to GDP exceeding that of the Visegrád countries by the middle of the decade. In terms of its structure, however, as in the Baltic countries, the FDI went mainly into the financial sector and property development and less into the tradable sectors.

With regard to labour relations, welfare provision, the innovation system and education, Bulgaria's story is very similar to that of Romania. In Bulgaria, too, workers responded initially to the economic recession and the difficulties entailed by the market reforms with strikes. The ability of the trade unions to mobilise failed to result in tripartite consultation and a neo-corporatist system. There is good reason to assume that in Bulgaria, the weakness of the state was the key factor ensuring that the agreements on social partnership were not followed by actions (Bohle and Greskovits 2012). The EU's poorest member state clawed its way back to achieving 66 per cent of its 1989 GDP in 1998; therefore, it was able to maintain a very reduced level of welfare services and educational expenditures. In terms of innovation performance, Bulgaria is ranked 26th among the EU member states (EBRD 1999:73, European Commission 2012).

The growth of the 2000s was accompanied in both countries by (primarily external) macroeconomic imbalances, which, even before the 2008 crisis, foretold stalling growth.

4.7 A Unique Feature of the Central and Eastern European Model: Modernisation Based on FDI

Having reviewed the transitions of the individual countries, I now summarise the conclusions that can be drawn on the basis of the capitalist transformation because, when making the comparisons, I was confronted with results that are inconsistent with generally held beliefs. Additionally, this summary allows me to verify the findings regarding the CEE model made in connection with the cluster analysis. I separately scrutinise a defining features of this process, namely, the fact that the modernisation process was founded on FDI.

4.7.1 Lessons of the Transition

The current crisis in the euro area has given broad scope for Eurosceptic thinking. Taking a longer historical view, it must be emphasised that in the post-socialist countries, the opportunity for EU membership and the preparations for this membership played an exceptionally important anchoring role in the course of building the market economies. The significance of these factors was enormous from two perspectives. On the one hand—as Csaba (2009a) analyses in detail—neither the economists of the post-socialist countries nor the advisors of the international organisations were equipped to carry out the transition from socialism to capitalism. Apart from a general framework outlining a combination of stabilisation, liberalisation, institution building, and privatisation, the specific recipe adapted to the region's characteristics was not available. In the absence of the appropriate theoretical background, after the initial steps of macroeconomic stabilisation, the adoption of community law provided a point of reference for building up the institutional system of the market economy. On the other hand, the efforts to join the EU also helped the transition to be carried through in countries where the internal power structure might have otherwise made it highly likely to become stuck in "patrimonial" (King 2007) or, to use another term, "uncoordinated" (Lane 2007) capitalism. Without EU membership, through their historical traditions and under the influence of post-communist forces, Bulgaria and Romania would have most likely drifted onto a path similar to that of Ukraine or other CIS countries. The IMF and international experts also influenced the transition, but countries turned to the IMF only as a last resort. Bulgaria's example is a good illustration of this limited scope of influence. The IMF attempted to reach agreement for years in vain, which yielded a result only when the internal political relationships changed in response to the protracted crisis. In places where the IMF was able to act more quickly and more effectively, such as Poland or Estonia, this process was made possible by the willingness of the government and society to reform.

In the literature, the steps necessary for the transition from a state socialist economy to a capitalist market economy are commonly referred to as the "SLIP" agenda, an acronym for Stabilisation Liberalisation,

Institution building, and Privatisation. A study of the individual countries has confirmed this to be a sound interpretive framework. The literature does not, however, support the commonly held view that what took place in the region was adherence to a consistent neo-liberal recipe suggested by international organisations. Csaba (2009a) points out that the contrasting of gradualism and shock therapy in the transition literature draws attention away from the more important issues. This assessment is emphasised by a study of the transformation of the individual countries. The general frameworks of the transition were determined by theoretical insight; however, the choice of specific solutions can be much more effectively explained by the historical legacy, that is, the political and economic circumstances, than by the impact of theory.

The transformation as a whole cannot be perceived as a comprehensive course of shock therapy; the privatisation took place at a different time than did stabilisation and liberalisation, even in the Baltic countries that chose the most radical transformation. Institution building in the economic—or, more precisely, the institutional economic—sense is by no means the same as formal organisational restructuring. The permanent alteration of the rules of play and the solidification of the new institutions are clearly possible only as outcomes of a longer historical process. In terms of the speed of stabilisation, the extent of the imbalances left genuine opportunities to choose in only a handful of cases. It can be said of Czechoslovakia that, in spite of the country's stable economic situation, Klaus announced a radical program of reforms that was—as we have seen—unacceptable for the Slovaks. In Hungary's case, one can talk about genuine gradualism only in the sense that the reform socialist measures involved the introduction of certain market institutions. After the change in the political system, the process of liberalisation and transformation of the ownership structure took place rapidly in comparison to the region's other countries. Romania and Bulgaria did not transform gradually, either, but instead postponed the reforms before taking the same steps that had been implemented immediately by the Baltic countries. We can talk about a deliberate gradual transformation only in the case of Slovenia, which was in a position to do so by virtue of its special characteristics, although it, too, has now reached the limit of this capacity.

Every country except Hungary experimented with the creation of national capitalism. In Hungary, this phase was omitted due to the country's high public debt, and even the strongly nationally oriented Antall government began to sell off corporations to foreign investors. This result indicates that the key role of FDI stemmed not from any commitment to a neoliberal doctrine, but rather from a lack of capital and management knowledge. In the Baltic countries, the governments' adherence to neoliberal economic policy was something of a means to an end; they saw in it a guarantee of emancipation from the former Soviet empire. As described above, this commitment was not the same for each country and was also proportionate to how threatened the countries felt by the Russian minority. A neoliberal conviction without any external compulsion was found where the Klaus government was concerned, but the launch of voucher-based privatisation showed that the government did not want to give preference to foreign capital. However, every country except Slovenia sooner or later made an effort to attract FDI. In Slovenia, however, non-foreign-owned property means state property, the well-known drawbacks of which had become serious and inevitable by the time of the 2008 crisis.

The importance of the historic legacy is also underlined by the development of labour relations. Nowhere—with the exception of Slovenia—did the workers' movements, temporarily strengthened by the change of political system, give rise to neo-corporatist employer and employee relationships similar to those of Western Europe. Thus, the region returned to the historic path that was characterised by weak representation of workers' interests, which is modified more or less as a formality by the requirements of EU laws.

4.7.2 Growth Opportunities and Limits in the Central and Eastern European Model

The literature fully agrees that a defining feature of the CEE transformation was modernisation based on FDI. In a comparison of the EU-27 member states, the unique character of the post-socialist member states lies not in the high volume of FDI relative to GDP, but in the asymmetry

of the sizes of the inward and outward FDI stocks (Table A.9). Among the OMS, the ratio of inward to outward FDI stocks does not exceed two, even in the countries with the lowest per capita GDP (Greece, Portugal); among the post-socialist countries, only Slovenia has a ratio below two, accompanied by the lowest GDP-proportionate rates, while for the others, these rates are between 2.82 and 61.53 (Romania's and Bulgaria's are above 60).

As seen above, King (2007) places emphasis on dependency when talking about the Visegrád states as liberal dependent countries. Nölke and Vliegenhart (2009) simply view dependence on FDI as an element that defines every material aspect of their model elaborated for the Visegrád countries. Bohle and Greskovits (2012) paint a more nuanced picture, pointing to the significance of the distribution of FDI between the sectors; that is, whether it went into tradable sectors because only in this case can it support sustainable economic growth.

The Commission produced an assessment on the fifth anniversary of the EU, in which it sees the influx of FDI as a source of successful integration of the NMS (European Commission 2009b). In the midst of the crisis, the World Bank's experts published a book on how the European model could be restored to its former glory, and in this, the successful FDI-based model of the CEE countries is compared with the unsuccessful model of the Mediterranean countries based on portfolio and other capital flows (Gill and Raiser 2012).

In order to assess the growth prospects of the CEE countries, we need to examine in more detail whether, based on experience to date, the region's long-term convergence can be ensured by FDI-based economic development. According to economic theory, FDI supports growth in the receiving country's productivity via two channels: directly through investments on the one hand and indirectly through the spill over effect on the other. The latter is especially important because this is how FDI can be expected to promote the modernisation of the domestic economy. A great many empirical studies have been made of these impacts on the CEE countries. From two wide-ranging literature reviews, it can be inferred that in the vertical backward linkages, the impact of FDI was clearly productivity boosting, while in the horizontal linkages, the majority of the studies could demonstrate only a weak relationship (Gorodnichenko et al. 2007;

Hanousek et al. 2010). A study by the ECB also listed extensively the often-contradictory empirical analyses found in the literature. Their own measurement found a positive linkage between FDI influx and productivity growth; however, the authores note that this is not automatic, but depends on the absorption capacity of the receiving country (Bijsterbosch and Kolasa 2009).

The aforementioned EU research (European Commission 2009b) and that of the World Bank both take into account the results of econometric studies on the role of FDI. However, they go beyond these and evaluate the development of the CEE countries along the lines of a very similar logic. According to both analyses, the chief strength of this model is that, in addition to facilitating economic growth, it facilitated the emergence of a capital-intensive export structure conforming to high technological standards. The openness of trade, the influx of FDI and the institutional development due to the EU accession were the main drivers of growth. The Commission's report highlights that, "during the period 2000–2008 accession the NMS an extra growth boost ... Model simulations suggest … the NMS enjoy a 50–100 basis point advantage relative to other emerging economies with comparable fundamentals" (European Commission 2009b: 17). The Commission's report also examines the processes from the perspective of the OMS. On the one hand, few jobs were lost to the relocation of production because some 70 per cent of the FDI went into market acquisition and services. On the other hand, in many sectors, it was possible to maintain competitiveness only by moving production facilities, while retaining the part of production that required specialist know-how, technological development, and ownership. The report does not, however, mention what kind of limitation these features of the FDI movement could represent in the longer term from the perspective of the convergence of the CEE countries.

Gill and Raiser (2012) emphasise that Europe is the only region in the world in which capital flows in the "right" direction; that is, into the poorer countries with a higher growth rate. They attribute the success of the convergence to the fact that the companies of the Nordic and North-Western countries restructured their value chain after the fall of communism. These companies relocated their assembly operations to the NMS, and the low wages there strengthened their competitiveness. This was also

beneficial for the NMS because it allowed them to integrate the global economy with increased productivity. They regard the EU as a three-speed union, with the leading Nordic and North-Western countries, the eastern followers, and the laggard southern countries.

None of the analyses asks the question of whether this model makes it possible to achieve, in the longer term, the ultimate goal of the CEE countries, namely, to converge with the living standards of the Western European countries. These studies outline a division of labour, in terms of production, between the North-Western countries and the CEE countries. Although this does not preclude the possibility of subsidiaries in the latter countries climbing higher up the value chain, there is no reason to assume that the parent companies will surrender their key positions in innovation, technology development, and strategic decision-making. The development of domestic companies—as the empirical studies quoted above have shown—is promoted considerably only among the suppliers by the technological transfer that comes with FDI; the horizontal impact is minimal. The third opportunity could be the accumulation of capital based on domestic savings, but in CEE, the high level of FDI influx was accompanied by a low level of savings, unlike in the emerging Asian countries.

As shown earlier in relation to Ireland, how difficult it is in an emerging country, even with several decades of deliberate economic policy, to narrow the productivity gaps between domestic and foreign companies. Empirical surveys show that even in the developed countries, there is a general tendency for the economic performance of multinational corporations to be better than that of domestic companies. Possible reasons for this include the fact that multinational companies are present in the sectors with a higher R&D content than the domestic companies; however, the state incentives for FDI could also put them at an advantage. From this, Bellak (2004) draws the conclusion that the differences in performance between the companies are determined not by their foreign or domestic nature, but rather by whether they are multinational or bound to a national economy. Therefore, economic policy should concentrate not on ownership, but on eliminating the performance gap. This distinction is appropriate in the developed countries. However, in the case of emerging countries that are weak in capital, the two approaches over-

lap considerably. The comparison of Ireland and Sweden by Andreosso-O'Callaghan and Lenihan (2011) showed that, in contrast to Ireland, Sweden's foreign companies are more evenly distributed across the industrial and services sectors, while the export-oriented and high-tech sectors are dominated by domestic companies. There are no data for a wider-ranging international comparison, but a good approach to the problem is to compare the productivity of the large corporate and SME sectors, for which EU data sources are available. The 2007 data are still unaffected by the impact of the crisis (Fig. 4.1).

Figure 4.1 clearly shows that—with the exception of Poland—the gap between the large corporate and SME sectors is the greatest in the countries that are struggling with the greatest difficulties in the present crisis. Among the post-socialist countries where FDI was on a large scale and flowed into the manufacturing industry and where the contribution of the large corporate sector to GDP matches or exceeds the EU average, it was possible in Slovakia only to reduce the productivity gap between the SME sector and the large corporations to the level of the North-Western member states. The reason why a far weaker performance is shown in Slovakia at the level of the medium-sized corporations cannot be deduced from the statistical data. Estonia and Latvia lack an FDI-based large corporate sector similar to that of the Visegrád states, which is also related to the small size of the former two countries.

Overall, the development model of the CEE countries undoubtedly led to successes. If, from the period after the transformational recession, we treat 1995 as the baseline (this, importantly, being the first available data in the Eurostat database) and compare this with the year before the crisis, then in terms both of GDP and of final consumption, which better expresses the prosperity of the population, with the exception of the two richest states, the Czech Republic and Slovenia, a growth of 10–30 percentage points could be observed. A comparison with the 1989 baseline could also be made, but due both to the quality of the statistical data from that time and to the quality of the commodities making up GDP back then, this comparison is suitable only as a very approximate guide (Table 4.2).

However, it is also clear from the foregoing that the features of the current CEE model do not support the thinking that prevails in the EU doc-

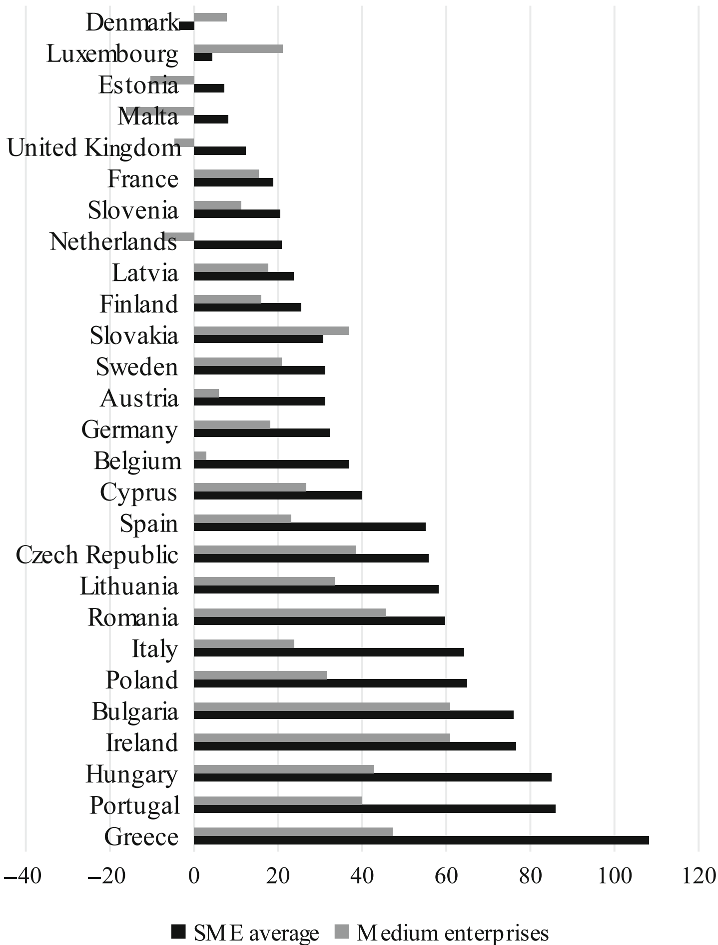

Fig. 4.1 Difference in labour productivity between large and medium-sized enterprises and between large companies and the SME sector, relative to the average for the whole economy, as percentage points, in 2007. *Source*: Author's calculation based on Wymenga et al. (2011). *Note*: Labour productivity is measured in terms of gross added value per employed person

uments (for example, the Commission report discussed above), namely, that the new, post-socialist member states are on a growth path that only from the OMS differs in quantitative terms and that convergence is only a matter of time. We can realistically define the current position

Table 4.2 Convergence of the post-socialist countries in terms of per-capita GDP and per-capita actual individual final consumption, at PPP, compared to the EU-27 average and to the GDP of 1989

	Estonia	Latvia	Lithuania	Poland	Czech Republic	Slovakia	Hungary	Slovenia	Romania	Bulgaria
Per-capita GDP, EU-27 = 100										
1995	36	31	35	43	77	47	51	74	33	32
2007	70	56	59	54	83	68	62	88	42	40
Per-capita final consumption, EU-27 = 100										
1995	36	34	38	44	68	38	49	75	35	35
2007	64	56	63	55	69	63	59	80	45	44
Per-capita GDP, 1989 = 100										
2007	150	124	116	169	139	154	135	151	120	107

Source: AMECO, Eurostat, EBRD (2008: 13)

Note: Actual individual final consumption is equal to expenditures on the consumption of goods and services by households and non-profit institutions serving households and in-kind social transfers

and future growth of the NMS by applying Porter's (1998) competitive advantage theory presented in Part I. To use Porter's terminology, the CEE economies are in the factor-driven stage because we have to classify them on the basis of the home-based economy.[16]

On the basis of Porter's (1998) theory, for the transition to long-term convergence and the innovation-driven stage—which was the goal of the EU's Lisbon Strategy and, later, the Europe 2020 strategy—FDI, the presence of foreign multinational corporations is necessary, but not in itself sufficient. Multinational corporations position their activities, which are present in the various phases of the value chain, in the various countries in accordance with their global strategy. In other words, the domestic base, as described above, remains in the home country in which the company has its seat. An emerging economy that bases its strategy only on multinational corporations could be destined to remain a factor-driven economy. In certain phases of development, the focus of economic policy must shift towards indigenous corporations.

In other words, the economic policy framework that the EU tends to designate (for example, in the study quoted several times above, ensuring macroeconomic stability, a sustainable balance of payments, effective use of subsidies from EU funds, and so on) is necessary, but not in itself sufficient to ensure that the NMS progress in the direction of convergence in the long term. The present institutional frameworks are adequate only for a growth path that perpetuates asymmetric mutual dependency between the OMS and NMS. The most important promise of the change in the political system was that the CEE countries, which were left out of the mainstream of development after the WWII, could converge with the more fortunate western countries within a historically foreseeable time frame.

The task of economics and political economy is to answer the question of what path can be taken by the NMS towards an innovation-driven, home-based economy. Among the countries that converged only very late, after WWII, only Finland shows convincing evidence that it has succeeded in entering this stage. Finland, however, had a means of travelling the path from the factor-driven economy to the innovation-driven economy. The global economic environment of the time made it possible, during the investment-driven stage, for the state—partly through

its ownership of large corporations—to play a key role in the modernisation process, and the source of capital accumulation was chiefly national capital. Even still, we are only talking about economic factors, and we have not gone into detail regarding the differences in terms of social capital relative to the CEE countries.[17]

If one aims to maintain convergence as a defining element of the system of economic policy targets of the post-socialist member states, a way to supplement the FDI-based model in the current stage of global economic and EU integration with a set of tools that facilitate the development of a innovation-driven, home-based economy in the original Porterian sense must be found. Additionally, all this should be achieved by building on genuinely extant social institutions, norms and attitudes and genuinely extant social capital.

If the 2008 crisis had not occurred, then due to the low income levels of the post-socialist countries, these questions might have remained theoretical for a long time, and the present model could have assured growth potential for a long time to come. The Czech Republic and Slovenia might have been the experimental countries that either became stuck at the current level[18] or were capable of joining the core countries. The crisis, however, is transforming the entire landscape of the global economy, and the development opportunities available to the CEE member states need to be reassessed in this light, as does the question of whether, in the wake of the crisis, the individual countries in the region have embarked on differing paths of development or whether they can still be interpreted in the framework of a single model.

Notes

1. The number of clusters, based on Akaike's information criterion and its relative change, is almost always two.
2. The single cluster of new member states would have broken up only in the seven-cluster version, without any definitive economic explanation.
3. The Swedish reforms are discussed in detail by Freeman et al. (2010), the Danish reforms by J. G. Andersen (2011).
4. The authors' subtitle—Can the Bumblebee Keep Flying?—indicates that we are dealing here with something of a curiosity compared to the eco-

nomic mainstream. The analogy was borrowed from the Swedish prime minister. In theory, bumblebees should not be able to fly, given their large bodies and tiny wings. The IMF's meticulous authors restore the scientific world order at the end of their work, referring to a study in which physicists explain how such flight is indeed possible.

5. Hereinafter, the Eurostat on-line database (http://epp.eurostat.ec.europa.eu/portal/page/portal/statistics/themes) is referred to as "Eurostat".
6. When analysing social protection, it has been indicated that the process of liberalisation was not complete even at this time; due to political resistance, the Thatcher government stepped back from privatising the National Health Service (Pierson 1996).
7. Kirby (2010) provides a wide-ranging survey of the literature on Ireland's economic development.
8. A 30 per cent threshold was determined necessary for initiating a mandatory takeover offer (Houwing and Vandaele 2011: 130).
9. It is an interesting comparison that the community support provided to Spain—not including the agricultural fund—between 1986 and 2006 accounted for three times as much as the amount of the Marshall Plan (Royo 2008: 48).
10. http://estonia.eu/about-estonia/society/citizenship.html, date accessed 23 February 2015
11. For a related analysis of the Estonian Research and Development Council, see Tiitset al. (2003).
12. http://www.bbc.com/news/world-europe-17083397 date accessed 25 February 2012.
13. There are significant differences in GDP data among the sources. The data in this study are based on the Report of EBRD from 1999, on the one hand, because this organisation specialises in the research of this region and, on the other hand, by that time, corrections had been made. It is especially important to note because according to Mygind (1997: 58–59), on the basis of earlier EBRD data, the decline was more than ten percentage points greater in case of Estonia and Lithuania. These years are not included in the online database of Eurostat.
14. The public debt of all of Yugoslavia was 15.99 billion USD at the end of 1991, and the part controlled by the federation (one-third) was distributed in the agreement on succession issues. The successor states began negotiations with the international organisations and the "Paris Club" creditors. Negotiations had been conducted since 1988 with the "London Club" (which included the private creditors) about debt restructuring processes,

and as a result, by mid-1993, the debt of 7.3 billion USD shrank to 4.3 billion USD. This result was greatly facilitated by the fact that the Yugoslavian government bonds were purchased for 20 per cent of their book value on the secondary market; thus, basically, the states themselves acquired their own debt (Stanič 2001: 758–761).

15. Please note that for those Romanians who belong to the Romanian Orthodox Church, the day of the execution was an ordinary day, not Christmas day.
16. The competitiveness report of the World Economic Forum places these countries higher in the classification—with the exception of Bulgaria—and these countries are in the innovation-driven stage or are on their way there, that is, in a transition phase (Schwab 2009). However, in the report, the aspects of the assessment broke away entirely from the original theory of Porter (1998); the basis of comparison was per capita GDP compared at market rate and the exports of mineral products as a share of overall exports. In this study, in assessing the prospect of the CEE model, Porter's aspects are more relevant; therefore, these aspects will be reviewed.
17. The survey of Eurobarometer in 2004 reveals the differences in social capital among the member states rather well (Eurobarometer2005).
18. The Czech Republic has not been able catch up as far as final consumption is concerned since 1995 (Table 4.2); the structural problems that were hiding behind Slovenia's spectacular economic performance would have spoiled the achieved consumption level anyhow, even without the crisis.

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