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# Neoliberalism, Embedded Neoliberalism and Neocorporatism: Towards Transnational Capitalism in Central-Eastern Europe

DOROTHEE BOHLE and BÉLA GRESKOVITS

*This article analyses the key features and origins of three variants of transnational capitalism emerging in Central-Eastern Europe: a neoliberal type in the Baltic states, an embedded neoliberal type in the Visegrád states, and a neocorporatist type in Slovenia. These regimes are characterised by their institutions and performances in marketisation, industrial transformation, social inclusion, and macroeconomic stability. Explanations for regime diversity are developed at two levels. First, it is argued that the legacies of the past, and their perceptions as either threats or assets to these countries' future, have had deep impact on regime types. Legacies and initial choices were no less crucial for the degree of democratic inclusion, and the different patterns of protest and patience on the paths towards the new regimes. Second, the article demonstrates the importance of transnational influences in industrial transformation and social inclusion.*

Three capitalisms emerged from the transformation of Central-East European (CEE) societies: a *neoliberal* type in the Baltic states, an *embedded neoliberal* type in the Visegrád states, and a *neocorporatist* type in Slovenia. This diversity is puzzling both in light of where these societies departed from and where they have been heading. Their point of departure, state socialism, is widely seen as a system that had been remarkably successful in forcing uniform economic and political structures and institutions on the CEE societies. Moreover, once the system fell apart, its pieces moved 'from the fire to the frying pan', as they entered the global economy that many analysts view as no less powerful a homogenising agent. How to explain, then, that these countries embarked, in a patterned rather than a random way, on radically different trajectories, which led to a diversity of market societies instead of a single post-socialist variant?

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To understand their origins and logic of emergence, we adopt Polányi's theory of the 'Great Transformation', and analyse these regimes above all as products of a contradictory double dynamics in the uses of state power to build market economies and simultaneously preserve their social cohesion. In the following section, we demonstrate that the different vigour with which the transformation agenda has been pursued led to particular institutional configurations and varied performances in the key areas of marketisation, industrial transformation, social inclusion, and macroeconomic stability.

Our explanation of regime diversity stresses the interplay of two main factors. First, we argue that initial political choices mattered. Subsequently, we demonstrate that the decisions concerning the new regimes have been motivated both by the legacies of the past and their perception as either threats or assets from the viewpoint of national sovereignty and economic independence. Recognising these differences also helps us to understand the varied amounts of protest provoked by the three regimes, the pattern of political competition characterising them, and the variation in the form of their democracies. Second, we take seriously the formative role of transnational and international influences as well as their diversity. We then demonstrate how the pressures of the European Union, and the influences of varied types of transnational corporations (TNC) in interaction with inherited industrial profiles and domestic policy choices, have locked the new regimes into paths able to reproduce many of their features. In the concluding section we summarise our findings on CEE's varieties of transnational capitalism, and specify our own contribution to understanding post-socialist diversity.

### **The Matrix of Regime Performances and Institutions**

The first impression one gets from some essential facts on the CEE transformation paths is that of *similarity* rather than divergence. In but a decade, all these countries consolidated some form of democracy. They became integrated in the global and European economy. Their trade with the EU approximates or exceeds their gross domestic product (GDP). Via substantial foreign direct investment (FDI) their assets have been incorporated into Western systems of production, commerce, and finance. Foreign control became the norm in their major export industries, services, and utilities. They are members of important international organisations.

The question, then, is: are these small states anything else than playgrounds for powerful international forces? Could they at all retain or develop any measure of influence over their development? Evidence suggests that they could. Indeed, fair degrees of effectiveness, regulatory, and enforcement capacities set the CEE states apart from the rest of the former Soviet bloc and place them among the better-governed states of the world (Kaufman *et al.* 2002). However, they differ in how vigorously they imposed public constraints over private economic activity to pursue conflicting aspects of transformation.

*Regime Concepts*

As Polányi would have predicted, CEE's post-socialist development has been driven by conflicts and compromises between 'two organising principles in society', economic liberalism guiding the establishment and institutionalisation of markets, and 'the principle of social protection aiming at the conservation of man and nature as well as productive organization' (Polányi 1957: 132). Accordingly, we define our regimes as capitalist political economies in which marketisation and social protection has been pursued and institutionalised with different amounts of vigour and in varied forms.

The unconventional element of our approach is that, in accordance with Polányi, we consider economic protectionism, aimed at sheltering inherited domestic and new transnational industries by tariffs, subsidies and special regulations, no less as a manifestation of the principle of social protection than social welfare policies. Although political discourse tends to contrast industry subsidies with social welfare expenditures on the realistic grounds that in any given moment spending on one purpose may directly limit spending on the other, the contradiction of these two kinds of protectionism might not be all that antagonistic. At the macro-level, state assistance that helps private actors to save existing jobs or create new ones may substitute for unemployment benefits or early retirement and disability pensions. Conversely, public spending on education and healthcare can partly be viewed as subsidies to firms that rely on skilled and healthy labour forces. In certain instances businesses' individual preferences can be compatible with such macro-social solutions. However, the micro-logic of firms is likelier to contradict any macro-logic requiring that conflicting social groups take responsibility for each other. Hence the high probability of collective action problems and the need for state intervention to solve them (see Table 1).

CEE states have responded differently to the challenges of the new Great Transformation. In the Baltic states a reincarnation of economic liberalism as *neoliberalism* has been pursued in a rather radical and uncompromising fashion. The Visegrád countries are distinguished by their search for compromises between marketisation and *both* kinds of social protection. They arrived too late to the globalising European economy to implement the dominant post-World War II Western regime of protective industrial policies and generous welfare states that Ruggie (1982) termed 'embedded liberalism'. Thus the Visegrád group's compromises are more reminiscent of the limited balancing acts observed in the current 'embedded neoliberal' regimes of many West European societies, in which social protection has increasingly lost its former purpose and institutional underpinnings, and become 'subordinated to the overriding objective of neoliberal competitiveness' (Van Apeldoorn 2002: 181). Finally, in CEE only Slovenia's neocorporatist regime is characterised by a firmly institutionalised balance between marketisation and both kinds of social protection, whereby business, labour, and other social groups are accepted as partners in

TABLE 1  
INDUSTRIAL TRANSFORMATION

	Growth rate of industrial output (1992–2003 average %)	Complex exports (2000–04 average % of total exports)	Complex manufacturing FDI stock per capita (2002–04, US\$)	Sectoral, ad hoc, and horizontal state aid to firms (2000–04 average % of GDP)
Estonia	0.5	38	96	0.16
Latvia	–2.0	15	29	0.33
Lithuania	–3.1	31	107	0.37
<i>Baltic average</i>	<i>–1.5</i>	<i>28</i>	<i>77</i>	<i>0.29</i>
Czech Republic	3.1	56	1113	2.23
Hungary	6.5	67	875	1.13
Poland	6.4	44	244	1.30
Slovak Republic	2.5	50	–	0.54
<i>Visegrád average</i>	<i>4.6</i>	<i>54</i>	<i>744</i>	<i>1.30</i>
<i>Slovenia</i>	<i>1.0</i>	<i>49</i>	<i>198</i>	<i>0.73</i>

*Sources:* Column 1: EBRD Transition Reports various volumes; Column 2: authors' own calculation based on COMTRADE database of the United Nations Statistics Division. Complex exports are commodities coded 5 (chemicals) and 7 (machinery and equipment) in SITC classification; Column 3: Kettmaker (2005), and authors' own calculation based on data from national FDI agencies; Column 4: Eurostat.

shaping that balance (Schmitter 1974; for CEE see Tatur 1995). In empirical terms, our classification rests on a matrix of performances and their institutional bases in four important areas: marketisation, industrial transformation, social inclusion, and macroeconomic stability.

### *Marketisation*

The three regimes are least different in their achieved levels of liberalisation, privatisation, and market-oriented institution building. By the early 2000s the whole region had adopted the standards and institutional underpinnings of economic freedom and openness usual in Western market economies. However, there is systematic variation in the radicalism of the reform paths that led to this outcome. Assessing radicalism by the rate at which market reforms have been introduced and new institutions built, and using the annual advance on the transition index of the European Bank for Reconstruction and Development (EBRD) as a proxy to measure it, lead us to conclude that the Baltic states have been the most, and Slovenia the least market-radical. The Visegrád states occupy intermediate positions in this respect. Two important facts have to be considered to understand this variation. First, thanks to their long experimentation with reform socialism, Hungary, Poland, and Slovenia had relatively marketised economies already in 1989, while the Baltic states had to start 'from scratch'. Second, since state socialism persisted until 1991 in the Baltic countries, their reforms

began later than those of other CEE states. Evidently, it is only due to their reform radicalism that by the early 2000s the Baltic states could catch up with the Visegrád group and indeed overtake Slovenia.

### *Industrial Transformation*

Compared with other CEE economies the Baltic performance appears inferior in two key dimensions of industrial transformation, as it is characterised by deindustrialisation and deskilling (Table 1).

While in 1992–2003 industry recovered in the Visegrád group and Slovenia, the average growth rate of industrial output over the same period was negative in most Baltic states. Furthermore, in the first years of the new Millennium, the bulk of Baltic exports originates from resource- or unskilled labour-intensive industries, and thus exhibits the profile common to many less advanced countries. In contrast, the Visegrád states and Slovenia mainly export the same products as many advanced countries, which rely heavily on complex capital, technology, and human skills. Accordingly, we found that the infusion of FDI in the complex manufacturing industries of the Visegrád states exceeds, in per capita terms, the Baltic figure by a factor of 10. Finally, the divergence in industrial transformation appears to be consistent with varied patterns of state institutions aimed at fostering the transformation of inherited socialist industries into new foreign controlled and invested operations. The Visegrád states tried to mitigate the impact of market shock on their industrial legacy and at the same time accelerate foreign capital infusion by protective regulation and tariffs, export zones, foreign trade and investment agencies, investment support funds, tax exemption regimes, and public development banks. In contrast, industrial policies have not been pursued with comparable vigour in the Baltic states.

### *Social Inclusion*

While Gini coefficients, relative income shares, and other indicators of social inequality do not paint an overly gloomy picture of the region, the Baltic regime appears rather unequal and socially exclusive. Slovenia represents the opposite extreme, whereas the Visegrád countries are in between these polar cases in most measures (Eurostat). There is clear variation in the strength of institutionalised efforts to maintain social welfare (Table 2).

In light of this evidence, the Baltic subregion is hardly the place to live for anybody whose meagre living standards depend on state assistance. Nor is it the right place to be a worker. With their virtual lack of any negotiated industrial relations, the ‘volunteer Scandinavian’ Baltic states appear to be the least ‘Scandinavian’ in the region. Low union density, decentralised, uncoordinated wage bargaining and low coverage rates of collective agreements complete the institutional landscape of these disembedded societies. Neither do the Visegrád regimes perform much better in this latter

TABLE 2  
SOCIAL INCLUSION

	Total expenditure on social protection (2000–04 average % of GDP)	Per capita total expenditure on social protection (2000–03 average euro PPS)	Spending on passive and active labour market policies (late 1990s, % of GDP)	Collective bargaining coverage rate (early 2000s, % of employed)
Estonia	13.6	1300	0.16	21–30
Latvia	14.2	1120	–	11–20
Lithuania	14.5	1264	–	11–20
<i>Baltic average</i>	<i>14.1</i>	<i>1228</i>		<i>14–23</i>
Czech Republic	19.8	2752	0.50	21–30
Hungary	20.4	2439	0.96	31–40
Poland	21.3	2020	2.20	41–50
Slovak Republic	19.1	1982	1.10	41–50
<i>Visegrád average</i>	<i>20.1</i>	<i>2298</i>	<i>1.19</i>	<i>34–43</i>
<i>Slovenia</i>	<i>25.0</i>	<i>3920</i>	<i>1.72</i>	<i>91–100</i>

Sources: Columns 1, 2: Eurostat; Column 3: Riboud *et al.* 2002: 13; Column 4: Visser 2005.

respect. Slovenia is the only country where negotiation between business and labour, as well as coordination among social welfare, industrial, and macroeconomic policies, is fairly well institutionalised.

### *Macroeconomic Stability*

More than in anything else, it is in macroeconomic stability and balanced public finance that the strengths of the Baltic countries lie, although Slovenia is not lagging behind them (Table 3). Both the Baltic and Slovene regimes adopted the EU's 'stability culture' (Dyson 2006) and came close to meeting the convergence standards of the Maastricht Treaty that is likely to earn them early entry to European Monetary Union (EMU). Relative to their GDP, the Baltic countries operate the smallest and least indebted fiscal states of the region, continue to rely on the most restrictive monetary institutions, currency boards, and use most consciously their ERM-2 entry as an international pillar of their policies to lock in macroeconomic stability and acquire credibility in financial markets (Feldmann 2006a). In contrast, in the Visegrád states, with the recent exception of the Slovak Republic, neither the ministries of finance nor the central banks have succeeded so far in achieving dominance vis-à-vis the coalitions of rival institutions shaping their sizeable and heavily indebted state households.

### **Support and Contestation: The Politics of Regime Paths**

The significance of varied structures of state performance and institutions cannot be fully grasped without understanding *how* it came to be that way.



TABLE 3  
MACROECONOMIC STABILITY

	General government balances (2000–03 average % of GDP)	General government debt (2003, % of GDP)	General government expenditure (2000–03 average % of GDP)
Estonia	+2.3	5.3	35.5
Latvia	–2.1	13.4	35.7
Lithuania	–2.1	21.9	31.7
<i>Baltic average</i>	<i>–0.6</i>	<i>13.5</i>	<i>34.3</i>
Czech Republic	–7.2	38.8	42.4
Hungary	–5.4	57.4	49.8
Poland	–3.4	45.3	42.9
Slovak Republic	–6.9	42.6	50.4
<i>Visegrád average</i>	<i>–5.7</i>	<i>45.9</i>	<i>46.4</i>
<i>Slovenia</i>	<i>–2.6</i>	<i>29.3</i>	<i>48.1</i>

Sources: EBRD Transition Report 2005.

As we know from Gourevitch (1986: 17), ‘Policy requires politics... if an idea is to prevail as the actual policy of a particular government, it must obtain support from those who have political power’. How much support have the CEE regimes generated?

### *Social Protest and Electoral Challenges*

All in all, the policy choices of the CEE countries have met little social protest over the whole period of economic transformation, crisis, and recovery. This is the more surprising that especially the first half of the 1990s brought about extreme economic hardship and dislocation for massive groups (Greskovits 1998). However, within the generally low level of contention there is some variation across country groups. While strikes have been almost entirely absent in the Baltic states and Slovenia, contentious action has been somewhat more frequent in at least some of the Visegrád countries (Bohle and Greskovits 2006).

The outcome of democratic elections can be seen as a second indicator of the degree to which particular policy choices are approved or politically contested. In this respect, too, a quite consistent regional pattern prevails. Until most recently, citizens both in the Baltic states (with the exception of Lithuania), and in Slovenia regularly re-elected parties which represented the same political colour, economic philosophy, and, when forming new governments, ranked their tasks in much the same way as their predecessors. Thus over the whole period following the collapse of state socialism, centre-right parties and governments enjoyed broad support and uninterrupted hegemony in Estonia and Latvia. Slovenian politics exhibited no less continuity. However, in that country it was the centre-left that remained in power for a long period.

In turn, politics in the Visegrád countries has been marked by the regular alternation of right-wing and left-wing parties in power with incumbents usually voted out by the electorate. In Poland (and Hungary until 2006), no incumbent was able to govern for more than one term. In the Czech and Slovak Republics the left–right alternation occurred in two-term long intervals with the second term usually bringing about a weakened minority government of the left or the right. How can we explain the different patterns of support and contestation of the three regimes? More provocatively, how could the Baltic regime that neglected social inclusion be less contested than the Visegrád regime that made more efforts to protect society?

*Legacies, Initial Choices and Consequences for Politics and Polities*

In his influential ‘Capitalism by Democratic Design?’ Offe (1991) painted a pessimistic picture of the prospects for democracy in Eastern Europe. In his view, the state socialist countries faced a ‘triple transformation’ to nation state, capitalism, and democracy, which had to occur simultaneously rather than, as long ago in the west, in a sequence. This overloaded agenda was not only full of social conflicts, but its tasks also contradicted each other. Hence Offe’s conclusion that a whole Pandora’s box was opening, in light of which democratic breakdown was the most likely outcome.

In our cases, history proved Offe’s prediction wrong, since the CEE states mastered all challenges of transformation. Moreover, the reformers seem to have made choices about which task to prioritise and whether to perceive the legacies of the socialist system as a threat or an asset when performing them. Below we argue that different legacies, and the way they were perceived, as well as different reform priorities impacted on the patterns of political cleavages and conflicts, and the features of democracy. As a result, rather than democratic breakdown, we observe, with the sole exception of Slovenia, a variety of ‘low-level equilibrium’ democracies (Greskovits 1998). To characterise the variation, we adapt the terms elaborated for the Latin American context by Acuna and Smith (1994).

*The Baltic States: National Independence, Neoliberal Economics, and the Emergence of Exclusionary Democracy*

Among our cases the Baltic situation fell closest to Offe’s transformation trilemma. These countries could neither take their nation nor their state institutions for granted, and inherited the least favourable legacies in terms of economic institutions from state socialism. At the same time, these states felt the strongest urge to distance themselves from the legacies which equalled Soviet domination. How could they solve the trilemma in such a way that the solution even elicited permanent popular support?

Similar to other authors, we see a major reason in the fact that the revolutionary processes in all three countries started in the field of identity politics, that is the redefinition of the Estonian, Latvian and Lithuanian nation in time and space, and of their relations with Russia, the Russian minority, and the West (e.g. Lagerspetz and Vogt 2004: 71–3). Identity politics remained a major issue over the last 15 years, and shaped the form of democracy and capitalism in these countries. It allowed for democratic institutions to gain support even if the new democracies did not bring about social and economic progress: ‘gaining democracy, a parliament, president, political parties, was – and is – very important from the perspective of identity politics; acquiring all these was a confirmation of the Estonians’ “Europeanness”’ (Lagerspetz and Vogt 2004: 73).

However, identity politics led to exclusionary democracies. It is well known that Latvia and Estonia (but not Lithuania) introduced extremely restrictive citizenship laws in the early 1990s. In both countries citizenship initially was automatically only granted to pre-1940 citizens and their descendants. This excluded all those Russians who had arrived under the Soviet era – about 28 per cent of the Estonian and 32 per cent of the Latvian population. Moreover, both laws made it very difficult for minorities to acquire citizenship. Although – mainly due to the pressure of EU – the citizenship laws were later liberalised, still in 2003 22 per cent of registered residents of Latvia were non-citizens, most of them Russian-speaking (Smith-Sivertsen 2004: 102–3). In Estonia in 2002, some 13 per cent of residents did not have any citizenship at all, and some 6 per cent still held Russian citizenship (Lagerspetz and Vogt 2004: 75–6). The citizenship laws muffled potential conflicts. First, although the Russian minority was less enthusiastic about leaving the Soviet Empire than ethnic Latvians or Estonians, it had been deprived of a democratic voice to oppose independence. Second, it also lacked the political and organisational means of social contention.

Radical economic reforms were equally crucial for the defence of newly acquired national independence, since they were most suitable for cutting the ties with the Russian economy on which these countries depended heavily. In this respect, the reforms were successful: within a short period of time, external trade was reoriented towards the West, and national currencies were institutionalised. These achievements had high costs in social dislocation, which also had an ethnic dimension. Russian-speakers suffered most, as they were typically occupied in the industries built up under the Soviet Empire. However, since the crisis and reforms fragmented the organisations and dismantled the power of trade unions and business groups, the Russian minority that potentially could have become a strong opponent of the neoliberal regime was silenced as much in interest groups as in democratic politics. Political exclusion was coupled with and buttressed by social exclusion.

The goal of national independence also can explain why macroeconomic stability became a priority for the Baltic states. The national currency is an

important means and symbol of sovereign statehood. To establish the new currencies, the principles of sound money had to be respected. Fixed exchange rate regimes, and in Estonia and Lithuania currency boards, became guarantors of credible new currencies and thus the new nation states (Feldmann 2006a). At the same time, independent central banks and currency boards depoliticise monetary policy, as they ‘insulate key aspects of the economy from the influence of politicians or the mass of citizens by imposing internally and externally binding constraints’ (Gill 2003: 182).

*Slovenia: Favourable Legacies and the Emergence of Inclusionary Democracy*

In terms of the tasks it set itself, Slovenia seems at first sight to be closest to the Baltic states. Similar to them, it faced the challenges of transformation to nation state, democracy, and capitalism. In terms of its politics, however, it can be found at the opposite extreme, as it exhibits all features of an ‘inclusionary democracy, based on strong actors and an activist state’ (Acuna and Smith 1994: 44–6). How to explain the different outcome?

The fact that Slovenia could build on significantly different legacies provides an important part of the answer. Slovenia’s ‘triple transformation’ was a long and gradual process that had started way back under Tito’s Yugoslavia. As a republic of the Yugoslav federation, Slovenia had a long experience of relatively autonomous self-management that added a level of participatory decision-making unknown in other state socialist countries, and produced managers, unionists, and bureaucrats who had the skills and were habituated to seeking accommodation between economic and social considerations. Moreover, the Slovene economy was not only the most liberalised but also the most developed and western-oriented economy of former Yugoslavia and of the whole Soviet bloc. It was also much less dependent on Serbia than the Baltic states were on Russia. As a result, Slovenia’s transformation recession was the one of the less severe among the CEE countries (Stanojevic 2003: 288).

Last but not least, since the quest for democratic and economic reforms preceded nation building, identity politics never assumed as crucial a role in Slovenia as in the Baltic states. In fact, national self-determination became an important issue in Slovenian politics mostly only as a reaction to the attempts of recentralisation in the Yugoslav federation after Tito’s death and the victory of the hard-line faction in Serbia’s communist party in 1987 (Harris 2002: 155). Given this country’s ethnic homogeneity, nationalism could become a framework for an inclusive polity, not one which had to be defended against enemies from within and outside. Evidently, there was a moment when Slovenia’s national independence seemed to be under threat. Luckily, however, the war for independence was short.

Thus, Slovenia could build on a wide array of favourable legacies and use them as assets for inclusion. Self-management was transformed into

neocorporatist institutions, which included labour more thoroughly than many of their Western counterparts. The relatively mild transformation crisis served as a catalyst to remove the right-wing coalition that won the first independent parliamentary elections from power, and laid the foundation for rather stable centre-left hegemony. As Stanojevic (2002: 290) argues, 'From then on political exchange between centre-left governments and organized economic interests became a permanent feature and the key mode of interest concertation, giving social legitimacy to market reforms'.

*The Visegrád Countries: Compensation without Institutionalised Inclusion and the Emergence of Dual Democracy*

In terms of their legacies, the Visegrád countries seem to be located on the continuum between the Baltic states and Slovenia. Thus both the Czech and the Slovak Republics inherited rather unreformed state socialist systems. Their degree of dependency on the Soviet economy was lower, however, and their industries more competitive than those of the Baltic states. Both countries faced the tasks of nation-state building, but this process was perceived as much less threatened by external actors than in the Baltic countries. As a consequence, nation building never became the same overwhelming issue: least in the Czech Republic, the more developed and ethnically homogenous part of the federation. In the poorer and ethnically more heterogeneous Slovak Republic, nation building came into conflict with democratic state building for a period in the 1990s. Poland and Hungary had reform socialist legacies, which, as in the Slovene case, could become assets for the turn to democratic capitalism and its consolidation. In addition, both countries were lucky enough to escape the task of nation-state building. They were, however, severely constrained by the huge amount of external debts they had accumulated over the 1980s.

The distinct challenges posed by the legacies, and the political elites' reaction to them, seem to be at the origin of the intermediate position the Visegrád countries occupy with regard to social and political inclusion, as well as of the more fragile support for their regime paths. Visegrád reformers were well aware of the social hardship caused by the collapse and market reforms, but they could not fall back upon identity politics and disenfranchise large parts of the affected population to muffle protest as the Baltic states did. At the same time, they shied away from offering institutionalised voice to unions and the losers of reforms, the way Slovenia did. Rather, they decided to offer ad hoc compensation in the form of relatively generous targeted social protection packages in order to overcome opposition to reforms.

Poland offers a good example of this choice. Its reformers knew that 'shock therapy' would hurt industrial workers and the rural population, and create a pool of people left, at least temporarily, deprived of resources for survival (Balcerowicz 1995: 262–3). In light of this, they considered the

trade union wing of Solidarity a threat rather than an asset for the new polity. Thus, the initial reform package was prepared in a highly isolated institutional setting, while Solidarity leaders were asked or volunteered to silence the feared mass militancy. Inherited institutions of labour representation as well as local citizen committees that had emerged around the changes were dismantled (Grabowski 1996). As compensation, Poland introduced unemployment benefits, minimum wage regulations, and massive early retirement schemes 'from above' (Orenstein and Haas 2005).

While the Polish example is unique because of the Solidarity legacy, the transformational pattern of compensation without institutionalised interest representation is not. Hungary's social welfare system, extensively using disability and early retirement schemes (Vanhuysse 2006), is among the most generous in the region, while its record in institutionalising tripartite relations between labour, capital and the state has been less convincing. In the Czech and Slovak Republics, relatively encompassing systems of welfare were adopted too. In addition, both countries kept supporting their large enterprises and thus could slow down the dynamics of unemployment (Drahokoupil 2007: 11–12). The Czech and Slovak Republics initially offered labour institutionalised inclusion, but the governments' commitment to the tripartite bodies has been shaky in the Czech Republic, and broke down entirely in the Slovak Republic (Ost 2000: 512–13). It is because of the above pattern that we term the Visegrád polities 'dual democratic regimes', where selective and limited inclusion parallels, and occurs at the expense of, the exclusion 'of the remaining social actors by disarticulating and neutralizing their capacity for collective action'. This dual logic is complemented by an 'unequal distribution of resources, where benefits are only extended to allied sectors of business and labor' (Acuna and Smith 1994: 47).

Appeasing large social groups through ad hoc targeted welfare policies has, however, faced increasing political difficulties. In the Visegrád polities, political contention has been closely, albeit not exclusively, linked to the issue of social protection, i.e. its focus on economic versus welfare protectionism, as well as its conflicts with macroeconomic stability. Interestingly, as Polányi would predict, there has been no clear division of labour between the left and the right in the sense that the former has protected vulnerable social groups while the latter only the economy. Rather, all parties that hoped for mass popular support usually stressed the intrinsic relationships between economic and welfare protectionism, promised both kinds, and, once in power, tried pragmatically to implement some mix.

This is the background against which the nature of the Visegrád democracies, as well as their pattern of recurrent protest, be it in the form of strikes or punishing incumbent governments, can be understood. It is not least for their embedded neoliberalism's complex, contradictory, and institutionally unregulated agenda that the trial and error pattern of political success remains an inherent feature of Visegrád polities.

Indeed, as demonstrated by the new coalitions of the mid-2000s, under certain conditions these dual democracies can become vulnerable to illiberal challenges. The 2005 and 2006 elections put an end, albeit in different ways, to the hitherto prevailing centrist alternation. For the first time in Hungary's post-communist history, voters granted a second term to the incumbent left-liberal coalition, while extremist parties lost even their limited support. After the Czech elections, while support for communists as the only sizeable non-centrist party declined, both the left and the right seem incapable of forming a government. The prospects are even gloomier for Poland and the Slovak Republic, where alliances of a third force took over, involving radical nationalist, xenophobic, and anti-western parties.

The contrast in the political fortunes of illiberals invites the question: why are they on the rise in the latter and on the decline in the former group of countries? While a convincing answer requires in-depth research, our elaboration so far may offer helpful clues. Poland and the Slovak Republic have had to face unusually difficult social structural problems. Despite efforts to embed neoliberalism (at least until the early 2000s) these societies lag far behind other Visegrád countries in terms of actual achievements in social cohesion. They are not just leaders in CEE but in the whole of the EU in the rate of both unemployment and long-term unemployment. Moreover, the risk of becoming poor remains very high in both cases even after social transfers (Eurostat). Last but not least, both countries are plagued by grave sectoral and regional inequalities. Even if their elites for most of the transformation period have tried, they have so far failed to avoid the perils of dualistic societies, in which gratitude over the advance of others is rapidly overwhelmed by the apathy or fury of those who just cannot make it (Hirschman 1981: 49). Persistent deep social gaps combined with grave ideological and political divisions within elites prepared the ground for the rise of illiberals in Poland and the Slovak Republic, while in Hungary social dualism at least, and in the Czech Republic both social and elite divisions, have so far remained within safer limits.

### **EU Pressures, TNC Preferences, and the Socioeconomic Logic of Regime Diversity**

We found that early political choices mattered for the emergence of regime clusters. But is democratic national politics the only factor that has been important? After all, the regimes did not evolve in a closed national economy, or in a social vacuum. Consequently, all of the relevant opportunities and constraints might not be captured at the level where democratic national politics rules. Below we argue that although domestic politics has not lost its significance, by the late 1990s it had become increasingly constrained by the pressures of the EU and the preferences of transnational corporations.

*The Role of the EU*

Left on their own, the CEE regimes would have perhaps ended up as even more divergent: the Baltic states more market-radical, politically and socially more exclusive, the Visegrád states less macroeconomically stable, and Slovenia more protectionist. However, through (and beyond) the *acquis communautaire* proper, the EU seems to have promoted a certain model of capitalism too. That model consists of four pillars, the Single Market, the EMU, the Lisbon Agendas, and, subordinated to the former, a social dimension, each of which prioritises the very issue areas where the CEE regimes diverge. During and after accession various EU bodies and actors made efforts to keep divergence under control, cut back ‘extremities’, and guide the CEE regimes towards some balance. Thus, to comply with EU requirements, Estonia had to *deliberalise* its trade policies before entering the EU, whereas Slovenia was pressed to speed up its sluggish privatisation process, and let foreign capital take over its strategic sectors (Lindstrom 2005). Several Visegrád countries were repeatedly criticised for failure in keeping their macro-fundamentals in line with the Stability and Growth Pact, or, alternatively, for trying to catch up with old members by tax competition and social dumping. It can perhaps be argued that – albeit in a somewhat ad hoc fashion – the EU has tried to promote a form of embedded neoliberalism in CEE that mixed the contradictory regime features of older member states.

It is important to note, however, that in its interaction with would-be members the EU never merely functioned as a purely ‘external’ factor. Its influence is perhaps more adequately viewed as one implanting international and transnational dimensions and reference points into domestic politics without actually participating in it. On the one hand, domestic actors have frequently used EU requirements, and the voice of community actors and institutions monitoring them, for their own political purposes (Dyson 2006). On the other hand, the EU accession process has opened the CEE economies to TNC, which, similar to the EU, have not been enmeshed in domestic politics, but have had other means to intervene in, and leave their mark on, the emergence of regime diversity.

*The Systemic Power of TNC*

Most importantly, capital enjoys “systemic power” embedded in the institutional substructure of the economy... Perhaps the simplest way to think about the systemic power of business is in terms of “exit options” (Pontusson 1992: 233). This general concept can be tailored to fit the context of CEE transformation. First, given the scarcity of capital in the region, it is unsurprising that TNC became the leading fraction of the emerging business communities. Second, TNC disposed of systemic power *before* entering these economies: this stemmed from the option to refuse to enter and invest.



Third, *after* FDI materialised, the whole dynamics of exit, voice, and loyalty (Hirschman 1970) came fully into play, and shaped, depending on TNCs' strategies and cross-border mobility, the actual form and degree of their power vis-à-vis national governments. How have TNC responded to the signals of public authorities? How much have they invested and what have they invested in?

### *Foreign-led Reindustrialisation versus Deindustrialisation*

Above we pointed out that the divergence of regime performances in industrial transformation coincided with the variation in FDI inflows into complex industries. How did this variation come about, and what are the consequences? In the mainstream view, FDI is endogenous to the advance of market reforms. For this view, the meagre achievements of the Baltic states in attracting complex-industry FDI and the resulting deskilling of Baltic exports should present a puzzle. Why have these states proved so ineffective in attracting the main drivers of industrial upgrading if they have been so capable of creating many of its alleged conditions: radically reformed stable economies, low taxes, political stability, and national security? Why have complex-industry TNC consistently preferred Visegrád locations to the Baltic area? Our answer is that TNC location choices responded to the incentives stemming from a *dynamic interplay* between inherited and restructured industry profiles, inherited and newly-built market institutions, and special subsidy packages.

To account for TNC motivation we adapt Vernon's product-cycle theory (1971), and on that basis we argue that export-oriented, complex FDI had to flow first to those former socialist economies whose initial supply structures (that we proxy by the export structures of the late 1980s–early 1990s) had been relatively complex (i.e. intensive in technologically sophisticated physical capital and human skills). As a consequence, the Visegrád countries, which already specialised in the automobile, machinery or electronics industries during late socialism (Csaba 1984), could rightly expect larger inflows of industry-specific FDI than other (e.g. the Central Asian) states where this sector was virtually absent. In this respect, the Baltic states, which by the last decade of state socialism increasingly exchanged technology and skill-intensive goods with natural resources from other parts of the empire, had not been particularly disadvantaged. Given that on the basis of their supply structures all CEE countries initially seem to have had comparable attractions as new locations for transnational complex-export production, product-cycle theory alone cannot account for the diverging path taken by the Baltic and Visegrád states. How then did investors choose among them?

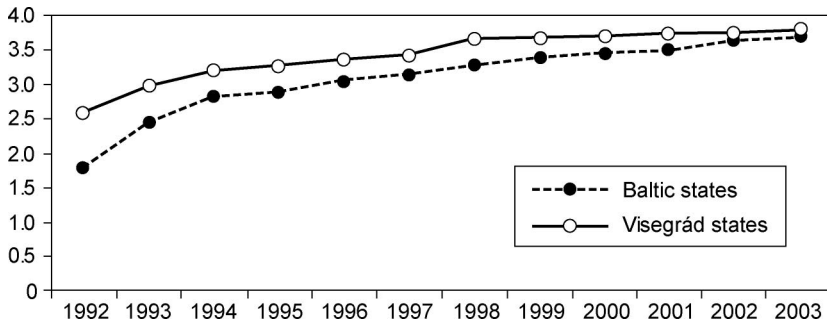
For an answer we have to consider that even similar supply structures might fail to raise investors' interest if institutional and policy barriers hamper access to the demanded local factors of production. It follows, then, that countries which, by the time investors were ready and able to cross the

former Cold War borders, advanced furthest in removing entry barriers and rebuilding their institutions and policy regimes were better able to attract FDI. Our evidence confirms that in the first half of the 1990s the Visegrád states outcompeted the Baltic states, which could start their quest for institutional convergence with the West only after a delay and from scratch (Figure 1). In the first phase of the transformation, then, in the context of rather similar supply structures, institutional advantages tilted the balance of investors' preferences in favour of the Visegrád countries. Complex FDI inflows had been endogenous to the initial levels of marketisation.

However, the interplay of structural and institutional factors seems to have fully reversed, and the endogeneity of complex FDI to marketisation levels failed to materialise after the mid-1990s. The Baltic states gradually worked off their institutional disadvantage, and by 2003 arrived at a high degree of institutional similarity with their regional rivals and the West. However, their institutional catching up does not seem to have been appreciated by transnational complex-industry investors. What seems to explain the Baltic states' inability to attract complex industry FDI after the mid-1990s is that their radical institutional convergence has been achieved at the expense of increasing divergence in supply structure terms (Figure 2). In the late 1990s, in the context of increasing institutional similarity, TNC continued to prefer the same Visegrád area locations mainly because of their enhanced structural similarity with the West, whereas the Baltic countries might have lost out due to the increasing divergence of their supply profile.

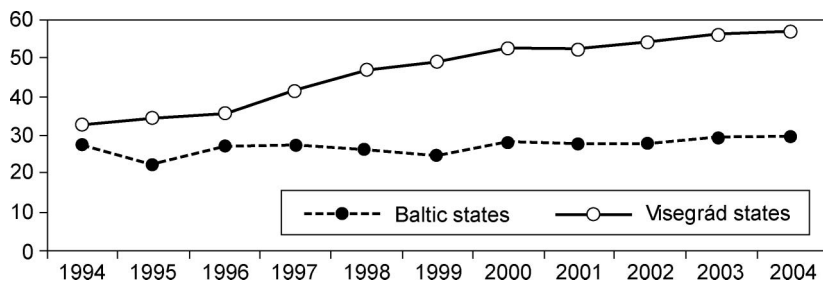
Initial investor preferences, motivated by a combination of structural and institutional factors, seem to have launched both virtuous and vicious circles of foreign-led capital accumulation. Their driving forces included the contrasting trends of industry upgrading versus deindustrialisation; the tendency for many more TNCs to 'follow the leaders', their rivals and buyers, to the initially preferred Visegrád locations; the concomitant

FIGURE 1  
AVERAGE TRANSITION INDEXES



Sources: authors' own calculation based on EBRD Transition Report various volumes.

FIGURE 2  
COMPLEX EXPORTS' SHARE IN TOTAL EXPORTS (%)



Sources: authors' own calculation based on United Nations COMTRADE database. Complex exports are SITC 5 (chemicals) and 7 (machinery and equipment).

clustering of the complex industries in the same area; and lastly the generous subsidy packages offered by the Visegrád states to TNCs.

Through FDI, the complex industries of the Visegrád states gained access to much needed tangible and intangible factors of production, upgraded their activities, and developed competitive strengths even in the more demanding Single Market. In contrast, deprived of the abovementioned means of upgrading and restructuring, these same industrial sectors could not stand the intense global competition in the Baltic countries. Thus the same sectors that propelled development in the Visegrád area all but lost their markets, factors of production, and policy influence in the Baltic states. Moreover, the radical course of liberalisation, rather than breaking the vicious circle, accelerated the atrophy and collapse of the complex industries. In a short time an entirely different sectoral profile emerged with traditional light and resource-based industries at its core.

TNC usually follow their rivals and buyers to new production locations, while the first investors try to fend off rival followers not least by enlarging their already existing facilities (Vernon 1971). This strategy, observed in all Visegrád countries, further contributed to the virtuous circles of accumulating complex-industry FDI. To be sure, the evolving TNC-led systems of production did not have much of a true national character. Rather, the clustering of complex industries brought about the tight cross-border integration of the Czech Republic, south-western Poland, the north-west of the Slovak Republic, and north-western Hungary that further enhanced their attraction. The Baltic states, due to the increasing divergence of their supply capacities, could neither establish linkages to the Visegrád cluster, nor attract adequate FDI to build their own complex manufacturing growth pole.

The competition within the Visegrád group that intensified in the first half of the 2000s made it even more difficult for outsiders to acquire new investments in these industries. More than the TNC themselves, which by that time could produce efficiently virtually anywhere within the cluster, these states, and especially ambitious latecomer the Slovak Republic, have

cared a great deal about whether a new car assembly or electronics transplant operated on their own, or their neighbour's, territory. The resulting 'bidding war' in incentives magnified the overall cost of complex FDI inflows and exacerbated the competitive disadvantages of countries outside the cluster, especially if they were structurally handicapped too.

Slovenia has been no less an outsider to this competition than the Baltic states. Even so, its complex industries could become more competitive in international markets. As mentioned above, this is mainly due to Slovenia's exceptional legacy: it could improve competitiveness essentially on the basis of its inherited domestic industries, and by much less transnationalisation than the Visegrád economies.

### *Social Consequences*

Industrial transformation is not the only area where the ambitions of national states might not suffice for certain regime properties to develop, because adequate TNC responses are indispensable for success. In a similar vein, social and labour inclusion is not purely a matter of political decisions either. Especially in small open economies, so characteristic of CEE, welfare and labour market policies depend on the consent of the business groups which mark the competitive edge of the economy, and on their willingness to enter, or not to use the exit option but to stay put.

How have TNC preferences and decisions played out in the course of the region's industrial transformation? Drawing on authors who trace various instances of labour-inclusive policies to business preferences (Frieden 1988; Shafer 1994; Iversen 1996), in an earlier study we proposed that TNC preferences and their impact have not been uniform, but varied over time and across leading industries (Bohle and Greskovits 2006). In other words, divergent paths of transnationalisation have posed different challenges both for labour and social welfare.

The collapse of the state socialist heavy industry core had the most profound impact during the recession of the early 1990s. Output and exports collapsed, and labour was crushed. Real wages dropped from two-thirds to half their level in 1989, firm-based social benefits disappeared, union density halved. Masses of workers became unemployed, were forced into early retirement, or sent back to the household. Fast re-employment at comparable terms had hardly been an option since foreign capital had not been in hurry to take over the giant steel mills, coal mines, and fertiliser combines. Yet Slovenia and the Visegrád states, front-runners in market reforms, did attract foreign involvement in their traditional light industries early on. Transnational businesses started to set up export-oriented subsidiaries and subcontracting operations. In combination, the collapse of the inherited heavy industry and the emerging transnational division of labour in the light industries produced an extremely hostile environment for labour. In the former sector, state managers sometimes tried but could do little to

protect workers from mass social dislocation. In the latter, union-free sweatshops of low-cost, low-skilled labour dominated the scene.

After the mid-1990s – earlier in Slovenia and the Visegrád countries than in the Baltic states – the decline of socialist heavy industries bottomed out and transnational capital took over in restructuring. Following the ‘leaders’ of the early 1990s, Western FDI began to pour into the capital- and skill-intensive industries of the Visegrád states (and in more modest amounts to Slovenia). Especially after 2000, we can observe signs of further upgrading: the relocation of more sophisticated production processes, as well as R&D facilities, marketing, logistics and other production-related services. Still, these processes that signal fair prospects for economic and social progress are unevenly distributed across CEE. First, the collapse of socialist core industries plagued the Baltic states longer than Slovenia and the Visegrád countries. Second, while no significant amount of capital- and skill-intensive manufacturing FDI has entered the Baltic economies, the accelerating eastward migration of transnational light industries from Western (and now even Visegrád) locations transformed them into hosts of many of the low-cost assembly sweatshops of the EU.

The diversity of CEE’s transnationalisation paths has had social consequences. We can detect its main impact in the superior performance of Slovenia and the Visegrád economies in terms of real wages and work conditions. Partly, this progress can be traced to their new industries’ reliance on high-skilled labour that is able to handle complex technological processes and equipment. Businesses are likely to be more willing to accommodate skilled workers’ demands, while skilled labour is in a better position to press for such an accord (Gourevitch 1986; Estevez-Abe *et al.* 2001; Mares 2003). The chances for a compromise are also improved by the relatively limited cross-border mobility of these industries that stems from the scarcity of high-skilled versus unskilled labour, the sizeable fixed costs of huge investments, as well as locally and regionally established supplier–buyer networks (and other agglomeration effects), which conspire against rapid relocation. However, the overall picture is not uniformly positive. To attract and keep complex-industry TNC loyal, generous incentives have to be provided which at the extreme may undercut welfare provisions. Thus, while firms in complex industries tend to be friendlier with their own employees, the incentives offered to them might force the rest of society, and especially its marginalised less vocal groups, to pay the costs of foreign-led industry upgrading.

In all the above respects the Baltic states’ situation differs. Their light industry TNC, rather than significantly investing in local facilities, usually subcontract production to a multitude of small or medium-sized domestic firms. Above all, it is keeping labour markets flexible, wages low, work conditions unregulated, and workers docile that these firms expect from their hosts, while they are less demanding in terms of protectionist state intervention. Cross-border hyper-mobility is their means to keep national authorities under pressure. In essence, then, the Baltic leading export

industries seem to make their own employees pay the costs of precarious transnational integration.

Finally, no matter how varied its paths have been, the recovery phase of industrial transformation has *not* led to the recovery of unions and negotiated industrial relations anywhere in the region (except in Slovenia, where labour power was never dismantled in the first place). Even the major skill-intensive investors seem to prefer individual case-by-case deals with their workers and public administrations to nationally or sectorally organised interest mediation.

### **Summary and Conclusions**

In our study we set out to map and explain different capitalist political economies that emerged from the transformation of CEE societies. We established the following regime variation. The neoliberal Baltic states excelled in market radicalism as well as macroeconomic stability, but lagged behind other states in industrial transformation and social inclusion. In the absence of significant protection by industrial policy or social welfare institutions, most social groups have been exposed to world market pressures. Fiscal and monetary institutions, small budgets, currency boards, and independent central banks acquired dominance in mediating the relationships between the international and the Baltic political economies.

In contrast, the embedded neoliberal and less market-radical Visegrád states achieved better results in building complex, competitive export industries. At the same time, they have been somewhat more socially inclusive too. It is precisely the established measures and institutions of industrial policy and social welfare that make their neoliberalism embedded and distinctive. This regime has mobilised substantial resources to ‘pamper in their infancy’, and later assist the expansion of, new transnational industries. In turn, welfare schemes helped large social groups to avoid, or at least slow down, their decline to underclass status. However, the institutions safeguarding macroeconomic stability have not become established in most Visegrád states so far.

Finally, only the least market-radical, neocorporatist Slovenia succeeded, in a balanced manner, in all the above areas simultaneously. Competitive industries and better social indicators did not come at the cost of macroeconomic instability. Dominant neocorporatist institutions, such as legally enforced negotiated management–labour relationships, and extended collective agreements have so far been able to deliver the compromises required for a balanced and inclusive agenda.

Our explanation of regime variation stressed the interplay of two groups of factors. On the one hand, we argued that initial political decisions mattered. The legacies of the past, and their perceptions by the reform elites as either threats to or assets for their countries’ future, had a deep impact on regime types. Legacies and initial choices were no less crucial for the degree

of democratic inclusion, and the different patterns of protest and patience on the paths towards the new regimes. On the other hand, we demonstrated the importance of transnational influences in mediating and consolidating the shape of industrial transformation and social inclusion. On these grounds we conclude that while initially politicians had considerable freedom of choice concerning their new regimes, later on their freedom has been constrained by the EU and TNC. Thus by the early 2000s we see the development of CEE societies as increasingly path-dependent.

This leads us to specify our own conceptual contribution. Clearly, we are not the first to discover and explore post-socialist diversity. Rather, in our study we build on earlier influential approaches. Among them, we drew on the core proposition of 'neoclassical sociology' that post-socialist 'capitalism can be most fruitfully perceived as a variety of possible destinations... a world of socioeconomic systems with a great diversity of class relations and institutional arrangements' (Eyal *et al.* 1998: 16; see also Stark and Bruszt 1998). Although these accounts rightly stress the salience of the varied inheritance of elite structures, institutions, and political decisions for the emergence of different types of capitalism, we found them wanting for neglecting international and transnational influences (Bohle 2000). Accordingly, we believe that our approach helps to think in a consistent manner about all important factors of post-socialist diversity, that is past legacies, political choices, and internationalisation, as well as their dynamic interaction over time and across a large number of cases.

Recent work in the neoclassical sociology tradition took the international dimension more seriously (Bruszt 2002; King 2002). King (2002: 28) defined two varieties of post-socialist capitalism: 'a patrimonial variety dependent on raw materials exports which produces "involution," and a liberal variety that is dependent on capital imports and manufactured exports, and that leads to some development'. These types are helpful to understand some of the contrasting features of post-Soviet and CEE capitalism. Yet, they sit uneasily with evidence on the considerable variation *within* CEE regarding growth, equity, and stability, and their sources. Compared with the internationalised version of neoclassical sociology, our contribution lies in unpacking the broad and general terms and separating varied patterns of transnationalisation, capital imports, and manufactured exports as factors of growth versus involution as well as social equity versus disparity. We also hope to have offered a more sophisticated picture of the politics of emerging diversity. For example, while King (2002: 8), following Eyal *et al.* (1998), argues that in CEE 'Monetarism and neoliberalism served as ideologies uniting the technocrats and dissidents intellectuals', we suggest a more complex interplay between neoliberalism and nationalism that highlights the importance of non-economic factors for the divergent CEE paths.

Attention to identity politics also characterises some of the most recent inquiries into the contrasts between Estonia and Slovenia (Buchen 2005; Feldmann 2006b). To contrast the extreme cases of these mini-states, these

authors adopt the Varieties of Capitalism (VoC) approach. We find their comparisons inspiring apart from one shortcoming that originates in the VoC framework. Authors in that group assume the prior existence, and hence the explanatory power of, established and consolidated *national* institutions, which can withstand global pressures towards uniformity (Hall and Soskice 2001). However, this assumption cannot hold in the same way in the post-socialist regimes, as most institutions coordinating their economic activities currently were not in place before their transformation and internationalisation. Rather, as we have argued, their emergence and consolidation were much more thoroughly shaped by the influence of transnational factors than in the case of Western liberal market and coordinated market economies. That is why in our future research, rather than directly importing the VoC framework, we prefer to elaborate on the details of our own approach to Eastern Europe's varieties of transnational capitalism.

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