

## GRADUAL VERSUS COMPREHENSIVE REFORM

*William A. Niskanen*

Oleg Bogomolov has made an acute analysis of the problems of the Soviet economic system and of the partial, tentative, and noncommittal measures to restructure this system during the past five years. And he has concluded, I believe correctly, "that the existing system cannot be improved by partial perestroika." Four of his insights, I suggest, are especially important.

### Positive Reform Measures

First, the steeply progressive tax rates on labor income and enterprise profits limit both the incentives for increased output and the willingness of the population to accept the necessary price reforms. In American terms, measures to improve the "supply side" of the economy are a necessary component of an effective economic reform.

Second, the Soviet Union has a huge amount of assets but little capital, primarily because individuals and enterprises do not have the opportunity to reallocate these assets to higher value uses. A comprehensive privatization of state property, which is presumably owned in the name of the people, is the necessary first step to create a capital market. Moreover, as Bogomolov correctly observes, the individuals and enterprises that receive this property must have the right, in turn, to sell it or to borrow against it.

Third, at some stage, the package of economic reform measures must be subject to approval by democratic processes but it is a mistake to subject individual measures, such as the necessary price reform, to a referendum. This is a controversial issue but, I suggest, Bogomolov's position on this issue is correct.

Finally, I wish to reinforce his conclusion that "one of the most important tasks will be to define in unambiguous terms the permissi-

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ble forms and limits of political intervention in the economy.” The constitution of a free people must define the island of governmental powers in the ocean of individual rights. The Soviet Union is now best described as a set of islands of individual rights in an ocean of governmental powers.

## A Comprehensive Reform Strategy

My one major disagreement with Bogomolov is his recommendation for a gradual industry-by-industry reform, beginning primarily with the agricultural sector. There are two problems with this approach, one economic and one political. Each successive reformed sector would still face artificial prices and state controls on the necessary inputs from other sectors yet to be reformed. And the gradual approach would allow the opponents of reform to concentrate their opposition on each successive step. To illustrate my perspective, let me make a distinction between a comprehensive reform strategy and a “big bang” approach. A comprehensive reform strategy *initiates* all of the necessary reform measures at the same time but allows each measure to proceed at its own appropriate pace. A “big bang” approach, in contrast, attempts to maintain this same schedule for each of the reform measures, an attempt that I believe cannot succeed.

Many years ago, Friedrich Hayek demonstrated the difficulty of maintaining a credible gradualism in economic policy, because the population cannot discern whether each step is part of a longer series of steps to which the government is committed or is only a tentative step that may later be reversed. In the latter case, the response of the population would be much more cautious, slowing the effects of the reform.

We do not have a good theory or much evidence that bears on the appropriate *sequence* of reform measures, so some errors will surely be made. A comprehensive strategy that jointly addresses all of the reform measures, however, would minimize the costs of these errors.

A comprehensive reform strategy also puts pressure on all of the bureaucracies and opponents of the reform at the same time, reducing their opportunity and incentive to collude to oppose each successive step in a gradual reform strategy.

## Lessons from New Zealand

In conclusion, I would like to offer five lessons from the most ambitious economic reform of the 1980s—that by the Labour govern-

ment of New Zealand, as summarized by a senior representative of that government:

1. A country's crisis also creates a "window of opportunity" for fundamental change.
2. Electorates are more sophisticated about the importance of reform than most politicians believe.
3. Comprehensive reform is clearly easier than piecemeal reform.
4. Establish credibility early by choosing the first reform measures wisely, demonstrating that reform works.
5. Once a government is committed to reform, it can never move too fast to achieve it.

Those who wish to transform the Soviet system should pay special attention to Roger Douglas, the architect of the New Zealand reform.

# INDIVIDUAL RIGHTS, DEMOCRACY, AND CONSTITUTIONAL ORDER: ON THE FOUNDATIONS OF LEGITIMACY

*Roger Pilon*

## Introduction

After more than 70 years of Communist rule, the people of the Soviet Union today face an enormous challenge—to make the transition to freedom. Never in history have so numerous and diverse a people as those who live in today's Soviet Union undertaken so fundamental and difficult a transition as is envisioned by the move from a planned to a free society. Were the transition going in the other direction, it would be relatively easy, of course; for as theory and history demonstrate, socialism is brought about simply by taking what is privately held, from land to labor, and putting it under public control. Getting out of socialism, however, is much more difficult, not least because, over time, many of the conditions that characterized the pre-socialized order—such as a distribution of private holdings—and enabled that order to function and evolve—such as a system of private law and the culture that sustains it—have been all but destroyed. It will not be easy to revive those conditions or to create them anew. Yet for all the difficulties, the transition must be undertaken; the chaos and suffering that are the inevitable products of the planned society must be brought to an end.

Important as it may be to focus on the difficulties, however, it will be even more important to keep in view the prospects that lie ahead

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