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EAST CENTRAL EUROPE**

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The Balkan model and the balkanization of East Central Europe

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Abstract

East Central Europe (ECE) has shown marked flaws in its institutional system throughout its transition process compared to Western benchmarks. These were deeper in the Balkan countries than in the Visegrad countries (V4). However from the mid-2000s and especially after the 2008 crisis, also V4 altered institution development path away from the benchmarks. The existing and increasing differences in the political and economic institutions of the ECE versions of the “transatlantic model of capitalism” and the failure of the comprehensive application, moreover the politically and socially easy U-turn in the development process of these countries can be explained with the existence of another local model of capitalism the “Balkan model”.

JEL: D72, H82, P16, P31

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1. Introduction

East-Central European (ECE) transition process has been regarded as historical success story (Kornai, 2006). Of course, the various states’ development process was not identical. Institutional solutions as well as the timing and sequencing of changes varied

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(Roland, 2000). Some countries were regarded as forerunners (the Visegrád countries: Poland, Czech and Slovak Republics and Hungary, the V4). Others seemed to perform some flaws. Cernat (2006) called the Romanian capitalist model “cocktail capitalism” referring to the fact that a rather heterodox mix of institutional solutions was applied. There has been a consensus that ECE countries’ development was, however, more or less successful and conform with the (neoliberal) expectations of the international advising community and the European Union. This fact was sealed by the entry of ECE countries together with the three Baltic states to the European Union. Further to the East other post-soviet countries’ transition has not been regarded equally. A main division line seemed to be present not only because of stronger Russian influence and less EU dominance, but also because of differences in the basic values of the political and economic institutions in that area.

Compared to this Eastern division line, another, southeastern one could also be figured out, though the influence of the EU and the international advising community has always been significant in the Balkans. Romania, Bulgaria and Croatia became EU members, membership negotiations with Serbia are in an advanced status. Nevertheless, the admission of the three above mentioned countries was postponed because of important institutional weaknesses, and in some important areas (corruption and organized crime) extra supervision has been carried out. So, there have been significant differences between the V4 and Balkan countries’ institutional systems. To sum up, V4 and Baltic countries’ transition process was mostly in line with the international and European expectations. Balkan countries also qualified but showed serious and continuous flaws compared to the Western benchmark. Other post-soviet countries entered different capitalist development model that substantially differed from the Western ideal model of the competition state.

In the ideal Western development model that was applied most effectively in V4 in the nineties, the political sphere was by and large characterized by party competition in democratic political institutions with control on corruption. The economy underwent fundamental restructuring and modernization, concerning its activity and product structure, technological sophistication and ownership pattern. Foreign direct investments (FDI) played a crucial role in this process. Visegrád countries became integrated part of the single European economic space. Political and economic systems

evolved institutionally independent. Both spheres relied on the buoyance of competition, hence this classic transatlantic model is called competition state. I argue in this paper that observers of European capitalist models (scholars of the Varieties of Capitalism literature) have been engaged with the variations of the transatlantic model of capitalism, the competition state. In their contributions ECE countries' analysis serves the purpose of classifying these countries' development according to the features of this models' variations. Cernat's (2006) cocktail capitalism describes an incoherent mix of systemic features coming from different types of the transatlantic competition state. I try to set up a new hypothesis in this paper that describes ECE countries' development and capitalist model in a fundamentally different conceptual framework: the rent-based model of the Balkans.

The presence of a different, not competition-based logic in the economy and politics in ECE countries became more obvious after the 2008 crisis. While Romania, Bulgaria and Croatia have never enjoyed the same high level of trust in their institutional stability than the V4, a U-turn and speedy departure from the expected transatlantic competition state model has been observed in the V4 countries too after 2008 (Kornai, 2015; Blaszczyk, 2017; Kozarzewski and Baltowski, 2017; Szanyi, 2016). Appel and Orenstein (2018) explained this by the so called "signaling effect": ECE countries applied the expected neoliberal suit with all the hardships and handicaps because of their strong dependence on the goodwill of the international advising community and the European Union. The demise of the concept after 2008 as well as the achievement of the most important strategic goals that required the strong support, accession to EU membership reduced the importance of the signaling effect. Though Appel and Orenstein (2018) describe the establishment of alternative institutional solutions in Hungary (crony capitalism and the illiberal state), they stress the concept's Russian origins. I argue in this paper that the relatively easy, unimpeded illiberal transformation of Hungary, but also the existence of similarities with the Polish and to some extent also the Czech institutional changes required a more fundamental explanation. It is not just a matter of a few populist politicians who tried to import some authoritarian political and economic solutions from the East. The rather widespread social acceptance of the new system needs a more fundamental explanation.

I argue in this paper in line with the concept of Acemoglu and Robinson (2012) that the historic social development patterns of this region differed substantially from any variation of the transatlantic model. But they were not close to the Eastern, Russian model either. What seems to be most influential is the Byzantine heritage that determined the development process of the Balkans, but stretched out historically also to the ECE region. ECE countries have always shuttled between East and West in their development. This “ECE-pendulum” is similar to the wellknown Polanyian pendulum (Polanyi, 1944), in the sense that the Western (transatlantic) model is regarded more liberal, while the Eastern (Balkan) model is rather autocratic and centralised. In order to better understand the rather unexpected recent U-turn in the ECE region we must first understand and define the Balkan model. This paper sets up a primary hypothesis with the most important model features. Some empirical evidence is also presented mainly for illustration of the model’s logic. There is still a long way to go until the solid empirical evidence is gathered. For the time being, one important empirical survey was carried out on the impact of ECE region’s historic path dependence on the transition process (Djankov and Hauck 2016).

The paper is structured as follows. After the introduction the general features of the Balkan model of capitalism are described in a normative, deductive manner. The next chapter discusses more in detail the core concept of the model, how business capture can serve the political stability of a selected elite. Chapter 4 is more inductive and contains empirical evidence on Balkan model’s impact in the V4 in three aspects: concrete actions of the establishment of business capture, the changing forms of rents and rent seeking and the upcoming ethnic conflicts that help governments driving away public attention from core issues of business capture. Finally I conclude.

2. Main features of the Balkan model of capitalism

In recent past historic roots of development patterns were included in international comparative studies (Nölke, 2014; Szanyi and Szabó, 2020). This thread of research seeks answers to the question why the neoliberal economic agenda reinforced by international financial institutions, the advisory community and finally the European Union did not work outside of the classic transatlantic core region. The 2008 financial

crisis is a mile stone in this regard. During the preceding two decades major imbalances and flawed development patterns occurred only in emerging market economies. The core transatlantic region's development pattern was rather smooth hence the period between 1990 and 2008 was called the time of "great moderation". The repeatedly occurring currency crises in the developing countries were explained by weak market economic institutions and were thought to be overcome by strengthening them. But the 2008 crisis hit mainly the core transatlantic region therefore the belief in the omnipotence of the neoliberal suit was shaken. So was the neoliberal theoretical background of ECE transition process (the post-Washington Consensus' SLIP²).

The classic Varieties of Capitalism (VoC) literature has been based on the neoliberal concept. The main authors of the thread (Hall and Soskice 2001; Amable 2003 and their followers) tried to extrapolate the transatlantic model to all countries in the world regardless of special local circumstances. This applies also for the ECE region (Bohle and Greskovits, 2007; Farkas, 2016). Some scholars noticed that the original model does not fit perfectly the countries in the European periphery and tried to expand the original idea with some modifications. Yet, the basic structure of the comparisons did not change, scholars strictly followed the original approach searching for institutional nuances in the originally suggested six markets. The results of the empirical tests were not really convincing concerning the ECE region (Farkas, 2016; Prochniak et al., 2016).

Nölke and Vliegenhardt (2009) suggested the amendment of the VoC toolkit with a new aspect that seemed to be highly relevant for at least some ECE countries: the extensive role of foreign direct investments (FDI), and its consequences for economic development and economic policy options (the dependent market economy DME model). Szanyi (2016) called attention to the still existing freedom of the ECE countries' governments in shaping the institutional environment thus exercising strong impact on the economic development patterns. Both amendments of the original VoC structure were applied for the ECE countries in order to better understand why these countries do not fit into the classic transatlantic model framework. It seemed that both the role of FDI (dependence) and the strong role of the state in shaping economic development patterns have historic roots in the ECE region. More generally the role of cultural and

² Stabilization, liberalization, institution building and privatization

historic heritage in ECE countries' development pattern has already been tested empirically (Djankov and Hauck, 2016). In the following sections I summarize the most important features of a Balkan development model that stand out of the classic transatlantic focus of VoC schemes.

Historically the region that I regard was the territory of the Austro-Hungarian Empire, and the Ottoman Empire. Geographically this consists of all ECE countries south of Poland including current day Czechia. Tentatively we can also include southern Poland (former Galicia). The historic heritage of the region is shaped by continuous wars and heavy war damages (including human lives and de-population), ethnic suppression and repeated wars for national independence from the two empires. The historic sentiments still play crucial role in mindset of the populations of these countries. After the Turkish wars that ended in 1715 in the Hapsburg empire and 1878 in the Balkans with the establishment of independent Romania, Bulgaria and Serbia massive concerted migration took place in the region. Previously important spontaneous migration of refugees from occupied Balkans took place already during the 15-16. centuries. But migration intensified and its direction was partly reversed from the North and West to the South of the Hapsburg Empire. The original idea was to fill depopulated areas. Later, especially in the 19. and the 20. century ethnically mixed populations were deliberately created in order to avoid and control ethnic independence ambitions. The classic example of this also politically motivated migration process was historic Banat region (today divided between Romania and Serbia), where no less than five different ethnic groups were settled in a chessboard-like pattern (Hungarians, Serbs, Romanians, Germans and Slovaks).

The late Hapsburg empire but also its 20. century successor states pursued policies to ethnically homogenize the mixed population. Historically Hapsburgs wanted to Germanize, Hungarians to Hungarianize ethnic minorities. The same ambition has been typical for the successor states as well. Without going into the endless details of these policies the explicit usage of which started with Joseph II (1780-1790), we only state that the policies served as explosive fuel for ethnic conflicts. The hostility has continued up till most recently and what is most important it has always been intensified deliberately through active political measures of most governments in the region regardless of their political orientation.

The first unique feature of the region is its patchwork-like ethnic pattern, the mixture of several nations in relatively narrow geographic space. This situation resulted in historically accumulated ethnic rivalry and conflicts in the region among all nations that has always been used and fueled by political parties and governments to cover other, socially important flaws of their development process.

After the dissolution of the two big empires (the Hapsburg and the Ottoman) newly created successor states could not avoid to become dependent from those big countries that dominated the region. After the two empires that directly controlled the region first Nazi Germany than the Soviet-union took control. Finally, after the 1990 collapse of the Soviet rule the European Community exercised decisive economic and political control over the countries in question. Foreign domination and dependence shaped the political and economic development process as well. The new patrons supported each country of the region (except for Serbia and Czechia during WW II by the Germans), or at least they promised some future reward for establishing close ties. The deepest reaching dominance feature was perhaps the two Munich decisions in 1938 and 1940 that resulted in very important territorial (border) changes in the region. As a compensation the patron usually required a civilized treatment of social and ethnic conflicts. These were usually not cured but just temporarily swept under the carpet. When the dominance weakened conflicts reemerged.

This applies also for the transition processes of the region. The desire to get rid of the Soviet dominance urged the countries of the region to consider options of another type of dominance, that of the European Union. The transition process of the countries was deeply influenced by the image of developed market economies in the neoliberal sense. Therefore, transition economies followed the suit, and applied policies, created market economic institutions according to the requirements of the exponents of the suit. Critics accused the international advising community with reinforcing their own (business) interests already at the beginning of the process. Nevertheless, a kind of status quo was achieved between them and local social and business representatives. In some countries (e.g. Hungary's DME model) more, in others less of Washington Consensus' SLIP was implemented. Some countries formally introduced some market institutions that have never worked properly. Already prior to the 2008 crisis after the legal act of accession was completed sometimes not even the image of compliance was maintained.

This also had an effect on the previously mentioned social and ethnic conflicts. During the 1990s these produced grave wars and street fighting in several countries of the region. When the EU dominance and the promise of the accession was manifested, all of a sudden the negatively perceived actions disappeared. Their control was in fact an important requirement for the negotiations over the EU membership. After EU accession tensions immediately became fierce again.

Control over nationalism and chauvinism is important to improve the economic performance of the ECE countries. The neoliberal agenda emphasized the importance of most effective employment of the institutions of the competition state. In some ECE countries the option was seriously considered, yet could not be flawlessly applied. Other countries did not seriously intend to comply with the requirements. All in all, when pressure declined all ECE countries started to amend the already existing institutional system in the direction of less competition, less transparency, less influence by multinational companies and more influence of the local political elites over the economy. I believe that this new institutional setup reflects the “natural” systemic features of the region.

The second feature of the model is therefore the role and dominance of influential power centers over the political and economic developments of the countries in the region. Historically, dependence was manifested towards major economic powers (Germany, Soviet Union, EU) and today also in relation to multinational business.

These above mentioned features of the institutional system create the economic fundamentals of the special Balkan model. On the bottom line of this model is rent seeking. Instead of competition protected market positions are created and captured by politicians and their cronies in order to secure their personal enrichment (Szanyi, 2019). Corruption and the close ties between business and polity is also a historic tradition in the region. Needless to say, it does not fit into the logic of the transatlantic competition state. The stability of the system is provided by two factors. First, the broad society is kept at low levels of education and knowledge. It is also manipulated by the information monopoly of the political center. Nationalism and chauvinism have always been a major tool of controlling and directing social attention. Today it is complemented by anti-

globalization rhetoric, counter-EU propaganda, frightening with migration. In the background rent-based economic structures are developed.

The second factor of stability is bound to multinational business. In the world of globalization rent-based economies cannot compete the competition driven economies. Although the ECE countries do their best to weaken global organizations (most evidently the European Union) they cannot survive without international business linkages. The small ECE countries do not possess rich natural resources like many post-soviet economies that could help them keeping the levels of national income high enough to secure a modest living standard for the society. Instead, they are forced to rely on multinational business activities that can be highly competitive internationally, also due to the depressed ECE wage levels. These revenues help governments finance a minimum level of social security and maintain macroeconomic stability. The Janus-faced relationship of ECE governments concerning global business is very much transparent. The Hungarian government has pursued selective policies with the various multinational firms (Szanyi, 2019). The use of selective policy measures is also an important general feature of the system. Cronies are favored, business rivals punished by the measures.

The usage of selective measures and curtailment of free competition in the economy but also in politics also results in high and increasing corruption. The liberal principle of separating business and polity does not apply. Crony capitalism is also supported by state institutions, the judiciary and police. Plenty of evidence can be found in various ECE countries on the selective usage of these later systems too. This is also indicated by the fairly low levels of good governance indicators (e.g. in World Bank, 2019; World Economic Forum, 2019; see also the charts in the Appendix). Another important tool is the big and expanding state-owned sector. Though this aspect is treated also in the later versions of the traditional VoC literature, it is always meant as lever of the developmental state concept. There is some historic evidence that even if national development was one of the drivers of state owned industries, it always supported also the development of crony ties and the creation of rent seeking opportunities.

The third element of the model is the basic importance of the rent-based economy of the ECE countries. The rents are deliberately created through a variety of protectionist

economic policies that create sources for rent seeking, and attached to this also systemic corruption. Negative social impacts (e.g. slow development, increasing inequality) are hidden away from social attention through the manipulation of public opinion. These impacts are partially compensated through increasing central redistribution of incomes that also serves the wellbeing of crony business. Also, external income sources play an important role in the compensation. These stemmed from the subsidies paid by the hegemon. More recently they are retrieved from payments by multinational business.

As is seen, the logic of the Balkan model fundamentally differs from the traditional transatlantic one. Competition, the separation of economy and politics, existence of functioning political and social control devices is fundamental for the competition state. These systems are not valued by the alternative model, on the contrary. These institutions were introduced without conviction after 1990 and they were rolled back immediately after the political goal of their introduction (mainly EU-membership) was achieved. This process is said to be justified and also covered by rhetoric of economic patriotism.

Retreat was also made possible because institutions of the competition state could not get embedded deep enough in local societies mainly due to the historic Byzantine heritage. No substantial social protest or fundamentally different political alternative is seen. The deliberate destruction of the political and social control devices also serves this purpose. The public opinion is strongly influenced by the government propaganda spread by the monopolized mass media news. Disinformation of the mass contains political attacks against non-existing or hugely exaggerated problems that are delivered as threats. Among others we can see again issues of ethnic rivalry.

The applicability of the Balkan model may vary among countries. In a sense the three points describe the archetype of the model. It certainly applies for the countries belonging to the former Hapsburg and Ottoman empires with the potential and partial exception of Austria, Czechia (because of their longer democratic traditions and stronger institutions) and Slovenia. On the other hand, much of the essence of the three points applies to some extent in other ECE transition economies (most importantly Poland).

It seems, that there is a main division line between the analyzed ECE countries and their model and the post-soviet countries (less the three Baltic countries). The unhealthy

business-polity linkages and rent seeking are widespread also there, but the disciplinizing power (e.g. the role of the European Union as an anchor) does not play a role. Instead in most countries the Russian authoritarian influence dominates. Due to less political, social and external (international) control cronyism, rent seeking and corruption is even higher there than in ECE. Most of these countries are resource abundant or are supported by Russia (external finance).

3. Fundamentals of the rent-based economy

Our conception of the rent-based economy of the Balkan model uses the recent research findings of Mihályi and Szelényi (2017; 2019). Their main concern is the separation of profits and wages on the one hand and rents as income source on the other. The differentiation is crucial because the levels of profits and wages are determined by the market process and competition in a positive sum game situation (dynamic efficiency). In comparison rents exhibit a zero sum game: rentiers increase incomes at the expense of others. Rents do not deliver incentives to economic agents and therefore they deteriorate the allocative and dynamic efficiency of the economy. Rents were essential parts of all pre-capitalist societies. The exceptional historic acceleration of economic development occurred when the traditional feudal sources of rents (privileges) lost importance and non-privileged classes of the society took over the command in the economy. The Weberian entrepreneurship succeeded in the transatlantic world, however, this does not mean that rents disappeared altogether. Mihályi and Szelényi (2017) argue that certain types of rents (e.g. in the social security system) they even play an important positive role in stabilizing the society. But rents should be only secondary sources of income behind profits and wages. As it was already mentioned, the rent-based economy does not share the values of the competition state: separation of the spheres of business and politics, political and economic competition, political and social control over politics and business. The primary goal of the system is the opposite: the creation of close ties between the two spheres and capturing the business by a usually autocratic political regime.

Business-polity linkages have always been present not only in transition economies, and there have been frequent personal overlaps among business and political elite. This

is not transition specific issue. Stark and Vedres (2012) collected a number of cases from US and European economies to evidence existing relationships even personal overlaps in most liberal market economies like the USA or Germany. But long periods of democratic development strengthened political and market institutions there. In their case there is appropriate civil control and the relationships cannot be used for open exchanges. Business is also stronger and its competitiveness is less dependent from political and state support than in V4 and other transition economies. Therefore, polity and business remains institutionally separated securing political and economic competition, the existence of competition state. However, circumstances of formulating political democracy in transition economies differed largely from the West-European democracies' types of ECE political institutions. "The stable party competitions and Weberian states of post-war Western Europe were founded on strong elite commitments to democracy and socially embedded through sustained productivity growth and universally rising living standards. But those conditions never existed in Central Europe. Consequently, their states were not consolidating as those of post-war Western Europe..." (Innes, 2013, p.1.). These countries' political development followed therefore different model that made the region particularly vulnerable.

The archetype of close business-polity ties is state capture. It is defined as a type of systemic political corruption when private interest significantly influences the decision-making process of the state to its own advantage through unobvious channels that may not even be illegal (Kaufman and Vicente, 2011). The influence is carried out through a variety of state institutions including legislature, executive, ministries and the judiciary. Unlike simple corruption where the outcome is not certain, in case of captured state the outcome of a decision is known and is almost certainly beneficial for the captors of the state. While in case of simple corruption there is plurality and competition of corruptors to influence policies, in case of captured state decision makers are usually in a position of agents to the principals (the captors) and are in monopolistic position. The level of corruption in this case depends on political power relations and parliamentary control, as well as on efficiency of civil control. Weak political parties and state institutions are frequently captured by wealthy business producing situations of more "traditional" corporate state capture (Hellman et al, 2000).

Using the World Bank Governance Indicators (control of corruption) Innes (2013) differentiated two groups of countries in ECE concerning the type and degree of state capture. The Czech Republic, Slovakia, Latvia, Bulgaria and Romania proved to be more vulnerable and could not reduce the risk level even after their joining the EU. Estonia, Slovenia, Poland and Hungary scored better in the period between 1996 and 2011. However, both Poland and Hungary saw deteriorating control of corruption performance during the “duration of notably anti-system governments, those of Law and Justice in Poland (2005-7) and FIDESZ in Hungary (2010)” (op.cit. p.3.). Similar decline was reported for the “government effectiveness” indicator. This tendency meant that these two countries approached the inherently weak positions shown by the first group of countries³. This development is in deep contrast with the all too optimistic predictions about the consolidation of ECE states, which was based on expectations of Western-like robust competition between political elites (regulated by the social consensus on democratic values of the post-war area there).

I think that the fundamental difference of the starting point of democratic institution building in Western Europe and in ECE, as well as differences in economic development and welfare generation (as primary social task) can largely explain differences in current day developments between East and West. But in order to understand the split in ECE, as well as to obtain a dynamic perspective for the process, further details need to be elaborated. Split between various ECE countries concerning levels of state capture and corruption in the first period of the transition process can be explained by pre-transition political development, the existence or absence of dissident oppositions and reformist groups (Gryzmala-Busse, 2007). In the successor states of more orthodox communist regimes reluctance to build more strictly regulated state institutions did not only provide large private benefits for parties but created a system of long-term incentives for primarily entrepreneurial party behavior. “What followed was less the incidental exploitation of the state than the evolution of parties into brokerage firms, a ... systematically corrupt development.” (Innes, 2013, p.6-7.). This self-reinforcing system did not allow these countries of the first group to improve state-building capacities even after 12 years in EU membership.

³ Latest development in the indicators is shown on the charts in the Appendix.

In my view, erosion of the political advantages of reform-socialist countries and the deterioration in state building capacities particularly in Poland and in Hungary can be attributed to declining party competition due to failure and collapse of competing program parties mainly on the left (but also on the right like Hungary's MDF). This is also in contrast to more stable political systems of the West, where party crises do not lead to long-term decline in political competition unlike in Hungary after the collapse of the Hungarian Socialist Party. Party failures in ECE can be largely attributed to failed government policies based on program promises of parties that could not be fulfilled because they were more ambitious (after the West European models to be copied) than what ECE economies could afford. Kornai (1992) drew attention very early to problems of "premature welfare state" in ECE warning for accompanying fiscal difficulties.

Besides of the fiscal hazards of too high election promises a further important feature of ECE political systems contributed to the unexpected collapse of several ideological parties. Kopecky (2006) found that political parties in ECE had weak ideological underpinnings and their voters revolved among parties in large share and rather frequently. Ideological values were hardly transferred to the general public. In the first phase of the transition process dominantly liberal ideological values were transmitted based on de facto consensus among the main political parties. Later this consensus was broken and other traditional values and also populist promises started to replace the neoliberal agenda. The weak ideological determination of voters and the consequently high degree of revolving strongly contributed to the failure and collapse of program parties. Program parties were stronger in countries with dissident and reformist-led parties, where leaders of these parties retained ideas stemming from pre-transition political era (Poland, Hungary). Cohen (1999) called supporters and leaders of these parties "ideological elites" (with various nationalist, social-democratic, liberal, etc. background). In contrast to ideological elites and their program parties Cohen wrote about the "mass elite" to describe a political elite with the characteristics of the mass, the average voter. This elite is militantly repressive to communism but is ideologically not committed and is motivated rather by short term personal self-interest (Cohen, 1999, pp. 5-6), and form "business-firm" parties.

ECE business-firm parties were formed by members of the political "mass elite" rather than by business representatives seeking for political influence like many of the

populist parties of Western Europe (e.g. Forza Italia). This process was described for the Czech Republic by Innes (2013) and Romania by Schoenman (2014). Such parties got established by monopolizing and stripping state resources and information and protected their positions by disabling existing formal state oversight on government actions, and weakening social and civil control. An important tool of maintaining their influence was patronage, the support of clients using monopolized state resources.

Parties with ideological commitments developed into electoral-professional parties with some historical roots, seeking to maintain credibility of their normative ideological identity. However, like their West European counterparts, program parties faced important political and economic challenges when in government. In many cases, due to these challenges the important pillar of the competitive structure the social democratic left was knocked out by deepening fiscal constraints of competition for lower income voters. Details of the process were described by Innes (2013, pp. 14-19). With the change in party system party state capture quickly followed from the side of business-firm parties using nationalist appeals requiring the renewal of the state and closing down failed democratic competition. Strong role of the “mass elite” in the first group of ECE transition economies, and their advance in more competitive political systems indicate that party state capture may continue increasing.

4. The retreat of the ECE region to the Balkan model

In this section empirical evidence is collected mainly from Hungary and Poland on three main aspects of the Balkan model. These two countries were regarded champions of the transition process during the 1990s. During the 2000s the institutional development of the competition state lost momentum here. Instead elements of the Balkan model were introduced and/or strengthened. First the process of business capture and steps of rolling back of the institutional background of the competition state are described. This is followed by the description of the emerging business rationale, the rent based economy of the model. Finally I collected three small case studies of ethnic conflicts to illustrate how public attention is driven away from systemic rent seeking.

Monopolization of politics and business: business capture

The overall decline of the neoliberal suit and the advance of “business firm parties” was a straight consequence of the 2008 crisis that shook beliefs on the theory’s omnipotence (Appel and Orenstein, 2018). Traditional program parties of the transatlantic world lost credits because of this failure and also because of the shrinking material base of welfare institutions (Szanyi, 2019). Traditional political program parties’ popularity declined especially much in the ECE region, where their positions began to erode even before the 2007/8 crisis. Business-firm parties as defined by Cohen (1999) gained high social support. Already prior to the 2008 crisis right after obtaining their EU membership ECE’s business-firm parties and their governments started eliminating the compromises that were made at the expense of national sovereignty. Newly emerging populist parties have been led by charismatic leaders. FIDESZ-Civic Party in Hungary is led by Viktor Orbán, the party of Law and Justice (PiS) in Poland is led by Jaroslaw Kaczynski, Action of Dissatisfied Citizens (ANO) in Czechia by Andrej Babis. These politicians became prime ministers and made attempts to change the system of competition state to a more authoritarian regime. Their program suggested the defence of national interests and the completion of the transition process without the compromises made in favour of the incumbent post-communist elites. At first sight these goals were interpreted as a correction to the liberal competition state model (Drahokoupil, 2008), as well as their replacement with a new system that concentrates on strengthening the local bourgeoisie and national sovereignty against foreign influence.

V4 countries had made important steps towards the establishment of a fully fledged liberal democracy and market economy, the transatlantic competition state model. Their retreat is somewhat surprising but not unexplained. In the case of ECE societies the imprinted behavioural patterns and convictions have been less supportive for liberal democratic values than in case of classic democracies. ECE history shows continuous shuttling of the countries between the Western liberal democracy and Eastern autocracy (the ECE pendulum). Poland’s Pilsudski era and Hungary’s Horthy regime were autocratic regimes run by charismatic leaders, despite of their functioning parliaments and political party systems. Elements of appreciation towards these autocracies is present also today. The current departure of Hungary and Poland from the concept of

liberal democracy can be interpreted as returning from democracy to historic autocracy. Even some visible elements of the predecessor regime 80 years earlier is reconstructed, such as Kossuth Square's Horthy-era layout (the square in front of the parliament building in Budapest). The ECE pendulum can also be treated as a normal function of ECE societies, hence, the current concept of illiberal democracy⁴ is not unprecedented. However, in some ECE countries, especially in Czechoslovakia the democratic track record was longer and included the 1920s and 30s⁵.

An important area of increased national sovereignty is regaining control over the economy from multinational business. An effective tool of this ambition is renationalization of multinational firms' property (Szanyi, 2019a). During and after the 2008-9 crisis ECE countries' governments have gone against the current and did not limit increased state economic intervention like their Western counterparts, but rather continued and even increased it after crisis shocks eased. This has been manifested for example in public property management. Poland was reported to have undertaken steps aimed at strengthening statist policies in state property management. Some of these measures were already taken by the Civic Platform before the crisis (Naczyk, 2014). The currently reigning right-wing populist PiS government continued and expanded this policy. In Hungary, the populist FIDESZ government also introduced protectionist policies in favour of local businesses that run counter to various EU regulations (mainly in the field of competition policy). But Mihályi (2015) showed that the socialist governments of the 2000s had also pursued interventionist policies. Thus, the departure from the neoliberal suit started before the crisis both in Hungary and Poland. The tendency can be interpreted as a general political and societal reaction to the crisis of the far reaching application of neoliberal policies. It revitalized the socially embedded appreciation of various forms of state paternalism that was depressed during the first decade of ECE's transition. Another important purpose of economic patriotism in ECE is the reconfiguration of power relations among various elites. The Hungarian case shows

⁴ The term was introduced to political science with pejorative connotation by Fareed Zakaria: 'Democratically elected regimes... are routinely ignoring constitutional limits on their power and depriving their citizens of basic rights and freedoms....we see the rise of a disturbing phenomenon in international life - illiberal democracy.' (Zakaria, 1997, p. 22)

⁵ Despite of this, Cisar (2017) reported that trust and appreciation of democratic institutions in Czechia has been also low allowing the populist ANO to win the support of especially the young generation voters on the 2013 elections. Similarly to Poland and Hungary, traditional parties also lost much of their popularity due to serious corruption scandals.

that selective measures have been applied to favour particular agents. The aim of such steps is not the conveyance of a general backing for the broad citizenry, but the promotion of selected clients and members of politically loyal local elite.

The dominance of the polity over the economy that Yakovlev (2006) called business capture has been enhanced by the monopolization of political power. In order to maintain political monopoly, governments of the 'business-firm' parties in ECE begun rolling back democratic political institutions. Kornai (2015) described the process in Hungary. The Hungarian case can be regarded as an archetype of restructuring towards the Balkan model, since the distinguished majority of the governing party allowed the government to fundamentally change the legal system. The constitution was rewritten and passed by FIDESZ MPs' 'voting machine' in the parliament. Smaller majorities of other ECE countries did not have the same opportunities to reconstruct the legal system in line with their interests. In Hungary, the executive and legislative branches were essentially fused and they became controlled by the governing party through personnel changes. The constitutional court, the state audit office, the fiscal council, the competition office, the monetary council, the National Bank of Hungary, the ombudsman's office as well as the central statistical office was filled by loyal personnel.

The new constitution was complemented by 32 so-called cardinal laws passed by the super majority in the parliament (Kornai, 2015). It allowed the governing party to change any law, whenever required by its political or business interests. Thus, people in power are now above the law. In several cases laws were changed retroactively to justify unlawful, fraudulent actions of party members. All this undermined the basic principles of the rule of law. Jurisdiction had also been put under party control. The Chief Prosecutor was chosen and appointed by the prime minister and approved by the parliament's voting machine. The prosecution service regularly rejects the investigations on fraudulent cases of the governing party's members or their cronies. Members of the Supreme Court as well as of the judicial colleges were also selected in a partisan manner: a 2018 law reduced the age threshold of active judges from 70 to just 62, expelling the older less loyal generation from duty. Poland's populist PiS government also introduced many of these measures recently (Błaszczuk, 2017).

Properly working democracies have a second political control system as well. Besides the inbuilt checks and balances (the legally incorporated control devices), civil society organizations also play an important role. NGOs are regarded by business-firm party governments as public enemies. Witch-hunting originates in Russia, but it was soon carbon copied in Hungary, later also in Poland. Hungarian government-controlled mass media launched massive campaigns in 2014 stigmatizing NGOs as enemy agencies of foreign powers. The hate rhetoric was not disturbed by the fact that many of the affected institutions were sponsored by NATO- or EU-allies of Hungary. No consideration regarding their scope of activities was made either: NGOs in the field of poverty reduction, education, preservation of the Hungarian cultural heritage were treated in the same manner as anti-corruption organizations. Any support that came through uncontrolled mainly foreign channels was suspicious. The stigmatization of foreign-sponsored civil society organizations was reinforced through legal actions as well⁶.

Viktor Orbán's almost unlimited political license was used for the destruction of democratic institutions and the manipulation of public opinion in Hungary, in order to cement his and his cronies' political leadership. This continued despite the loud, but rather inefficient protest of local opposition and the international community. Unfortunately, similar tendencies and practices emerged in other ECE countries as well. This process indicates a kind of common systemic similarity, the impact of the Balkan model in the region (weak democratic institutions and historical precedents of autocracy). The process of destruction was less pervasive in Poland, mainly because of the Polish government's limited power. Nevertheless, the PiS government openly declared that it would love to copy the Hungarian authoritarian development pattern (Budapest in Warsaw, Naczyk, 2014). Blaszczyk (2017) provided a comprehensive list of the antidemocratic measures taken by the Polish PiS government that show considerable similarity with the Hungarian measures. The Polish constitutional court and the judicial system at large, the competition office as well as the Polish financial supervision authority were weakened when their scope of action was curbed and key positions were filled by cronies of the government. The Hungarian example was also copied through actions against the free media, the weakening of NGOs and in the

⁶ For further details on how Viktor Orbán has destroyed democratic institutions and established his system of patronage in Hungary see: Kingsley, 2018 or Kornai, 2015.

centralization of public services from local governments to nation-wide institutions (health, education, and utilities).

Destruction of the rule of law and public support of corruption is present in other ECE countries as well. In the case of Romania for example, Tudorel Toader Minister of Justice suggested the firing of Laura Codruta-Kövesi, president of the Romanian Anti-corruption Prosecution (DNA) in February, 2018. The main objection against her was DNA's overstepping its role, when she initiated prosecution with regard to the passing of a government decree in January, 2017, a measure that lifted prosecution control on corruption cases less than RON 200.000 (EUR 50.000) value. Essentially this amendment of the penal code can be interpreted a quasi-legalization of small-scale corruption. Other objections included her non-loyal behaviour and the accusation that her actions caused the defamation of Romania abroad. The Romanian President first rejected the minister's request, but a few months later Codruta-Kövesi was dismissed by him. This case illustrates also the fundamental clash of the transatlantic and the Balkan models. Despite of loud protests by the Romanian government dismissed Codruta-Kövesi was appointed the first Chief Prosecutor of the newly established European Public Prosecutor's Office on 14 October 2019.

Hungarian and Polish governments were also active in demolishing market economic institutions, first of all the rule of law, which they replaced with a patronage system. State property management stood out from this respect. In a previous paper I pointed out that privatization logic's reversal aimed to achieve the transition process' opposite (Szanyi, 2016a). During the 1990s, privatization was reinforced not only to create responsibly acting market agents, but also to reduce the state's economic involvement to prevent the survival of paternalistic links between business and polity (Szanyi, 2016a). The reversal of privatization's logic meant an increase in the size of the state sector so that the system of patronage could capture a larger part of it. I call this practice business capture. In general, business capture has devastating effects on property right enforcement and the rule of law. Rapaczynski (1996) emphasized that state property management practices and governments' track record concerning private property (especially forbearance from encroachments) played an outstanding role in strengthening the soft social institution of property right enforcement and obeying the law. Expansion of the state sector sends a bad message to the market, especially if it is

achieved by curbing private property rights. This is exactly what has happened frequently in both Hungary and Poland (Voszka, 2013; Kornai, 2015; Szanyi, 2016a, 2016c; Mihályi, 2015; Baltowski and Kozarzewski, 2016, 2017; Blaszczyk, 2017).

Changing forms of rent seeking⁷

Less political competition in the V4 resulted in spreading state capture. This process opened new opportunities for rent seeking and legalized corruption. This does not mean that corruption was absent in the previous more competition based period, nor does this mean that program parties of the ideological elite would have been free from it. What is new is the form and pervasiveness of rent seeking, which has become institutionalized when business-firm parties captured the state. Material rents stemming from political power positions occur in all political systems. The extent of the rents and the forms of rent seeking vary. They depend on the efficiency of political and social control, and the existence and quality of democratic institutions. The prevailing private interest must be curtailed by control devices. However, effective control does not eliminate the drivers. The transition process in East Central Europe could be interpreted as a competition for the redistribution of economic power. Privatization meant the redistribution of existing assets. The process was designed and executed by state institutions. It was the first main area of competition for personal enrichment through state agencies in transition economies.

This early transition period was dominated by the concept of the competition state. The leading elite served the transition process according to the international advising community's neoliberal principles. The main social and political aim was making systemic change irreversible. ECE governments collaborated with the "reformers". The 'comprador elite's' material wellbeing and enrichment was based on the existence and strong influence of multinational companies. Salaried positions in firms, their advisory background institutions' as well as in banks' boards and in their management were provided. Business and administrative positions were filled and there were regular exchanges of personnel between administrative and business positions (Drahokoupil,

⁷ This section relies on parts of another paper, Szanyi, (2020)

2008). The main beneficiaries of this setup were the segments of the elite which supported multinational business to gain influence in ECE countries.

Later on, the main areas of rent seeking shifted from property acquisition and tunnelling, or entering the interest sphere of multinational business popular in the 1990s' privatization to another area: controlling and running enterprises. As it was shown in the previous section of the paper the privatization logic was reversed during the 2000s. Slowing privatization in Poland and nationalizations in Hungary were aimed at maintaining and expanding the influence of the party-controlled state, while ensuring rent seeking from state owned enterprises (SOEs). In this period, state ownership served the enrichment of other elites that previously did not join the 'comprador elite group'. Of course, the limits of available state assets to be privatized also contributed to this. Remaining state assets by the late-2000s were mostly loss-making companies (like mines in Poland) that were not worth owning. Another group of firms, the large service providers could not be easily transferred to rent seeking private hands. Nevertheless, they were very much suitable for large scale milking. As third, the spread of partisan firms alongside SOEs has been a new development of the 2000s. Politicians and their clients directly control significant parts of private business. This sector is also used for rent seeking.

Stark and Vedres (2012) conducted a survey with data including 1696 large and medium sized companies in Hungary for the period between 1987-2001. Party members and cronies took controlling positions in less than 10 % of the firms at the eve of the transition process in 1989. This number steadily grew to almost 20 % by 2001. In terms of capitalization, the share of politicized firms grew from less than 10 % in 1989 to over 40 % in 2001. The authors differentiated between the political influence of the then competing main coalitions (right and left) and found that after elections, winning parties' influence increased and losers' declined. Similar empirical findings were reported for Czechia by Skuhrovec (2014). However, the magnitude of these fluctuations declined over time. They became less dependent on government changes. In my interpretation this meant a marked shift from control over SOEs, towards privately owned companies – the management of which remained largely immune from political changes. Stark and Vedres (2012) also show that struggle over dominance of SOEs became a less significant way of combining political and economic power by the end of

the 1990s. Besides multinational firms' influence, partisan private firms started to capture the lion's share of politicized business in Hungary during the 2000s.

During the first decade of transition in post-communist ECE economies democratic and market institutions evolved, business and political systems were largely separated, albeit they influenced each other. Firms competed for capital, labour, suppliers and customers, parties competed with each other in democratic electoral system for political power in order to fulfil their programs. The main assumption of this view (the 'legacy concept' elaborated by Stark, 1996; Stark and Bruszt, 1998; Eyal, Szelényi and Townsley, 1998) was that increasing sophistication of the two institutional systems will lead to declining business-polity interaction that was regarded a main risk of the systemic change, a potential route from 'plan to clan' instead of 'plan to market' (Stark, 1991). The clan-concept returned in the analyses of the transition during the 2000s, but in a completely different setting (Stark and Vedres, 2012; Sallai and Schnyder, 2015). Business-polity relationships intensified and featured new characteristics: increasing political and material rent seeking, polarized character, large-scale personal entanglement, coevolution of political and economic structures. The concept of sharply separated fields of business and polity was undercut in the two spheres. Business needed insider knowledge and government support in its competition to expand its markets (e.g. in public procurements). Meanwhile, polity needed funds for party financing, election campaigns and rewarding political allies and clients. The coevolution process meant a development of occasional transactions towards long-term alliances. While the economic and political fields remained institutionally separated, firms and parties became organizationally entangled. The business capture concept reflects the dominance of political parties over significant parts of the economy (Yakovlev, 2006).

After 2010, the Hungarian government started to increase government control over multinational business as well. An attempt was made to split the strong representation of foreign firms and undermine their political influence. The Hungarian government introduced selective advantage and disadvantage measures (Szanyi, 2016). In many cases, measures introduced intended to support allied Hungarian partisan firms' market positions against foreign-owned competitors (e.g. in retail trade and banking). But selected multinational firms were also treated as 'friendly business'. The 'strategic partnership program' of the Hungarian government re-established the lobbying

platforms of selected foreign firms. In exchange, the government requested support for politically important programs.

Cases of current re-emergence of ethnic conflicts in ECE

Increasing corruption and rent seeking is covered by intensive government propaganda. As an illustration I picked three events of ethnic conflicts in the region all happening most recently in the Summer of 2019. Other topics have been migration, EU-related issues (e.g. the new budget as well as the EP election campaigns in 2019) or anti-globalization slogans.

Case one: interception of a Serbian military delegation from a commemoration visit of the Jasenovac death camp of Croatian Ustasha during WW 2. Yugoslavia was established in 1918 as Serbian-Croatian-Slovenian Kingdom with clear Serb dominance and was dissolved in and after 1992 in the bloody Yugoslav war. The history of the state was plagued by ethnic conflicts from the very beginning. Most brutal violence of the uneasy partnership in the multiethnic country happened in 1928 as a Montenegro MP shot dead three Croatian MPs in the parliament assembly hall. Violent conflicts repeated throughout the short history of the Yugoslav state most frequently in the WW 2 period when under German occupation the state ceased to exist. During this period nations of Yugoslavia fought against the Germans and also each other. Paramilitary troops were in use on all sides. The Croatian Fascist Ustasha state established death camps under German guidance where several thousands of Serbian civilians were massacred. Jasenovac was the most infamous of the camps. A Serbian military delegation wanted to visit the memorial place on 7th September 2019. They were not allowed to enter Croatian territory. Both countries' governments picked up the issue and made political declarations accusing each other with provocation.

Case two: Desecration of the Austro-Hungarian military cemetery in the Úz-valley on June 6, 2019. The Carpathian mountains had been the historic border line of the Kingdom of Hungary. In the defense of the border both in WW 1 and WW 2 many Hungarian, Austrian and German soldiers died here. One larger military cemetery is located in the Úz-valley. It was documented and described several times: since it was erected to the West of the front-line exclusively Austro-Hungarian and German soldiers'

corps were buried there. The area of the cemetery belongs to the territory of Csíkszentmárton municipality, a village populated dominantly by ethnic Hungarians. The community council kept the place clean and respectful. In April 2019 the village council of Darmanesti, the Romanian village at the Eastern edge of the Úz-valley let erect 52 concrete crosses in the cemetery to commemorate Romanian soldiers who fell in the same region and were buried eventually in Romanian cemeteries. The crosses were placed partly over existing Hungarian graves. The community of Darmanesti erected the object without having a license from the responsible construction authorities, moreover they did it in a territory that did not belong to that municipality. Ethnic Hungarians tried to block the consecration ceremony on June 6. 2019, but the gathered Romanians outnumbered them, successfully broke down the entrance and forcefully occupied the territory where then the orthodox pope delivered the ceremony. The Hungarian government protested against the multiple violations of existing laws and construction regulations. On 24 October, 2019 the major of Darmanesti decorated with a village order those who first broke through the Hungarian blockade in June.

Case three: Hungarian ministers' direct intervention in the Ukrainian parliamentary election campaign in July 2019. It is not only "true Balkan" countries that have been engaged in the process of mutual generation of ethnic conflicts. Hungary has not been an exception either. While in the case of the Úz-valley provocation Hungary's role was the defensive one, the Hungarian government also took the lead in other provocative actions. In the case of the Ukrainian parliamentary elections highly ranked Hungarian officials (the head of the prime minister's office, the minister of foreign affairs as well as state secretaries) directly campaigned for the candidates of the ethnic Hungarian political parties in the Zakarpatski region of Ukraine. The action called for protests from the Ukrainian side both officially and unofficially. After the Russian sponsored war in the Donbass region of Ukraine and the occupation of the Crimea, Ukrainian governments have been very sensitive when any of their ethnic groups seemed to threaten with the violation of the country's territorial integration. I can rightly understand that ethnic Hungarians do not feel like to fight for the Ukrainians' national interests in Donbass (several dozens of soldiers of Hungarian origin have already died there). Nevertheless, the personal appearance of highly ranked Hungarian officials in the election campaign events was regarded as direct provocation by the Ukrainian government and it also

violated the Geneva Convention. Ironically, the Hungarian action fired back on the Hungarian parties in Ukraine: no Hungarian politician won a seat in the Rada.

5. Conclusions

Up till the 2008 crisis comparative economics was strongly influenced by the belief in the omnipotence of the neoliberal economic thought. Political and economic developments of the past ten years in the ECE region (but also elsewhere in the world) called for the application of alternative concepts and analytical tools. The previous conviction of the superiority of the transatlantic world's competition state has changed. Mounting empirical evidence illustrated the rather sticky existence of alternative economic and social models and the hardships of replacing or at least reforming of them. This paper does not query the superior performance of the liberal competition state concept. It describes how parts of the ECE region's political elite utilizes the region's historically determined special circumstances for its own enrichment outside the rules of the competition state. This practice resembles historic development patterns of this European periphery that have always thwarted the economic and political convergence towards more developed parts of the continent. The ECE pendulum is still at work.

The paper is novel with its sketch of a rather stable local model of capitalism, the Balkan model. On the base line of this model the most important role is played by rents. They are created by political will, distributed among actors who are politically loyal and support the political supremacy of the ruling elite. Since rent is the main source of material wellbeing and only to a smaller extent profits, economic agents are more interested in competing for privileges distributed by the authoritarian regime than in any other productive form of competition. Therefore the Balkan model lacks the traditional competition driver of the transatlantic models of capitalism. Growth and limited prosperity are financed from external sources. Historically these sources were subsidies of regional hegemons. Today it is EU transfers and contributions of multinational business to the central budgets.

The political stability is also supported by limiting the knowledge base of the local society as well as manipulation of the public opinion through the monopoly over mass media. In the Balkan model important role is played by ethnic rivalry and conflicts in

this vein. Rent seeking and the intensity of ethnic conflicts and other problems that occupy the public media declines when the external influence of the actual hegemon increases. Nowadays it is mainly the European Union that can play an anchor role in the region. Unfortunately, the mounting functional problems of the European integration process reduces the disciplining pressure in the region. This evidently contributed to the reemergence of the ethnic conflicts and increasing rent seeking.

The new “mass” elites of the region formed business-firm parties that could effectively monopolize political power and also capture much of the business with the help of populist policies. Weak political and social control institutions could not prevent this. They themselves fell prey of the establishing authoritarian regimes. Paradoxically, political attacks against them also became part of the manipulation campaign over the public opinion. The weak political cautiousness of the society is also a historic feature in the region. The business-firm parties in power used their mandates for rolling back the democratic political institutions as well as basic market economic institutions: the primary control devices over their rent seeking practices. By doing so they made extensive damage to their societies’ responsiveness towards the principles of the competition state.

World Bank’s Worldwide Governance Indicators illustrate rather clearly the main message of this paper (see them in the Appendix). The set of six measures crucial from the transatlantic capitalist model’s viewpoint are displayed by the indicators⁸. Bulgaria, Romania and Serbia usually score in the 40-60 % range. This means that roughly half of the countries in the observation list perform better. Hungary, Poland and Czechia score between 60 and 80 %. The difference is rather obvious. The paper explains the relatively low features of the three Balkan countries with the less efficient performance of the Balkan model. However, the Visegrad countries, especially Hungary and Poland showed markedly declining performance in several indicators during the last two decades. In my interpretation this is the result of rolling back the institutional system of the transatlantic competition state in these countries. The choice of the Balkan model deteriorated the quality of institutions.

⁸ The measures are: Voice and Accountability, Political Stability and Absence of Violence/Terrorism, Government Effectiveness, Regulatory Quality, Rule of Law, Control of Corruption. They are all aggregate measures.

Szanyi and Szabó (2020) described the effect of the ECE pendulum on historic development trends in the ECE region. The conclusion of that paper was that the authoritarian development periods provided stable, however rather slow progress. More liberal periods were rather controversial: drawbacks of the Balkan model did not allow the full utilization of the buoyancy of the competition state. This happened also to the transition process. It was half-hearted, corruption plagued and did not bring the expected results in terms of convergence with the material wellbeing of the benchmark West-European countries. But the historic pattern will continue also in the future, the pendulum will sooner or later move back towards a more liberal environment. A new try can be made.

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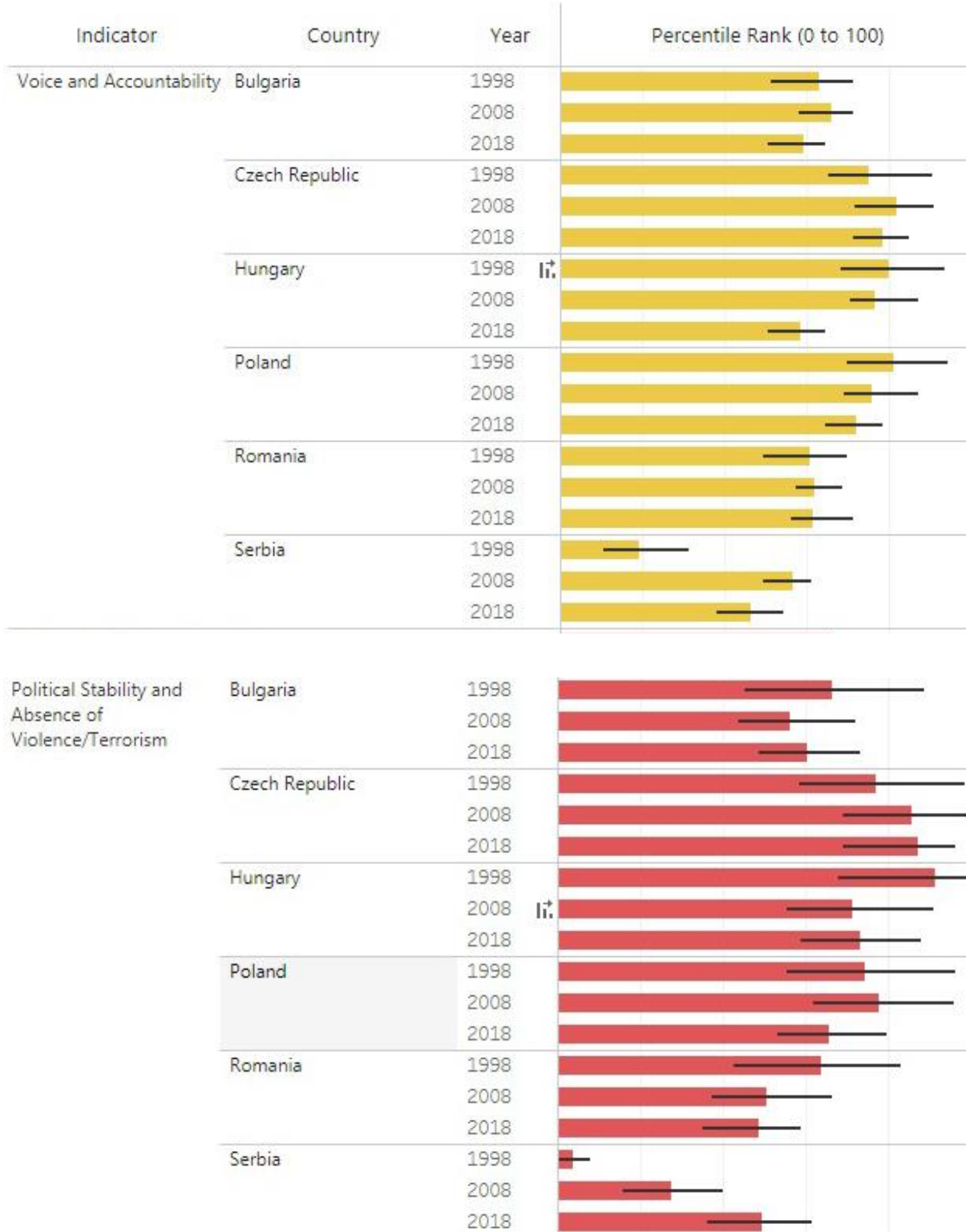
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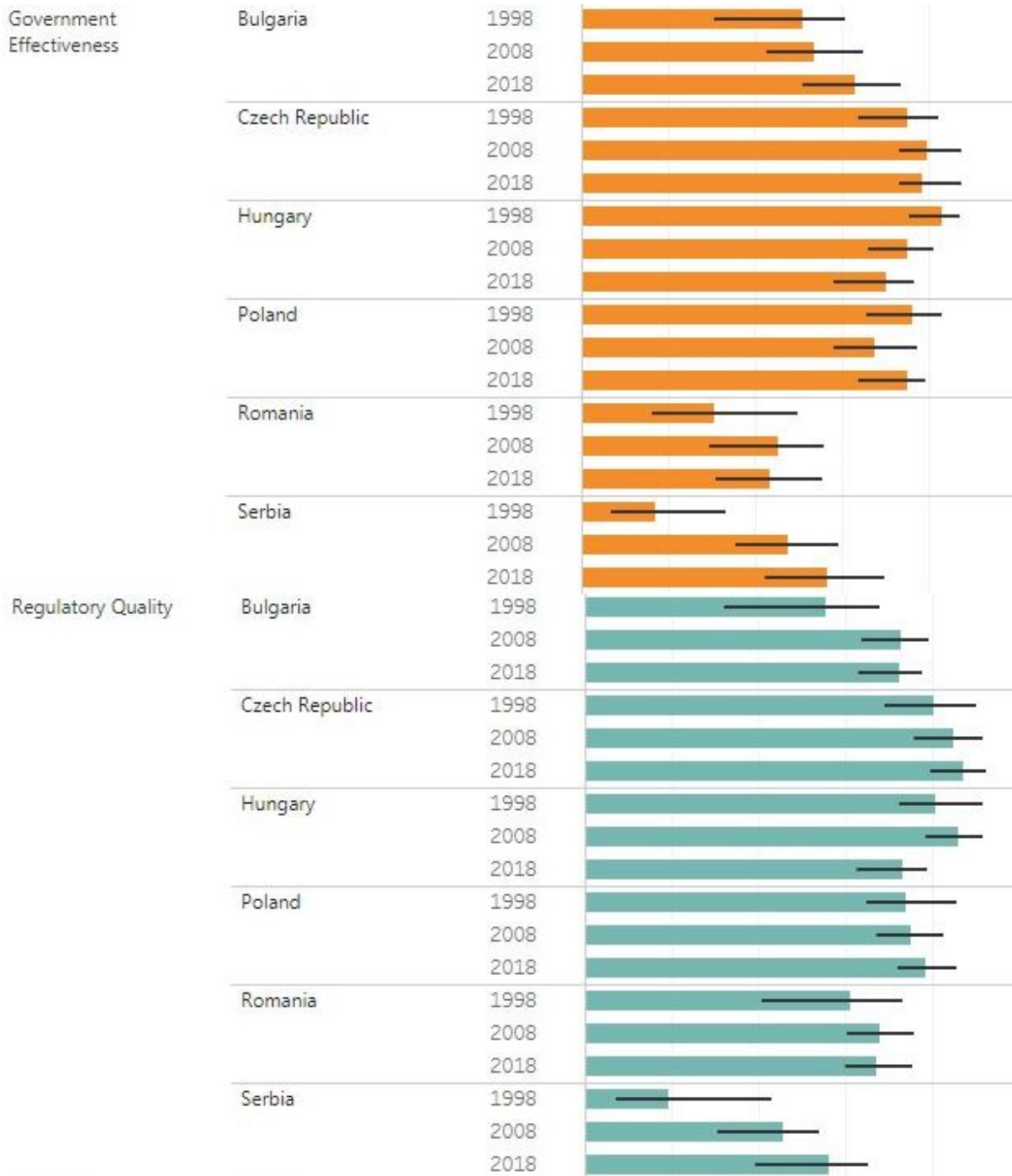
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Appendix

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