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**FROM PARTY STATE CAPTURE TO PARTY BUSINESS CAPTURE**

**MODEL FEATURE OF VISEGRÁD COUNTRIES?**

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# From party state capture to party business capture Model feature of Visegrád countries?

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### Abstract

The FDI-led development path of the Visegrád countries has been queried most recently. The paper analyses one of the potential reasons of this strategic turn: the struggle between political elites. One elite was bound to the strong presence of multinational business and the institutions of the “competition state”. Their positions were challenged by another political elite that allied mainly with local bourgeoisie. One main arena of conflicts is the economy where political elites try to widen their influence in order to gain financial support. New forms of rent seeking and corruption became possible after the V4 accession to the EU when the flow of financial aid increased. Aid was channeled to partisan firms in public procurement tenders that made legal corruption possible. Political and social control over this practice declined with the demise of classic program parties’ role in politics and the raise of populist “business firm” political parties.

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### **Introduction**

Visegrád countries (Poland, Czech and Slovak Republics and Hungary, the V4) have been regarded as forerunners of political and economic transition in the 1990s and early 2000s. Though their transition process was not free from contradictions, institutions of

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political democracy and market economy were established and fine-tuned. Institutional solutions varied of course according to avenues and features of the transition process, nevertheless, 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. Political and economic development though sometimes controversial, enabled V4 to enter the European Union in 2004.

From then however, the once so rosy and promising perception of the capitalist development path in the region has begun to change and also negative processes started to unfold in some countries. Macroeconomic balances started to lull and even deteriorate already before the 2008 crisis (with the exception of Poland), corruption seemed to increase and reach high political circles, populist political parties won significant support on elections (true, also in other more established democracies). Achievements of the once so successful FDI-led development model (Szanyi, 2003) have been questioned and new economic arrangements have been searched for with more emphasis on national capital and state control over market institutions. This type of change has been observed in all V4 countries, however with different patterns and significance, of course. An explanation of increasing nationalistic and statist policies is due.

In this paper I make an attempt to interpret this process as a logical outcome of the political and economic transformation process in the V4. I argue that the development of the political party system did not copy exactly the patterns of West-European democracies and left more room for elites and their political parties to dominate political and economic institutions (party state capture). Captured by governing parties market institutions and civil control could not effectively limit state influence that aimed at favoring clients through selective measures (party business capture). Significant political (party) control in the economy is observed also in neo-corporatist models of Europe (e.g. in Austria). But this influence has been under more effective political and

social control due to influential democratic institutions. Weak institutions of V4 countries allow stronger party control that may result in capturing both polity and the economy by ruling parties. Such a change is contrary to the FDI-led development of the region. I emphasize mainly the role of direct state intervention in the economy through politically motivated changes in regulation and in the ownership patterns. The state can effectively alter conditions of competition on various markets through its monopoly of regulation and also through state owned companies. Captured states can use this opportunity to favor political clients and “friendly business” at the expense of other competitors. Thus, competition and competitiveness may be switched off as factors of business success. Polity-business interactions will be looked at primarily from the angle of enrichment of the elites in the analysis. Policies of Hungary will serve as illustrations of the process.

In this paper first I discuss the evolution of elites during the transition process. With some simplification literature differentiates among two main groups: an elite that established itself in cooperation with multinational business and coordinated the establishment of institutions of political democracy and free market economy, the components of the “competition state” alongside liberal concepts during the first phase of transition in the 1990s. The other group allied with local bourgeoisie and contested the competition state and multinational dominance. In the second section of the paper an analysis will be given on party development in the V4 countries showing an erosion of traditional parties supporting the competition state concept based on political and social consensus. This erosion process gave way to the emergence of “business-firm” parties which won massive electoral support using populist phrases instead of ideologically determined programs. Since the argumentation of the paper highlights political and personal rent seeking as a main driver of the polity-business relationship, the third and fourth sections deal with its opportunities. These changed over time from direct state asset appropriation to tapping state and EU sources through partisan going concerns: state-owned enterprises and genuine private companies. Finally we sum up and conclude.

*Elites*

CEE transition process was designed by an interplay of local political forces and the international advising institutions the recommendations of which stemmed from neo-liberal concepts. The aim of shaping social progress supporting the emergence of local bourgeoisie was an important aspect of the transition process. Liberal concepts of ownership change and the role of privatization emphasized the political impacts of the process. The reduction of state property was regarded as crucial element in institution building mainly because of its role in limiting chances of survival of paternalism between state owned enterprises' managers and politicians at various levels (Boycko et al, 1996; Rapaczynski, 1996). The liberal concept emphasized the liquidation of incumbent management's power position in order to make transition process irreversible (Friedman and Rapaczynski, 1996). Concerning the practical implementation the general concept did not make strong recommendations e.g. in favor of foreign investors. Therefore, privatization practice varied among transition countries. Yet, privatization was a key issue of the transition process in all transition countries.

Political economic approaches of the privatization process soon directed attention to the empirical fact that incumbent management's influence and economic power could not be eliminated (Stark, 1996; Stark and Bruszt, 1998). Nevertheless, fears of reversing transition proved to be unfounded. Instead, new power networks evolved that included old and new players in the economy and in polity as well. New types of alliances were set up, new elites were created. In contrast to earlier expectations, the development of business-polity alliances and networks did not lost steam but the process even accelerated rather over time (Stark and Vedres, 2012). In the first phase of the transition process penetration of multinational business was very quick in transition economies' markets, local companies' and entrepreneurs' adjustment process lagged behind (Szanyi, 1996). Therefore, market power shifted very quickly away from local firms and bourgeoisie to foreign companies. Foreign penetration increased to unusually high levels. The process was extremely powerful in many sectors of the Hungarian economy (automotive, electronics, retail trade, financial services/banking,

telecommunication), more sporadic in Poland (financial services/banking, retail trade) with Czechia and Slovakia somewhere in between.

The process of economic restructuring was also reflected in relationships between business and polity. Both foreign and domestic business organized itself into various interest groups. Drahekoupil (2008) analyzed the emergence and impact of the new elite around foreign-owned companies. He regarded this elite as the ultimate winners of the transition process in the V4 countries (as compared with the position of the incumbent technocratic-managerial elite and the new entrepreneurs). He called this elite “foreign investors with their comprador intellectual allies”, and claimed that “the domestic comprador forces rather than their foreign allies had ... a major role in domestic politics” (p. 361). The rise of this sector was intertwined with the consolidation of the “competition state” the main aim of which was the insertion of the local economy into the structures of global capitalism. It is important to note, that the “domestic comprador elite” bound to foreign investors can but need not necessarily be a proprietor class. Based on the “strategic-relational state theory” Drahekoupil et al. (2008) argued that the social relations of production, institutions and ideas constitute “a (strategically selective) environment that provides advantages to some actors and certain strategies over others” (p. 363). If this environment is determined by one or another type of elite the advantages will be received by actors bound to the given ruling elite.

The dominance of one or another elite may or may not be politicized and bound to parties in power. In this regard we find observations for both solutions. Drahekoupil (2008, 2008a) stated that the political support of the competition state went beyond party divisions in CEE. Thus, the connected “comprador elites” might work under the rule of various political parties. We can add that his was based on social consensus concerning the eminent role of privatization and liberalization of trade and capital markets in transition process, preconditions for significant foreign direct investments that was also strongly recommended by the international advising community. Nevertheless, post-crisis experience showed a more partisan approach towards foreign investors in some CEE economies, most importantly in Hungary and in Poland.

Another concept was developed by Schoenman (2014). He made the type of business-polity connections conditional to political and economic uncertainty, and the strength

and degree of organization of networks (lobbying platforms). According to him all three above mentioned elites might or might not act in non-partisan ways in relation with polity, depending on their level and strength of organization and the level of political uncertainty of the ruling parties. In this approach the dominance of a certain type of elite may be challenged when determinants change. Moreover, Schoenman (2014) found different patterns of business-polity cooperation in the various CEE countries. We come back to this issue later.

Local business has developed representative organizations, but also direct links between businesspeople and politicians persisted over time. Incumbent management of pre-transition state-owned enterprises as well as petty entrepreneurs formed local business (Lengyel, 2007). The empirical analysis of the Hungarian business elite of the 1990s showed that most influential entrepreneurs of the time have had some kind of pre-transition career, either as party members and chief or second line managers of SOEs or petty entrepreneurs (Laki, 2002). It also turned out that local entrepreneurs could not keep pace with the dynamic development, superior technological and market competences and wealth of multinational competitors (Laki and Szalai, 2015). Typically, influential Hungarian entrepreneurs participated in various service businesses (trade, logistics, hotels, business services, gambling, etc.), real estate development, construction and banking, much less in manufacturing. They maintained good personal relationships to politicians and frequently became also officers of various parties. Therefore, the representation of Hungarian business towards polity was much more based on personal linkages than on representative organizations.

Be it a temporary or long lasting phenomenon, business-polity elites do whatever they can in order to stabilize their privileged positions. State and corporate functions of the elites are integrated through personal ties, institutional channels, material benefits and recruiting patterns. There is a frequent personnel exchange between business, polity (state, regional and local administration) and supporting institutions (consulting firms, developing agencies, law offices, etc.). Many persons hold several positions in various areas. Interactions between the state and business are usually institutionalized. Due to important agency problems the flows of material benefits between government and business are also frequent, giving way to rent seeking and corruption. Last but not



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least, personal careers usually combine positions in the various areas of business-polity interplay. The recruitment system gives preference for broader professional experience including both business and government positions. While Drahekoupil (2008) provided evidence on the establishment of FDI-based elites in various CEE countries, other authors described similar process featuring local business (Schoenman, 2014; Naczyk, 2014; Stark and Bruszt, 1998; McDermott, 2002). Politically motivated changes in high and medium levels of state apparatus and SOE management is a major difference to other statist regimes, for example the East-Asian developmental state. The success of that model is frequently mentioned by representatives of CEE “illiberal states” as an alternative to the liberal competition state. But competent and experienced state bureaucracy cannot evolve in party captured V4 states, which is one of several conditions of the success stories which were absent in current day Central European transition economies.

#### *Changes in the political party system*

As it was mentioned above, business-polity linkages have always been present 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 outstanding cases from US and European economies to evidence existing relationships even personal overlaps in most liberal market economies like the USA or Germany. But we must stress that long periods of democratic development strengthened political and market institutions there. In their case there is appropriate civil control 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 those relevant for West-European democracies the antitypes of CEE 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 to both party state capture and corporate state capture.

State capture 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 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. Unlike in case of simple corruption where 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) who are in monopolistic position. In case of party state capture political parties in power occupy the command positions of relevant institutions. 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 on the other hand 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 CEE 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 countries. This development is in deep contrast with the all too optimistic predictions about the consolidation of CEE 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 CEE, as well as differences in economic development and welfare generation (as primary social task) can largely explain differences between East and West. But in order to understand the split in CEE, as well as to obtain a dynamic perspective for the process, further details need to be elaborated. Split between various CEE 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.

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 CEE 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 CEE economies could afford. Kornai (1992) drew attention very early to problems of "premature welfare state" in CEE warning for accompanying fiscal difficulties.

Besides of the fiscal hazards of too high election promises a further important feature of CEE political systems contributed to the unexpected collapse of several ideological parties. Kopecky (2006) found that political parties in CEE 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 introduced the idea of “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.

CEE 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 is 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 CEE transition economies, and their advance in more competitive political systems indicate that party state capture may continue increasing in CEE.

### *Rent seeking in state capture*

The mounting political failures of ideological elites’ program parties gave way to the rise of mass elites’ business-firm parties in those V4 countries too, where the party setting was not dominated by them from the beginning of the transition process. Hence, influence of private interest in policy making intensified. Less political competition resulted in spreading state capture. This process opened new opportunities for rent seeking and legalized corruption. I would like to emphasize, that state capture opened new opportunities but this does not mean that corruption was absent in the previous 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 the state was captured through business-firm type parties.

Material rents stemming from political power positions occur in all political systems. The extent of the rents as well as channels of rent seeking depend on the efficiency of political and social control, democratic institutions. Nevertheless, we should not forget about the major driving force of the establishment of modern political democracy: curtailing the prevailing private (or close group) interest over the society as a whole. Strong control institutions are important because they limit the opportunities of rent seeking; political competition increases its political risks. However, this does not mean the elimination of drivers. The transition process in CEE could be interpreted as competition process for the redistribution of economic power. In case of privatization

this meant the redistribution of existing valuable assets, a process which was of course designed and executed by state institutions. The privatization process was the first main area of competition for personal wealth generation through state agencies in transition economies.

There were various political goals to be achieved with privatization ranging from eliminating the business background of incumbent management, communist party members (Frydman and Rapaczynski, 1994) through the establishment of basic market institutions like the stock exchange or strengthening property right enforcement (Rapaczynski, 1996). Contributions to this string of literature were influenced much by the activity of World Bank and the “global advising community” (Appel, 2004). They usually took the position of neutral observer or reformist politician governed by theory-based principles in the process of policy making (in this case the neo-liberal paradigm). From the distance of two decades we may conclude that this was a rather naïve approach: self interest has always played a significant role especially in those areas that were directly attached to property acquisition like privatization policy.

Walder (2003) treated privatization from the angle of elite opportunities of state asset appropriation. In his view barriers to asset appropriation varied among transition economies with the extent, pace and form of privatization and the concentration and liquidity of assets. Different combinations of the circumstances jointly affected the extent to which old and new elites obtained ownership or control over privatized assets, used political positions to extract large incomes, moved into salaried elite occupations or provided any other new opportunity for elite enrichment. Effective constraints on asset appropriation were applied in countries that resisted (China, Vietnam) or slowed (Slovenia) privatization. When state property was not intended to be quickly privatized, opportunities of obtaining high incomes from state property were possible (in forms of salaried positions, hidden asset conversions and tunneling), but no direct appropriation of state assets by incumbents was allowed. However, acquired benefits could be similarly high then in case of property appropriation. The other setting in which asset appropriation was relatively constrained was bound to orderly privatization that transferred assets through transparent and competitive policies. In this case incumbent elites either lost their positions too quickly to appropriate state assets or the

privatization process was well regulated and monitored and incumbents' access to property was designed under state control (East Germany, Poland, Hungary).

Constraints on asset appropriation were weak in cases when ruling communist party survived intact and maintained political control in the transition process under new name after abandoning its commitment to superiority of public property and central planning (many post-soviet countries). State assets could be channeled to the hands of officials, their clients and associates who might want to remain in politics or change onto business entirely. Pervasive state asset appropriation became possible also when a nation during the quick regime change rapidly privatized state assets without establishing barriers to incumbent managers to seize control over the process using it through various ways to increase their private wealth (Russia, Ukraine). I see the main difference between the two patterns in the pervasiveness of state asset appropriation by incumbent oligarchs in the latter case.

From the viewpoint of the V4 Walder's Type 1 setting is relevant which is characterized by high extensiveness of regime change and relatively strong regulatory constraints on asset appropriation. This gave way to the participation of multinational firms in V4 (with the significant exception of Poland). New elites were recruited with those with higher education and skill more likely to enter salaried positions. This argument corroborates well with Drahekoupil's thoughts on the "domestic comprador elites" serving multinational business – the main proprietors of CEE economies. In some countries (mainly in Hungary) incumbent management effectively supported FDI-based privatization policies and joined the "comprador elite" instead of becoming proprietors, which was an obtainable option for only relatively few. Nevertheless, control over state asset appropriation was not perfect in none of the V4 countries either. Asset tunneling occurred rather frequently (Poland, Hungary), political insiders gained assets cheap (Slovakia). Nevertheless insider trade did not become the main tendency in these countries. The emergence of the "domestic comprador elite" alongside with dominance of multinational business can be regarded as the main characteristic of V4 development.

In this setting of "competition state" the "comprador elite's" material wellbeing and enrichment was based on the existence and strong influence of multinational companies in the V4 countries. Salaried positions in the boards and management of firms and the

advisory background institutions as well as banks were filled by governing party members and their clients. Business and administrative positions were frequently mounted and there was regular personal exchange between administrative and business positions (Drahokoupil, 2008). The main beneficiaries of this setting were those segments of the elite who supported multinational business to gain much influence in the V4 countries. From the ideological viewpoint mainly liberal parties took this role, but they were regularly allies of other larger parties that did not refrain from liberal policies either. The other main party group, the conservative-nationalist and christian-democratic parties preferred strengthening national bourgeoisie and typically did not enter the “comprador elite”. “Business firm” parties of V4 usually supported the nationalist agenda.

There is some empirical evidence showing the occupation of corporate boards and advisory committees by politicians and clients in various countries. Of course, it is much easier to take controlling positions in state owned companies. It can be regarded as general practice to change not only the supervision but the complete management of SOEs after changes in government. Most of the empirical evidence is based on this group of companies. Skuhrovec (2014) for example reported peaks of personnel change in Czech SOE supervisory boards after election years. This practice on the one hand eliminates the conflicts between management and politician. But this gives also an opportunity of 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 not just 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, donate charity organizations or various activities of the government and politicians. SOEs are also used for the rewarding clients of the politicians by for example financing expert fees.

Unlike during the heydays of privatization of the 1990's main areas of rent seeking thus shifted from property acquisition and tunneling or entering the interest sphere of multinational business towards controlling and running enterprises. As it was shown by Szanyi (2016) the privatization logic was reversed to the opposite during the 2000s. Slowing privatization in Poland and nationalizations in Hungary aimed the maintenance



and expansion of party controlled state influence and rent seeking from SOEs. In this period state ownership served the enrichment of elites that previously did not join the “comprador elite group”. Of course the decline of available state assets to be privatized also contributed to this. The remaining for the 2000s state assets were either notorious loss-making companies (like mines in Poland) that were not worth for insiders of possessing. Another part was large service providers that could not be easily transferred to rent seeking private hands but were very much suitable SOEs for mass scale milking. Another reason of keeping state assets might be the changing domestic and international environment. International organizations were not concerned so much about privatization any more than they used to be during the 1990s. Therefore international pressure for privatization declined.

Another interesting and more detailed empirical study intended to elaborate party-dominated companies’ external networks in Hungary (Stark-Vedres, 2012). In earlier papers Stark called attention to the possibility of previous SOEs’ incumbent managements’ survival and the transfer of their economic power into new business forms using informal networks (Stark, 1996; Stark and Bruszt, 1998). This concept was changed in the light of new empirical findings: the dominant networks of the 2000s do not pose a political threat of systemic reversal. The new networks even if they are controlled by former SOE’s managers or communist party members work inserted in the new economic environment. What is new is the spread of partisan firms, that is politicians and their clients control very significant parts of private business besides SOEs that are also used for rent seeking (we come back to this issue in the next chapter). According to the survey of Stark and Vedres (2012) which was conducted with data of 1696 large and medium sized companies in Hungary for the period 1987-2001, party members and clients took controlling positions in less, than 10 % of firms at the eve of systemic transformation (1989) but this number steadily grew to almost 20 % by 2001. Moreover, 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 two competing main coalitions (right and left) and found that after elections winning parties’ influence accelerated and losers’ declined. However, the magnitude of the fluctuation declined, influence became less dependent on government

changes. In my interpretation this meant a marked shift from controls of SOEs towards privately owned companies, the management of which remained largely immune from political changes. This phenomenon needs further analysis.

*From party state capture to party business capture*

Analysts of the first decade of transition in post-communist economies agreed that in CEE but especially in the V4 countries democratic and market institutions evolved, business systems and political systems were largely separated, albeit they of course influenced each other. Firms competed for capital, labor, suppliers and customers, parties competed with each other in democratic electoral system for political power in order to fulfill 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 danger of the systemic change, a potential route from “plan to clan” instead of “plan to market” (Stark, 1991). In this concept clan meant reincarnation of communist political and economic power through the development of “recombinant property”. The clan-concept returned in the analyses of transition during the 2000s again, 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. We call this new type of relationship party business capture rather than clan economy: the dominance of political parties over significant parts of the economy.

Despite of the political consensus in the 1990s about developing democratic institutions based on competing political parties and market economy based on free competition (the “competition state”) the coevolution process of the two systems soon directed the attention of both business and polity to potential alliances. The concept of sharply separated fields of business and polity was undercut by the logic of competition in the two spheres. Business needed insider knowledge and government support in competition for markets (e.g. in public procurements). Polity needed cash 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.

In Hungary, the first period of transition the relationship was dominated mostly by business (Sallai and Schnyder, 2015). This is the time of the heydays of the “comprador elite”, with strong influence of multinational business. It is also shown by Stark and Vedres (2012) that by the end of the 1990s struggle over dominance of SOEs became less significant way of combining political and economic power. Besides multinational firms influence, partisan private firms started to take the lion’s share of politicized business in Hungary during the 2000s. After 2010 Hungarian government started to increase government control also over multinational business. In a trial to split the strong representation of foreign firms and undermine their political influence Hungarian government introduced selective advantage and disadvantage measures (Szanyi, 2016b). The measures intended in many cases supporting 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 reestablished the lobbying platforms of selected foreign firms. In exchange the government required support of politically important programs. Business-polity relationships of the 2000s have been increasingly dominated by partisan business in Hungary. The emergence of partisan business means an increasing politicization of business: the capturing of business by political parties, the conversion of state power into economic power. The economy like the political arena becomes increasingly polarized. Competition for markets and income establishes as part of competition for votes and political influence. In this setting cooperation patterns among partisan firms strictly follow political alliances: firms of political allies do business with each other but not with firms of the opposition (Stark and Vedres, 2012).

Wedel (2001) distinguished between two qualitatively different stages of business capture in CEE. The return of state capitalism in this part of the world is linked to more profound transformation of the state and the underlying party-driven elite structure

than in cases of other regions and periods (e.g. models of developmental state in South-East Asia or authoritarian regimes in emerging states). Wedel classified most transition economies as “partially appropriated states”, where informal groups take over from the state certain functions or collaborate with state authorities, but the group is not synonymous with the authorities. This relationship can be also classified as state capture: state authorities work under the influence of business interest groups. On the other hand, Wedel’s “clan state” is one where certain clans (interest groups) are so closely identified with particular state authorities or institutional segments of the state, that “the respective agendas of the government and the clan become indistinguishable” (p. 11.). The “clan state” is controlled in most obvious cases by a charismatic leader and his/her subordinated political allies collected in political parties (most probably in business parties). The concept of “clan state” corroborates with Schoenman’s concept of patronage state (Schoenman, 2014). Both concepts describe various aspects of business capture.

The “clan state” as a form of business capture can be the product of the business-polity coevolution process which starts with largely independent actors working on fulfilling mutual interests. If however polity is able to take over the higher end of the relationship it becomes increasingly dominated by political interest which is expressed mainly by personal and largely informal pressure. The political resources that once independent firms wished to obtain may transform to a golden cage. “Firms have to be ‘locked into’ this golden cage of political ties to survive, but these ties allow the state at the same time a close control over firms.” (Sallai, 2014, p.5.) This process was described on the example of Russia by Yakovlev (2006). But state (party) control over firms can be also developed intentionally: many of the partisan firms were established as such to serve various rent seeking purposes. New forms of rent seeking require loyal partisan firms.

When privatization and other forms of state asset appropriation were exhausted new forms of elite enrichment were discovered. These forms were as we argued bound to existing and functioning business that is the rents stem from operation and not so much from capital transactions. Since the number of SOEs could hardly be expanded (despite of nationalizations in Hungary), party controlled private business took the lead in

obtaining rents. New forms of rents were bound to ongoing business activity: much of them could be realized in legally undisputable ways through means of “legal corruption” (Kaufman and Vicente, 2011). Legal corruption is based on a broader definition of corruption that regards all kinds of transactions conducted with the participation of public actors that serve private interests at the expense of the public interest, even if the transaction is not illegal.

The new source of rent seeking from public procurement through partisan firms gained momentum after the V4 accession to the European Union. Up till then, structural policies used mostly fiscal measures providing supported industries and companies tax holidays on state and also local levels. The most known example of this tool kit is investment promotion policy (Antalóczy et. al., 2011). Tax measures can certainly alter competitive positions on markets, but they are rather “tools of the poor governments”. They redistribute future incomes which in most cases would not exist otherwise. Redistribution of existing incomes that is financial support schemes spread on mass scale only after 2004 when V4 state policies were streamlined with the *acquis* of the EU. The preference on financial support meant an opportunity to redistribute real money. At the same time the structural funds of the EU were opened for the new member states widening potential financial sources greatly.

Party controlled firms for example could be filled with public procurement orders if tender conditions were formulated in appropriate ways. Limiting competition or even the complete elimination of it in public procurement tenders is a frequently used tool of legal corruption in Hungary (Fazekas, et. al. 2013). There is ample evidence about the swings in market shares of companies participating in public procurement tenders (op. cit. 76.o.). This reflects the changing preferences of the political leadership for particular clients’ firms (for details see: Sallai and Schnyder, 2015.). The analysis of EU sponsored projects in Hungary showed that 33,8 % of the contracts between 2009-2012 received only one bid (no competition). Modifying of contracts after awarding took place in 17,7 % of the cases: a potential way of creating rents to be extracted (Fazekas, et. al. 2013, p. 78.).

## **Conclusions**

This paper is an attempt to combine and interpret business-polity linkages of CEE and especially the V4 countries from the viewpoint of institutionalized rent seeking. A profound change was identified during the early 2000s in patterns of rent seeking and in its enabling policies. With the demise of privatization accessible state property disappeared. Leftover firms were not lucrative but financially problematic. Practice of rent seeking changed to mass scale milking of SOEs. A new source of cash flow also emerged: EU-sponsored development projects could be effectively drifted towards genuine partisan firms in order to realize profits on mass-scale development project spending.

Changing patterns of now partly legalized corruption became possible when the state became captured by political parties. Political competition started to decline when traditional program parties and their “ideological elites” lost credibility during the 2000s. The political vacuum was filled by business firm parties that had no solid ideological underpinning but served as political platforms of the “mass elite”. Since these parties had no ideological obstacles they could start weakening or eliminating control institutions of the “competition state” including both political and social control institutions. This practice helped them to monopolize political power as well as various rent seeking opportunities.

The paper combined new findings of various strings of literature: elites and their political parties, rent seeking and corruption, business-polity networks. It aimed to further develop the theory of Central European model of capitalism, particularly to the dependent market economy model (DME) developed by Nölke and Vliegenhart (2009). Fitted into the varieties of capitalism literature this paper argues, that one important specificity of the model is strong and corrupt relationships between business and polity the main carriers of which are partisan firms. In another paper I argued that arbitrary involvement of the state in changing the ownership patterns of the Hungarian economy would bring important systemic risks (Szanyi, 2016). State favoritism creates similar risks. Basic market economic institutions like the security of private property regime and the rule of law can be seriously undermined if the government does not apply the

laws consequently for his own transactions. The decline of normative regulation and preference of selective measures will deliver the wrong message to economic agents that their success will more depend on the development of their network capital than own business activity. Selective advantage and disadvantage measures can effectively change market conditions in favor of clients against strong multinational competitors. This process may alter dependency on foreign investments emphasized by the DME model. However, not increased competition but increased corruption and less market efficiency is provided in exchange.

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