Making Markets and Eastern Enlargement: Diverging Convergence?

LASZLO BRUSZT

MARKET MAKING AND EUROPEANISATION

The 1990s was the decade of market making in both parts of Europe. This was the decade of the radical extension of the internal market and the creation of the conditions for the European Monetary Union in the Western part of Europe. This was also the decade in which the former communist countries undertook to transform their economies, to create functioning market economies, and, as of the second half of the decade, to build up the conditions for entry into the EU internal market. Market making in the former communist countries was influenced in several ways by the other part of Europe. In undertaking to transform their economies, the political elite in these countries used the ideology of 'Europeanisation' extensively, and the promise of potential EU accession played a considerable role in shaping political cleavages and the political agenda within these countries. As of the early 1990s, the EU also played a considerable role in setting the criteria for Europeanisation in the economic transformation for these countries, and actively participated in building up capacities to meet these criteria.

This study discusses the broad question of the extent and content of 'Europeanisation' of Central and Eastern European (CEE) countries at the level of market making. It argues that, for the most successful CEE countries, Europeanisation at the level of market making meant the emergence and the strengthening of a state with strong capacities to preserve and regulate markets, while having at the same time increased administrative and transformed planning capabilities. By the end of the 1990s, those CEE countries that had such states had come close to meeting the EU's demanding convergence criteria. Countries that did not have such states diverged both from the successful CEE countries and the EU. However, even the most successful CEE countries 'converged' on a moving target. While undertaking to meet the Copenhagen criteria of *national-level* market making they were 'converging' on EU member countries that themselves were busy diverging from these criteria in order to meet the Maastricht criteria of *supranational* market making. The content of these criteria diverged, and so did the consequences of meeting them.

The Copenhagen criteria of national-level market making that were the official compass for the CEE countries coupled neo-liberal policy prescriptions aiming at the rapid exposure of these countries to supranational markets with considerable demands on establishing domestic market order by way of building the institutional capabilities of national states. The Maastricht criteria of transnational market making, on the other hand, coupled domestic level policy demands with the transfer of basic domestic state capacities to the supranational level. The most successful CEE countries met the criteria of Europeanisation at the level of market making with relatively strong regulative states that were busy (re)creating, transforming and further strengthening their planning capacities. Within the EU, at the same time, national states were losing a large part of their capabilities to manipulate economic processes. Substantial parts of the economic powers of the national states were transferred to the supranational level and the placing of the domestic governments within a Europe-wide competitive regime further decreased their scope of action.

On the other hand, and largely as an unintended side-effect of supranational market making, organisations of non-state actors and their co-operative institutions became considerably stronger in several of the EU member countries. This development led in several EU countries to the partial mitigation of the social consequences of supranational market making being undertaken in the absence of supranational welfare state making. During the 1990s, however, non-state actors and various co-operative institutions in the CEE countries remained weak or were even further weakened. As a result, those CEE countries that are achieving most progress in Europeanisation at the level of market making diverge considerably from the newly emerging EU 'model' of capitalism itself, consisting as it does of different sub-types of 'embedding' markets. This emerging EU model of capitalism mixes elements of supranationally regulated markets with weakened national states and, in most of the member countries, relatively stronger non-state actors with co-operative institutions that seek to maintain competitiveness and to alleviate the social consequences of increased competition. While several of the CEE countries have well functioning market economies, most of the institutions that could make markets more inclusive, and/or support the process of catch-up growth of these economies, are weak or absent.

The emerging capitalism in CEE countries looks like an institutional desert, at least in comparison to the form(s) of capitalism evolving within the European Union. Institutions that would improve the market power of the different categories of economic actors and allow for the emergence of 'win–win' forms of co-operation among them are lacking. All in all, the good news from Central Europe is that the countries most developed in market making have relatively strong states. The bad news is that in most of these countries only the state is strong, while all other major economic actors, such as domestic business, labour or the local and regional self-governments, are weak.

The configuration of strong states and weak social and economic actors might have afforded the leading CEE countries a relatively calm arrival at the gates of the EU. Yet this configuration might also become the biggest liability for these same countries during the next stage of Europeanisation, that is, once they are within the EU and approaching the semi-periphery of Europe. The major argument of this study is therefore that while progress in state making was the *sine qua non* of Europeanisation at the level of market making, the constellation of forces noted above might become the major obstacle facing these countries in their efforts to cope with the social and economic problems of participation in the next stage of supranational market making.

The next section gives a sketchy general overview of the processes of convergence and divergence among the CEE countries, as well as between these countries and the existing EU member states at the level of market making. The following section then discusses the specifics of national-level market making in the CEE countries, focusing on the factors that explain divergence in Europeanisation at this level. The final part discusses the 'diverging convergence' between the CEE and EU member countries at the level of the organisation of economic actors and their co-operative institutions.

CONVERGENCE AND DIVERGENCE

In assessing developments during the last decade at the level of market making from the viewpoint of the highly demanding EU performance criteria, we can see considerable *convergence* between the two parts of Europe. According to the regular reports on the progress towards accession, the five leading reform countries of the region basically meet the so-called

Copenhagen criteria, that is, they have a 'functioning market economy with the capacity to cope with the competitive pressure and market forces within the Union'.[2] According to the same reports, several other countries are also on their way to meeting these criteria in the medium term. The degree of economic integration that these countries have achieved with the Union even prior to accession, as measured by the volume and range of products traded with EU member states (the evidence used by the EU of the ability to take on the obligations of membership) is also impressive. The CEE countries have doubled their exports since the beginning of the 1990s, and by the end of the decade almost 80 per cent of these exports went to the Western countries. In terms of the structure of the regulations taken over from the EU, and in terms of the structure of their trade, finances, organisation and ownership, the leading reform countries have already integrated into the EU economy even before the actual accession.[3]

Behind these indicators of convergence there are several processes of considerable *divergence*, which, although not challenging the processes of convergence noted above, might still impose important constraints on the longer term European integration of the economies in the region. The first of these is the serious divergence in economic developments within the region itself. Following nearly a decade of experimentation with economic reforms, we find signs of the consolidation of the market order and competition only in the leading reformist countries in the region. In many of the post-communist countries that have rapidly undertaken the liberalisation of prices and trade and the privatisation of property, we find anything but signs of the emergence of a functioning market order. The most important difference between the two groups of countries is perhaps that while the latter have states with the capacity to uphold economic freedoms, to maintain the rule of law, to resist state capture and to regulate relations among economic actors, the former do not have such states. The constitution of a market making state in several of these countries was blocked by the dominance of a nationalistic political agenda and/or the presence of strong economic groups that captured the state.[4] The creation of states with the capacity to constitute and preserve the market order is therefore a task that still lies ahead for several countries in the region.

In accounting for this type of divergence, as will be discussed later, legacies of the past, the characteristics of constitution making and bad economic policies played the major role. The EU itself could play only a partial, albeit non-negligible role in re-making states in the region. The criteria of Europeanisation of the CEE economies, the so-called Copenhagen criteria, include several elements of state making as conditions of creating functioning markets, and through various programmes, the EU directly participated in the upgrading of the administrative and institutional capacities of several of these states. The EU also played a role in influencing the formation of national political agenda in several of the South-Eastern European countries through various incentives. However, in addressing the problem of state capture, the anti-corruption measures and policies suggested by the EU proved inadequate. Unlike corruption itself, which is a general problem in both parts of Europe, state capture can be linked to a specific power structure within the state, and cannot be cured without considerably changing the structure of representation.[5]

The second process of divergence can be observed between the EU member countries and the leading CEE reform countries at the level of building institutions of economic development. Market making in both parts of Europe was strongly and directly linked to the (re)making of the state and to the strengthening of the institutional capacities of the (supra)national state to preserve and regulate markets. Within the EU the strengthening of the regulative capacities of the supranational quasi-state went hand in hand with preserving and, in several cases, with strengthening various non-market institutions of economic governance at the national, regional, local and workplace levels. Linking diverse groups of non-state actors with diverse metrics of success in economic development, these co-operative institutions facilitated combining the creation of the conditions to improve competitiveness with a wider range of developmental goals, and so allowed diverse actors to frame markets in a socially and economically less exclusive way.[6] Examples include the renewal of national level social pacts, the extension of social dialogue at national, subnational and supranational levels, the (re)emergence of various institutions of developmental partnerships at sectoral and regional levels, or the new forms of cross-border collective bargaining.[7] In the other part of Europe, institution-building efforts were concentrated on strengthening solely the capacities of central state agencies. The different organisations of labour, business or local self-governments are weak, and the diversity of co-operative institutions characteristic of the EU, albeit sometimes formally present in the region, do not play any significant role in framing markets in a more inclusive way. This type of divergence from the 'European model' can largely be explained by domestic conditions, including the weakness of diverse non-state organisations, their problems of legitimacy, or the largely exclusionary policies of national governments.[8]

In the emergence of this type of divergence, however, problems of the 'self-definition' of the EU as a distinctive model of economic development also played a considerable role. Putting it briefly, while the strengthening of regulative state capacities is part of the evolving neo-liberal 'European model', the diverse co-operative forms of economic governance largely form the 'optional' part of the model, and as something that is mainly seen as a matter of the domestic business of the member states.[9] To be sure, the struggle within the EU to 'Europeanise' such institutions, that is, to make them part of the 'model', has achieved some success, but, perhaps reflecting the ongoing fight for the redefinition of the model, EU pressure on the new applicants to take over such institutions has been weak.[10] While the EU put strong pressure on the applicant countries to modernise the administrative, regulative and developmental planning capacities of their states both at the national and local level, its pressure on the applicants to extend the scope of co-operative institutions that could frame markets in a more inclusive way proved rather lukewarm.[11]

Largely related to this institutional void, the third process of divergence could be observed inside the non-EU member countries in the form of growing disparities across regions, sectors and social groups, as well as between the 'internationalised/Europeanised' parts and the rest of the economy. As argued below, the co-operative institutions might well play a central role in the reduction of such disparities. Finally, at least in the first decade of economic transformation, there was not much evidence of convergence at the level of aggregate indicators of economic development and quality of human life conditions between even the best performing CEE countries and the EU member countries.[12] While the EU did include a country such as Portugal, with relatively poorer economic and social indicators, the persistence in the relative backwardness of the CEE countries might be seen as an indirect proof of the weakness of a developmental strategy based solely on the market enhancing capacities of state bureaucracies.[13]

To summarise, the Europeanisation of the economies of the CEE countries in the first decade of transformation was primarily about state making and less about non-state institution building. As is discussed in the next part, those countries that have a functioning market economy in the region have a market preserving state and a regulative state. While some of the countries of the region have states that, according to surveys, are weaker then states in Sub-Saharan Africa, others have considerably higher market preserving and regulative capacities.[14] One of the lessons of the last decade of reforms has been that neither privatisation, nor the introduction of all the regulations of the developed world, as happened in many of the countries of the region, will create a market economy if the state is too weak to resist the pressure of redistributive groups. Such state capacities might be strengthened if power is less centralised within the state and if the 'non-hierarchical elements of the state' are correspondingly stronger.

MARKET MAKING AND STATE MAKING: DIVERGENCE AMONG THE CEE COUNTRIES

Diversity in economic development is not a new feature of economic change in Eastern Europe. Even before the political regime change in 1989, countries in the region had widely diverged in their patterns of industrialisation, and, as a consequence, in their patterns of industrial distortions. They have also differed in terms of their structure and patterns of foreign trade. Some were closer to autarchic patterns of economic development; others had gradually opened up their economies to the world market. They had different levels and forms of economic imbalances, and had experiences with different types of economic reforms. While the share of the private sector was generally low, in some of the countries the share of the so-called 'second economy' was higher. While in most of these countries the role played by market institutions was also limited, in some countries in the region it was possible to find an extensive use of such institutions. What was common to all the countries of the region was the unstoppable deterioration of their positions in the world market throughout the 1980s and the slowing down of their economic development.

This divergence in economic development remained a constant feature of the region even after the political regime change. In the 1990s, however, it has appeared in a much more dramatic and historically unprecedented form. In some of the countries of the region, after a relatively shorter period of transformational recession, economic recovery began early, and by the second half of the decade these countries were approaching the level of economic development they held in 1989 as measured by GDP.[15] In these countries, economic restructuring has been considerable, and most are now on the path to what can be called sustainable economic growth. The number of such countries is still very small, however. The majority of the citizens in the region still live in countries where after the loss of 40–60 per cent of GDP, it is only the inequalities that have grown, and their economies continue to stagnate or decay.[16]

Washington vs. Brussels

Economic reformers throughout the region were pushed and pulled in two diverging directions at the beginning of the economic transformation. On the one hand, the recipes coming from across the Atlantic and forming part of what was called the Washington consensus, have stressed the importance of de-statisation and de-regulation in the process of market making. While it has never been formulated in the framework of an encompassing blueprint, the message coming from Brussels was at least as clear: market making is about the re-making of the state, about re-regulation of relations among economic actors, and about the re-institutionalisation of the economy. The proponents of the Washington consensus measured progress in economic reforms in terms of the level of freedom from the state. The criteria of success formulated by the EU, on the other hand, besides the level of liberation, consisted of measures such as progress in the regulation and development of state capacities, including administrative and developmental planning capacities. According to the experts of the international financial institutions in Washington, market making was primarily about making economic activity a private business. The Eurocrats visiting the region, however, have left no doubt about their seeing the market as one of the state-made social institutions, and as a specific structure of state-made rights and obligations continually policed and monitored by the regulatory state. The more concrete prescriptions based on the Washington consensus were formulated as measures liberating economic activity from the state: liberalisation of prices, liberalisation of trade and privatisation. These measures were supposed to 'get prices right', thus allowing the price mechanism to effect co-ordination among economic actors undisturbed by the state, and so leading economic development towards the radiant future.

While measures of economic liberalisation also formed part of the policy proposals coming from Brussels, the EU prescriptions were mainly about 'getting institutions right' as a condition of getting prices right, and also as a condition of being considered for accession to the EU. 'Getting institutions right' was mainly about strengthening state capacities to create and preserve the market order, to police and monitor competition, and to enable non-state actors to improve their market positions by creating and monitoring diverse non-state institutions of economic governance. As of the second half of the 1990s, this also includes increasing developmental planning capacities at the various levels of the state apparatus.

In the first few years of economic reforms, it was basically the Washington consensus that shaped policies in the region. Extensive regulation of the economy began only in the middle of the decade and the building up of regulative state capacities also began long after the introduction of liberalising measures in most of the CEE countries. Within the region, however, progress in this field is highly uneven, and, as will be seen below, it is still divergence that is the major defining characteristics of the situation.

The most important lessons of the first decade of reforms from this viewpoint could be summarised as follows. First, liberalisation of prices and trade brought about beneficial economic effects in those countries where states had the capacity to re-regulate relations among economic actors and prevent their misuse in asymmetries in economic power.[17] Second, privatisation has improved the functioning of the economy in those countries where states had a strong capacity to uphold property rights, to maintain the rule of law, to create a predictable policy environment, and to regulate relations among economic actors.[18] Third, liberalisation and privatisation have led to economic restructuring and economic growth in those countries that had states with a strong capacity to uphold rights and preserve competition, but only those countries that had states with robust defences against state capture had market preserving and regulative capacities.[19] Finally, the introduction of even the most extensive regulations did not improve the quality of the markets if the legal effectiveness of the state was low; the use of legal transplants and even the introduction of extensive legal reforms were not sufficient in countries with states that had a weak capacity to maintain the rule of law and to enforce their own laws.[20]

TABLE 1
REGIONAL AVERAGES OF THE CREDIBILITY INDICATOR AND ITS COMPONENTS

Region	Credibility indicator	Components of the credibility indicator				
		Predict-ability	Political stability	Violence	Reliability of judiciary	Lack of corruption
All countries	3.23	3.21	3.25	2.80	3.04	3.86
High-income industrial countries	4.14	3.85	4.27	3.64	3.98	5.04
South and Southeast Asia	3.69	3.55	3.56	3.28	3.94	4.12
Middle East and North Africa	3.28	3.36	2.86	3.57	2.61	4.01
Central and Eastern Europe	3.22	2.93	3.51	2.72	3.14	3.82
Latin America and the Caribbean	3.12	3.17	3.60	2.43	2.63	3.79
Sub-Sahara Africa	2.91	3.06	2.57	2.59	2.76	3.55
Commonwealth of Independent States	2.69	2.87	2.91	2.16	2.35	3.16

Source: Aymo Brunetti, Gregory Kisunko and Beatrice Weder, 'Credibility of Rules and Economic Growth: Evidence from a Worldwide Survey of the Private Sector', *The World Bank Economic Review* 12/3 (1998), pp.353–84.

Table 1 offers measures for the regional averages of the credibility indicator and its components. These measure the perception by private firms of the extent of credible state commitment to preserve the market order. Based on this survey, we can speak about progress in market making if states are in place with the capacity to build up among economic actors a stable expectation that their property rights are safe, that they can count on the state to enforce their contracts in case of disputes, and that they do not have to fear losing their gains as the result of sudden changes in policies by unpredictable or corrupt governments. As can be seen from the table, the expectations of private economic actors about state capacity to enforce contracts or produce predictable policies without being corrupted are actually lower in the former Soviet Republics than even in the Sub-Sahara African countries or in Latin America. On the other hand, the subjective evaluation of state capacities to preserve the market order are significantly higher in the Central and Eastern European countries.

Networks and State Capture

In 1989, the year when the political and economic changes began in the region, the neighbouring EU member countries had states with robust capacities to preserve market order, enforce competition and regulate relations among economic actors led by some commonly acceptable notion of public good. More specifically, these states had a well-developed capacity to uphold economic rights, enforce obligations, maintain predictable policy environments for economic actors, and prevent the misuse of asymmetries in economic and informational power. These state capacities were sustained by intra-state mechanisms that reduced the dangers of arbitrary policies and hence also reduced the risks of a general regulatory capture by powerful economic groups. Most of the Central and East European nations did not have such states at that time.

The rapid devolution of the economic power of states in micro-decisions to private actors in many of these countries did not result in the emergence of market order, competition and the re-emergence of economic development. Instead, in the countries of the region where the states and democratic institutions were weak, market reforms resulted in the economies that were dominated by predatory groups and of states that were dominated by the same groups. Contrary to the expectations of the reformers, the post-privatisation property regimes in the region were not based on forms in which management and ownership were separated and in which corporate governance was conducted by banks or through transactions on the stock exchange. Rather, the dominant role in the new property regimes, at least in the first half of the decade, was played by different forms of under-regulated cross-ownership of firms and financial institutions, with, in several cases, state agencies co-owning these firms and banks.[21]

The formation of these networks was closely linked to the enormous growth in the uncertainties caused by rapid liberalisation, and, in many countries, to the insecurity of property rights. The evolution of the balance of power between these networks and the state was the major factor determining the path of economic development in these countries throughout the 1990s. The relative powers of the financial-industrial groups and states were largely shaped by the level of economic distortions inherited from the past regimes, the speed of the liberalising policies, and the characteristics of the states themselves.[22] In countries where the inherited economic distortions were high, market reforms meant a dramatic redistribution of economic opportunities and powers for a large number of firms and regions that lacked the capacity to adjust to the exigencies of the market. The more rapid the liberalising measures, the more firms were pushed to form networks – first, in order to survive, and later for 'going for the state' as a strategy of survival.[23] Countries that inherited economies with highly distorted economic structures, that introduced liberalisation too rapidly, and that had newly formed states in which power was strongly centralised, represented the worse cases. In these countries, mainly the post-Soviet republics, states lacked the capacity to resist these networks and hence were easy prey.[24] In the Central European countries, on the other hand, the inherited levels of economic distortions were much lower, the speed of reforms was slower than in the post-Soviet republics, and states had stronger capacities to resist capture. It was in these countries that the regulative state could emerge by the second half of the 1990s.[25]

State Capacity

To date, there are three elements of state functions that remain in short supply in the region. The first is the state's capacity to uphold the general rights of economic actors and to create a predictable policy environment for them. According to the World Bank survey summarised in Table 1, such state capacities are at their weakest in the world within the countries of the former Soviet Union, being weaker even than in the countries of Sub-Sahara Africa or Latin America. In the Central European countries the capacity of states to uphold rights and maintain a predictable policy environment is stronger, yet still weaker than what can be found in the most advanced capitalist societies.[26] The second type of state capacity in short supply is the capacity to prevent the use of state institutions by powerful private groups to redistribute wealth and opportunities to themselves. According to a recently published survey, in many of the Eastern European countries economic actors can reasonably expect that competitors can literally purchase policies and regulations at the different branches and levels of government.[27] Perception of such state capture by private groups is low only in a smaller group of post-communist countries. Finally, the third type is the capacity to regulate relations among economic actors in a balanced way and prevent the misuse of asymmetries in economic and information power within the market. Again, according to recent surveys, most of the states of the region could not introduce extensive and effective regulations enforcing competition and/or market orientation even in such decisive areas as the financial markets.[28]

These are exactly those state characteristics that shape the overall capacity of states to constitute and preserve the market order, and to enforce competition and market orientation. In the absence of these capacities in several of the countries of the region, economic actors are hesitant to invest in the formal sector of the economy and prefer to enter into only very elementary forms of economic transactions, such as barter. In several of these countries predatory groups dominate 'markets' and states are captured by those very same groups.[29] Problems of social and economic development in these countries are different than in those that have more or less functioning market economies. While the question the latter countries face is how to correct the economic and social problems of otherwise functioning market orders, in the former countries economic and social problems are related to the non-existence of functioning markets, or more precisely, to the corruption of states and markets by self-seeking groups.

Decision Making

The capacity of states in democratic countries to constitute functioning markets is largely the result of the way decision making about social and economic issues is structured within the state. While in countries with corrupted markets and captured states decision making is excessively centralised and limitations on executive powers are weak, in the leading reform countries state power is more decentralised.[30] In the latter countries, when state executives make their policies they have to take into account diverse representations of the public good – represented by coalition partners, parties in different houses of the legislature, different levels and branches of the government, autonomous state agencies, and the organisations of civil society and economic society. In such a state, the horizontal accountability of executives by other autonomous state agencies reduces the risk of misusing state power and the encroachment on the rights of non-state actors. Independent judiciaries with the powers of judicial supervision, and rules that make any change to basic rights an arduous task, prevent executives from taking arbitrary decisions and hence force them, and the non-state actors, to honour the law. The existence of autonomous state agencies that can force incumbents to respect specific rules in the use of public resources, and of state agencies that represent specific rights or the rights of specific minority groups, further extend the accountability of executives. It is through the institution of distributed authority and the permanent pressure on executives to take diverse representations of public good into account that the likelihood of state capture is reduced. On the other hand, the state is up for grabs in countries where power is concentrated and where mechanisms that would tie the hands of executives and prevent them from arbitrarily intervening in the economy are lacking.[31]

After nearly a decade of struggle to liberate economic activity from the state, many of the countries in the region now face the problem of how to liberate a state that has been captured by economic groups. If they want to create a functioning market order, they will need a state that is capable of regulating the highly uneven distribution of economic power in a balanced way. But, in order to re-balance their economies, they first need states liberated from the hold of powerful economic groups. The task of (re)making states with the capacity to constitute and preserve market order still lies ahead in many of the countries of the region.

Functioning Regulative States

Based on these various features, it is possible to conclude that Poland, Hungary, the Czech Republic, Slovenia and Estonia have well functioning regulative states, with Lithuania, Latvia, Bulgaria, Slovakia and Romania lagging behind. The task of market making and, correspondingly, state making, still lies ahead in the remaining 14 countries in the region, including nearly all the former Soviet Republics as well as some of the South Eastern European countries. This rank order basically corresponds to the 'success' indicators used in comparative transition studies and to the EU reports on accession countries.[32] The countries belonging to the first group undertook a considerable restructuring of their economies, their economic growth started in the second half of the 1990s, and some are now among the fastest growing economies in Europe.

The emergence of a functioning market-preserving and regulative state in these countries was largely the result of domestic political and economic processes, although the EU also played a considerable role in helping to consolidate and upgrade their regulative and administrative capacities. In addition, the promise of participation in the EU social and economic cohesion programmes played a considerable role in renewing and re-making the developmental planning capacities of these states. The EU role in this field was partly direct, by setting mandatory goals in the form of the *acquis* and by giving financial and technical help for the implementation of these requirements. The EU also played a considerable indirect role by placing these countries in a regulative competition framework through the more or less forced opening up of their economies. That said, the Europeanisation of states in these countries is still highly uneven, and state building has affected mainly central governments that are hesitant to share their powers with other branches and levels of government. Moreover, the autonomy of the newly created regulatory agencies is questionable in several of these countries (for example, the Czech Securities Exchange Commission, or the Hungarian Banking and Capital Market Supervisory Authority), while the cohesion and autonomy of the state bureaucracies in some of these countries is weakened by the remaining elements of the 'spoils system', and by the possibility that the staff or the organisation of the state bureaucracy could be changed according to political criteria. Finally, local development is under the control of central governments in most of these countries and hence financial and political autonomy at the local levels is weak.[33]

DIVERGING CONVERGENCE?

The economic developmental problems of those CEE countries with a more or less functioning market economy differ almost on a country-by-country basis within the region. Nevertheless, they all face the challenge of 'inventing' institutions of economic development that could increase the competitiveness of their economies, make development socially more inclusive, and support the process of their catch-up growth. While the specific countries within the current EU belong to different 'sub-types' of capitalism, nearly all of the institutions that are cited as providing them with a competitive advantage are weak or absent even within the leading reform countries of Central Europe.[34] The often cited institutions of 'co-operation for competitiveness' of the continental European forms of capitalism, including co-operative industrial relations and established long-term relations among banks, firms, regional and local governments, labour and business associations, are basically lacking in the region. And while a considerable role has been played by the old and the newly invented forms of developmental associations of diverse non-state actors in transnational market making within the EU, in the CEE countries it was the regulative state that was basically the prime mover of economic development during the first decade of reforms.

Industrial Relations

Both trade unions and business associations are weak and fragmented in most of the CEE countries. Although institutions of tripartite concentration are present, they are under-utilised in most of these countries. Nevertheless, during the early 1990s, several national-level tripartite pacts did help to encourage governments to initiate large scale reforms. Once these were introduced in most of the countries of the region, governments turned to labour-exclusive policies, further weakening organised labour and, in some of these countries, also organised domestic business.[35] The number of firm-level collective agreements is low, there are very few sector-level collective agreements, and the coverage of labour through collective agreements, ranging between 20 and 50 per cent, is much below the EU level. The growing competitive pressure on governments, sectors and firms in many of the continental EU countries led to the re-making of collaborative institutions at firm and sector level, and in many countries the movement to EMU led to the rebirth of social pacts at the national level. In the Central European countries, by contrast, managers and state bureaucrats dominate economic restructuring without any significant concertation. While the Copenhagen criteria include elements of strengthened social dialogue at various levels, these prescriptions form the 'soft' part of the *acquis* and are not enforced by the EU.

One cannot expect any automatic convergence in industrial relations once the first group of CEE countries is inside the transnational market making regime. The organisation and the fragmentation of labour and business differs from one country to another within the region, and change in this field will depend on the existing conditions and the strategies of the non-state (trans)national organisations in both parts of Europe. In some of the CEE countries, the desire to join the EMU and meet its economic criteria might well encourage political elites to considerably upgrade the system of industrial relations – as was the case in Ireland or Italy in the 1990s. In other countries, the persistent fragmentation of labour and business might induce national governments to weaken labour further and push the system of industrial relations more in the direction of the Anglo-Saxon model of 'disorganised capitalism'. Finally, the inclusion of labour and business representatives in the national, sectoral and regional development planning processes – another unenforced chapter in the 'official guidelines of Europeanisation' – might alter the balance of forces between governments and organised economic actors.[36]

Developmental Planning

One of the unique features of Europeanisation at the level of market making has been the introduction of developmental planning in those CEE countries that are busy leaving behind their dysfunctional planned economies. To be sure, this 'European' developmental planning differs dramatically in its principles from the central planning of the state socialist regimes. Labelled as the 'dictatorship over needs', the later provided the central party state with exclusive and uncontrolled prerogatives to define the goals of economic development. Linked intimately to the European new left's 'Third Way' ideology, the recent European developmental planning embodies diametrically opposing principles. These include the empowerment of diverse social and economic actors to participate in the framework of local and national partnerships together with the organs of the state in designing and implementing developmental programmes under the conditions of extended and multi-level accountability.[37]

The social and economic cohesion policy of the EU that funds national, regional and sectoral developmental programmes might considerably alter relations between central governments, local and regional self-governments, and various organised social actors. At the moment, in most of the CEE countries, the economic and political autonomy of local and regional actors is weak, and restructuring is moving in many countries towards decentralised administrative self-empowerment of the state. Except in Poland, and as a result of recent changes, in the Czech Republic, political decentralisation that would increase regional autonomy is almost absent, the political organisation of local self-governments is fragmented, and the regional organisation of labour and business is weak. Weak local financial autonomy, as well as the centralisation and centralised redistribution of locally generated incomes, further weaken the potential developmental role of localities.

The CEE countries first joining the EU might gain access to EU development funds in the range of 1.5 to 2.5 per cent of their GDP, an amount that equals or in some countries even surpasses the present volume of FDI they recently receive. The terms of conditionality regarding access to these funds might considerably alter the developmental possibilities of non-state actors in these countries. They might further strengthen the prerogatives of central governments, or they might empower local, regional and national-level non-state actors. As things stand right now, in the 'first planning period', between 2004 and 2007, the EU Commission might decide to go for the funding of a single National Development Plan in each country only, changing its previous practice of funding a centralised sectoral and several decentralised regional programmes. But although this change in policies might prove convenient for the Commission, it might also directly effect the development of relationships between central governments and other social and economic actors. Central governments in the accession countries have been doing their best to preserve their prerogatives and the change in the policies of the EU could give them further encouragement. The institution of development planning was introduced in the late 1980s as a mechanism to empower non-state actors to frame markets from below in a more inclusive way, and as a prime mover in decentralised democratic experimentation. Ironically, it could well turn out that the same institution in the CEE countries will instead become the mechanism by which central states become (re)empowered.

In conclusion, the constellation of strong states, weak non-state actors and forms of social and economic governance has played a considerable role in shaping the social and economic characteristics of market making in the region in the first decade of Europeanisation. This study was not intended to speculate about the probable social and economic consequences of joining the next stage of transnational market making under the conditions of the general weakness of forms of social and economic governance that could frame markets in a more inclusive way. The persistent weakness of the organisations of non-state actors and forms of governance, together with the expected rapid transfer of the accumulated powers of domestic governments to supranational levels, might have dramatic consequences from the viewpoint of the citisens of these countries. Adjustment to the new conditions will almost certainly prove path dependent, and will be shaped by the already existing conditions within these countries. But it will also be largely influenced by the characteristics of EU policies vis-à-vis these countries.

NOTES

1. See, for example, B. Greskovits and D. Bohle, 'Development Pathways on Europe's Periphery: Poland and Hungary Compared' (ms. Central European University, Budapest, 2000).
2. These are, the Czech Republic, Estonia, Hungary, Poland and Slovenia (European Commission, *Regular Report From the Commission on Progress Towards Accession*, 2000).

3. On the issue of the integration of CEE countries to the EU economy see the insightful analysis of Laszlo Csaba, 'Az Union keleti politikája és a kibövités'. *Europai Szemle* 12/1 (2001), pp.95–103.
4. Laszlo Bruszt, 'Heterarchies and Developmental Traps', in K.K. Hinrichs and H. Wiesenthal (eds.), *Kontingenz und Krise, Institutionenpolitik in Kapitalistischen und Postsozialistischen Gesellschaften* (Frankfurt, New York: Campus Verlag 2000); B. Greskovits, 'Hungary's Post-Communist Development in Comparative Perspective', in Werner Baer and Joseph L. Love (eds.), *Liberalization and its Consequences. A Comparative Perspective on Latin America and Eastern Europe* (Cheltenham: Edward Elgar 2000).
5. Laszlo Bruszt, 'Market Making as State Making: Constitutions and Economic Development in Post-Communist Eastern Europe', *Constitutional Political Economy* (forthcoming).
6. On the social and economic impact of such co-operative institutions see A. Hicks and L. Kenworthy, 'Cooperation and Political Economic Performance in Affluent Democratic Capitalism', *American Journal of Sociology* 103/6 (1998), pp.1631–72.
7. See among others Marino Regini, 'Between Deregulation and Social Pacts: The Responses of European Economies to Globalization', *Politics and Society* 28/1 (2000), pp.5–33; Michael J. Gorges, *Euro-Corporatism? Interest Intermediation in the European Community* (Lanham, MD: University Press of America 1996); Michael F. Kluth, *The Political Economy of Social Europe: Understanding Labour Market Integration in the European Union* (London: Palgrave 1998); Michel Freyssenet *et al.* (eds.), *One Best Way? Trajectories and Industrial Models of the World's Automobile Producers* (Oxford: Oxford University Press 1998); Giuseppe Fajertag and Philippe Pochet (eds.), *Social Pacts in Europe – New Dynamics* (Brussels: OSE – European Trade Union Institute 2000); Robert Boyer *et al.* (eds.), *Between Imitation and Innovation: The Transfer and Hybridization of Productive Models in the International Automobile Industry* (Oxford: Oxford University Press 1999); Kathleen Thelen and Ikuo Kume, 'The Effects of Globalization on Labor Revisited: Lessons from Germany and Japan', *Politics and Society* 27/4 (1999), pp.477–505; Philippe Pochet (ed.), *Monetary Union and Collective Bargaining in Europe* (Brussels: Peter Lang 1999).
8. See Greskovits and Bohle, 'Development Pathways'; David Stark and Laszlo Bruszt, *Post-Socialist Pathways: Transforming Politics and Property in Eastern Europe* (New York: Cambridge University Press 1998).
9. Martin Rhodes, 'Capital Unbound? The Transformation of European Corporate Governance', *Journal of European Public Policy* 5/3 (1998), pp.406–27.
10. On the ongoing fight to redefine the 'European model' see, for example, Jon Erik Dolvik, 'Redrawing Boundaries of Solidarity? The ETUC, Social Dialogue and the Europeanisation of Trade Unions in the 1990s', in Emilio Gabaglio and Reiner Hoffman (eds.), *The ETUC in the Mirror of Industrial Relations Research* (Brussels: European Trade Union Institute 1998), pp.295–347. For a different perspective, see Wolfgang Streeck, 'European Social Policy after Maastricht: The Social Dialogue and Subsidiarity', *Economic and Industrial Democracy* 15/2 (1994); and Wolfgang Streeck, 'The Internationalization of Industrial Relations in Europe, Prospects and Problems', *Politics and Society* 20/4 (1997), pp.429–51.
11. Elena Iankova, 'Converging with Europe? Central and Eastern Europe's Return to Capitalism' (Cornell University, Institute for European Studies Working Paper 99/1, 1999).
12. Greskovits and Bohle, 'Development Pathways'.
13. Portugal joined the EU in 1986 with a per capita GNP that was 27 per cent of the EU average, much lower then the contemporary figures for the leading reform countries of CEE. See 'More Members for the EU? A Report on EU Enlargement', Helsinki: EVA Center for Finish Business and Policy Studies, 1997, cited by 'Converging with Europe?'.
14. Aymo Brunetti, Gregory Kisunko and Beatrice Weder, 'Credibility of Rules and Economic Growth: Evidence from a Worldwide Survey of the Private Sector', *The World Bank Economic Review* 12/3 (1998), pp.353–84.
15. The concept of 'transformational recession' stems from Janos Kornai, 'Transformational Recession: The Main Causes', *Journal of Comparative Economics* 19/1 (1994), pp.36–63). For reliable data on post-communist divergence, see the *Transition Reports* of the European Bank for Reconstruction and Development (EBRD) from 1997, 1999 and 2000 (London, EBRD).
16. For an excellent overview of economic conditions in the region see the EBRD *Transition*

Report 1998.

17. J.E. Stiglitz, 'Whither Reform?' World Bank Annual Bank Conference on Development Economics, Washington, DC, 1999; Bruszt, 'Heterarchies'; J. Hellman, 'Winners Take All: The Politics of Partial Reforms in Postcommunist Transitions', *World Politics* 50/2 (1998), pp.203–34.
18. K. Pistor, Martina Raiser and Stanislaw Gelfer, 'Law and Finance in Transition Economics', *Economics of Transition* 8/2 (2000), pp.325–68; Andrei Schleifer and Robert Vishny, *The Grabbing Hand: Government Pathologies and Their Cures* (Cambridge: Harvard University Press 1998); Stiglitz, 'Whither Reform?'
19. Bruszt, 'Market Making'; Hellman, 'Winners Take All'; Stiglitz, 'Whither Reform?'; D. Weimer (ed.), *The Political Economy of Property Rights: Institutional Change and Credibility in the Reform of Centrally Planned Economies* (New York: Cambridge University Press 1997).
20. Pistor *et al.*, 'Law and Finance'.
21. J. Johnson, 'Russia's Emerging Financial Industrial Groups', *Post-Soviet Affairs* 13/4 (1971), pp.333–65; Y. Kuznetsov, 'Learning in Networks', in J.M. Nelson, C. Tilly and L. Walker (eds.), *The Post-Communist Political Economies* (Washington DC: National Academy Press 1997), pp.156–77; G. McDermott, *The Communist Aftermath: Industrial Networks and the Politics of Institution Building in the Czech Republic* (Cambridge: Massachusetts Institute of Technology 1998); Stark and Bruszt, *Post-Socialist Pathways.*
22. On the role of the legacies of the past, economic distortions and state characteristics see Bruszt, 'Heterarchies'; Greskovits and Bohle, 'Development Pathways'; Greskovits, 'Hungary's Post-Communist Development'; V. Popov, 'Output Change During Transition: The Role of Initial Conditions and Economic Policy', *Voprosy Ekonomiky* 7 (1998), pp.1021–47 (in Russian); V. Popov, 'Internationalization of the Russian Economy: What Went Wrong', *Emergo: Journal of Transforming Economies and Societies* 5/2 (1999), pp.53–85.
23. Bruszt, 'Heterarchies'.
24. Ibid.; Hellman, 'Winners Take All'; J. Hellman and G. Kaufmann, 'How Profitable is Buying State Officials in Transition Economics?', *Transition* 11/2 (2000), pp.8–11
25. On the differences in the speed of reforms see Greskovits and Bohle, 'Development Pathways'.
26. Brunetti *et al.*, 'Credibility of Rules'.
27. Hellman and Kaufmann, 'How Profitable'.
28. For an extensive survey on the divergence in the level of effectiveness and extensiveness of state regulations of financial markets in the region see the EBRD *Transition Report 1999.*
29. Hellman, 'Winners Take All'; Stiglitz, 'Whither Reform?'; Bruszt, 'Heterarchies'; L. Polishchuk, 'Misssed Markets: Implications for Economic Behavior and Institutional Change', in Nelson *et al.* (eds.), *Transforming Post-Communist Political Economies*; D. Woodruff, *Money Unmade: Barter and the Fate of Russian Capitalism* (Ithaca: Cornell University Press 1999).
30. Bruszt, 'Market Making'; Hellman, 'Winners Take All'; Stark and Bruszt, *Post-Socialist Pathways*; EBRD *Transition Report 2000.*
31. Bruszt, 'Market Making'.
32. See, for example, EBRD *Transition Report 2000.*
33. An example from Hungary from an EU expert dealing with regional developmental issues: 'According to some estimations more than half of the Hungarian municipalities would not be able to apply for the Structural Funds under the present system because they do not possess sufficient financial resources. This means that a large part of the Hungarian territory and population would be excluded from direct contributions from the European Union to improve their economic and social situation': see Luis Madeureira Pires, 'Study on the Present Institutional Structure of Regional Development in Hungary and its preparation for the EU Structural Funds' (Budapest: Pharc 2001).
34. On the literature on comparative capitalism in general, see Stark and Bruszt, *Post-Socialist Pathways*; on capitalist divergence within the EU see Rhodes, 'Capital Unbound'. See also J. Hollingsworth, Philippe C. Schmitter and Wolfgang Streeck (eds.), *Governing Capitalist*

Economies (Oxford: Oxford University Press 1994); Philippe C. Schmitter, 'Sectors in Modern Capitalism: Modes of Governance and Variations in Performance', in Renato Brunetta and Carlo Dell'Aringa (eds.), *Labour Relations and Economic Performance* (London: Macmillan 1990): and Wolfgang Streeck and Philippe C. Schmitter (eds.), *Private Interest Government: Beyond Market and State* (London: Sage 1985).

35. A. Tóth, 'Attempts to Reform a Workers' Movement without Mass Participation', in Jeremy Waddington and Reiner Hoffmann (eds.), *Trade Unions in Europe Facing Challenges and Searching for Solutions* (Brussels: European Trade Union Institute 2000): A. Tóth, 'Diverging Convergence: Organised Labour as a Factor in the Hybridisation of Production and the Consequences for Convergence of Subsystems of National Industrial Relations Systems' (ms, Budapest, Institute of Political Sciences, 2001); A. Tóth and R. Langewische, 'Introduction: Challenges of Transformation and Preparations for EU Accession', *Transfer* 6/3 (2000), pp.370–85.
36. In Hungary, for example, a 1999 Act excluded representatives of both labour and business from participation in developmental planning at all levels.
37. For an insightful analysis of the origins of EU developmental planning see Liesbet Hooghe, 'EU Cohesion Policy and Competing Models of European Capitalism', *Journal of Common Market Studies* 36/4 (1998), pp.457–77.