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Autonomy and Capacity: A state-centred approach to Post-communist transition in central Europe

Zoltán Ádám

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University College London
Centre for the Study of Economic and Social Change in Europe
Senate House, Malet Street, London, WC1E 7HU
Tel: 44(020) 7863 8517
Fax :44(020) 7862 8641
Email: csesce@ssees.ucl.ac.uk

Autonomy and Capacity

A state-centred approach to post-communist transition in Central Europe

By Zoltán Ádám

Research Economist, Kopint-Datorg Rt., Budapest; and
Ph.D. student, Debrecen University, Faculty of Economics

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Abstract

The paper examines state characteristics and their policy implications in five Central European post-communist countries. It argues that policies on macroeconomic stabilisation, privatisation and FDI had been shaped by state-society relations, which, in turn, had been affected by policy outcomes. Curiously, though, whereas structural and institutional developments exhibited a great deal of path-dependency in some countries, in others significant policy shifts took place. The conceptual tools of state capacity and autonomy are used to describe both dynamics, as well as to explain the spectacular variation in the role of FDI across the region.

1. Introduction

The purpose of this paper is to examine state characteristics and their policy implications during post-communist transition in five Central European countries: the Czech Republic, Hungary, Poland, Slovakia and Slovenia. States are understood here as institutional actors playing a key role in economic development. How they fulfil this function, depends on their policies, which are significantly influenced by such state characteristics as their autonomy vis-à-vis societal actors and their internal capacities to implement policies. However, not only policies are affected by the degree of autonomy and the quality of capacities, but policies impact upon state characteristics too. Thereby, a degree of path dependence is entailed, usually resulting in polices supporting existing state capacities and privileged social groups. Nevertheless, at times of restructuring, path dependence becomes challenged by policy shifts that potentially rearrange state-society relations and may alter state capacities.

What we have witnessed in post-communist Central Europe in the past 15 years was an intense period of structural change in which state characteristics have changed to different degrees in different countries. Policies on stabilisation, privatisation and foreign direct investment (FDI) played a crucial role in this.

Nevertheless, not everything has changed. Some countries exhibited extraordinary path dependence while others conducted more policy shifts. First of all, the way and depth of initial macro stabilisation varied significantly because of dramatically different state-society relations and initial economic situations. Second, while some countries started off with one privatisation strategy an ended up with another, others insisted on their initial policy choice. Third, in relations to this, some countries became highly penetrated by FDI, while others resisted remarkably. The basic question of this paper is what accounts for all these variations that occurred within essentially identical external circumstances. In trying to address this, conceptual tools of state capacity and autonomy will be used throughout the analysis, enlightening the importance of state characteristics in conducting transformation policies. Utilising the merits of a state-centred approach, an understanding of FDI-lead economic restructuring will be provided.

2. State capacity and autonomy in institutional theory

There is no doubt about the economic impact of state policy, and development economics has been for a long time concerned with the role of the state in improving economic conditions (Stiglitz et al. 1989; Meyer and Stiglitz 2001). In addition, institutional economics argued that societal rules (i.e. "institutions") determine economic performance, and emphasised the role of the state in formalising and maintaining such rules as laws and regulations (North 1995). The neoweberian turn of the 1970s and '80s created a new institutionalist theory in political science and political economy too, that realised the internal dynamics of states and interpreted them as individual institutional actors. Theoretically, states were no longer considered as an arena of interest representation by societal actors but started to live their own life, pursuing their own interests, and acting in line with their own policy goals (Evans et al. eds. 1985; Katzenstein 1985; Stepan 1978). This paper belongs to this third tradition, and considers institutions to be actors and not to be rules. However, this is in perfect agreement with development economics, and the views of transactions cost economics are not diametrically opposed either. For in the latter's view, organisations (i.e. formal institutions in political science) play a key role in formulating institutions (i.e. rules) that determine transactions costs. Thus, state policies are of primary interest in all three approaches, and by examining policy formation and implementation, synergies can emerge (cf. Chang 1994; Chang and Evans 2000).

The notions of state capacity and autonomy, under scrutiny here, are principally elaborated in political science. Within the neoweberian school, Theda Skockpol (1985) defined state capacity as an ability "to implement official goals, especially over the actual or potential opposition of powerful social groups or in the face of recalcitrant socioeconomic circumstances." However, resistance to powerful opposition also relates to the concept of state autonomy, defined by Skockpol as ability to "formulate and pursue goals that are not simply reflective of the demands or interests of social groups, classes, or society."

D. Michael Shafer (1994, pp. 6-7) argued similarly when he claimed that "autonomy is the extent to which the state is not merely an arena for conflict but is distinct from nonstate actors." Nevertheless, "autonomy is not enough; states must be able to act. But whereas autonomy is always relative [to societal actors], it is useful to think state capacity as both absolute and relative. Absolute capacity is the extent to which the state has the authority and means to extract and deploy resources: a technocratic, meritocratic, and internally cohesive bureaucracy; and effective monitoring and regulatory capabilities. [However,] state capacity must also be seen in relation to the interests, resources, and capabilities of salient societal actors." Thus, actual capacity in relation to societal actors is called "relative capacity" at Shafer.

Development economics has been also aware of the fact that economic development can be hindered by lack of state autonomy. "State capture" by privileged societal groups may deteriorate the quality of economic policy making as a number of authors argued regarding post-communist transition in Central and Eastern Europe (Csaba 2004, Hellman and Kaufmann 2001, Hellman et al. 2000). Vested interests of 'oligarchs' and other social groups that have privileged access to power may have hindered transition in Russia as well as other post-communist countries.

In political economy scholarship, Mancur Olson (1982) has come up with a comprehensive theory of 'distributional coalitions' that are formed between state bureaucrats and influential societal actors. Such coalitions, based on common interests in maintaining economic status quo, may prevent from structural adjustment to altered circumstances unless a major political event, such as a revolutions or a war challenges the incumbents.

Developing countries are especially prone to such power sharing arrangements as state bureaucrats tend to be less endowed with administrative and financial resources, hence being less autonomous vis-à-vis societal actors. This phenomenon is well depicted by Joel Migdal's (1988) concept on "strong societies and weak states" that could be easily applied to Russia in the 1990s (Holmes 1997). In this context President Putin's ambition to strengthen the Kremlin's grip on the regions and the "oligarchs" can be understood as efforts to overcome the weakness of the Russian state.

However, one can argue *against* state autonomy as well. This line of argumentation, exemplified by Evans (1995), Stark and Bruszt (1998) and Bresser Pereira et al. (1993), emphasises the costs of exclusionary policies in terms of insufficient democratic control, narrow-minded policies and lost institutional knowledge. At Evans, overwhelming state autonomy can result in „predatory states" that pursue exclusives interests of state bureaucrats and their close associates, demonstrated by such third world dictatorships as Zaire (Evans 1995, pp. 45-47). At Bresser Pereira et al., exclusionary policies entail democratic deficits and hence reduced economic capabilities to conduct adjustment. Stark and Bruszt argue for alternative coordination mechanisms for both the state and the market, and identify networks as possessors of unique capabilities in transition. Economic policy making is necessarily embedded in the nexus of societal relationships, while overwhelming autonomy is associated with irrational shock therapies that ignore accumulated institutional knowledge.

In this framework, state autonomy, whether exercised by third world dictators or Washington consensus-minded technocrats, is anything but instrumental to achieving economic success. Overly autonomous states suffer from the lack of relevant information in policy making, hence their capacity to formulate development policies are limited. The solution is a peculiar type of 'embedded autonomy', typically enjoyed by states of such countries as Japan, Korea and Taiwan. Policy-making bodies are characterised by professional excellence and a high degree of internal cohesion, nevertheless strongly tied to business communities through informal networks. This allows for additional information and policy implementation capacities, essential for the creation of *developmental states* (Evans 1995, pp. 47-60). Interestingly, Evans extended his theory to European corporatism (namely to Austria), and argued that such institutions as the system of tripartite negotiations among employers, employees and the state can also enhance policy making capacity as they help situating policy in the relevant social context (Evans 1995, pp. 240-247).

However, it is important to realise, that both those who consider state autonomy to be a virtue and those who regard it as a danger argue for political accountability. In the first case, state autonomy prevents from privileged social groups' exclusive access to power that would limit democratic accountability because of a *weak* state. In the second one, state autonomy creates a dangerous possibility of a *strong* state infringes democratic norms.

Indeed, democracy seems to be crucial in achieving economic success in transition: EBRD's comprehensive Transition Report (1999) argued that the contestability of political power, i.e. a full fledged political democracy has been strongly correlated with the contestability of markets, i.e. a full fledged market economy. It is true, nevertheless, that successful economic policy making in transition has often relied on exclusionary policies (or 'shock therapies') such as the Balcerowicz plan in Poland or the Bokros package in Hungary (Greskovits 1998). Even more embarrassingly, dictatorships have achieved considerable economic progress in particular cases, such as Korea after WWII (Chang 1994) and Chile under Pinochet (Larroulet ed. 1993). However, having reached a developmental threshold, states tend to be democratised, and capitalist development has been historically associated with liberal democracy (Fukuyama 1992). Similarly, reform governments in post-communist Central Europe had always been democratically elected, even if they lost the subsequent elections.

To be sure, the role of the state in post-communist countries has a lot in common with states anywhere else. Diffusion of power and limitations on state capacity to regulate economic behaviour are attributes of globalisation (Strange 1996). However, contrary to widely held assumptions, global capitalism can not dispense the state as enforcement of universal rules (such as copyright protection), and provision of technical infrastructure (such as financial markets) require state institutions to be in place (Evans 1997). According to empirical evidence, foreign direct investment does not enter a particular country unless the state is able to regulate markets and enforce private contracts (Bevan et al. 2001). Moreover, EU accession also relies on state capacities to adopt European standards and implement the body of European law.

European standards, again, imply the two-fold challenge of maintaining democratic accountability and achieving technical capability at the same time. Success in transition required the state's liberation from the power of local economic elites, and FDI played a crucial role in this process. In consequence, state-society relations have been transformed, and the strength of local elites often diminished. Also, state capacities have become extended as a result of adopting European standards whose enforcement is supported by Brussels (Bartlett and Seleny 1998). However, as we are going to see, post-communist states showed a great variance in accumulating capacity and autonomy with dramatically different policy implications.

3. Capacity and autonomy of post-communist states

Historically, communist states possessed substantial capacities and autonomy during state socialism. After all, the system was based on highly centralised economic and political decision making. Planning authorities were considered the elite bodies of state administration, endowed with highly skilled and roughly speaking uniformly trained staff. Communist states enjoyed substantial autonomy vis-à-vis societal actors as private ownership and autonomous political initiatives were eliminated. East European socialism had been a state-centred modernisation effort, perpetuating a Rostowian take-off by shifting economic resources from agriculture to industry. Alike in East Asia, the state had played a highly instrumental – if extremely oppressive – role up-until about the mid-1960s.

However, as economic growth started declining due to the model's exhaustion, efficiency of state co-ordination deteriorated. 'Reform socialist states,' such as Hungary, Poland and Yugoslavia attempted enhancing the role of market co-ordination within the system, resulting in disintegration tendencies (Kornai 1992). In an attempt to improve standard of living and resist political pressure from dissatisfied societal groups, states introduced welfare systems and kept on subsidising falling industries beyond fiscal capacities.

As a result, Hungary, Poland and Yugoslavia had started transition with a considerable degree of foreign indebtedness, limiting their room of manoeuvring in economic policy-making. As this can be understood as a constraint on state capacity, fiscal consolidation should be considered as a means to enhance it. In addition, social institutions such as trade unions, employer representations and tripartite negotiations, by mediating between government policy and societal actors, as at Evans (1995), could also increase state capacity.

3.1. Policies of macroeconomic stabilisation

The point of departure in analysing state autonomy and capacity in early transition is policy makers' strategic choice on stabilisation policies. Whereas Poland introduced tough policy measures – often called 'shock therapy' – at the very beginning of transition, Hungary did not use radical macroeconomic stabilisation up until 1995. On the other hand, at microeconomic level, the Hungarian transition was the toughest in the region during the early 1990s. Czechoslovakia and Slovenia, similarly to Poland, introduced harsh macroeconomic policies, but remained softer in hitting particular companies and industries than Hungary.

A possible explanation is the different political economic features of Hungary from other countries of the region. Due to the government's extremely secured parliamentary position[1] and the lack of institutionalised interest representation, Hungarian policy makers were not forced to accommodate particular societal actors' interests. Hungary was the only country in the region in which the first democratic government enjoyed a four-year term parliamentary majority that was never effectively challenged, and a reasonably stable party structure emerged right after the first elections. Furthermore, Hungary has a unicameral legislature in which no particular regions, institutions or social groups have privileged representation. Trade unions and employer associations have been traditionally weak and marginalized, and civil society organisations, although large in nominal figures, have not been particularly strong either.

[1] Because of the so called 'constructive no confidence vote', adapted from the German parliamentary system, the government can only be dismissed if by the same vote a new prime minister is being elected. Moreover, the Hungarian election system is based on individual constituencies in which majority vote prevails, enhancing the position of the strongest party if there is one.

On the other hand, Czechoslovakia, Poland and Slovenia had rather fragile parliamentary majorities at the beginning of the 1990s with substantial changes in the party system and altering governments within the first parliamentary terms. Election systems were based on party lists, and broadly defined coalitions emerged, often characterised with internal conflicts. No confidence votes could prove decisive, as dismissing governments demonstrated in Poland, Slovakia and Slovenia. Furthermore, the dissolution of Czechoslovakia naturally transformed a whole set of state institutions.

Poland and Slovenia have had traditionally strong trade unions and relatively important bi- and tripartite institutions of social bargaining. The Czech Republic, Poland and Slovenia have all had bicameral legislatures with upper houses consisting of regional representatives, in the Slovenian case accompanied with employer and employee representatives.

Thus, whereas Hungarian economic policy making capacities were constrained by an overstretched budget and a heavy burden of foreign debt, Hungarian policy makers enjoyed a considerable degree of autonomy vis-à-vis domestic interest groups. The Czech Republic was probably characterised by a relatively high degree of both autonomy and capacity, as its macroeconomic situation was reasonably good and neither managerial elites nor employees had strong interest representation. In Slovakia, although it had sufficiently good macroeconomic indicators, state capacities were weakened by the vulnerability of new institutions, reinforced by clientelistic policies that constrained state autonomy vis-à-vis powerful business groups. In Poland, policy making capacities were enhanced by the IMF's external help that provided room for radical stabilisation measures in January 1990, but state autonomy vis-à-vis companies was constrained by strong employee representation within companies and key sectors. Slovenian economic policy making proved to be extremely capable at the beginning of the 1990s, when macroeconomic stabilisation was implemented and Slovenia emerged from the Yugoslavian economic chaos very successfully. However, microeconomic reforms were less straightforward, and business elites as well as employee representatives remained very powerful, continuing the tradition of Yugoslavian self-management of 'socially owned' enterprises.

In this theoretical framework, successful macroeconomic stabilisation policies can be attributed to sophisticated policy making capabilities, able to fine-tune economic factors at the macro-level. This is relatively easy within a certain grace period called 'window of opportunity' by Balcerowicz (1995) because the population is more likely to be enthusiastic about political changes at the beginning of transition.

Initial stabilisation policies in Poland and Czechoslovakia, for example, provided a competitive advantage for domestic producers by devaluating the zloty and the crone more than their real purchasing power would have implicated (Aslund 2002), even if this effect was later diminished by subsequent real appreciation. By doing so, Polish and Czechoslovakian policy makers were buying time for less efficient domestic producers at the cost of general standard of living. However, in a political economy characterised by relatively strong interest groups and limited scope of autonomous state action, that should be hardly surprising.

In Hungary instead, in the absence of strong interest representation, harsh microeconomic policies were implemented, by first hitting less privileged groups. Unemployment was rising most rapidly in backward industrial areas and remote villages, and the hardest-hit were those with low interest representation skills: the less educated, women and many times the Roma. Macroeconomic stabilisation, on the other hand, was effectively postponed up until 1995 in an attempt of incumbent governments to sustain popular support as long as possible. Most probably because of the liberal character of the previous communist regime, the window of opportunity effect was less at work in Hungary than elsewhere. At least the so-called taxi driver strike, evoked by rising petrol prices and resulting in spectacular civil disorder in October 1990, could persuade the government about the difficulties of implementing harsh macroeconomic policies.

As the strike was completely unlawful and spontaneous, and not initiated by any established organisation, the importance of institutionalised interest representation became obvious. In seeking this, the centre-right government of 1990-94 was indeed conducting tripartite negotiations with employer associations and trade unions, and established the self-governance of the pension and healthcare funds, controlled by the unions. Nevertheless, a genuine corporatist system did not emerge mainly as a result of weak social support to employer associations and trade unions. Interestingly, the institution of tripartite negotiations was weakened consciously by the social-liberal government of 1994-98, which eventually implemented harsh macroeconomic stabilisation in 1995 (Greskovits 1998). Thus, economic policy-making remained exclusive vis-à-vis societal interest representation, and this has continued so ever since in the Hungarian transition.

In contrast, Slovenian economic policy making has been accommodating towards interest representation by trade unions and employee associations since the early 1990s. The four large unions and the Chamber of Commerce have always played a crucial role in setting wages, which has been done through peak-level bargaining among government, employer and employee representatives. In this sense, Slovenia has been a similar case to the Austrian corporatist 'embedded autonomy.'

Such a degree of institutionalised interest representation is, indeed, a unique phenomenon in post-communist Central Europe. Although stabilisation policies in the Czech Republic, Poland and Slovakia accommodated much more particularistic societal interests than in Hungary, state-society relations in neither of these countries could be compared to Slovenian 'embedded autonomy.' However, macro stabilisation was not the policy field in which Slovenia has stood out the most in the region.

3.2. Microeconomic restructuring: policies on privatisation and FDI

Privatisation has been on agenda since the mid-1980s in developed market economies (Clarke and Pitelis 1993). In addition to western economic thinking, reduced budgetary resources also raised the issue of privatisation in post-communist countries. Budget deficits and indebtedness especially characterised Bulgaria, Hungary, Yugoslavia and Poland. Others, like Czechoslovakia and Slovenia, did not suffer from financial imbalances.

Although initial financial situations had certainly played an important role in choosing privatisation policies, they were by no means the only determinants of policy decisions. For example, while financial constraints did certainly play an important role in going for revenue maximisation in Hungary, Estonian policy makers, acting similarly, were pursuing national security considerations in the first place.

As a policy choice on privatisation, Hungary went for direct sale through competitive bidding, a method that favoured the most affluent bidders while foreign investors were allowed to participate (Mihályi 2000). This policy option was enabled by the weakness of local business elites and the strength of political institutions. In contrast, Slovenian policy makers, facing well established managerial groups and employee associations, but not constrained by external indebtedness and excessive budget deficits, opted for policies favouring employees and managers of 'socially' (i.e. publicly) owned companies. Czechoslovakia chose the middle-way when introduced a voucher system as a principal tool for giving away state owned companies: this method meant distribution of state-owned assets among the general population regardless of the individuals' financial capabilities and association to particular companies, but in real terms entailed little change in actual control over enterprises (Pavlinek 2002). This may reflect an intermediary position of Czechoslovakian state authorities, which inherited a stable macroeconomic situation but experienced internal political instability, resulting in a reasonably capable but not entirely autonomous state, somewhat similarly to the Slovenian case. However, Czechoslovakian policy makers faced relatively weak managerial elites and employee representation, just as in Hungary. Finally, as another in-between case, Poland employed both voucher and employee buy-out techniques.

In consequence of privatisation methods, the Czech Republic, Poland, Slovakia and Slovenia had all proved to be slower and more cautious in employing FDI to initiate structural economic changes than Hungary. Thus, while the first four countries transformed indigenous population and elite groups into private owners on a large scale, Hungary did so to a much smaller extent. Another important difference was that whereas privatisation policies pursued direct societal interests and hence resulted in limited efficiency gains in the first four countries, Hungarian exclusionary policies delivered extraordinary efficiency gains (EBRD 1999).

Multinational companies (MNCs) rapidly integrated the Hungarian economy into the EU. Export performance was spectacularly enhanced, not only in quantitative but also in qualitative terms (Soós 2000). Large-scale presence of FDI contributed to a swift economic restructuring that was hardly the case in most other countries in the early 1990s. The secure position of Hungarian policy makers allowed for effective regulatory measures, such as a harsh and actually implemented bankruptcy law, truly exceptional in the region (Kornai 2001). In effect, an insulated state could stand up against local economic elites that may have well preferred avoiding sweeping structural changes.

Subsequently, however, as the process of institutional learning took place and states became more autonomous vis-à-vis local elite groups, other countries followed suit and adopted direct sale methods in privatisation and allowed for a large scale FDI entry. This was a policy shift evoked by economic constraints as well as institutional changes.

At the macroeconomic level, growing current account deficits threatened the Czech Republic, Poland and Slovakia. At the enterprise level, domestic companies faced increasing external competition, resulting in losing ground in European markets even by the developed Slovenian manufacturing industry (Landesmann 2000). Also, as it has been argued above, state institutions were strengthened over time, and a relatively stable party system emerged, creating increasingly secure parliamentary majorities. This enabled governments to embark upon direct sale methods, preferring well-financed foreign strategic investors in key industries. The result was a proliferation of FDI across the regions, with Slovenia resisting it still the most.

However, direct sale methods have provided room not only for inviting FDI, but also for building clienteles. As it had been the case in the early 1990s in a number of transition countries (in Central Europe most prominently in Slovakia), governments supported privileged business groups through means of privatisation during advanced transition too. Using such measures, in fact, indicated a degree of embeddedness of the policy making process. Whereas in some countries, such as Russia, this was rather a result of state capture, in others, such as Hungary, increasing embeddedness could be understood as a rational policy shift.

Table 1. The political economy of privatisation in Central Europe

	Czech Republic, Poland, Slovakia	**Poland, Slovenia**	**Hungary**
Dominant method in early transition	**Citizen voucher**	**Employee voucher, MEBO**	**Direct sale**
Technique	Give-away redistribution of public property	Give-away redistribution of public property	State-controlled direct sale of public property
Preferred investors	Citizens	Managers, employees	Well-financed, often foreign investors (FDI)
Economic result	Quasi market/state co-ordination, limited efficiency-gain	Market co-ordination, limited efficiency-gain	Market co-ordination, strong efficiency-gain
Dominant method in advanced transition	**Direct sale**		
Technique	Direct sale to well-financed foreign OR well-positioned domestic economic actors		
Preferred investors	FDI or domestic investors		
Economic result	Market co-ordination, strong efficiency-gain OR quasi market/state co-ordination, limited efficiency gain		

4. Policy shifts on FDI-led restructuring

Whereas in the 1990s post-communist governments were competing with domestic businesses about ‘who privatises whom’ (Bruszt 2002), structural positions have altered by the end of the decade. Having gone through a process of institutional learning and securing their policy functions, governments of Central European countries found themselves in an increasingly international arena, in which competitive positions must have been secured vis-à-vis external political and economic forces rather than domestic big business. Therefore it seems to be a rational policy to strengthen domestic enterprises that formulate the economic ‘hinterland’ of the state.

To be sure, democratic governments virtually always have their own clienteles exactly because they are ‘embedded’ in a relevant social network. Hence, state autonomy in democracies is never unlimited, as Evans (1995) has already emphasised. In this context, clientele building can be interpreted as an attempt to enhance embeddedness that may, of course, result in less state autonomy than, for instance, Hungarian ‘under-institutionalisation’ would imply.

The Hungarian centre-right government of 1998-2002, that for historical reasons were socially less embedded than its left wing political counterparts, may well have realised that less autonomy could actually mean more capacity in such a case. Its mild anti-FDI turn, on one hand, meant that whereas MNCs and domestic companies both received state subsidies in a framework of investment promotion, the primary target group was domestic small and medium companies. On the other hand, the government also tried to strengthen privileged domestic big-business groups by providing exclusive access to highway building and other infrastructure projects. Thus, whereas FDI had dominated most part of the 1990s, a revival of domestic companies was attempted, for rather understandable reasons.

In effect, although this policy had prevailed until the centre-right lost the 2002 elections, it could not be considered a spectacular success. Promoted Hungarian companies did not become technologically advanced ‘national champions,’ and their efficiency had not really improved. Other domestically controlled companies, in turn, which were too big and too internationalised to (fully) belong to the government’s clientele even if partly state-owned, such as MOL, OTP and Richter, became outward oriented regional players in their respective industries. In fact, this seems to support the argument of Strange (1996) about the limits of state capacity in a WTO-governed global economy, and shows the difficulty of deviating from the dominant policy course of FDI-led restructuring.

However, even dominant global policies may be difficult to apply if local circumstances considerably differ. Hence, Slovenian economic policy makers to a significant degree failed to open up towards FDI after the 2000 elections. The centre-left government, enjoying a clear parliamentary majority and even a junior centre-right coalition partner, initiated the privatisation of the two largest state-owned banks, NLB and NKBM by inviting foreign strategic investors. Well, neither one succeeded according to original plans: NLB was partially privatised allowing only 34% for a strategic investor, while NKBM’s privatisation was cancelled under strong political pressure by local elites. Thus, the Slovenian state, possessing a high degree of policy making capacities materialised in remarkably good macroeconomic performance, high wages and enviable human development indices, still lacked the authority to privatise large banks to foreign investors. This suggests that although competitive positions of the state over domestic business elites for controlling the policy making process have strengthened, 'embedded autonomy' reinforced its limits. Such limits, of course, can be observed in all corporatist countries from Japan to Germany. This is the flipside of 'embedded autonomy,' or if one prefers, Olsonian distribution coalitions at work.

However, as it has been argued, the Czech Republic, Poland and Slovakia have successfully shifted from an 'inward looking' privatisation policy to an 'outward looking' one towards the end of the 1990s. Why could their governments succeed in this move? First of all, economic crises have ridden all three countries around the end of the decade, resulting in rising unemployment. FDI was perceived as a medication that improved international competitiveness and stimulated job creation. Inward looking privatisation policies of the successive Klaus governments were associated with insufficient economic performance after 1997 in the Czech Republic. Similarly, the various Meciar governments' clientele building efforts through privatisation were perceived with increasing scepticism in Slovakia. Popular wisdom was not necessarily anti-FDI in Poland either, and the relatively stable 1993-1997 left wing governments started large-scale privatisation to foreign strategic investors around 1995. State autonomy increased as political institutions evolved in all three countries, and institutionalised interest representation, contrary to the Slovenian case, could not prevent from policy shifts. By getting rid of the burden of state owned banks and some of the loss making companies, state capacity was also enhanced. However, limitations, again, remained: Politically most sensitive industries, such as coal mining in Poland and steel production in the Czech Republic could not be sold out, similarly to Slovenian big banking.

Country characteristics notwithstanding, dilemmas of an FDI-lead economic restructuring prevail. First, capability of states to tax and regulate MNCs may become questioned as MNCs tend to pressure policy makers just as local business elites do. Thus, autonomy of states vis-à-vis MNCs may become questioned at some point. Second, even if autonomy enhances, the insulation of the state from relevant economic actors constrains its capacities. Lack of social embeddedness of political actors can be associated with the lack of economic embeddedness of FDI, resulting in poor local sourcing and networking by MNCs (Farkas 2000; Dyker et al. 2002). This can prevent from development of domestic enterprises, and limit the growth of local value-added creation. For the very fact of insulation, enabled by the presence of FDI, however, the state can hardly promote linkages between MNCs and domestic companies.

5. Conclusions

This paper argued that state characteristics by and large determined policies of macroeconomic stabilisation, privatisation and FDI in Central European post-communist transition. Privatisation outcomes and the role of FDI, in turn, have effected economic development and hence exercised an important influence on state capacity and autonomy. However, policies varied significantly across the region: Whereas the Czech Republic, Hungary, Poland and Slovakia used inward investment instrumentally to enhance state autonomy vis-à-vis domestic economic elites, Slovenian policy makers could do so to a lesser degree.

This was a result of Slovenian ‘embedded autonomy’ that limited available policy options, somewhat similarly to that of a captive state, such as Russia. However, there is a great deal of difference between capturing an essentially authoritarian state and socially embedding a democratic one. Whereas in the case of ‘embedded autonomy’ even privileged societal actors are interested in successful transformation policies because otherwise political incumbents become replaced at elections, in authoritarian countries state capture often prevents economic restructuring. Surely, restructuring may not be an easy task in democracy either. Yet, democratic governments usually exhibit a significant degree of adaptive capacity (Bruszt 2002).

The phenomenon of FDI-led economic restructuring has been indeed associated with political democracy in post-communist countries, as inward foreign investment liberated states from rent-seeking domestic business elites (traditional distributional coalitions in Olson’s terms). In the absence of political democracy, FDI was either excluded or it did not promote restructuring, as the presence of oil MNCs in Central Asia contributed neither to democratisation nor to the modernisation of manufacturing.

However, FDI has come at a cost. Whereas in the short run FDI has significantly increased state autonomy and capacity in Central Europe, hence contributing to success in restructuring, long-run effects are somewhat more controversial. Although states have accumulated a pool of administrative knowledge and were strengthened by complying with EU standards, their capacity to regulate large businesses remained limited. There are two reasons for this: First, because of global competition for inward investments and diffusion of state power, traditional state capacity becomes universally challenged. Second, and more importantly in the Central European context, insulation from relevant economic actors reduces state capacity. In consequence, as a result of FDI-led economic restructuring, most Central European post-communist states still have a long way to go until reaching Evansian 'embedded autonomy.'

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