Europe’s periphery

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24 January 2011

The decimation of indigenous industry in central and eastern Europe has created a low-wage hinterland on the fringes of the highly developed core, writes Carl Rowlands. If the societies of central-eastern Europe are indeed in transition, it is very unclear what the destination will be.

The European Union now consists of 27 states. No fewer than 10 of these are former states of the Eastern Bloc, and this proportion is set to grow with the impending accession of the former Yugoslavian republics. Europe’s centre of gravity is shifting. And while the process of joining the European Union is driving change within these countries, it is also changing the nature of Europe itself.

At some stage in the 1990s, it became common to refer to eastern European countries as "transition states". This implies an optimistic future, a linear progression, a transformation from a failed communist past to a stable western European future. Surely one of the most obvious lessons from the financial crisis and recession of recent years, however, is that the idea of such a transition is misplaced. If the societies of central-eastern Europe are indeed in transition, the mode of transit is that of the covered trailer, haphazardly attached to a juggernaut, driven by remote political and economic forces. And it is very unclear what the destination will be, given the continued economic upheavals and displacement across the whole of Europe.

The result of the transition so far seems to have been the creation of a low-wage hinterland, a border economy on the fringes of the highly developed European core, and this has had wider political and social ramifications for the entire European project - in effect shifting the goalposts of what it means to be European. In this article I will attempt to define the accession states as an entrenched periphery grouping, and to identify the structural characteristics that reinforce this position.

Economic theory and reality

The nature of the economies which comprised the previous communist system has frequently been misinterpreted. Contrary to perceptions, the planned economies were never completely isolated from the rigours of the global markets, though there was a real failure to respond proactively, for example through increased labour productivity or the
promotion of innovation. As Mark Pittaway has argued, central and east European (CEE) economies began to come under pressure after the oil crisis in the mid 1970s. The fall-off in economic activity that produced unemployment in the West was absorbed in the East either through pursuing lines of credit with western institutions such as the IMF, or accepting a gradual deterioration of living standards. Nevertheless, in 1989 many of the peripheral countries were exporting to western countries, with specialisation in pharmaceuticals, chemicals, coal, textiles and food. Their main challenges at this time in fact related to overcapacity, under-employment and a lack of investment in education and research. [1]

Small and medium-sized private businesses in the central and east European economies had been insulated from international competition, through a peculiar symbiosis with the public sector. They did not take a proportionate part in bearing the public burden – such as tax and social security payments – and to a certain extent lived off the deficiencies of the public sector. Obviously, the subsequent removal of these factors has resulted in a very different operating conditions for such companies, causing them great difficulties. Though these conditions could not continue, what was to follow compounded their difficulties, resulting in waves of bankruptcies and closures.

For, rather than basing new policies on a critical assessment of the real problems facing their economies, policy-makers in the newly liberated countries were guided by ideology more than analysis. Many of the problems experienced by the “accession states” – and the associated problems experienced by the whole of Europe – resulted from the overwhelmingly ideological nature of the western response to eastern Europe, which was enthusiastically received by CEE governments. The new era saw a strong commitment to privatisation and widespread support for liberalisation, and big investment opportunities were opened up for eager foreign companies. All the emphasis was on privatisation, and little attention was paid to the costs of such wholesale changes.

The doctrine of “shock therapy” became popular – designed to engineer sweeping institutional changes within the internal structures of the CEE political economies (which of course also opened them up to maximum western penetration and influence). [2] This doctrine, masterminded by Jeffrey Sachs, was ostensibly intended to jar the economies of the region into capitalist modes of operation, with its harsh dosages of restrictive monetary and fiscal policy. Shock doctrine measures included the sudden removal of subsidies, fire sales of state assets, and the abrupt removal of the controls and subsidies that had formerly applied to wages and prices. Their effect was to break down existing trade patterns, almost overnight, leaving each country isolated within its own limited resources.

The shock was timed to occur before the establishment of financial markets within the region: and, in the absence of investment capital, restructuring efforts became focused on labour – on reducing the unit cost of labour in order to become “competitive”. The wave of mass unemployment that this generated in the early 1990s goes well beyond the experiences of British recessions of the 1980s, with unemployment in some regions reaching 80 per cent. Shock therapy deliberately engineered a slump in the economies of the region, by shattering the region’s economic links, and then creating a massive domestic recession.
Under-investment in R&D – a characteristic of the communist era – was perpetuated by the restrictive lending policies of the World Bank and European Bank of Reconstruction and Development (EBRD). Furthermore, such institutions made a conscious decision only to lend to private firms, or to lend money in order to facilitate the privatisation of services. So only private capitalist developments attracted money – and, of course, there were very few entrepreneurs with access to the credit necessary to set up valid initiatives.

With the decimation of indigenous industry, the role of financialisation and debt became crucial, as the new capitalist economies required a financial services industry that could support the growing tendencies towards property speculation and asset manipulation. Different vulnerabilities arose from the actions of different institutions, but the overall effect was to create state dependency upon foreign direct investment, and support from the World Bank, IMF and the specially created European Bank for Reconstruction and Development.

The general financialisation of the region led to huge increases in debt, both personal and institutional. Western banks in a number of smaller states, most notably Austria and Sweden, sought to boost their profits through increasing their market share in the CEE region, by aggressive lending to households. Drawing on the general expectation of CEE countries’ membership of the EU to borrow on the wholesale money markets, and taking advantage of financial deregulation and poor consumer protection standards in the region, they lent money denominated in Euros, Swiss Francs and Japanese Yen. This allowed them to offer consumers lower interest rates than those available for borrowing in domestic currencies. And this borrowing has driven eye-watering increases in levels of personal household debt – especially in Hungary, Romania, Bulgaria and the Baltic States.

An intended consequence of “Shock Therapy” was the pressure that it would generate on the European Union to open up western European markets to the CEE countries. The model that peripheral states adopted – of being low-wage export-based economies – depended on access to EU markets. A number of trade agreements were adopted during the pre-accession period to facilitate such developments, the first one of which, in 1992, was between the EU and the Visegrad countries (Slovakia, Czech Republic, Poland and Hungary). However, in the first half of 1993 the combined value of exports from all the CEE countries fell by 13 per cent in dollar terms as compared with the first half of 1992. [3] The numbers indicate that these initial agreements did not work to the benefit of the transitional states in the crucial period preceding accession.

Of course the transition states are not all the same, and they have not pursued exactly the same policies. Slovenia, the Czech Republic and Poland pursued more cautious, protectionist micro-economic policies, including delaying the restructuring of state enterprises in the 1990s. This preserved a more dynamic domestically owned SME-sector. Furthermore, Poland was able to restructure its debt in 1991, and this enabled the Polish state to act with a greater degree of autonomy and sensitivity than would otherwise have been the case. Hungary, on the other hand, decimated its own SME sector with tight monetary policy and an early adoption of punitive bankruptcy law.

Regardless of these differences, however, a system of incentives, both negative and
positive, forced through widespread privatisations, resulting in the more valuable assets falling into the hands of foreign companies. In 1989 the EU set up the PHARE fund (Poland and Hungary: Assistance for Restructuring their Economies), to direct capital towards the initial “modernisation” of Poland and Hungary, and it was subsequently expanded to all accession states. PHARE should be primarily considered as a support programme for Foreign Direct Investment (FDI), but it also enabled the establishment of privatisation agencies, set up as government bodies in eastern Europe. In general it has been very hard to trace the usage of the PHARE money, as it was so lightly regulated, but certain patterns of usage have been identified. The late Peter Gowan identified that PHARE was used to fund hundreds of studies of industries throughout the region, and argued that the western consultancies used to conduct the studies were directing their information westward: they were conducted specifically for the purposes of western companies, and had the potential to be used for anti-competitive purposes. [4] The information gathered with the support of PHARE enabled companies such as General Electric to swiftly identify areas for “rationalisation”. For example, upon buying Tungsram in Hungary they swiftly closed profitable product lines, and were able to remove a source of domestic competition from the market. Similarly, the Hungarian cement industry was bought by foreign owners, who then prevented their Hungarian affiliates from exporting; and an Austrian steel producer bought a major Hungarian steel plant only in order to close it down and capture its ex-Soviet market for the Austrian parent company. [5] These are just a few examples of the ways in which the “peripheral economy” status of the eastern European region was imposed.

After only a couple of years of “Shock Therapy”, much of the core industrial infrastructure of the peripheral states had fallen into the hands of multinational companies – from chains of shops, to power generating plant and steelworks.

With the accession of the 10 countries in 2004, PHARE was replaced by EU Structural Fund money. For the first time, money began to be used for social purposes. However, EU support has continued to consistently reflect a bias towards neoliberalism and private finance initiatives. Indeed the EU has an inherent tendency to introduce liberalisation wherever it spreads money. EU infrastructure projects are dominated by different layers of subcontractors. This creates a process whereby companies chase tenders in a culture of opacity and corruption, based on a system of casualised labour at the bottom. And the European Bank for Reconstruction and Development’s willingness to lend continues to be dependent upon the debtor states’ acceptance of the privatisation of public services.

The wider effects of the transition have provided multiple benefits for corporate interests, as well as helping to create a rich and often corrupt or even criminal elite within the CEE countries. German and Austrian multinationals in particular have proven adept at targeting their investments and intercepting EU funding, as part of their overall approach to cost and capacity control, and the management of labour shortages. The resulting effect within Austria and Germany has been the creation of a “dynamic comparison” model, whereby management can highlight the low wages and light unionisation of facilities in “transitional” countries. In turn, this has been used to create an argument for domestic neoliberal reform.

Social consequences
These economic policies have inevitably led to long-term structural unemployment. A controversial Lancet study in 2009 attempted to quantify the human cost of shock therapy: it described reduced life expectancy, heightened levels of disease and anxiety, and a “social tsunami”. [6] The increased burden on health and welfare services is now a further problem for indebted states.

Most affected by the abrupt nature of the transition have been groups of factory workers, the unskilled and those not able to retrain. Overnight, an underclass was created, one that forms a new army of the unemployed, in the absence of interventionist government with a job-creation agenda.

Some progressive social policies have survived both the transition and the following recession. Free childcare for children over 6 months old is still provided, in theory, across most countries in the region. The implementation of a minimum wage has been set, in most cases, at a fairly significant level. Pensions are usually set at a level that maintains most pensioners, and the same applies to social care for those unable to look after themselves. There has been continuing provision of preventative medical care. The massively popular residue of paternal communism, with “cradle to grave” social provision, often sits uncomfortably with the strictures of the new economic order.

In such a cold economic climate, social networks have become a pivotal resource for determining status and earnings: children from families of low social status have to work especially hard if they are to succeed – as they would in western Europe. But in the CEE countries even highly successful academic results are no guarantee of a well-paid job. Peripheral states are largely unable to provide the research facilities or salaries to compete with developed countries. This has marked a decisive break between merit and reward, which itself could be damaging for the future prospects of these countries. In the absence of decent rewards for academic achievement, the values of educational attainment are chronically undermined by patronage and family background.

The trade unions, despite playing a pivotal role in some of the democracy movements during the 1980s, have generally seen a massive diminution in their power and influence. Their members were particularly hit by all the redundancies and industrial closures. Whilst pockets of militancy amongst some skilled workers remain, a new generation has emerged with no knowledge of trade union membership, and seeing wage inequality and job insecurity as immutable facts of life. [7] Richard Sennett’s conclusions about the effects of casualisation on social relationships, as outlined in his book The Corrosion of Character, apply in double measure to the peripheral states of Europe. [8]

But of course, not everyone lost out. Shock therapy had its domestic supporters, people entranced by the ideas of neoclassical and Hayekian economics. Sometimes this was based on genuine intellectual engagement, as neoliberal western economists gained fervent followers in the universities and colleges of Warsaw, Prague, Bucharest and Budapest. More often, however, the new disciples of neoliberalism were cynical converts from communism, the prospectors of a new capitalist order. Through incorporation into western institutions, such as NATO or the EU, some of the new capitalists hoped to entrench their situations as the primary political arbitrators, a new elite of western-influenced reformers.
Political repercussions

Talk of a reduction in the capacity of the state was to become a self-fulfilling prophecy. There was a deliberate hollowing out of the state’s ability to regulate the economy, as the economies have become ever more dependent on inward flows of capital. There has also been western intervention into the CEE countries’ political processes, which has had the effect of weakening those political parties in favour of a degree of regulation of the economy. Many in the West, by the mid-1990s, were worried by the continued electoral success of post-communist political parties. Michael Ignatieff wrote in 1995 of a “civil society strategy” for the region. This, he argued, should be a set of programmes administered by the western states within the post-communist states to fund the mass media, opposition parties, the courts, judiciary and police. He argued that the strategy should begin by finding partners in wider society. [9]

Western governments, often in association with multinational companies, have been instrumental in putting these ideas into action, normally in extremely underhand ways. The system of election campaign funding throughout the periphery has in most cases become opaque, with allegations and counter-allegations of multinational and intergovernmental involvement. Such an environment has been extremely rewarding for local conspiracy theorists. Through their clumsy interventions, and by piping money to artificial “liberal” organisations, western institutions have helped to pervert and subvert politics even further in favour of economic interests. [10]

Since the administration of the shock therapy, voters have often opted en masse for parties of the left, in the hope that they would mitigate the worst social and economic effects of the capitalist transition. But these parties themselves have been heavily committed to privatisation and the main tenets of neoliberal economics, as part of their commitment to European accession. The ideological chaos that has ensued has assisted the emergence across the region of populist and right-wing movements, who have attempted to harness people’s discontent. Political forces that flourished in the time of the Austro-Hungarian empire have re-emerged - such as anti-semitic “christian socialism” and patriotic “national liberalism”.

With politics largely submerged by economics, and increasingly located within the geopolitical orbit of the “global national security” interests of a paranoid and overstretched United States, the legitimacy of the post-1989 elite has come to depend on “catching up” with the West. But in the aftermath of the financial crisis this aspirational strategy faces its largest test – one that could yet result in disastrous political consequences.

According to Gabor Scheiring, a member of Parliament for LMP, Hungary’s fledgling green party, those who bring capital into the country also become socially and politically important, and this reinforces the cultural hegemony of the values and ways of thinking of the economic and social elite. [11] There has been a loss of left-wing legitimacy, and the liberal left are not offering a critique of the processes of globalisation and the problems of the new political system. Disenchantment has therefore often combined with a far-right revival of ancient traditional culture.

The recycling of mythical nationalism is reflective of a desire to “escape from modernity” – an understandable reaction to the kind of western cultural hegemony characteristic of
peripheral states. For liberals from the former Eastern Bloc, who were expecting a new golden age of literature, music and art, the results have been disappointing. The mass culture of the periphery operates on the lowest common denominator, and on cheap US imports. According to Gabor Scheiring, liberalism has become swear-word: “It’s part of a global process whereby losers from economic transitions become isolationists. A new form of criticism is needed, combining human rights with social justice.”

**A new social geography**

After twenty years of “therapy”, the transition states are now developing a sociogeographic landscape that reflects the nature of their economies. Thus the ideal capital city of the periphery is now centred on retail, services and tourism: Michael Lake, EU Ambassador to Hungary in the period preceding accession, repeatedly referred to Budapest as a “City of Boutiques”. By implication, the other Budapest, an industrial city of nearly two million people, many of whom were blue-collar workers living in tower blocks, was to be disregarded.

The physical infrastructure of a periphery city can be best described as a mixture of protected heritage, unchecked urban decay, and questionable speculative regeneration schemes. Modern urban architecture, exemplified by bland office blocks, can often be as brutalist as its concrete Stalinist forebears. A lack of controls and planning checks applies to projects in business, retail and domestic architecture. Weak, underfunded, local authorities are often unable to enforce preservation orders, or are compromised by business interests. Formidably bureaucratic planning regimes are easily subverted by commerce and the promise of external capital.

The CEE states were formerly notable for their extensive transport infrastructure, but much of this is now in a state of disrepair. The private car is increasingly becoming the aspirational mode of transport. And with the spread of car-owning, encouraged by businesses and politicians, it is hardly surprising that air pollution in many areas is worse than it was under communism. As “Bankwatch” has reported, the EBRD continues to back a number of projects in eastern Europe which will have negative effects on the environment, including dozens of waste incinerators and motorways. Disregard for the environment is also evident in the large amounts of rubbish and detritus that are dumped across the cities and countryside.

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The industrial infrastructure of the peripheral regions can be said to consist of four main types. Firstly, there are massive derelict sites – plant declared bankrupt and abandoned in the 1990s. Secondly, there are post-investment, modernised facilities, almost always owned by a foreign company. Thirdly, there are franchise-type operations, where a local
business has established a contact with a foreign supplier or trader. And fourthly there are new plants, built by multinationals. As FDI, these are often subsidised by the government, with the company usually utilising cheaper labour costs and subsidies to relocate from a deprived area of western Europe.

The psycho-geographical composition of Europe’s periphery could present a genuine opportunity for political counter-currents to emerge. The obvious degradation of urban and rural environments can create formidable movements of opposition, some of which can develop an autonomous momentum. Competition for urban space, where subcultures attempt to humanise city areas, in opposition to the tendency towards speculative property development, can also represent an important opportunity for organising. These movements provide the opportunity to move alternative left perspectives out from the seminar room and into everyday life.

Conclusion

Despite the differences within the peripheral region, the common policy approaches of the 1990s have resulted in outcomes that reflect similar structural approaches, and comparable problems. The continuing overall aim of policy, as reinforced by the IMF, the EU and a host of international institutions, seems to be to maintain a debt dependency relationship. The result will almost certainly be the continued decline of communities and a further reduction in social cohesion, while states’ ability to maintain core levels of services and welfare will increasingly be under threat. An ageing demographic makes such problems increasingly acute, even for the more stable countries in the area.

Some possible responses include greater co-operation between countries in the CEE; the definition of an indigenous approach to development, whilst preserving access to crucial external finance; a relaxed fiscal policy, and the ability to devalue if necessary; and the improvement, rather than diminution or privatisation, of the state sector.

The permanence or otherwise of these “peripheral” characteristics is difficult to assess. Perhaps instead the question should be directed to the “core” European countries: how permanent are their positive characteristics? As the character of the EU changes with further absorption towards the East, an institutionally united yet socially fractured European economy may be emerging. If so, it will be an ultracapitalist mutation, with profound social and political limitations.

With thanks to Dr Mark Pittaway, Gábor Scheiring and Péter Kulcsár for their kind assistance with this article.

Mark Pittaway died in November 2010. Perhaps his generation’s most talented and luminous scholar of Central European history, he will be greatly missed by his friends and colleagues.

Footnotes

1. Mark Pittaway was one of the few academics taking a critical approach to the transition process from a social-democratic perspective, and his ideas inform the economics of this article. Quotations in this article are from an interview conducted on 24
February 2010.


3. See "Eastern Europe, Western Power and Neo-Liberalism".


5. See "Eastern Europe, Western Power and Neo-Liberalism".


**Published 24 January 2011**

Original in **English**
First published in **Soundings 46 (2010)**
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