect less well on Slovakia's democratic development. Under Prime Minister Dzurinda, guided by Finance Minister Mikloš, the Slovak government undertook radical second-generation reforms beginning in 2003. As in Estonia, the reform team comprised young, foreign-trained economists in the Finance Ministry; some had experience working for transnational institutions such as the OECD but were too young to have prior experience in Slovak politics.[15] Slovakia's reforms also reflected the influence of transnational policy networks; within a year of their enactment, at a conference entitled "Economic Reforms for Europe," representatives from the World Bank,

the Heritage Foundation, and the OECD held up Slovakia's policies as a model not just for the rest of the region but for Western Europe as well.[16] In Slovakia's under-institutionalized party system (Deegan-Krause, 2000; O'Dwyer, 2006; Stupňan, 2004), Mikloš's team was largely unchecked by a left-of-center opposition and was able to undertake these reforms without a meaningful social dialogue.

The proximate cause of this underinstitutionalization was the illiberal rule of former Prime Minister Vladimír Meciar from 1992 to 1998. Playing off ethnic tension first with Czechs and later with Slovakia's Hungarian minority, Mečiar's Movement for a Democratic Slovakia (HZDS) kept opposition parties divided and prevented the articulation of a clear socioeconomic cleavage in the party system (Deegan-Krause, 2000; O'Dwyer, 2006). Ironically, it was Mečiar's attempt to game the 1998 elections that finally forced the opposition to coalesce into a single, if still unstable, Party of the Democratic Coalition (SDK) that turned him out of power.[17] Between 1998 and 2002, the party system underwent another round of reorganization. Old opposition parties such as the postcommunist SDL' and the Movement for Civic Understanding (SOP) disappeared, while new parties like the populist *Smer* and the pro-business ANO vaulted to popularity. The 2002 elections resulted in the formation of a center-right coalition, which spearheaded second-generation reforms and which comprised reconfigured and renamed parties from the 1998-2002 government. Reflecting the ongoing lack of institutionalization, the two main government coalition parties since 2002, ANO and SDKÚ, experienced numerous defections by their deputies, leading to the loss of their parliamentary majority (Haughton and Rybář, 2004). Though weakened by these defections, this government was still able to pursue its reform agenda, thanks to the votes of breakaway MPs from both coalition and opposition parties (EIU on Slovakia, 2005: 13). Internally divided, unable to cooperate, and in the case of HZDS, opportunistically signaling its willingness to join Dzurinda's coalition, the main opposition parties *Smer* and HZDS offered little more than rhetorical resistance to the reforms (Žemlová, 2006).

In its first two years, Dzurinda's government leveled taxes to a flat 19 percent for both individuals and businesses and liberalized the Labor Code (EIU on Slovakia, 2004: 22). It courted foreign investors with ten-year tax holidays and subsidies for employee retraining and job creation (Gajdzica, 2003). The time required to start a business was halved, flexible working hours were introduced, and the time to recover debt reduced by three-quarters (Barrionuevo, 2005). The government began a restructuring of the health care and social welfare systems, including a privatizing pension reform (World Bank EU-8, 2004). Welfare cutbacks essentially halved benefits and required recipients to engage in some form of work (Fisher, 2004). These policies were implemented in the face of loud opposition from the country's unions. Ending an officially recognized tripartite bargaining system in place since 1989, the government dismissed the unions as a partner in the reforms ("Vláda," 2004; "Tripartita," 2004). Slovakia now has one of the least demanding regulatory and tax environments in Europe, combined with a minimal social policy. Low taxes and low welfare payments by employers are among the reasons why many West European businesses are relocating to Slovakia ("Slovensko láka," 2004).

Following the recent elections in June 2006, a question mark hangs over Slovakia's second-generation model. Campaigning against Dzurinda's economic reforms, the populist *Smer* party won a decisive victory, forming a coalition with HZDS and the

nationalist Slovak National Party. *Smer* has announced plans to increase taxes for the wealthy (Jančík, 2006) and lower the value-added tax on food and drugs (Hambálková, 2006). Given Slovakia's intentions to adopt the euro by 2009, however, observers suggest that *Smer* will adopt a pragmatic approach, adjusting rather than rolling back the reforms (Filipko, 2006).

*Estonia*

Like Slovakia, Estonia's most radical second-generation policies coincided with a period of party system flux and fragile coalitional politics. Reform came earlier in Estonia than in Slovakia—so early that it is difficult, temporally speaking, to separate its first- and second-generation reforms. As early as 1994, the government of Mart Laar was enacting a flat tax and privatizing pensions. Observers have called Estonia's economic transition "remarkable" and its record of containing inflation and supporting growth "enviable" (IMF on Estonia, 2004: 1).

Party system underinstitutionalization was crucial to Estonia's economic reforms; yet a feeling of crisis—more acute than in the Eastern European countries—also played a role (Feldmann, 2003: 518). A former Soviet republic, Estonia's economic dependence on the USSR was greater than Eastern Europe's. After independence in 1991, Estonia experienced hyperinflation, the collapse of its trade with the USSR, and plummeting industrial production (Feldmann, 2003). Laissez-faire economic policies were tools for cutting dependence on the USSR. Within a few years, Estonia had eliminated all import tariffs, introduced a currency board, achieved full currency convertibility, privatized much of its state-owned enterprise, and pioneered policies such as the flat tax that would later become the model for second-generation reforms in the rest of the region (Feldmann, 2003: 520).

As important as crisis was to Estonia's reforms, it cannot fully explain them. After all, economic crisis was typical after the fall of communism, but no one reformed as radically and rapidly as Estonia. Its policymakers were motivated by economic crisis, but they were facilitated by an underinstitutionalized party system that weakened vertical accountability and insulated them from organized political opposition.[18] As in Slovakia, an ethnic divide prevented the development of a clear economic-redistributive dimension in party competition (Mikkel, 2006: 42). Under Soviet rule, the massive inflow of Russian settlers reshaped the country's ethnic composition. The democratic opposition that developed under *perestroika* soon fractured on the question of citizenship for ethnic Russians (Smith, 2001: 72-74). The 1992 citizenship law, which was overwhelmingly endorsed by parties with conservative economic views, granted citizenship only to those who were citizens before Soviet occupation and their descendants—which excluded most non-Estonians. Parties with more left economic views were split on the citizenship issue; of the two biggest, the Moderates supported the exclusivist position, while the Center Party endorsed the "zero option," which would have granted citizenship to all residing in the country when it regained independence (Vetik, 1993: 274, 277; Smith, 2001: 81). Thus, although self-identified ethnic parties have been unsuccessful electorally (Mikkel, 2006: 23-25), the "national question" looms large in Estonian politics, and the perception that parties such as the Center were "overly compliant toward Russian-speaking settlers" has prevented the consolidation of a left opposition to neoliberal economic policies (Smith, 2001: 82).

Despite more recent signs of institutionalization, Estonia looked for most of the 1990s like its underinstitutionalized Baltic neighbors. As Marcus Kreuzer and Vello Pettai write, by standard measures of institutionalization "the three Baltic party systems appear so atomized and in flux that they barely resemble anything like established democracies" (2003: 83).[19] No Estonian government since independence has seen out its full term; they have all been multiparty coalitions whose internal differences eventually fractured them. This was the backdrop for Mart Laar's 1992-1994 government, which undertook the most radical reforms. It was a coalition of three loosely organized parties, two of them conservative (Laar's Fatherland Party and the National Independence Party) and one of them (the Moderates) more left-leaning. Though economically left, the Moderates shared their partners' exclusivist stance on the citizenship question (Smith, 2001: 81).

As in Slovakia, a cadre of young reformers in the Finance Ministry exploited the institutional autonomy afforded by the weakness of organized political opposition (Feldmann, 2003: 526-527). Just 32 years old, Laar exemplified the young Thatcherite technocrats whom his government placed in key positions; not only were they unconnected to the old regime, many were returned émigré Estonians. Capturing both the lack of public dialogue and the desire to emulate the West, Laar's reform slogan was borrowed from an American corporate advertising campaign, Nike's "Just do it!" (Smith, 2001: 83). As Laar acknowledged, his team found it unnecessary to explain their economic reforms to the public (Jaroš, 2004).

As in Slovakia, radical reforms undermined the government's popularity and, in 1995, it was replaced by a coalition that included the left-leaning Center Party and former *nomenklatura* Coalition Party. Surprisingly, this coalition did not reverse Laar's reforms, though its members had campaigned on this promise. In part, this reflected the difficulty of turning back such deep reforms, but the more important factor was the continued weakness of the left parties, who failed to define themselves in economic-redistributive terms. Their highly unstable coalition, riven by nationalist, former *nomenklatura*, and urban-rural divides, was "little more than a tactical alliance between parties with differing ideological viewpoints" (Smith, 2001: 96). When it fell in less than a year, the Coalition Party formed a new government with, of all things, the neoliberal Reform Party—which prevented any reform retrenchment. While a period of more left-oriented government and some greater degree of party system stability has hindered further reforms by Estonia's conservatives, the underorganization of the left has prevented any reform rollback.

The Laar government's main second-generation reform was introducing the region's first flat tax. The personal income tax is now 20 percent for all; the corporate tax on reinvested profits is 0 percent; and the social tax, which finances health and pensions, is 33 percent ("Flat Tax," 2005; EIU on Estonia, 2004: 33). It was the first government to launch structural reforms of the pension and social welfare system (IMF on Estonia, 2004: 1). To attract investors, foreign companies were permitted to buy and lease land. Relations with organized labor were not easy: the European Commission wrote that "the relationship between the Government and the social partners [is] still marked by difficulties in implementing effective tripartite social dialogue within the various newly established structures" (European Commission on Estonia, 2002: 76).

Successive governments did not significantly deepen these reforms, though they also did not undo them. Since 2003, the conservatives have returned to government

and have announced their intention to enact a new wave of foreign investment-oriented legislation, including lowering the income tax further. While too early to guess the fate of these proposals, it appears that the greater institutionalization of the Estonian party system in comparison with 1994 has weakened the government's hand. The time of radical economic policy shifts is drawing to an end as both sides of the party spectrum, conservative and social democratic, establish more stable constituencies, better defined programs, and predictable patterns of coalition formation.

*Romania*

In January 2005, a set of radical economic reforms took effect in Romania that closely followed the Slovak model. The underlying political conditions in the two countries also bore more than a passing resemblance. In both, elections antecedent to the reforms had been styled as a choice between Europeanization/modernization and more of the old (Gross and Tismaneanu, 2005). In both, the elections had been very close, with most votes going to parties representing the old power constellations. Yet, in both, the unsettled nature of the party system, in particular the possibility for innovative coalition formulas, allowed conservative newcomer parties to build unusual governing coalitions that then undertook reforms. Finally, the sociological profile of Romania's second-generation reformers closely resembled those in Slovakia and Estonia: the average age of the new Romanian cabinet was 44; with only two exceptions none of them had served in a previous government; and most of them were Western educated (Gross and Tismaneanu, 2005: 151).

Before the 2004 elections, the Romanian party system was characterized by party splitting and merging, the rapid rise of new parties, sweeping electoral reversals, and unpredictable coalition making—in short, persistent underinstitutionalization. As Table 1 shows, electoral volatility has consistently hovered around 70 percent, the highest rate for the countries considered here. Like Slovakia and Estonia, a clear economic-redistributive, left-right cleavage did not emerge in Romania; instead the party system was bisected by ethnic and political regime divides (Snyder and Vachudová, 1997). In 1989, former communists overthrew Ceausescu in Eastern Europe's only violent revolution. The former *nomenklatura* National Salvation Front government used exclusivist nationalism, and even force, to weaken the opposition. Successive splits and mergers have kept the postcommunist camp as an incoherent, shape-shifting entity. In 1996, it was replaced by a heterogeneous coalition of parties, the Democratic Convention of Romania; bitter conflicts among its five member parties made for an incoherent governing coalition (Popescu, 2003). The landslide 2000 election eviscerated the Democratic Convention, as shifting voter loyalties rewarded the latest incarnation of the postcommunist camp. Demonstrating the still underinstitutionalized character of the party system, an outsider party with an extreme nationalist-populist message, the Greater Romania Party (PRM), vaulted to second place in these elections.

The 2004 elections saw a new round of volatility and unpredictable coalition formation. As in 2000, a new electoral alliance surged past the established governing parties—the self-styled Europeanizers of the Justice and Truth Alliance (DA) (Gross and Tismaneanu, 2005). The DA's 31.3 percent vote share actually put it behind the left-of-center National Union electoral alliance led by the ruling Social

Democratic Party (PSD). Unexpectedly, one of the National Union's constituent parties, the left-leaning Humanist Party of Romania (PUR), defected to the DA after the elections, making possible a "patchwork" government of the DA, the Hungarian minority party, and PUR. Even the DA's chairman and Romania's president, Traian Băsescu, was embarrassed by the heterogeneous and improvised character of his party's governing coalition, calling it an "immoral alternative" to a minority government (Gross and Tismaneanu, 2005: 151). It is this coalition that has initiated Romania's second-generation reforms.

Before 2004, Romania's economic reform record was lackluster, as evinced by its poor record attracting FDI. Much of its progress toward market reform first came in the late 1990s, and then largely as a result of the requirements of the EU accession process (Vachudová, 2005). Even granting the liberalizing thrust of these reforms, they were not second-generation policies of the kind outlined above. The personal income tax rate remained progressive (ranging from 18 to 40 percent), and the Labor Code offered strong protections to employees (IMF on Romania, 2004: 3).

Romania's embrace of second-generation reforms was made possible by the election of an internally heterogeneous and unexpected coalition. Given its short time in office, this program is still being shaped, but already these are some of the most radical reforms undertaken in Romania since 1989 and self-consciously follow the model of Slovakia and Estonia. The government has introduced a uniform 16 percent flat tax for individuals and business (see Table 2). It has pledged to pursue additional economic reforms on a free-market model of minimal state involvement (Billings, 2005: 3). The declarations are apparently not enough for DA chairman Băsescu, who has been "critical of the government for moving too slowly to implement crucial reforms [and thus plans to] instigate a major cabinet reshuffle, if not call an early election" (EIU on Romania, 2005: 1).

### *Hungary*

Hungary excelled in first-generation reforms but, despite the efforts of its conservative-led government from 1998 to 2002, has only very selectively and partially implemented the second-generation reform agenda.

Like the Czech Republic, Hungary has exhibited a consistently high level of party system institutionalization (Toole, 2000). Since 1990, programmatically cohesive center-right and center-left governments have alternated in power, and each government has served its full term. All four parties currently in parliament have been present in the legislature since the early 1990s. As in the Czech Republic, two parties have anchored the party system, the center-left Hungarian Socialist Party (MSZP) and the center-right Fidesz-Hungarian Civic Union. The Socialists governed from 1994 to 1998 and returned in 2002 as the senior coalition partner. The conservative Fidesz led two coalitions, from 1990 to 1994 and from 1998 to 2002. In contrast to Slovakia and Estonia at the time of their second-generation reforms, the Hungarian party system is characterized by stable, programmatically defined, and socially rooted parties that behave in predictable ways in forming coalitions—all of which enhances vertical accountability.

By the mid-1990s, Hungary had smoothly accomplished the first generation of market reforms. The center-right coalition that came to power in 1998 promised

numerous pro-business reforms, including lower taxes. Given the strength of the opposition, these amounted to only modest changes; in fact, this government was criticized for spending too generously on social benefits. It loosened fiscal policy significantly during its last two years in office, increasing payments to pensioners and public-sector workers and raising the minimum wage by 75 percent before the 2002 election—exacerbating deficit problems (EIU on Hungary, 2004; IMF on Hungary, 2004).

Both Fidesz and the MSZP have promised pro-business tax cuts, but neither has been particularly successful. In 2004, the MSZP made modest reductions to income tax rates—from 20, 30, and 40 percent to 18, 26, and 38 percent, respectively. Overall, personal and employers’ taxes remain high and progressive. Only after missing out on some high-profile foreign investments did the government cut the top corporate tax rate from 18 to 16 percent, but efforts to reform the local business tax and the payroll tax have been postponed (EIU on Hungary, 2004). MSZP are now adopting a left-leaning rhetoric on taxes, with some influential officials advocating policies to narrow income inequalities and increases in social spending funded through a higher income tax (EIU on Hungary, 2004: 33).

Unlike Slovakia and Estonia, Hungary has preserved a strong voice for organized labor in negotiations over economic policy regardless of the government’s political stripe. The European Commission praised its progress in social dialogue and its involvement of social partners in decisionmaking (European Commission on Hungary, 2002: 30).

Neither Fidesz nor MSZP governments have weakened the state’s commitment to the welfare system. Although the healthcare system is in need of major reform, governments on both sides have postponed even pilot reform projects (EIU on Hungary, 2004). There are government “overruns in spending on health, housing subsidies, and interest payments.” The IMF has recommended scaling back housing subsidies, greater public sector wage restraint, “continuing pension reform, improving the targeting and structure of social benefits and subsidies, and reforms in education and health care” (IMF on Hungary, 2004: 1-3).

However these issues are resolved, it is clear that no Hungarian government has been able to commit to second-generation reforms—despite pronouncements from the right such as those from FIDESZ leader Viktor Orbán that the country “will have ‘no choice’ but to jump on the ‘flat tax bandwagon’ in order to maintain the country’s competitiveness and retain a fair share of foreign investments” (Quoted in “Flat Tax,” 2005). In Hungary’s institutionalized party system, the left’s ability to give political representation to those uneasy with reform has forced even strongly pro-business governments to compromise. For the while, the government has the luxury of waiting: given Hungary’s success with the first-generation reforms, it is still one of the region’s leading recipients of foreign direct investment per capita (see Figure 1). However, the rise in FDI flows to its neighbors is seen as a threat for the future (Condon, 2005; Schweizer, 2005).

### *The Czech Republic*

Like Hungary, the Czech Republic’s party system stabilized rapidly, with the early establishment of two anchoring parties on the right and the left, the conserva-

tive Civic Democratic Party (ODS) and the Social Democratic Party (ČSSD). Like Hungary, it has been reluctant to embrace second-generation policies. With high institutionalization and Social Democrats in government from 1998 to 2006, this reluctance was until recently overdetermined. Yet, in the June 2006 parliamentary elections, the conservative ODS won on a program proposing a 15 percent flat tax and reductions to social benefits (Patočková, 2005). It seems unlikely, given the party system's greater institutionalization, that ODS will be able to impose these policies after the fashion of their conservative counterparts in the second-generation frontrunners. Unlike Slovakia, Estonia, or Romania, there is a well-organized, socioeconomically defined left opposition that will not easily be coopted or picked off into supporting the reforms.

The trend of low and steadily declining electoral volatility illustrated in Table 1 is one indication of the institutionalization in the Czech party system.[20] Since 1989, government has alternated regularly and been composed of a manageable number of stable, programmatically distinct, and socially rooted parties. Thanks to this institutionalization, social discontent is effectively translated into political voice and opposition.

Although, like Hungary, the Czech Republic has been one of region's magnets for foreign investors, increasingly it feels compelled to adopt second-generation policies to remain competitive. Even the Social Democratic prime minister called Slovakia's policies "inspiring" ("Gross," 2004).[21] So far, the Czechs' adoption of second-generation policies has been selective and partial. The previous Social Democratic government reduced taxes, but very modestly. Effective January 2004, the corporate income tax fell to 28 from 31 percent. The upper rate of the value-added tax was reduced from 22 to 19 percent in 2004. The Social Democrats supported additional exemptions for investment in high unemployment areas, such as ten-year tax holidays for newly established firms (five years for already existing companies), low-cost land, and infrastructure support (EIU on the Czech Republic, 2004). Even as they adopted these policies, the Social Democrats were careful to distinguish them from Slovakia's tax reforms: Prime Minister Gross declared that his government would not copy Slovakia's flat tax ("Gross," 2004). As Table 2 shows, Czech tax reductions have been much smaller than the Slovak ones, and they have not changed the progressive nature of the tax system.

The Czech government has not been able deregulate without consulting organized labor. The doctors' strike in June 2003 and the civil servants' strike in April 2004 are examples of the voice exercised by organized labor in the process of economic policymaking (Shafir, 2003). The European Commission, for example, has noted that "effective tripartite social dialogue is well established" (European Commission on the Czech Republic, 2003: 33-35).

Far from attempting to reform the welfare system, Czech governments have sustained commitments that have drawn warnings from the IMF and the World Bank, who advised them to reform pensions, deepen social expenditure reforms, reduce labor taxes, and strengthen fiscal policy implementation (IMF on the Czech Republic, 2004: 3). Because of high spending on social subsidies, fiscal deficits are rising. Since the Social Democrats campaigned in 2002 on a promise to expand the welfare state, its reluctance to accelerate the pace of fiscal consolidation is not surprising. Social Democratic governments have been either reluctant or unable

to take steps to restructure the pension system—the largest single component of welfare spending. After 1998, they tightened requirements for unemployment compensation and reduced sickness benefits; yet Klaus and other conservatives have, with some justification, characterized these steps as "quasi-reforms." Against the conservative ODS's 2006 campaign program of fundamentally restructuring the welfare system, the Social Democratic prime minister affirmed his commitment to the current system (Paroubek, 2005).

Fought primarily over welfare reform and the flat tax, the June 2006 elections brought a very narrow victory for the conservative ODS but, thus far, have resulted in a coalitional impasse (Jánská, 2006). The parliament is evenly split, with 100 seats for right parties and 100 for left ones. The greater institutionalization of the Czech party system will likely preclude any kind of coalitional maneuvering as in Slovakia, Estonia, or Romania. All parties clearly defined their policy profiles in the campaign, and their electoral support is stable enough that they are unwilling to jeopardize it to join a government coalition that does not fit their program ("Česi sa dohodli," 2006). With Czech conservatives forced into policy compromises with the left, their second-generation program, if it occurs at all, will be slower and less radical than they hoped. The most likely scenario now appears a minority government until early elections in 2007.

## Conclusion

We have argued that a new kind of economic reform is emerging in the postcommunist countries now joining the EU and that extant models of economic transition offer little purchase for explaining who adopts it, to what degree, and when. The pioneers of the new reforms are the laggards of the first generation of postcommunist market-building reforms. Counterintuitively, the newfound reform capacity of former laggards results from their persistent political underdevelopment. Party system underinstitutionalization insulates economic policymakers from political opposition, allowing them to undertake radical reforms hard to imagine in a developed democracy. By weakening vertical accountability, underinstitutionalization prevents the translation of even considerable social opposition into effective political opposition.

Our comparison of Slovakia, Estonia, Romania, the Czech Republic, and Hungary supports this hypothesis. Though, in each of these countries, competition for investment and the influence of transnational networks of policy experts have produced strong pressures for deregulatory reforms primarily benefiting business, the timing and extent of these reforms reflect the degree of party system institutionalization.

How well does the argument travel beyond these countries? If we take the status of flat tax policies as an indicator of receptiveness to second-generation reforms, a survey of the other postcommunist EU member and applicant states reveals a pattern largely consonant with our argument.[22] Latvia and Serbia have had a flat tax since 1995 and 2003, respectively. In both, the policy appeared at a time of very high underinstitutionalization and under a government led by economic conservatives.[23] In Slovenia and Croatia, also underinstitutionalized party systems, recently elected, economically conservative governments have active proposals to introduce a low flat tax (Rabushka, 2005a). Poland, Bulgaria, Macedonia, and Albania are under-

institutionalized party systems without economic conservatives in government; none of them have active flat tax proposals.[24] The one anomalous case is Lithuania, which enacted a competitive flat tax in June 2005,[25] under a left government.[26]

Even Western European countries are feeling the pressures of competitive deregulation and could provide a further test of our hypothesis. Most Western European democracies enjoy a higher level of party system institutionalization than even the most developed Eastern European countries, but their conservative parties are increasingly open to radical pro-business reforms of the Eastern European variety. When, in Germany's last parliamentary elections, the conservative CDU-CSU indicated that it would nominate a flat tax proponent, Paul Kirchhof, as finance minister, the Social Democrats seemed at last to find their message against the conservatives, painting Kirchhof as a dangerous radical and the CDU-CSU as too extreme economically ("Germany's Election," 2005). In an election that turned on economic reform, the CDU-CSU let slip what initially promised to be a landslide victory. Given the stable constituencies and coalitional tendencies of its well institutionalized political parties, second-generation economic reforms appear unlikely in Germany, and in most of the rest of Europe.

## Notes

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1. Quoted in Zsilleová (2004).
2. Without using the term "second-generation reform," Bohle and Greskovits (2006) present a nice characterization of the concept: see also Zsilleová (2004), "Dancing" (2004), Jaroš (2004), "Gross" (2004), and Mikloš (2004).
3. Ireland is an exception: its business-friendly reforms—and the growth trajectory they initiated—are the model that second-generation reforms seek to emulate ("Dancing," 2004).
4. Even while emphasizing the influence of the second-generation discourse and the economic pressures underpinning it, we must add that these policies are hardly inevitable. There are political obstacles to enactment given their social costs. There are also compelling arguments that this is not the best model for economic development, that enhancing public infrastructure is a better draw for investors than simply reducing the costs of doing business. In interviews conducted in the Czech Republic, economic officials—appointed under the then Social Democratic government—contrasted their economic strategy with Slovakia and Romania's. Vice Prime Minister for Economic Affairs Martin Jahn stated that the Czech government sought to attract quality FDI, not low-cost producers. Rather than competitively deregulate, the Czech strategy was to court companies that invest in technology and labor using both targeted incentives and the provision of public infrastructure (2005).
5. To be fair, this literature dealt with first-generation reforms.
6. Even while noting the international aspect of these policies, we must emphasize that they are not sponsored, or even encouraged, by EU institutions like the Commission. They were not required by the Copenhagen Criteria, nor are they part of the *acquis communautaire*. In fact, the hard-edged neoliberalism of these policies goes against the European social model implicit in much of the EU's regulatory framework. In a public presentation entitled "European Economic Competitiveness and EU Enlargement," Slovak reformer Ivan Mikloš contrasted his policies with what he called the less competitive model of western EU member-states (2004). Not surprisingly, EU institutions such as the Structural Funds have been a site of opposition to these policies: France, Germany, and Belgium have suggested limiting Structural Fund assistance to countries like Slovakia that engage in "social dumping."
7. For a good discussion of the literature on transnational policy networks, see Orenstein (2006).

8. See, for example, the Hoover Institution’s blog, “The Russian Economy,” <http://www.russian-economy.org/comments.html>.
9. In testing Przeworski’s argument, both Hellman and Frye operationalize executive dominance and insulation in terms of the strength of the presidency (Frye, 2002: 324; Hellman, 1998: 214, 231, fn. 46).
10. Russia and Georgia more closely resemble Przeworski’s reform scenario. Under Putin, the epitome of a super president, Russia adopted a flat tax in 2001. After leading the 2005 Rose Revolution, Georgian president Mikheil Saakashvili introduced a flat tax. It also should be noted, however, that both presidents’ autonomy was enhanced by extreme party system underinstitutionalization.
11. According to Mikloš (2004), the IMF told him his reform team’s plan was too radical, that they should implement it gradually over a period of at least three years. In Mikloš’s telling, the team replied, “No way; we‘ll do it now while we have the opportunity.“
12. The formula for calculating volatility is $V = ½\Sigma \mid v_{p,t} - v_{p,t-1} \mid$ where $v_{p,t}$ stands for the vote share of a party in election t, and $v_{p,t-1}$ stands for its vote share in the previous election (Pedersen, 1979: 4-5). Because frequent splits and mergers represent lack of institutionalization and confuse (perhaps intentionally) voters about parties’ records, we count splits and mergers as new parties. This maximizes volatility, but it is consistent and avoids judgment calls about party continuity.
13. This ordering is not affected by differences in payroll taxes, which were virtually the same in the Czech Republic, Hungary, and Slovakia in 2005 (48, 46, and 48 percent, respectively). In Estonia and Romania, a lower payroll tax (35 and 36 percent, respectively) widens the tax “advantage” from second-generation policies (World Bank, EU-8 2004: 2; Budina and van Wijnbergen, 1997; Gheorghiu et al., 2004: 38).
14. Others note that Slovakia’s tax policies were key to winning Kia’s investment (Bohle and Greskovits, 2006: 21).
15. Mikloš received a portion of his economics training at the London School of Economics; he was also president of M.E.S.A. 10, a Slovak policy NGO with close ties to American and European academics, and vice-president of the East-West Institute, an American NGO working in postcommunist Europe. Mikloš’s economic advisor Martin Bruncko exemplified the sociological profile of second-generation reformers with a graduate degree from Harvard‘s Kennedy School and experience working for the OECD (Tzortzis, 2005).
16. For a description, see <http://www.ineko.sk/euroreform/index.htm>.
17. Attempting to disqualify the smaller opposition parties, Mečiar changed the electoral law to require *all* parties, even those in electoral alliances, to win 5 percent of the vote for representation (Haughton and Rybář, 2004: 125).
18. Though the communist-era suppression of civil society organizations has created an organizational deficit across the postcommunist region, this legacy is, if anything, stronger in Estonia than in the other countries considered here because Estonia experienced direct rule from Moscow.
19. Kreuzer and Pettai argue that Estonia began to show signs of party consolidation in 1999 (2003: 94). Since Estonia’s most radical reforms occurred in the still chaotic party system of the early 1990s, this is consonant with our argument. Moreover, it has been difficult to continue radical reform since the party system began to stabilize.
20. See also Toole (2000); Deegan-Krause (2000); and O’Dwyer (2006).
21. In interviews conducted in July 2005, economic officials in the then Social Democratic Czech government were extremely cognizant of Slovakia’s economic reforms (Jahn, 2005; Sedláček, 2005). A survey of the major Czech newspapers of during the summer of 2005 uncovered numerous articles drawing unfavorable comparisons between the Czech Republic and Slovakia; see Mášová (2005).
22. Since the rationale for second-generation reforms is to realize investment opportunities opened up by EU membership, we do not consider states without near- to medium-term accession prospects. For a description of party system institutionalization in the countries mentioned below, see O’Dwyer (2006: 177-182).
23. In Serbia, it was the 18-party bloc that overthrew Miloševič which began reforms. Despite internal splits and even the assination of the prime minister, a team of technocrats grouped around the Democratic Party and the so-called G17 Plus pushed thrugh the flat tax. Latvia’s flat tax was born under the conservative Latvia’s Way government.
24. Poland is interesting because its Civic Platform, the economically conservative party, had announced plans for a flat tax in March 2005, only to lose elections later that year (Rabushka,

2005c). In the elections, the socially but not economically conservative Law and Justice party had criticized Civic Platform's economic proposals with advertisements showing homes with empty refrigerators. Law and Justice's coalition with the catholic-nationalist League of Polish Families and the populist Self-Defense dispelled any chance of a Polish flat tax in the near future (Rabushka, 2005a). Had Civic Platform, and not Law and Justice, formed the government in 2005, Poland would most likely have a flat tax now.

25. While Lithuania nominally had a flat tax on wages since 1994, observers did not consider it a "true" flat tax (Rabushka, 2005b). It was (at 33 percent) much higher than others in the region, and other forms of income were taxed at different rates.
26. Unfortunately, space does not permit a discussion of this anomaly here. One hypothesis, advanced by one country expert, is that left-right socioeconomic labels do not apply to Lithuanian parties (Ramonaitė, 2006).

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