MARKET INSTABILITY AND ECONOMIC COMPLEXITY:ECONOMIC LESSONS FROM TRANSITION EXPERIMENTS

Abstract

Washington consensus and shock therapy forgot Keynesian lessons from the Great Depression: market instability and the active role of government in promoting growth. The severe output decline in East Europe and former Soviet Union (EEFSU) was triggered by simple-minded policy of liberalization and privatization, which ignored economic complexity and multiple equilibriums under division of labor. New fundamental issues, such as chain reactions between macro instability and micro behavior, the government role of creating learning space in development, interactions among economic openness, sustainable growth, social stability, can be revealed from comparative experiments between China and EEFSU, including exchange rate regime, price dynamics, trade policies, and reform strategies. The tremendous cost of the Transition Depression sheds new light on theoretical limitations of demand-supply analysis, hard-budget constraints, microfoundations theory in macroeconomics, and property right school in institutional economics. New development policy based on learning, innovation, and decentralized experiment will broaden our scope of economic thinking.