THE REVERSAL OF THE PRIVATISATION LOGIC
IN CENTRAL EUROPEAN TRANSITION ECONOMIES*

(An Essay)

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The main ambition of this study is to explain the unexpected change in the transition process of some Central and Eastern European (CEE) countries starting in the second half of the 2000s. Special attention is paid to changes in and the attitudes of governments toward state ownership. Although statist approaches gained momentum in the economic policy of various states in and after the 2008/2009 crisis, this did not mean a fundamental reorientation expressed in changes in the main economic conditions such as ownership patterns. Nevertheless, governments in some CEE countries seem to flirt with such ideas too in the general policy of increasing state economic intervention. The privatisation process was stopped and in a number of cases, formerly privatised assets were re-nationalised. Governments strengthened their influence in the governance structure in mixed-ownership companies. The main body of the present paper provides a better understanding of this change in state property policies. We also call attention to the risks of a reversal of the privatisation logic. An increasing role of the state as proprietor may today strengthen similar negative political and economic consequences and risks as the ones against which the privatisation agenda of the 1990s was suggested. It can reduce competition, give way for political and personal rent-seeking, and weaken the functions of market economic institutions.

Keywords: Central and Eastern Europe, privatisation, public property, crony capitalism, rent-seeking, varieties of capitalism

JEL classification indices: D72, H82, P16, P31

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1. INTRODUCTION

An important school of the comparative research on the economic development of Central and Eastern European (CEE) countries evolved within the broader framework of the Varieties of Capitalism (VoC) literature, with the most frequently cited contribution by Hall – Soskice (2001).1 Among the many ensuing contributions we find analytical ones that compare various quantitative measures of the systemic features of capital and labour markets, education, social security, and innovation systems. CEE countries were repeatedly tested whether they fitted in one or another existing model, or whether they should be rather treated as a separate model. Research results were rather mixed.2 Another string of literature used the political economy approach and concentrated on the interplays between polity and economy during the transition process. Authors of this approach (King 2007; Bohle – Greskovits 2007; Blanke – Hofmann 2008; Schoenman 2014) state that the establishment of political and market economic institutions and the redistribution of political and economic power went hand in hand. Therefore, the concrete layout of the systemic elements of the market economies largely depended on social and political developments in the transition process. Some authors emphasised different features of the transition economies and tried to work out various models for CEE (Bohle – Greskovits 2007; Lane 2007; EC 2008; Rodrigues 2009). Others concentrated on strong similarities and argued that there was little difference among CEE countries, but rather a significant gap between countries in Central Europe and the post-soviet countries (Lane 2007; Csaba 2007; Szanyi 2012). The main drawback of the approaches concerning the CEE economies is that they do not provide a positive description of the CEE model.

Nölke – Vliegenhart (2009) wrote an important paper in which they tried to conceptualise the CEE economic model. They picked out the role of foreign direct investments (FDI) in shaping the structure of the emerging market economies of the Visegrád countries (Czech Republic, Hungary, Poland, and Slovakia). They argued that the high share of multinational companies in the production and trade of these economies strongly influenced the development of certain other economic and social sub-systems as well. Their impact on national innovation and education systems was negative because their operation did not need high-end inputs from these systems. Furthermore, strong bias was exercised on a variety

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1 They distinguished between two main models, the Anglo-Saxon and the continental model.
2 For an excellent overview of the relevant literature, see Farkas (2011). Her paper also contains a rather comprehensive econometric analysis of quantitative variables of the above-mentioned features.
of national policies since multinational companies’ tax reliefs deprived governments of financial tools, and also because their operation was largely independent of national policies. Nölke – Vliegenhart called their CEE model the dependent market economy model (DME). The DME model was criticised for the limited scope of analysis, for the lack of a comprehensive approach of the determinants shaping national systems (Szanyi 2012). Nevertheless, the DME model was the first contribution that elaborated one major systemic element of the CEE economic model.

In an earlier paper (Szanyi 2012), I listed a number of factors that shaped institutions and influenced economic performance of CEE in addition to FDI. The most important of these was the state. In the present paper, I would like to contribute to the DME model with the analysis of one important aspect of state policies: direct economic intervention through publicly held enterprises. The importance of the issue has been highlighted recently through various statist government measures mainly in Hungary, but also in some other CEE countries. They have been aimed at changing the FDI-dominated status quo and increasing state influence. The most striking among these steps were aimed at a revival of direct state economic intervention through state-owned enterprises (SOEs), which were never privatised.

The Hungarian government, for example, repeatedly declared its intention to increase national ownership in so-called “strategic” sectors like banking, retail trade, media, utility service providers, and certain manufacturing branches. Through the nationalisation of the assets of private pension funds, it acquired a minority share ownership in a large number of companies. This ownership share has been further increased in some firms (e.g. Rába, MOL) through additional share purchases. The state also acquired various banks and utility companies (electricity, water, and gas). In Poland, through the more sluggish privatisation process, substantial state ownership remained and privatisation was significantly decelerated after 2011 (Baltowski – Kozarzewski 2015). Moreover, the Polish government also nationalised at least partially the assets of private pension funds (Financial Times 2014). But the state spared ownership positions in several hundreds of Czech companies as well and there is no sign of further privatisation ambitions in that country either.

State and public ownership is not unknown in any established market economy. Corrections for many types of market failures can be most easily achieved by the public provision of certain services. Also, one of the main instruments of the developmental state are the SOEs. If we look at the ownership structure of coordinated market economies such as Austria or Germany, or mixed market economies (France and Italy), we find a large number of SOEs in each of these countries. Although the de-nationalisation of the state-owned sector was on
the agenda in several countries in Europe (UK and France) and in the Americas (Mexico and Chile) especially during the 1980s, these privatisation deals rather concerned individual companies and not complete economies. Unlike in transition economies, they were not part of a systemic change.

Privatisation in transition economies on the other hand was always regarded as a key element of the transition process. The usual tasks and properties of SOEs were overshadowed by the political and institutional goals of transition policies. They were determined by the neoliberal mainstream ideology, which was transmitted by the international financial institutions and development agencies. Privatisation was regarded as a tool for increasing the popularity of the transition process too (Appel 2004), either by the usage of give-away type privatisation methods, and/or by ideological and political (anti-communist, nationalist) argumentation. In Hungary, the economic reform traditions provided a very fertile soil for pro-market arguments. In Poland, the privatisation process was based on stakeholder consensus rooted in the strong self-management desire of the Solidarity movement. Variations between the privatisation policies in CEE were reflected in the well-known gradualism vs. shock therapy debate, which was mostly about the social acceptance of transition measures and the potential threat of reversal by opposing “nomenclature” and incumbent communist political forces.

The strong political charge of privatisation and the equally strong neoliberal influence on the transition process resulted in a high emphasis on the speed and depth of privatisation in CEE, regardless of the actual technical solutions (voucher scheme, insider buyout, or sales method). Not surprisingly, according to the EBRD transition reports, over two-thirds of GDP production in all CEE countries was private by the end of the 1990s, regardless of the substantial differences in privatisation policies (Schoenman 2014). Similarities continued also later on, for example after 2000, when disappointment in the results of the transition process swept over the CEE transition economies. Privatisation was then a major area of debate, the general public opinion regarded it as organised theft (Appel 2004). More serious, albeit not quite nuanced critics also characterised the transition process of the 1990s as a period when free market ideology had been aggressively pushed onto post-communist governments (Stiglitz 1999). Appel (2004) argued that the role of ideology in post-communist economic policy-making was much more nuanced than what is reflected in earlier debates and later criticisms. She called for the considerations of the individual and group interest of agents, “the beliefs and preferences of actors on the ground deserve much more recognition than Stiglitz allows for” (p. 6). Thus, while the overall attitude towards transition

\[3\] For a good summary, see, among others, Roland (2000).
policies had a heavy ideological charge, the actual implementation of policies was always influenced by local personal and group interest.⁴

Based on Kopecky (2006), Schoenman (2014) stated that political parties in CEE had weak ideological underpinnings and voters revolved among parties frequently. Ideological values were hardly transferred to the general public. In the early phase of transition, the ideological values of the “international adviser community” were transferred in cooperation with local political leaders and officials. Their role was to ensure public support from various groups of society. In doing so, they could use ideological argumentation to bring legitimacy for political decisions. But more frequently, they used either coercive mechanisms (the threat or actual use of force) or remunerative measures (economic incentives). Naczyk (2014) interpreted the most current (ideological) changes in Polish and Hungarian economic policy as simple shifts in the content of “economic patriotism”. He argued that during the 1990s, the most important national goal was a quick departure from communism and from central planning, which was backed most efficiently by the neoliberal idea. During the late 2000s, when the earlier goals were effectively achieved, a new content was given to economic patriotism: the strengthening of national business presence and a halt on the further internationalisation of CEE economies. Both the Hungarian and the Polish transition history provided many examples of similar changes in policy preferences.⁵

An important message can be drawn from the above discussion, which will be used in the argumentation of this paper. The relationship of politicians and political parties of CEE to economic issues is less ideological than in the case of more established market economies, but rather pragmatic. The actual implementation of economic policies is determined by several factors. First, there is an ideologically underpinned “mainstream” influence of the international adviser community (which found general support during the 1990s, but was rejected in many cases after the 2008/2009 crisis). Second, the implementation of policies

⁴ Mihályi – Sztankó (2015) cited the case of the privatisation attempts of the Hungarian electricity company, which was effectively opposed by the incumbent management, regardless of the ideological orientation (liberal, nationalist) of various succeeding governments. In Poland, the role of the Solidarity movement could never be neglected and this led to a slower, but social consensus-based privatisation policy.

⁵ Among others, Naczyk (2014) mentioned Krzysztof Bielecki, who was Prime Minister in 1991 during the Polish shock therapy who later, in 2014, called himself a “pragmatic liberal” and as member of the Council of Economic Advisers to the Tusk government, supported the promotion of national champions and other steps reflecting increased economic patriotism in Poland. In the case of Hungary, the political career of Viktor Orbán, the current Prime Minister, and his party reflects a similar flexibility in ideological underpinnings, ranging from liberal ideas during the first half of the 1990s to economic patriotism and a vision of the illiberal state in Hungary most recently.
was always strongly influenced by domestic pressure groups, including business groups (local and also international) or even individual entrepreneurs as well as by social organisations such as trade unions, but less by civil society to various degrees in the CEE countries. Last, but not least, policies were influenced by the self-interest of political parties or even their strong leaders.

I will argue in this paper that changes, even U-turns in economic policies, were increasingly initiated by this later factor (polity) after the 2008 crisis because the first two factors lost much of their influence. The international adviser community lost its influence because the underlying mainstream economic thoughts were largely discredited by the crisis. Unions and other social groups were also subdued by the hardships of the crisis and had to comply with government policies. Last, but not least, controls weakened in the new member states of the EU largely because the main attention was driven away from the new members to the euro crisis and the Mediterranean economies. In such cases, when the legitimacy of governments does not come from ideologically underpinned, tested principles (as was demonstrated previously), policies may fall victim to individual or group (party) interests.6 One of the main messages of the current paper is that this type of “pragmatic” economic policy seriously undermines market economic institutions because of its arbitrary nature. The lack or weakening of normative policy measures threatens the rule of law.

2. PRIVATISATION AND STATE ASSET MANAGEMENT IN CEE TRANSITION POLICY MIX

The role of state ownership in established market economies is described mainly as a policy tool to correct market failures, and the debate is mainly over the optimal size and efficiency of the state sector. In the case of transition economies, state property is usually regarded as part of the economic system of the previous political regime that should be reduced in order to give way to the institutions and players of the establishing new market economic system. Therefore, state ownership is regarded in a complex manner, including not only business considerations or the usual aspects of overcoming market failures, but also general aspects of systemic change. As Frydman – Rapaczinsky (1994) stated a long time

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6 Of course, party and individual interests always play a role in modern societies. As Drahokoupil (2008) noted, the Central European transition economies of the 1990s were characterised by the emergence of a new political elite, the “comprador service sector”, that effectively supported and complemented the spread of multinational businesses in the region. Thus, the economic regime of neoliberal economic thought also served certain individual and party interests.
ago, privatisation was an outstanding issue from a political point of view, since it could contribute to the elimination of the economic power of the elite of the previous political regime. This impact on the systemic change together with the then overwhelming neoliberal theory put considerable pressure on policymakers to privatise as much and as quickly as possible. The campaign-like expectations of the international institutions was repeatedly articulated and expressed in strong messages such as the Transition Index of the EBRD, already mentioned above.

Privatisation was treated not only as being politically important, but also as a tool of economic restructuring. In this sense, two main aspects gained importance. One was the improvement of corporate performance (the inherited state-owned companies suffered from a variety of serious weaknesses). The importance of privatisation in strengthening corporate performance was highlighted in the literature mainly by scholars of the gradualist approach (Kornai, Roland, Portes, Aghion, and others). The other aspect was the general support of institution building, which included the strengthening of capital markets and enabling various social strata to become the new owners of productive property. The desire to improve performance dominated the Hungarian privatisation process, while capital market development and the maintenance of social consensus prevailed in Poland, and the creation of a bright social strata of a new bourgeoisie was the aim of the Czech voucher privatisation scheme. The fierce activity of various interest groups could be observed in the background of the various privatisation policies. They all wanted to shape the details of the general policy aims in ways preferential for them. In Hungary, for example, spontaneous privatisation started even before the political change. Self-appointed new owners from the incumbent management of state firms successfully stripped state assets to create private companies. Later, in the real privatisation process, the implementation of various tools depended very much on the cooperation of incumbent managers. The so-called “indirect privatisation scheme” of medium-sized companies required managers to initiate and complete the privatisation of “their” companies – the state privatisation agency only controlled and approved. Also, the specific bankruptcy regulations in Hungary gave way to insider tricks to obtain state property (Szanyi 2000). The various channels of transforming state property into insider-controlled private ownership created important but internationally not really strong local owners. The new Hungarian owners suffered a number of weaknesses that made local ownership inferior to multinational firms concerning company performance.

Arguments for strengthening corporate performance exceeded the generally used rather simplistic neoliberal statements about the superiority of private ownership. Boycko et al. (1996) argued that private ownership increased the cost of enforcing political considerations over the business rationale, privatisation therefore contributed to the reduction of political influence in exchange for more
efficient company functioning. State-owned firms could be more easily influenced to care for politically motivated goals such as excessive employment than private firms. Another string of literature highlighted the important impact of private property in reducing governments’ toolkit in taking arbitrary economic policy steps that could deteriorate the efficiency of market institutions. Rapaczynski (1996: 93) also stated that from the viewpoint of property right enforcement, the biggest danger might come from excessive state ownership. The state can refrain from excessive takings and the increase of state ownership for a longer period of time. This track record would convince market players that the state respects private property. An excessive and continuous increase in state property (especially if this is carried out by direct or indirect takings) indicates that the state does not respect private property and increases the room for (often arbitrary) increased direct state intervention.

The complex role of privatisation in the transition process increased the impact of the methods and also determined the outcomes on the current economic development of countries in East Central Europe. The two and a half decades of ownership changes contributed to the establishment of an overall business and investment climate and typical government policy practice. In Hungary, for example, there were two influential systemic components: foreign company ownership, integration into multinational value chains, and the crony capitalism of local politicians and capital owners. The two drivers were not separated, but they established the two poles of a dual economy. The Hungarian governments often pursued policies to favour one or the other pole. The activity of foreign companies was usually influenced by indirect legal measures (taxes, license conditions and the like), which often contradicted the principle of equal treatment favouring or punishing them. Local business was more often helped informally, giving way to the emergence of crony capitalism.

In my understanding, crony capitalism means a legally unregulated (badly regulated) interaction between polity and business that works against the principles of free enterprising and fair competition. Policymakers and influential business people cooperate to create preferential treatment for “friendly business” in exchange for the material support of parties, politicians, and election campaigns. This type of cooperation is not unknown in developed economies, though a more developed institutional background and strong civil society control may limit the harmful impacts of cronyism on market economic institutions. If the financial support of political parties is transparent and lobbying for industry (company) interests is institutionalised, then crony capitalism is under social control. It does not mean, of course, that the markets are free of marginal interest enforcement. If cronyism is not transparent, it may lead to very high social losses and even illegal transactions. A major difference between most of the established market
economies and most of the transition economies lies in the level of institutional and social control of polity-business interactions. Loose control in transition economies deteriorates investment and business climate, which is expressed in the rather low level of rankings in competitiveness reports and the high cost of financing.

Interaction between polity and business has been surveyed in the CEE region by many scholars. Well known contributions by Stark (1996), Stark – Bruszt (1998), and McDermott (2002) highlighted that the creation of ownership structure in CEE was marred by cronyism and favouritism, and established new clans/interest groups. The clans incorporated representatives of the political sphere as well. Papers of the 1990s expressed fears of the re-establishment of the economic power of the “nomenclature”. This argument is known also from the papers of the mainstream literature (as it was cited earlier from Boycko et al. 1996). Nevertheless, as time passed by, the fears of a political return to the pre-transition communist rule proved to be impossible. However, instead of a political retreat to communism, increasing cronyism posed new threats to the development and efficiency of market economic institutions.

A new contribution to the just mentioned string of literature on the role of networks and clans is Schoenman (2014). This book differentiated among CEE economies according to the type and strength of polity–business interactions. The intensity and main values of the relationship were determined by the level of uncertainty in polity and of doing business (political changes, regulatory environment, macroeconomic policies, etc.), and the structure of business networks. Broad networks link cross-sectoral coalitions and facilitate collective action. The role of networks is especially strong in societies with weak institutions. Instead of institutions, networks may become the more important channels of interest representation. Business networks tend to develop political ties in cases when there is political competition and politicians and parties need (financial) support, and there are mutual benefits in the relationship. The process is accelerated in the presence of political and economic uncertainty. Based on Kitschelt (2000), he also states that in the case of strong business networks, institutions more likely become “broadly distributive”, providing for a wider layer of business normatively (i.e. independent from agents’ political sympathy and support). In contrast, “selective advantage” institutions distribute benefits to targeted recipients who are among the supporters of the ruling political party.

Under a high level of uncertainty, collective action evolves in the presence of broad networks. This is because of an efficient information flow that increases the threat to reputation in the case of selective agreements. Under high levels of uncertainty and narrow networks, cooperation between business and polity is unlikely because the value of political promises is low due to the lack of business
support, and does not spread due to inefficient information flows. Consequently, business turns directly to the state and not in a concerted manner. In the case of a low level of uncertainty and narrow business networks, polity is not afraid of political competition and can exploit atomised firms. Under low levels of uncertainty and broad networks, the state is likely to enter into collusive relations with firms. The four types of relationship are summarised as follows:

**Table 1. The effect of networks and uncertainty on the state**

<table>
<thead>
<tr>
<th>Uncertainty</th>
<th>Low</th>
<th>High</th>
</tr>
</thead>
<tbody>
<tr>
<td>Network structure</td>
<td>Narrow</td>
<td>Patronage</td>
</tr>
<tr>
<td>Broad</td>
<td>Embedded corporatist</td>
<td>Concertation</td>
</tr>
</tbody>
</table>

*Source: Schoenman (2014: 50).*

Different consequences result from the distinct settings concerning polity (state)–business relationships. In a high uncertainty environment, broad business networks tend to establish regular cooperation links with polity and the state that work in favour of the broad business community. In exchange it provides the necessary financial stability to political parties. The state develops mutually beneficial institutions for concentration in the long run. The state broadly functions as a coordinating agent, channels information, and mediates among interests. When networks are narrow (business elites do not create cooperation) and uncertainty is low with a stable, monolithic political structure and solid economic environment, the state applies “selective advantage”-type institutional solutions and picks the winners. This setting is called patronage. In the case of high uncertainty and narrow business networks, economic elites dominate political elites, potentially leading to state capture. Finally, low uncertainty and broad networks describe the

**Table 2. Networks, uncertainty, and state types**

<table>
<thead>
<tr>
<th>Uncertainty</th>
<th>Low</th>
<th>High</th>
</tr>
</thead>
<tbody>
<tr>
<td>Network structure</td>
<td>Narrow</td>
<td>Patronage states: Czech Rep., Latvia, Estonia, Slovak Rep., Slovenia, Romania</td>
</tr>
<tr>
<td>Broad</td>
<td>Embedded corporatist</td>
<td>Concertation states: Hungary, Lithuania, Poland</td>
</tr>
</tbody>
</table>

*Source: Schoenman (2014: 174).*
embedded corporatist state. In this case, well established political elites do not face uncertainty and cooperate with business networks. In Schoenman’s opinion this setting is unlikely to happen in competitive election systems.

Schoenman (2014) presents a factor analysis using various proxy measures of uncertainty and network density for CEE economies. While the indicators and also the actual relevance of the results may be discussed, the typology is remarkable (Table 2). Patronage and captured states corroborate with the concept of state and business capture (Yakovlev 2006). The typology can also be used in the explanation of recent changes of polity–business relationships in Poland and Hungary.

3. THE IMPRINT OF INCREASING ECONOMIC PATRIOTISM IN CHANGING OWNERSHIP PATTERNS

In Hungary, the left-wing Bajnai government declared the privatisation process completed in 2008 (Hungarian Government 2009). This meant that there remained a substantial effective state ownership. The statement itself could be also understood as a statement that potentially allowed nationalisation. And indeed, this happened sporadically until 2010 and on a larger scale since then under the right-wing governments. In terms of asset volume, re-nationalised property after 2010 was smaller by one order of magnitude than privatised assets after 1990 (Mihályi 2015). Nevertheless, the turn in attitude towards state ownership has far-reaching impacts. The importance of the relationship has not declined since the 1990s when it was a most topical issue. Rapaczynski (1996) explains the complex role of the state in enforcing property rights, including the need for occasional nationalisations. The state routinely engages in economic regulation, which in some cases results in encroachments that are not considered compensable takings. General protection from an excessive spread of such takings can be provided by the political system together with economic pressure groups “that ensure that the state does not go ‘too far’ in interfering with the owner’s control over assets. This politically determined thin line may be understood as the real definition of property rights conferred by the state … In fact, without a significant historical record of state forbearance from excessive and redistributive regulation, it is hard to make the state’s commitment credible. The threat posed by the state to the security of broadly defined property rights is particularly severe

7 There have been occasional re-nationalisations in the 1990–2010 period as well, which were usually followed by quick re-privatisations. The Hungarian state did not intend to increase the volume of state assets in this period and the role of nationalisations remained marginal in this period.
when the state also happens to own a significant proportion of national assets” (Rapaczynski 1996: 93). This danger threatens any government regardless of political affiliation.

Voszka (2013) and Mihályi (2015) compiled a comprehensive list of re-nationalisations in Hungary after 2010. Using this information, we would like to describe the main and typical reasons for these transactions and their potential beneficiaries and possible political aims. Each transaction was explained in some kind of government communication. The explanations shed light on potential general concepts of state property management policies which have not been described conceptually until now. It seems that various, sometimes only loosely connected reasons and considerations worked behind the most important takings. They fit together only at a very high abstraction level of the general (rather populist) attitudes of the government towards economic clients, multinational firms, the expected business–government relationships, and the overall desire for ad-hoc arbitrary decisions instead of normative accountable regulation. Instead of a general policy concept, we can rely mainly on the statements of Prime Minister Viktor Orbán and Minister of the Economy (later President of the Hungarian central bank, MNB, György Matolcsy). The Prime Minister, for example, repeatedly stated that the new economic policy required that at least 50% of the Hungarian banking sector should be in national (not necessarily state) ownership, and that public utility firms must work on a non-profit basis. The repeated anti-globalisation attacks targeted mainly the largest multinational companies in various services industries. The reduction of dependence from the globalised world economy, for example, required that financial institutions be in national hands (if public, the better). Achieving the desired level of state assets was made possible through various transactions.

Taking the list of re-nationalisations (Mihályi 2015: 17), the overall picture shows that between 2010 and 2014, 209 companies were affected and the total value of the transactions was slightly over HUF 1,573 bn (cca. EUR 5 bn). This amount included the sales price paid to previous owners, the increase of share capital, and other commitments as well. The numbers and amounts seem to be very high, especially if we consider that Hungarian governments accumulated public debt in excess of the Maastricht criteria already prior to the 2008–2009 crisis. However, as Mihályi (2015) explains, these transactions did not increase state gross debt since they represented a simple change in the asset structure, a kind of securities swap of more liquid assets. Yet, if we look at the list of transactions, we find that the overwhelming majority of the financial commitments stemmed from transactions in the energy and banking sectors (HUF 1,366 bn). Also, the number of the affected companies was boosted by a large number of small savings banks (137 financial institutions altogether).
Various political aims can be detected among the different reasons of re-nationalisation. The first outstanding transaction was the nationalisation of the second pillar of the pension system at the turn of 2010/2011. The official explanation called for the security of the accumulated pension funds to be taken out of the hands of the private pension funds, which failed to bring the expected returns (“played with hazardous securities”). Account holders of private pension funds were called to withdraw and channel their savings into the state pension system at the risk of losing their pension rights in the pay-as-you-go state pension system. The government applied the “opting out” trick, meaning that those who wanted to keep their pensions untouched had to face the threat and, additionally, they were required to go through a complicated administrative procedure. Those who accepted the government policies did not have to move their fingers at all. Thus, in the end, 2.8 million account holders channelled back their savings into the state pension system at a value of approximately HUF 3,000 bn (EUR 10 bn), equivalent to 10% of GDP. Most observers believe that the “voluntary” nationalisation of the private pension funds was aimed at using the obtained assets for debt relief (which, on the other hand, was accumulated partly by the social security system). Despite the propaganda campaign, the blackmailing of the citizens was received as a major shock. Nevertheless, the transaction brought large amount of government bonds back to the state budget, together with a substantial and diversified portfolio of corporate shares and bonds. Thus, this campaign was the first major, albeit unintended step of increasing state ownership in a fair number of commercial companies.

A larger number of transactions and regulatory changes over a longer period of time were undertaken under the umbrella of cutting utility costs. The promise of savings on utility costs was a major campaign tool of the 2010 and 2014 election campaigns. The government soon prohibited the price increases of the public utilities. Later on, prices were set by government agencies at significantly lower levels than before, thus eliminating profits from this sector. This was the first measure that directly affected the profitability of private business. Later, new taxes were introduced, among others, on financial transactions, mobile telephone calls, ATM cash withdrawals, and advertisement revenues of the media (over a certain threshold"). Limiting utility costs through price decrease resulted in companies going into the red. Owners soon felt encouraged to sell their loss-making firms. This process can be called regulatory taking: company revenues

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8 The advertisement tax was targeted against the German media group RTL with the largest revenues. Government communication explained the measure with the company’s suspected tax evasion. Yet, it was never explained why, if there was something illegal in RTL’s taxation, this had not been repaired by the responsible state institution, the tax office.
dry up because of unfavourable changes in market regulations or excessive taxes. Many of the utility firms were thus sold to central or local public bodies. Some of them received quite generous compensations (for example German RWE). The purchase of utility firms can be explained by the government’s utility cost reduction policy.\(^9\)

The re-nationalised utility firms were in foreign ownership, and the regulatory takings against them heralded a third important consideration that seems to have some explanatory power: the unfriendly relationship to selected foreign companies. The Hungarian governments repeatedly enacted market regulations and changed the tax system to bite the cash revenues of large multinational firms and create more favourable conditions for domestic capital owners. Nevertheless, this policy targeted certain types of companies: financial institutions, media firms, large retail chains, and telecom companies. Their negative treatment was explained in governmental communication with the argument that they do not contribute to the material (real economic) production platform of the Hungarian economy. This kind of populist confrontation of the various economic branches has not been put forward since the beginning of the transition process.\(^10\)

In 2013, the method of regulatory capture (Yakovlev 2006) was applied in the case of the cooperative of local deposit collecting financial institutions. First, the state increased the level of required funding capital. Since small banks could not meet the new obligation overnight, the state itself provided them with the necessary capital and connected this transaction to the acquisition of a controlling share of ownership. Owners of the small banks were not asked beforehand, but were given an ultimatum in case they would reject the generous offer. In 2014, the Hungarian state acquired MKB Bank from the German owners. The German parent bank was unwilling to run the Hungarian daughter at a loss and sold it to the only serious buyer: the Hungarian state. The losses, however, were caused by various negative changes in the business environment initated by the Hungarian government (extra tax on banks’ profits, tax on financial transactions), and the

\(^9\) It is, of course, another question whether the current sales revenues are sufficiently high for the necessary investments. Observers state that public utility companies are still in extremely bad financial conditions and do not invest any more, which may even threaten the quality of their services.

\(^10\) To my knowledge, the last major Hungarian policy campaign to be explained by similar vulgar Marxist arguments was the reconstruction program of the Hungarian textile industry at the turn of the 1980s. The industry’s obsolete technology was replaced by more modern equipment from borrowed money. At the same time, the services infrastructure remained very much underdeveloped. For example, obtaining a new subscription wired telephone line required several years and was in many cases only possible if another subscriber died or gave up his/her subscription. Ironically, after the systemic change, the then new capacities of the Hungarian textile industry were soon scrapped, and the development of the telecom market skyrocketed.
losses due to the government-initiated debt relief program offered for the accommodation of increased debt burdens on foreign currency denominated loans of Hungarian citizens. The achievement of a 50% national ownership presence in the banking sector was heralded soon after. Later that year, a 25% stake in FHB Bank was purchased by the Hungarian Post, increasing national ownership to over 60% of bank assets.

A further important consideration behind the re-nationalisations is supporting clients or personal rent-seeking. This can take place if market regulations change in favour of the domestic market players. Another possibility is selling (privatising) acquired assets to clients. In some cases, the clients’ loss-making companies were bailed out by the state through generous acquisitions of assets. The most striking example of this type of transaction was the redistribution of tobacco sales licenses. Tobacco sales were limited to specialist shops (normal retail stores were deprived of the right to sell tobacco products), and the new sales concessionary licenses were tendered by local authorities. In several cases, evidence was found that the tenders were not competitive. The political importance of supporting loyal domestic business people was emphasised several times by the Prime Minister (Mihályi 2015: 19). However, not only loyal capital owners are supported, but also a wider range of state and party officials who need positions and revenues from the company boards. This is the simplest way of rewarding clients. The right to appoint loyal persons into positions is not necessarily bound to dominant state ownership, but definitely makes it easier.Rewarding clients is perhaps the most commonly used additional, secondary (rent-seeking) aim of takings.

In the case of Poland, state property management practice has not yet been reversed. At the beginning, privatisation in Poland was slower, mainly due to the continuous search for social consensus and the necessary approval of stakeholders in every case. After the rather sluggish practice of the 1990s, 1999 and 2000 witnessed a skyrocketing privatisation activity in Poland. This was due to the then favoured direct sale method and the denationalisation of some large banks and service providers. However, this momentum stopped in 2001 when the previous sluggish insider-oriented methods continued. A new revival of privatisation sales began when the Tusk government came into power. After the necessary preparations, privatisation revenues started to grow in 2009, peaking in 2010 with over US$ 6 bn and producing half of that level in 2011. The net privatisation income of the Tusk government between 2008 and 2012 reached US$ 15.5 bn (WSJ 2012). The same source already heralded the change in concept: large firms were regarded “strategic” and not to be privatised. This meant that the new, still rather ambitious privatisation program for the years 2012–2013 was not enforced with the momentum of the previous years. A curious halt in selling the controlling shares of some “flagship companies”, mainly in the financial sector, was ob-
served by The Economist (2011) already in the otherwise successful privatisation campaign of 2008–2011. The Polish government seemed to pull the emergency brake on the privatisation train. This practice of maintaining state assets is quite similar to the conceptual changes of state asset policies in Hungary.

Instead of the systemic, fiscal aspects gained importance in the state property policy of the Polish government after 2011. While only minority shares were sold that in most cases did not eliminate effective state control, the fiscal revenues of the central budget were increased by dividend payments from state-owned companies (Kozarzewski 2015; Blaszczyk – Patena 2015). The growing importance of budget revenues of profits from running SOEs demonstrates an important departure from the systemic aspects of privatisation and state property management in Poland. Naczyn (2014) analysed a series of steps taken by the Polish governments towards strengthening state control over firms with mixed ownership. The governance structures of these firms were transformed and “poison pills” were incorporated that gave the state extra veto rights even in the case of minority state ownership. This meant that the Polish government too dedicated long-term emphasis on maintaining and using SOEs for various policy purposes.

4. FURTHER REASONS FOR REVERSING THE PRIVATISATION LOGIC

Boycko et al. (1996) calls excessive employment the most typical political ambition that is forced on companies, thus deteriorating their efficiency. But other forms of political opportunism and rent-seeking are also plausible. They mention an article that described the perverse crediting policy of the state-owned Credit Lyonnais bank of France that favoured clients of the ruling party. Although the case was mentioned as an exception, I believe that in CEE, this type of rent-seeking has always been more important than employment issues for vote collection. When I speak about the reversal of the privatisation logic, I mean that steps were taken in CEE countries that targeted political and personal interest rather than the social interest concerning state property policies. Privatisation and the dominance of private property were regarded as safeguards against this type of rent-seeking. The increase of the economic role of the state sector can be regarded as deliberate actions to create more potential for abuses.

I distinguish various types of actual cash transfers from the economy to politicians and their clients. One of them is outright corruption and bribing (moral hazard). In our case, bribes go from the business to the politician and the bureaucrats to buy preferential treatment or simply a license of operation. The corrupt politician and the bureaucrat may expand this activity to the extremes as it was conceptualised by Yakovlev (2006) with the notion of business capture, and
Viktorov (2013) on corporate raiding. CEE’s conditions are of course by far not as bad as in Russia, but corruption also exists in CEE. High-level scandals that involved government officials and other highly-ranked party politicians or their clients revealed that countries such as Hungary, Poland, Slovenia, or the Czech Republic are not immune to this danger either (EU transfers to Bulgaria and Romania were effectively suspended due to high-level corruption).

Corruption, especially by highly-ranked officials, is sanctioned by law. But there are other, not necessarily illegal, albeit seriously unethical opportunities of money transfers from the business to the polity. State ownership is most relevant in these. Positions at the commanding heights of SOEs are regularly filled by clients of politicians. This practice eliminates the conflicts between the management and politician. But this also provides an opportunity for milking the SOE through various channels. A SOE is useful for this purpose regardless of its potential efficiency. The social cost of this practice is no longer simply foregone profits, but continuous cash flow from various state institutions (the state budget) that are transferred from the SOE to private uses. SOEs may finance various social and cultural events, deliver red carpet treatment to politicians, and donate to charity organisations or various activities of the government and politicians. SOEs are also used for rewarding politicians’ clients, for example by financing expert fees.

Of course, the use of SOEs for these purposes is not new and is observed not just in transition economies of CEE. However, this fact does not spare me the conclusion that current policies at maintaining state ownership are aimed at widening the rent-seeking activity of political parties and governments. It is made possible exactly because of the low level of transparency and social control, and the activity causes the same types of problems that were described in the privatisation papers of the 1990s, and it is therefore very harmful for the future of market institutions in CEE. The reasons of intensive rent-seeking in CEE are manifold. Apart from personal gain, we can point to the lack of regulated party financing. Political parties’ budgets are very meagre, and parties spend far more, especially on election campaigns, than what they are expected.

There might be some changes in the practice of milking state assets during the 25 years of transition in CEE. Initially, the main source of cash revenues was privatisation. It is not just corruption that surrounded the process, but even more importantly, the support of clients to obtain valuable state assets at low prices. The process was well documented in the case of Russia, and some anecdotal evidence is also known for Slovakia. However, this practice was not absent in

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11 Skuhrovec (2014) reported peaks of personnel changes in Czech SOEs’ supervision bodies after national election years.
other Visegrad countries either. In some recent Hungarian cases, a potential re-distribution of assets re-emerged, the government declared itself to be ready to re-privatise some firms, although there is no evidence whether this has happened. Nevertheless, opportunities of privatisation are quite rare today in Hungary. In the case of Poland, rent-seeking during the privatisation process was perhaps less widespread due to the more transparent privatisation transactions.

Today, one reason for less privatisation and more state ownership may be the changing structure of rent-seeking activity by the politicians. Of course, the decline of available state assets also contributed to this: the remaining assets are either notorious loss-making companies (like mines in Poland) that are not worth possessing for insiders, or they are large service providers that cannot be easily transferred to rent-seeking private hands. But SOEs in their present forms are all quite suitable for mass-scale milking. Another reason for keeping state assets may be the changing domestic and international environment. International organisations are no longer concerned as much about privatisation as they were during the 1990s. Therefore, international pressure for privatisation declined.

In 2004, the Visegrad countries became members of the EU. Attention was directed rather to fiscal deficits rather than to the conditions of market institutions or the level of state ownership. Of course, the status of the state budget is also influenced by the performance of SOEs as well as their state subsidies, but this is already an indirect link which can be easily covered. Also, the important business rationale of privatisation declined in the meantime. The overall condition of all transition economies improved (maybe not because of improving SOE performance, but mainly due to the increased activity of multinational companies and de novo private firms), and thus the presence of a number of loss-making SOEs could be more easily tolerated. Consequently, the third, political rationale, the redistribution of assets or, more recently, the control of cash flows became the strongest factor in the question of keeping or selling state property.

The reversal of the privatisation logic imposes the danger of an increased obscurity and arbitrariness of economic policy as well, which can lead to an overall decline of the effect of market institutions against politically determined influences. This may be expressed in the growing impact of “selective advantage” measures against “broadly distributive” institutions, or, using the categories of Schoenman (2014), a shift from concerted relationship and effective institutions towards a patronage state and less effective market institutions. Some government declarations expressed a deliberate shift in Hungary, explaining the failure of the markets and calling for more government intervention. This increased government intervention seems to push the polity–business relationship towards the patronage state, and weakens already established market institutions.
Changes in state property management were complemented by a series of other steps of state favouritism in Hungary, ranging from public procurement to market regulation. Many of these steps seriously contradicted normative regulation and violated the principle of equal treatment and EU competition law. For example, only in the first half of 2015, three major procedures were launched in Brussels against the Hungarian government. The levy on retail trade supervision and tax on tobacco products were suspended, and grants for road construction to Hungary were suspended due to the ongoing competition policy procedures. In the first two cases, tax policy measures were designed in such a way as to favour a selected number of politically linked players. The public procurement cases were investigated because of unusually high prices, but road construction was regarded by observers also as one of the main areas of patronage.12

Selective advantages have been provided to clients and simultaneously, competitors of clients were frequently punished by unfavourable regulation. This is most clearly visible in the example of punishing certain representatives of multinational businesses by selective disadvantages (extra taxes, exclusive regulation), while other members of the same community were rewarded and included in the close circle of the strategic partners of the Hungarian government. The simultaneous steps in opposite directions can be interpreted as a deliberate policy aimed at splitting the established business networks (that of foreign companies/multinational business). Using Schoenman’s typology, this is a move towards narrow networks and the patronage state (business capture), since political uncertainty is perceived as very low by the government since FIDESZ won elections twice in succession with a two-thirds majority in Parliament.

These cases illustrate the departure from the “competition state” (Drahokoupil 2008). The concept of the illiberal state decreases the free market system and democratic institutions. The above cases as well as the whole departure process from Western values has been conceptualised in Hungary and is therefore regarded by the Hungarian government as a sovereign decision to establish a new economic system. Populist followers of the Hungarian agenda can be found also in Poland. The PiS party openly declared his appreciation of the concept, declaring that hopefully there will come a time when there will be a Budapest in Warsaw. But the essence of the opinion of Polish observers is that the concept of economic patriotism has already been introduced in Poland as well. This is reflected, among others, by the changes in state ownership policies.

12 Until 2014, construction tenders were won to a very high degree by the companies of Lajos Simicska, an old friend and former treasurer of FIDESZ. He criticised the government rather vehemently in 2014 and, as a consequence, his companies were barred from participation in public procurement tenders for three years in 2015. This was a clear application of the selective advantage/disadvantage policy (see at various internet news portals, e.g. Origo 2016).
5. CONCLUDING REMARKS: THE RELEVANCE FOR THE CEE MODEL OF CAPITALISM

What message does this analysis deliver to the concept of the CEE model of capitalism? I believe that changes in political attitudes have an important role in the model. Increasing direct state intervention in the economy changes the rules of the game rather quickly in ways that were described in the paper. Weaker social institutions and deliberate government policies aimed at increasing discretionary decisions and limiting transparency will limit also the area of the rule of law. Uncertain and increasingly arbitrary business conditions will influence not only domestic, but also foreign owners in their operations in CEE. Foreign firms’ role as an anchor of the economy may decline, as they either change their operations or leave the region if they are unwilling to adjust. Contrary to the assumption of the DME model, I think that governments can also influence multinational firms’ activities either for good or bad as was evidenced by the Hungarian cases cited in the paper. Governments may try to use the fuzziness of conditions to their advantage, sometimes even at the risk of the withdrawal of foreign companies. This policy is easily sold to societies by populist statements of their governments.

The populist argument frequently refers to the fact that there are good examples of successful and efficient SOEs. Indeed, the idea of incorporating SOEs into the economic system is not from devil. I do not think, however, that SOEs’ role in CEE models is identical with any of the other European capitalist models. We should not forget the conditions for adequate SOE activity, which is effective social, political, and economic control. Moreover, state companies must support economic policies in deliberate ways. However, SOEs in CEE are used by politicians rather for political and personal rent-seeking. This threatens the social acceptance of basic market economic institutions and the rule of law. Strengthening control institutions over public policies in general is a precondition of maintaining democratic values and withholding the pendulum from further moving to autocracy. Controlled direct state intervention in the economy should serve public welfare and not private interest.

Therefore, a further lesson for the CEE model is the outstanding importance of social and political control institutions. CEE models implicitly assumed that foreign control can withhold governments from flirting with illiberal political and economic solutions. It seems that this control lost its efficiency after 2004. The loosening of democratic control tempted ambitious politicians to move the economic and political system away from traditional Western norms towards an authoritarian model more typical in the East. In fact, this type of shuttling between East and West, democracy and autocracy has always been characteristic of the region’s countries. The greatest harm is caused by the shuttling itself because
it is always linked to sizeable institutional changes, which are always very costly. But even more damage is caused by the unreliable, constantly changing environment that makes long-term business planning impossible. From the viewpoint of doing business, a predictable environment with some secure institutions (security of property rights) may be more valued even in an autocracy.

REFERENCES


