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WHY DID ESTONIA PERFORM BEST? 
THE NORTH–SOUTH GAP IN THE 
POST-SOCIALIST ECONOMIC TRANSITION 
OF THE BALTIC STATES

Zenonas Norkus

After more than a decade of post-socialist political and economic transformation one can distinguish two groups of transition countries – ‘successful’ (with a consolidated liberal democracy and working market economy) and ‘unsuccessful’ cases. The first group is represented by the countries of Central Europe and the Baltic states, and the second by the Balkan countries and most of the former Soviet republics. Today, all three Baltic countries belong to the first group. However, in 1994 Estonia was praised by foreign analysts as ‘a shining star from the Baltics’, whereas the economic performance and reputation of Lithuania was rather low. What was it that enabled Estonia to perform best during the first decade of market transition: was it better initial economic conditions, peculiarities in the political process (e.g. the exclusion of a significant part of the ‘non-ethnic’ Estonian population who could have been the potential electorate for a post-communist party like the Lithuanian ‘Laborists’), a Protestant cultural legacy, or perhaps even better public relations? This article discusses alternative answers and elaborates on a Weberian explanation.

Keywords: Baltic states; post-communist transformation; Max Weber; Herrnhuter movement

As early as 1994 Estonia was hailed by foreign economic analysts as ‘a shining star from the Baltics’ (Hansen and Sorsa 1994) for its economic performance. As for Lithuania, its reputation was less than mediocre. That same year Zbigniew Brzezinski

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similarly described Estonia as having already advanced into the second stage of transition, whereas Lithuania, together with countries like Bulgaria, Romania, and Slovakia, remained in the first (Brzezinski 1994; see also Jakubowicz 1995; Lauristin and Vihalemm 1997, 2002). In 1997, the European Union (EU) recognized Estonia’s stronger performance by inviting it to begin negotiations on accession two years ahead of the other Baltic states.

As the data on gross domestic product (GDP) dynamics presented in table 1 suggest, the decline in GDP during the period of economic recession in Estonia was smaller than in the other two Baltic states. Moreover, recovery of the economy in Estonia started earlier, and it achieved better macroeconomic results. After the recession caused by the Russian crisis, the economic development of Lithuania speeded up, although the improvements in the country’s economic indicators can be explained in part by better functioning taxation and statistics offices that increased the number of economic activities accounted for. In 2003, Lithuania, with an annual 9.7% growth in its GNP, outstripped not only Estonia but all the other countries of the European Union. Nevertheless, the gap in economic performance between the Baltic countries remains far from being closed. In 2004 Estonia was the only Baltic state whose GDP surpassed the level achieved in 1989 (EBRD 2004, pp. 123, 147, 151). More importantly, Estonia now has the reputation of being one of the most highly developed information technology nations in the world, while the current economic growth in Latvia and Lithuania is nourished mainly from the sources of the passing

### TABLE 1 Dynamics of GDP in central and eastern Europe, the Baltic states, and the Commonwealth of Independent States (CIS)

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<td>-3.6</td>
<td>0.4</td>
<td>3.9</td>
<td>5.5</td>
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Source: EBRD (1999, p. 73).
industrial age. International organizations and rating agencies almost invariably rank Estonia higher than the other Baltic states, and, according to some highly reputed rankings (e.g. the Economic Freedom Index, Global Competitiveness Ranking, Corruption Perception Index), Estonia belongs among the world’s top performers. However, to focus my analysis more sharply, I will limit the temporal scope of this article to the first decade of post-socialist transformation (1989–99), when all of the Baltic countries were affected by the so-called ‘Russian crisis’ which broke in August 1998. I will also focus on the specific questions of why the economic recession in Lithuania was deeper than in Estonia, and why economic recovery in Estonia began earlier than in Lithuania and led to superior macroeconomic results.

The gap between the Baltic south and the north is obviously down to more than just economics. When the political transitions of the three countries are compared, they score in opposite ways, with Estonia (and Latvia) as problematic cases due to their exclusionary citizenship laws, and Lithuania a normal case. However, the explanation for this ‘democracy gap’ is unproblematic, since researchers generally attribute it to the differences in the ethnic composition of these Baltic countries. The much more intensive immigration into Estonia and Latvia during the Soviet period meant that the share of the titular nationality within the overall population had declined to 62% in Estonia and 52% in Latvia by 1989 (EBRD 2000, p. 22). In Lithuania, by contrast, ethnic Lithuanians continued to make up 80% of the total population, so neither the broad masses of ethnic Lithuanians nor their political leaders perceived inclusive citizenship as a threat to the dominant status of the ethnic majority.

Estonia’s superior economic performance during the first transition decade has generated much interest and a variety of different explanations. Ritsa A. Panagiotou (2001) has divided these into three ‘schools’, each of which emphasizes a different explanatory factor, as follows: (1) Estonia’s geographical location (Hansen and Sorsa 1994; Kala 1994; Kallas 1996; Weber and Taube 1999); (2) its economic structure upon attaining independence (Nørgaard et al., 1999; Nørgaard 2000); and (3) its macroeconomic choices after independence (Hansen and Sorsa 1994; Saavalainen 1995; Budina 1997; Nørgaard et al. 1999). Explanations (1) and (2) can be described as purely economic, whereas explanation (3) can be classified as political-economic, in that it emphasizes political differences – chiefly the fact that, unlike Estonia, Lithuania was ruled during the period of transformation (1992–96) by a post-communist party with a preference for a ‘gradualist’ economic transition policy (Mygind 1997). According to Panagiotou’s own explanation, the social and cultural capital accumulated over the Soviet era was larger in Estonia than in Lithuania and Latvia. In particular, the preparations for implementation of the IME (self-managing Estonia) program in 1988–91 meant that Estonia had a more competent elite to reform the economy. Panagiotou therefore expands the list of ‘schools’ to four with a culturalist explanation.

Intriguingly, however, the heightened interest in the reasons for Estonia’s success has not generated any real controversies. In part, this is understandable: in so far as multiple conjunctural causality is a characteristic feature of economic and political change (see Ragin 1987, pp. 19–33), one cannot assume that only one factor was causally relevant to Estonia’s success. Geographic location, economic structure after
independence and many other factors could all have played a part and, characteristically, many authors represent more than one ‘school’. Nevertheless, I do not believe that one can engage in explanatory ecumenism by assuming that all factors are equally important.

The depth of recession and time and speed of recovery can be measured by variables at the interval or ratio level. One can ask how much variation in these variables is explained by each of the independent variables that can be assumed to be relevant for theoretical reasons. One can assess the role of each separate causal condition only through a controlled experiment that enables the researcher to isolate the causal condition under investigation and to control the remaining conditions. Unfortunately, there are too few cases \( (N = 3) \) to answer this question by means of quantitative (statistical) analysis, which is an imperfect substitute for the experiment. The value of \( N \) is also too small for the application of the technique known as qualitative comparative analysis (QCA), which has the advantage of taking into account the conjunctural interaction between many causes of an outcome (Ragin 1987).

However, the Baltic states do offer considerable scope for the application of the classical version of the comparative method known as ‘most similar systems design’ (MSSD; see Przeworski and Teun 1970, pp. 31–46; Lijphart 1971, pp. 687–9). While they are very similar in many respects, they differ sharply in a few remaining ones. Most importantly, these differences do not overlap but intersect throughout all three countries. Therefore, one can control statements made on the grounds of differences and similarities between the Baltic north (Estonia) and south (Lithuania) using the case of Latvia, which is in some relevant respects similar to Lithuania, but in certain others to Estonia. Although too many relevant differences remain between the Baltic countries to eliminate all competing causal hypotheses except one, the comparison helps to minimize their number. I will proceed from the assumption that small differences matter as contributory causes far less than bigger ones. A hypothetical explanation will be considered less credible if it is incompatible with another explanation that is already firmly established. I will reject hypotheses if there is ambiguous or contradictory evidence about their truth value, and I will consider clear implications about the research necessary for its testing as an important advantage of a hypothesis.

The next section contains a critical discussion of the purely economic and political-economic explanations of the north–south gap. As they are presented by many researchers, I will work with stylized and most representative versions of the arguments without discussing the twists and turns in their elaboration by individual authors. In the third section I will discuss culturalist explanations by Panagiotou (2001) and Mattusch (1996, 1997). Mattusch relates variation in the economic performance of the Baltic countries to differences in their distant religious and cultural pasts, with particular reference to Max Weber’s famous Protestant ethic thesis. In presenting my criticisms of her explanation, I make an attempt to elaborate Weber’s thesis to make it defensible (in the fourth section). In the fifth and final section I discuss possible criticisms of my version of the culturalist explanation, elaborate upon it further and describe additional research necessary to test it.
In what follows, I maintain that Estonia’s main advantage was its Protestant Pietist legacy, while Lithuania was disadvantaged by the prevalence of a rural Catholic mentality even in urban environments. However, in saying this I am not arguing for a ‘monocausal’ culturalist explanation. My argument is that although purely economic factors could be important, they alone cannot explain variation in the timing and outcomes of the economic performance of the Baltic countries during the first decade of post-socialist transformation, because differences in economic initial conditions were too small in comparison with those outcomes. I argue that the bulk (though not all) of the variation in outcomes can be explained by differences in initial cultural conditions that are legacies from a distant pre-Soviet past.

**Economic and Political-Economic Explanations**

In order to carry out a systematic comparison and assessment of the alternative explanations of the gap between the Baltic north and south, it is necessary to provide an analytical framework to organize these comparisons, to draw distinctions between relevant and irrelevant conditions, and to evaluate the relationship between these conditions. In this regard, I will employ the analytical scheme of transformation elaborated by Leszek Balcerowicz in 1995 (see figure 1). This scheme distinguishes between the economic and socio-political spheres of society, which are related by causal interaction. Changes in each of these areas and their consequences are determined, first and foremost, by initial conditions. The course and outcomes of economic and socio-political change are influenced also by external (international) conditions, and by the economic policy of the government. Initial internal and external conditions, as well as those changes in the economic and socio-political spheres that have already occurred, place constraints upon this policy, drawing the line

![Diagram of Transformation Scheme](image)

**FIGURE 1** The analytical scheme of transformation.  
*Source: Balcerowicz (1995, p. 154).*
between what can be done and what can no longer be done, opening and closing
the windows of opportunity.

Comparing external conditions, Estonia could have had an economic advantage
due to its geographical proximity to Finland. The abolition of all export and import
duties made Estonia an attractive place for weekend shopping tourism. However,
doubts remain as to whether these differences are sufficient to explain the variation
in the economic performance of Baltic countries. I will go back to the role of the
‘Finland factor’ in the closing section of this article. At this point, I would simply like
to highlight the fact that Finland’s economy was in a deep recession in the early 1990s,
caused by the breakdown of traditional economic relations with the former USSR
following its dissolution. This recession meant that Finland could barely play the role
of ‘economic locomotive’ for Estonia. In terms of geographical distances (implying
lower transportation costs), Lithuania and Latvia are nearer to the core of the
European economy, and only they have ice-free ports.

Proceeding to differences in internal economic initial conditions, one can find
more similarities than differences between Baltic countries, and eliminate many
explanatory hypotheses. All three countries are in the same climate zone and are
more or less similarly endowed with natural resources. The only important difference
is the presence of oil shale mining in Estonia, although given world prices for energy
resources in the 1990s and environmental pollution this seemed to be more of a
liability than an asset for Estonia’s economy. Many authors (e.g. Nørgaard 2000,
pp. 85–127, 175) have found that the initial conditions – both the level of
modernization and the factors inhibiting development – were slightly better in Estonia
than in Latvia and Lithuania.

These findings, however, are contradicted by another analysis carried out by
the European Bank of Reconstruction and Development (EBRD 1999, pp. 28–9;
De Melo et al. 1997). This found that initial conditions in all three Baltic countries
were very similar, and less favorable than those enjoyed by the top performers in the
post-socialist transformation: Poland, the Czech Republic, and Hungary. How, then,
was Estonia able to achieve a performance similar to that of these Central European
countries, even though initial internal conditions in the country were closer to
those of the other Baltic states and the former republics of the European part of
the USSR?

For many of the differences in the initial economic conditions that slightly favor
Estonia, one can find differences that slightly favor Lithuania, such as a slightly
younger population and slightly more productive agriculture. More importantly, one
can raise a methodological objection against attempts to explain Estonia’s superior
economic performance in purely economic terms: namely, is it reasonable to attribute
significant differences in economic outcomes solely to slight differences in initial
economic conditions, when one can find very marked differences between Lithuania
and Estonia in the socio-political and cultural spheres?

In socio-political terms, the most obvious distinguishing feature of Lithuania was
the spectacular victory by the successor to the Lithuanian Communist Party
(Lithuanian Labour Democratic Party – LLDP) in the parliamentary (Seimas) elections
of 1992. The fact that the LLDP government was in power during the critical years of
market reform has led many authors to hold it responsible for the relative
backwardness of Lithuania, the implication being that it enacted policies which possibly corresponded to the short-term interests of the electorate but which retarded the country’s long-term progress (see, for instance, Mygind 1997, p. 144; Aslund 2002, pp. 3–4, 109–12, 191–6; Rothacher 2002, pp. 12–16).

In Latvia and Estonia exclusionary citizenship laws denied voting rights to a population that was potentially the core electorate for post-communist or populist leftist parties. After the question of citizenship rights for Russian-speaking immigrants became top of the political agenda, rightist nationalist parties were able to win the majority of the votes and build governments that could enact market reforms in a much more sustained way than the LLDP in Lithuania. The political-economic explanation thus implies that the deficiencies of the political systems that made Estonia and Latvia ‘ethnocratic’ rather than ‘liberal’ democracies preserved them from post-communist government and postponement of economic reforms. This implication can be expressed by the counterfactual assertion that if Russian-speaking immigrants had been granted citizenship rights then the first parliamentary elections after independence would have brought leftist governments to power that would have prolonged the transformational recession, with an outcome similar to that in Lithuania. Who else but leftist and populist parties could have won the votes of the majority of the Russian-speaking population, if Estonia and Latvia had had citizenship laws similar to those in Lithuania?

This political-economic explanation, however, is only *prima facie* plausible in that not only the outsiders (e.g. Bulgaria, Romania), but also some of the pioneers (Poland, Hungary) of post-communist transformation have undergone periods of rule by former communist parties. The most difficult challenge for the political-economic explanation is the Latvian case. Although initial socio-political conditions in Latvia were much closer to those in Estonia than they were to those in Lithuania, the macroeconomic policy of Latvia’s rightist governments differed from Estonia both in terms of consistency and results, resembling the Lithuanian case in both these respects. I will come back to the Latvian case in the fourth section of this article.

**The Culturalist Explanation: ‘Weber’s Thesis’ and the Baltic Countries**

Some authors have argued that the social and cultural capital accumulated over the Soviet era was larger in Estonia than in Latvia and Lithuania, and that owing to the IME program Estonia had more ideas and people available to reform the economy (Van Arkadie and Karlsson 1992, pp. 103–4; Panagioutou 2001). The IME program, however, was built on the assumption that Estonia would remain part of the USSR. It was a plan to build ‘market socialism’ in one country, and differed very much from the radical neoliberal reforms that were implemented later (mainly by the government of Mart Laar) during 1992–94. Even more importantly, the Laar government implemented a *de facto* lustration, thereby largely removing the former communist elite that served as the main carrier or embodiment of cultural and social capital from the Soviet era. In Lithuania, on the other hand, the bulk of the national communist
‘old cadres’ were able to keep their jobs and positions. Fredo Arias-King (2003) considers radical de-Sovietization as crucial for Estonian success. He argues that youth, courage and the low level of administrative competence on the part of the Estonian leaders implementing reform often benefited rather than inhibited the reform process at the beginning of this period of extraordinary politics.

Yet de-Sovietization was barely any less radical in Latvia. Many of the functionaries within the state apparatus and a majority of senior managers of state-owned enterprises were ethnically non-Latvian, and most aligned themselves with the pro-Moscow ‘Interfront’ during the struggle for independence. Their political discrediting meant that they could be removed after August 1991, paving the way for young ethnically Latvian officials with a politically correct record. The career of the famous president of Latvia’s central bank, Einar Repše, can serve as a case in point. So the differences in the cultural capital of the governing elite in Lithuania and Estonia, although obvious and important, are barely sufficient in themselves to explain Estonia’s comparative success.

The differences in culture that could have more important economic consequences were located not only in the governing elite but also in the broader population. They are documented by the findings of the European Value Survey Group and World Value Survey network from 1990, just before the start of the market transition (see table 2). This is the summary description of these differences by German researcher Katrin Mattusch, who used the data to substantiate another

<table>
<thead>
<tr>
<th>Table 2: The differences in basic value orientations between Lithuanians, Estonians, and Latvians in 1990 (percentages)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Lithuanians</strong></td>
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<tr>
<td>Religion is important in respondent’s life</td>
</tr>
<tr>
<td>Respondent was educated in a religious family</td>
</tr>
<tr>
<td>Respondent believes personal God</td>
</tr>
<tr>
<td>Death is inevitable, it is pointless to worry about it</td>
</tr>
<tr>
<td>General disapproval of abortion</td>
</tr>
<tr>
<td>General disapproval of divorce</td>
</tr>
<tr>
<td>When jobs are scarce, employers should give priority to men</td>
</tr>
<tr>
<td>In the long run, hard work usually brings a better life</td>
</tr>
<tr>
<td>The course of events is decided by particular people</td>
</tr>
<tr>
<td>If an unjust law were passed by the government I could do nothing about it</td>
</tr>
<tr>
<td>Income should be made more equal</td>
</tr>
<tr>
<td>The state is under an obligation to warrant high living standards for elderly people</td>
</tr>
<tr>
<td>Enterprises should be directed by the state or employees</td>
</tr>
</tbody>
</table>

Source: Mattusch (1997, p. 82).
version of the culturalist explanation of the gap between the Baltic north and south in the economic transition:

Lithuanians remained very religious despite the pressure of Soviet atheism, they take guidance from traditional values in family life, are personalistic, fairly authoritarian, have high demands of equality to community, believe that one can achieve little in life and society by her/his own efforts and are less disposed towards capitalist ideas of property and distribution. Estonians are more secularized, they conceive family roles in a less traditional way and display the individualistic, autonomous, and achievement-oriented understanding of their role in the society. They have internalized to a lesser degree the requirements of equality (although they accustomed themselves to the socialist provision state (Versorgungsstaat) too). They provide more support for capitalist ideas of management and differentiation. With respect to all these basic value ideas, Latvians take the middle position between Lithuanians and Estonians. It seems that this culture is characterized by a mixture of different traditions. (Mattusch 1997, pp. 81–2)

These differences are huge, and can hardly be less relevant than slight differences in the purely economic sphere. They reflect features of cultural tradition and mentality inherited from the pre-Soviet era. Throughout the Soviet period, the central government in Moscow considered all three Baltic countries to be part of the same economic region (Pribaltika), subject to uniform economic and cultural policies. The populations of all three countries were exposed to the same ideology, and to a cultural policy that pursued the goal of educating a ‘new human being’. Cultural differences that existed between the Baltic countries in 1940 or 1945 could only be lessened by the shared experiences of the Soviet era. The findings of the 1990 survey can therefore be explained only by factors that were already at work prior to this.

Referring to the respective historical role of the Catholic and Lutheran Protestant traditions, Mattusch asserts that ‘Lithuanians are the most traditionalist and have internalized capitalist culture to the least extent; Estonians are the most antitraditionalist and are most strongly attracted to capitalist values’ (Mattusch 1997, p. 87). In her view, the reemergence of the gap in economic development between the Baltic north and south can be explained most readily by Max Weber’s well-known ‘Protestant ethic’ thesis (Weber 1958):

The ‘Protestant Ethic’ worked in the Baltics as a switchman for the ‘breakthrough’ of capitalism and its rapid consolidation, because the initial state in Estonia was more favorable than that of Lithuania which was shaped by Catholic traditions. This initial level was represented by Protestant traditions, and, after its separation from its religious roots, by the norm structure that still retained its shaping power after 50 years of socialism. (Mattusch 1997, p. 91)

Although the survey data provide support for a causal hypothesis relating the reemergence of the north–south gap in economic development to cultural differences, they are insufficient to corroborate Mattusch’s much more specific statement that Estonia’s superior performance can be explained as a another case of Weber’s well-known thesis. Weber’s precise statement was that not all kinds of Protestantism
are equally favorable to the emergence of the type of economic activity and economic system designated by him as ‘rational capitalism’. He attributed the contributory causal role only to the currents of Protestantism described by him as ‘ascetic Protestantism’. A causally important aspect of this kind of Protestantism was a set of values and informal norms constituting a specific economic ethic with the idea of ‘professional calling’ as its core. Weber excluded from the scope of his thesis Lutheran Protestantism, classifying as ‘ascetic Protestant’ only Calvinism, some Protestant sects and so-called ‘secondary’ forms of ascetic Protestantism (Pietist movements in Calvinism and Lutheranism, and Methodism in the Anglican Church). However, the dominant confession in Estonia and the larger part of Latvia was orthodox Lutheranism, which was never considered ‘ascetic Protestant’ by Weber.

However, a more elaborate analysis of the religious history of Baltic countries provides sufficient evidence – or so I will argue – in favor of an explanation of the recent differences in the performance of Baltic countries along the lines of Weber’s thesis. More specifically, one can find in the history of Latvia and especially in that of Estonia religious movements that had sufficient power to influence the course of everyday life in the direction of its rationalization and systematization. These movements inculcated the Latvian and especially the Estonian folk culture and economic mentality with features that can be considered as a lasting cultural legacy of these movements. In the next section I will supplement Mattusch’s argument with an analysis of the historical-cultural specificity of this legacy and its origins.

The Herrnhuter Movement in Livland and Estland

There is another strong argument against the straightforward application of Weber’s thesis to the Baltic countries. The Christianization of Estonians and Latvians was somewhat superficial both before and after the Reformation, because Lutheranism was closely associated with German landlords hated by the local peasant populations. The offices of Protestant pastors were under the patronage of landlords, and the pastors were simply their attorneys. Furthermore, the absolute majority of pastors comprised Germans, many of whom had an insufficient knowledge of local languages. ‘Given the different languages and given that the spoken Latvian of the clergy was frequently seriously flawed, there must have been many misunderstandings if not, at times, the absence of effective communication’ (Plakans 1995, p. 58). During the revolutionary events of 1905–07, German pastors stood next to German landlords as targets of revolutionary terror (Petersen 2002, pp. 87–91). However, there was no terror against Catholic priests in Lithuania during similar events during fall 1905. One can even be tempted to explain the much weaker religiosity of contemporary Estonians and Latvians (cf. table 2) by the less deep inculcation of their cultures with Christian faith in the distant past.

However, it is wrong to assume that the history of Protestantism in the Baltic countries is identical to that of official Lutheranism. In the eighteenth century, the provinces of Estland and Livland in tsarist Russia were among the most important areas of diffusion for the Pietist movement known as ‘Herrnhuters’ or Moravian Brethren. The origins of this movement go back to the fifteenth century,
when in Czechia and Moravia the followers of Jan Hus staged a general rehearsal for the Reformation. Early in the 1700s, the Moravian Brethren relocated to Saxony, fleeing prosecution by the Habsburg authorities and the Catholic Church. In Saxony, they settled on the estate of Count Nicholas Zinzendorf in the locality of Herrnhut (this explains the broadly used name of their denomination). Zinzendorf became involved in the internal affairs of the community, and presided over its renewal. Under Zinzendorf’s leadership, the evangelical Brethren community (evangelische Brüdergemeine – another of its many designations) existed for some time as a part of Saxony’s Lutheran Church, but was later reestablished as a distinct and separate Protestant Church.

Max Weber considered the Herrnhut denomination as one of the ‘secondary’ forms of ascetic Protestantism (Weber 1958, pp. 128–39, 178, 247–9), the most significant of which are the Pietist movements that emerged within the Calvinist and Lutheran Churches at the turn of the eighteenth century. For Pietists, ‘true’ Christianity was consistent not with dogmatically correct belief but with piety, love of God, deep inner religious experience and daily conduct in life. In the last respect, there were no significant differences between Pietism and other forms of ascetic Protestantism. In Germany, the Brethren community was one of the three currents of Pietism alongside those of Halle and Württemberg. However, only the Herrnhuter movement embarked on large-scale missionary activity and thereby managed to acquire more than local significance.

In the Baltic provinces of tsarist Russia, Moravian brothers began their activities during the 1730s in the locality of Volmar (present-day Valmiera). They were invited by Magdalene Elisabeth Hallart, the widow of General Ludwig Hallart who served in the Russian army. In 1736, Zinzendorf himself visited the Baltic provinces, and in 1738 a seminary of Moravian brothers was established in Volmar with the goal of educating preachers of ethnic Estonian and Latvian origin. From Volmar, the Herrnhuter movement spread to Estonia, where it managed to put down much deeper roots than in Latvia.

At the behest of a significant part of the Lutheran clergy, the Russian government banned the Brethren community in 1743. Yet the favorable attitude and tacit tolerance of many landlords enabled the Herrnhuters to continue their activities in spite of the formal prohibition. Landlords were captivated by the changes in peasant behavior in localities with a strong Herrnhuter presence, which saw a sharp decrease in levels of drinking, premarital births, and petty crime. An account from 1791 by Baltic German artist Karlas G. Gross depicts Herrnhuters as more well-to-do and better educated than other peasants, and claims that ‘Even the best pastors with their reasonable sermons cannot accomplish anything comparable to the results obtained by a simple mitten-maker from Zinzendorf’s school. These preachers have a wonderful influence on the virtues of the people; the weak grow strong, the lazy work hard, the irascible turn cheerful and the drunkards and the dissipated mend their vices’ (Abols 2002, p. 79).

Although many Lutheran pastors perceived Herrnhuter deacons and presbyters as competitors, they were impressed by the Herrnhuters’ achievements in the fight against folk customs that were considered by them as remnants of heathenism. Of course, these achievements led to the disappearance of the many features and
traditions of the traditional folk culture (Raun 2001, p. 53). The characteristic features of the Herrnhuter way of life were temperance, cleanliness, choral singing, religious self-education and the writing of autobiographies. These autobiographies are the oldest surviving documents providing literary expression of the inner world and subjective experiences of the common Estonian and Latvian people.

The size of the Herrnhuter community never exceeded 50,000. However, its influence was much more significant than one would surmise on the basis of numbers:

Herrnhuters were the first national movement of Latvians and Estonians that won public acceptance and this has great historical significance because of the following reason: although at the culmination point they were not in the absolute quantitative majority, it is beyond all doubt that they were a morally dominant power for rural people. (Tobien 1930, p. 124)

Admission into the Brethren community, and especially into its inner circle (second and third hour (Stunde)) was a highly desirable symbol of social recognition that could be won only by exemplary behavior. The following is a description of the position of Herrnhuters in Livland’s rural society, provided by Baltic German historian Alexander von Tobien:

Herrnhuters not only included into their ranks the most affluent and influential people among rural folk, but also had such high authority in the general opinion of the people that nobody dared to act openly against the Brethren community. The majority of those who did not belong to Herrnhuters considered this formation as a higher untouchable community and considered their views as more or less authoritative also for themselves. The peasants with higher status: the community judges, the elementary teachers, the supervisors and other officials employed as the landlords’ estates – belonged to Herrnhuters as a rule and filled higher positions in the society. (Tobien 1930, pp. 134–5)

Because Herrnhuters enjoyed the reputation of being ‘reliable people’, they were preferred by German landlords when hiring estate managers and appointing officials for local rural administration. This was an advantage that could be used by those in its possession during the period of agrarian reform (‘land-surveyor time’) in the mid-nineteenth century. During this time, the stratum of capitalist agrarian entrepreneurs (‘gray barons’) emerged out of the local rural population. One can hypothesize that the percentage of those descended from Herrnhuters within the modern professions (including urban professionals) was greater than that within the population as a whole, since these professions became accessible to un-Germanized Estonians and Latvians during the second half of the nineteenth century.

Catholic counter-reformers made similar efforts to discipline the peasant masses in Lithuania during the seventeenth and eighteenth centuries (Raila 2001; Bumblauskas 2005, pp. 277–429). Yet the imprint that the Baroque period left on Lithuanian folk culture and mentality was markedly different from the Pietist legacy in Latvia and Estonia. Alongside monasteries, pompous church buildings, the sentimental cult of the Blessed Virgin Mary, and numerous shrines serving religious feasts, the
Catholic counter-reformation also bequeathed a taste for ceremonies and rituals, ornament and tasteless luxury. All of these belong to the distinctive features of Lithuanian culture and public life, distinguishing it from the more no-nonsense and sober Latvian and Estonian style.

The earlier onset of modernization in the Baltic north, moreover, fundamentally transformed the Pietist cultural legacy in Estonia and Latvia, obliterating its religious origins. The fact that urbanization did not begin before the Soviet era in Lithuania meant that Lithuanians remained a predominantly rustic people during the first half of the twentieth century, preserving characteristic features of a traditionalist mentality going back to the Baroque era and the rural way of life. In Estonia, ethnic Estonians already constituted the majority of the urban population by the beginning of the twentieth century, while Latvians constituted 42% of the population of Riga by 1897 (Mattusch 1996, pp. 122, 127).

Although ethnic division of labor was a characteristic feature of the social structure in Estonia and Latvia, it was much less marked than in Lithuania, where handicrafts, industry and trade were the traditional employment of the Jews, who constituted the majority of the urban population. It was only during the interwar period that ethnic Lithuanian entrepreneurs infiltrated these occupational sectors, but they were able to compete only with the more experienced and skilled Jewish entrepreneurs owing to the development of a broad cooperative movement, which was strongly supported by the Lithuanian state as part of a policy of ‘positive discrimination’.10

The Jewish population in Lithuania was almost completely exterminated during World War II. By the end of the Soviet era, the majority of the Lithuanian urban population consisted of people of rural origin who in terms of mentality resembled Sicilian and Calabrian migrants to northern Italy more than they did urban and modern Estonians and Latvians. Thus, at the start of the market transformation Lithuania had fewer human resources for the construction of ‘rational capitalism’ compared to Latvia and Estonia. In these countries, the populations contained relatively more individuals socialized in microenvironments that preserved the experiences and memories of life under the conditions of a market society.

When foreign observers compare Lithuanians with their northern neighbors they describe them as ‘Baltic Italians’. In my opinion, it would be more appropriate to compare the Baltic countries with different regions of Italy as regards their cultural traditions and the conditions for the formation of the social capital created by these traditions. In Italy, one finds a sharp difference between the industrial, urban, civic and universalist north (first of all, Lombardy), and the agrarian, rural, ‘familist’, and particularist south (first of all, Sicily and Calabria), notorious for corruption and organized crime (cf. Putnam 1993). One could therefore describe Estonians as Baltic Lombiards, and Lithuanians as Baltic Sicilians or Calabrians. Tellingly, of the three Baltic countries only Lithuania has a ‘national’ mafia with an established reputation in international criminal spheres, while it also harbors the regional Baltic center of the smuggling trade – the marketplace of Gariūnai near Vilnius.
Difficulties with the Culturalist Explanation

One obvious problem with the culturalist explanation relates to the Latvian case. Like Estonia, Latvia is a country with a Protestant cultural heritage, yet its economic achievements during the post-socialist transformation do not exceed those of Lithuania. The version that is presented in this article, however, is able to account for this fact more satisfactorily than the earlier work by Mattusch, for it maintains that it is not the Protestant (Lutheran) but rather the Pietist legacy that matters. In this regard, the Pietist movement penetrated only the one third of contemporary Latvia (Vidzeme) that belonged to tsarist Russia from the early eighteenth century. It took root in neither Catholic Latgale nor Kurzeme (Kurland), which until 1795 was a semi-independent state (Duchy), formally under the suzerainty of the Polish–Lithuanian state. Kurland remained Lutheran, but the authorities of the Lutheran Church in Kurland effectively suppressed all Herrnhuter missionary activities from the very beginning.

Even more importantly, in no other former republic of the USSR did the ethnic composition of the population change more dramatically than in Latvia during the Soviet era. Intensive immigration transformed Latvia into a bi-cultural country with an ethnically non-Latvian population that is economically dominant. The ethnic division of labor created by the Soviet system had more in common with the Central Asian republics than it did with the other Baltic countries (Dreifelds 1996, p. 159). Immigrants constituted the majority not only of unskilled and semi-skilled industrial workers but also of engineers, technicians, highly skilled workers and representatives of other modern professions.

These tendencies intensified even further after 1990, as exclusionary citizenship laws made it harder for the Russian-speaking population to find employment in the public sector. In keeping with what is described as ‘Petty’s law’ (see also Weber 1958, pp. 39–40, 189), representatives of the Russian-speaking population with entrepreneurial dispositions thus directed their energies towards self-assertion in the private sector. Latvian data show that by the middle of the 1990s as many as 80% of entrepreneurs in Latvia were drawn from non-titular nationalities (Bleierle et al. 2005, p. 434). These entrepreneurs used the opportunities that Latvia enjoyed as a transit country and provider of offshore services for Russian businessmen. Capitalism in Latvia thus assumed many of the features usually attributed to ‘wild’ Russian capitalism, with comparative international indexes demonstrating that corruption in Latvia is even worse than in Lithuania. In so far as the dominant economic culture in Latvia is largely non-Latvian, this case can hardly be used to deny the causal significance of different religious histories in explaining the respective progress of Estonia and Lithuania.

Yet why was the Russian minority in Estonia incapable of attaining an economic position comparable to that of its counterpart in Latvia? In part this can be explained by the smaller size of the Russian-speaking population, as well as its concentration in a region (north-east Estonia) which did not become the center of the country’s economic life. The key factor, however, was most likely a privatization policy which
gave preferential treatment to those with citizenship, most of whom were ethnic Estonians. Thus:

the Estonians took over by far the greater part of management positions in the former state enterprises when privatization was implemented. True, the Estonians were already in possession beforehand of a higher share of management positions than the non-Estonians, but the Estonians increased their share as a result of privatization, and the non-Estonians almost completely disappeared from management positions in all the counties of Estonia. (Andersen 1999, p. 409)13

The political elite in Latvia also attempted to use privatization in order to consolidate the economic power of the mainly ethnic Latvian citizenry. However, the predominant position of the Russian-speaking population within industry (including management positions) and the advantages that Russian (and Russian-speaking Jewish) entrepreneurs could derive from international business networks dominated by Russian capital made it impossible to find a strategy that would simultaneously reshape the institutional environment in the direction of a working market economy and tip the power balance in favor of ethnic Latvians. In the words of Nørgaard et al. (1996, p. 147), ‘some Latvian politicians have sought to prevent Russian managers from controlling industry. The delays and confusion that these conflicts have brought into the legislation process, however, have created a legal vacuum which resulted in comprehensive and uncontrolled spontaneous privatizations.’14 Complaints from radical nationalists that privatization would end with Russians hijacking Latvia’s economy led to vacillations and zigzags in the policies of the rightist government. These in turn impeded and slowed down economic recovery.

One can therefore defend a culturalist explanation with reference to the weaker historical influence of Pietist Protestantism in Latvia, an influence that was further diluted by changes in the ethnic composition of Latvia’s population. The fact that political cleavages and the political agenda were basically identical in Latvia and Estonia means that differences in economic performance cannot be explained solely by reference to the socio-political sphere.

**Problems for Further Research**

The political-economic and culturalist explanations are not the only plausible hypotheses as far as the emergence of the north–south gap is concerned. Serious consideration, for instance, should be given to the claim that Estonia’s early success derived from its geographical proximity to Finland. If one reflects further on precisely why this proximity might be important, however, one arrives at conclusions that provide supplementary evidence for a cultural explanation rather than undermining it. As stated above, it is doubtful whether the purely economic impact of this proximity was so important, because in the early 1990s the Finnish economy was in a deep recession. More relevant is the fact that Estonians understand the Finnish language,
and that during the Soviet period residents of northern Estonia could watch Finnish television. This ensured that the population of Estonia was not isolated from Western influence to the same extent as the other Baltic countries. However, Western influence was effective only in so far as it enhanced the vitality of Estonia’s own cultural traditions and slowed down its erosion by the daily experience of life under state socialism. Otherwise, it would be difficult to explain why, for example, the exposure of the Russian population to Western cultural influence on a large scale during the early 1990s did not lead to revolutionary changes in Russian economic culture.

Another very plausible explanation for Estonian success refers to the foreign investors who came to the country at the very onset of privatization in 1992–93. As a result, the number of foreign investments in Estonia in the 1990s was significantly larger than in Latvia and Lithuania: in 1993–95 in Estonia it was US$366 million, in Latvia US$143 million and in Lithuania only US$42 million (Aslund 2002, p. 436). Yet how should one explain investors’ preference for Estonia? Perhaps the Estonian government simply invested more heavily in public relations activity in order to create a positive international image of the country, or employed specialists who were more skilled? Some of the facts related by Mart Laar in his memoirs would seem to support this supposition:

One of the most significant projects was a campaign in the international media, the cornerstone of which was the purchase of a supplement to Newsweek magazine. Money from a World Bank loan was used for this purpose, despite not having been intended for such a purpose. It was not merely the supplement itself which was important, but also the contract which specified that Newsweek would publish further articles about Estonia. It was precisely these follow-up articles which had the greatest effect. (Laar 2002, p. 248)

The success of public relations work, however, depends not only on how much you invest, but also on whether you manage to strike a chord with those whom you address. Here again, one can hypothesize that Estonia’s success in competing for foreign investments is explainable at least partly by the peculiarities of its cultural tradition, which place it closer than its Baltic neighbors to the Scandinavian, Anglo-Saxon, and German-speaking countries. Managers of large companies who made a general decision to invest somewhere in ‘the Baltics’, but initially perceived the three countries as a single unit, could be swayed in Estonia’s favor by certain small details signaling that Estonians are ‘closer Others’ than their southern neighbors. Even the seemingly insignificant fact that English speakers find Estonian surnames (e.g. Adamson, Kask, Lepik, Viikberg) easier to pronounce (and remember) than Latvian and especially Lithuanian (Abromaviciute, Brazauskas, Juškevičius) ones could be important for this perception of cultural proximity. Initial investments imbued the image of the ‘shining star from the Baltics’ with real substance and made the mechanism of self-reinforcing expectations work: Estonia received more investments because it looked more ‘Western’, more attractive and better than other Baltic countries; and as it attracted more and more investments, its outlook became even more attractive.
Of course, one cannot exclude the possibility that a deeper and more technical economic-historical analysis applying advanced econometric techniques would detect purely economic differences in the initial conditions that have secured a comparative advantage for Estonia. Yet the Pietist Protestant hypothesis would nevertheless seem to invite further historical-sociological research focusing on whether, for instance, Latvian Pietists and individuals with Pietist roots were more broadly represented among entrepreneurs and in modern professions than ethnic Latvians who were orthodox Lutherans, Orthodox, or Catholics, or whether Latvians from Kurzeme (with no Pietist influence) were more or less broadly represented in the emerging Latvian elite than those from Vidzeme. These are questions for ‘doable’ research (Lieberson 1985, pp. 6–12) that could help to decide the fate of the culturalist explanation.

The culturalist hypothesis itself requires further elaboration through the specification of social micromechanisms explaining how differences in the cultural heritage of the Baltic countries were causally significant in the situation of the reemerging market economy. I would like to close with two hypotheses about these mechanisms. First, one can hypothesize that Estonia’s history bequeathed informal institutions that were more compatible with the formal market institutions (known as the ‘Washington consensus’) introduced from above during market reform. Ceteris paribus, such compatibility lowers the level of transaction costs (Klump 1996; North 1990; Blümle et al., 2004). Second, one can ask whether the cultural heritage of Estonia had positive causal relevance for the readiness to learn to act under conditions of an emerging market economy, and for the speed of this learning. How one responds to changed conditions depends upon how these are interpreted, and this process of interpretation proceeds within the framework of certain available shared mental models or worldviews. If one assumes that these models derive from a prior process of individual and collective learning, it necessarily follows that cultural traditions are not insurmountable obstacles for capitalist development. As beings capable of learning from their experiences, human actors adapt both their ‘cold’ (cognitive) and ‘hot’ (normative) expectations to changes in the environment of action. However, the culture-specific stock of available models is critically important in determining the speed with which these expectations adapt to the new reality. The crux of the matter is that a change in expectations by the majority of the population is tantamount to a change of social reality itself.

Depending on the character of the prevailing models, a decline in individual welfare can be considered either as a personal problem attributable to insufficient effort, character flaws, or lack of talent or it can be blamed on the ‘government’ or the ‘system’. Sociological survey data would tend to suggest that the first response is more characteristic of Estonian culture, and one can infer that this facilitated and speeded up the process of learning and adapting to new conditions. By contrast, the slower (by one to two years) progress of reform and later start of economic recovery in Lithuania can be explained by a slower process of learning how to act in a market environment, which was conditioned by mental models inherited from a traditional rural Catholic social environment. However, as the examples of Ireland and Bavaria show very well, a Catholic cultural legacy is by no means an insurmountable obstacle to competing in the race for economic progress.
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Notes
3 See also Aslund (2002); Nørgaard (2000); Smith, Pabriks and Purs (2002).
4 On the state of the economies of the Baltic countries at the beginning of economic transformation, see Haavisto (1997); Shen (1994); Van Arkadie and Karlsson (1992).
6 Weber (1958, pp. 95–6, 144).
7 Estland and Livland are not identical with contemporary Estonia and Latvia. The government of Estland encompassed northern Estonia, and that of Livland, southern Estonia and one third of contemporary Latvia (Vidzeme).
8 On the history of the Herrnhuter movement in Baltic countries, see Harnack (1860); Nerling (1956); Plitt (1861); Tobien (1930, pp. 116–39); Weermann (1956); Pivoras (2000, pp. 30–1).
9 ‘Generally, one can assert that Pietism was spread much more widely in Estland (or generally, in the territory with an Estonian speaking population) than in the part of Livland with Latvian speakers; this fact explains its greater cultural significance in Estonia’ (Weermann 1956, p. 156).
10 This policy was inspired by the economic success of farming cooperatives in Denmark during the second half of the nineteenth century. On the cooperative movement in Lithuania, see Simutis (1942, pp. 32–42). For a discussion of how Denmark’s agrarian development influenced strategies for economic modernization in Eastern Europe, see Kingston-Mann (1999).
13 On privatization in Estonia see also Terk (2000).
14 See also Nissinen (1999, pp. 216–44).
15 See Denzau and North (1994).
16 It has even been suggested that evolutionary selection has a role to play in this regard. I would maintain that mechanisms of individual and collective learning are
more important than mechanisms of evolutionary selection. However, the importance of rational learning compared to other forms of learning remains to be established. For a discussion of these issues, see Camerer (1997); Güth and Kliemt (2004); Mailath (1998); Vanberg (2002).

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