Central and Eastern Europe Buttressed by the European Union

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The changes currently underway in Eastern European territories are the product of both the profound transformations made by the imposition of the Soviet model between 1945 and 1989 and the new economic dynamics set in motion since 1989. If the first decade of post-communism was marked by the collapse of the traditional industrial and agricultural milieus, the arrival of foreign direct investment (FDI) in certain sectors and the blossoming of private initiative, the second decade is characterized by the emergence of poles of development hinging on European aid, particularly structural funds. The radical reconfiguration of the production environments inherited from the former regime led to a major reorientation of trade towards the West in the 1990s. The territorial disparities once contained by the communist egalitarian policy widened after 1990 as a result of the polarization of development. The notions of metropolization, cluster and cross-border cooperation that structure economic development in the West have now taken hold in the East as the basic categories for development, sustaining growth rates considerably greater than the EU-of-15 average.

Communist legacies and territorial polarization

Development of heavy industry and incomplete urban development

The Eastern European territories have been deeply marked by the imposition of the Soviet model, for which the size of production complexes and their sectoral and regional concentration were the two major levers of development. In that light, the primary aim was not to wipe out the entire industrial base, as with the

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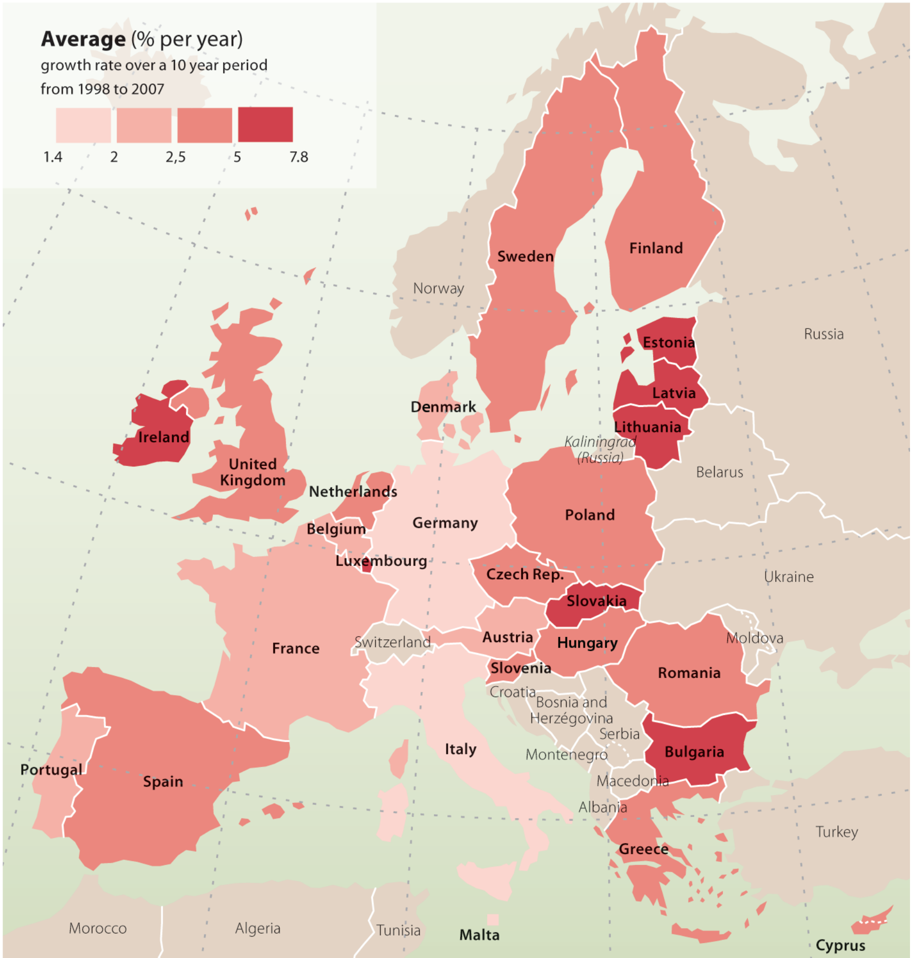
figure 51: **Annual GDP growth rate of EU states, 1998-2007**



Source : compiled by Dorian RYSER, from Eurostat.

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liquidation of the propertied classes. On the contrary, the aim was to reinforce industry where it existed by concentrating activities within huge production units, and to create industries in places where they did not yet exist, particularly in the eastern territories. The former mining and steel manufacturing areas of Lower Silesia and Upper Silesia in Poland, of Moravia and Sudetenland in Czechoslovakia, of northeastern Hungary and of the Jiu Valley in Romania—all legacies of the first and major wave of industrialization that took place in Central Europe in the 19th century, and for regions such as Silesia and Moravia two centuries earlier—were thus largely privileged. It was in these gigantic plants, which often employed over 10,000 workers, that the authorities intended to shape the "new man".

To hasten the process, investment was lavish: it reached considerable sums, about 20% of the total public investment, so that new industrial areas could be created, devoted exclusively to heavy industry at the expense of so-called "light" or consumer industries. New towns rose suddenly up out of the ground in rural areas right next to the factories, some of which were never completed. Examples were the steel manufacturing city of Eisenhüttenstadt near Frankfurt-an-der-Oder, Nowa Huta ("the new steelworks") next to Kraków, Dunaújváros in Hungary and the steel-producing area built at the gates of Sofia. Yet even if urban development experienced a considerable boom, it did not enable the East to catch up with the West. Worse, the new urban ensembles did not invert the historic tendency specific to urban networks that were denser in the western parts of the various countries, often particularly those with a Germanic tradition, whereas their eastern counterparts in the Russian or Ottoman tradition typically lagged behind, as is generally the case with eastern regions characterized by considerable spatial dissemination.

Collectivization of the Eastern European countryside and East/West disparities

Alongside the working-class bastions that were the mines and the steelworks, the energy and utility sectors as well as the metallurgical and mechanical industries, the Communist authorities intended to operate in the same way in agricultural areas. In this case, however, the industrial organization of production was imposed by force via the creation, often *ex-nihilo* as well, of collective farms, even if in several countries the agricultural dualism inherited from past centuries had made large farms part of the Eastern European landscape. This was true of the large Junker estates throughout Mecklenburg and Pomerania, in the once German Pomeranian territory that was now Polish, and in Hungary. Conversely, in the Balkan countries, the end of the Ottoman Empire led to extreme fragmentation of land holdings. The model imposed was the Soviet-type *kolkhoz* developed in the 1930s in the USSR. Very soon, in the 1950s and 60s, technical specialization led large farms to appear, specializing in stockbreeding or crop farming. These farms regrouped several dozens of thousands of workers and sometimes had a farm machinery station added (on the *sovkhoz* model). Lastly, in the vicinity of the state farms, tiny plots of land were left at each family's disposal, parcels that varied in size over the years but whose economic, social and local importance was vital, given that they guaranteed economic survival and more generally the transmission of peasant know-how. The entire area under communist domination was covered by these large industrial agriculture units—cooperatives or state farms—with the notable exception of Poland, where nearly 75% of the arable land remained privately owned, but with the average holding scarcely exceeding 6 hectares in 1989, compared with 1,300 ha for state farms.

The dynamics of territorial development thus underwent considerable upheaval due to such excessive industrialization, all the more as development

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throughout the continent was conceived simultaneously in terms of an integrated market in the East as well as conflict, even war, with the West. For this reason, areas bordering the now-enemy Western countries were hermetically sealed and dotted with watchtowers, barracks and military training fields, resulting in considerable degradation of the soil, the renovation of which took up the better part of the 1990s. The old territorial balances suffered the effects of Cold War geopolitics, and entire territories were cut off from their traditional hinterlands, such as those lying near the border between the two Germanys but also those situated between Bulgaria and Yugoslavia or between Poland and Germany. The north of the German Democratic Republic, which had never been developed, was rapidly industrialized, particularly to compensate for the loss of ports, all located in the West (Hamburg, Bremen and Kiel) or handed over to Poland (Szczecin). In Czechoslovakia, investment was concentrated in the eastern part of the country (today's Slovakia), particularly for military production. Hungary went through a similar evolution.

Post-1989 dynamics

Starting in 1989, the deep restructuring of Soviet-style economic organization as well as a flow of foreign direct investment upset the balances created over the course of nearly 45 years in Central Europe. These two factors made the countries eligible for European pre-accession funds starting in the year 2000, and for structural funds which, beginning in 2004, made regional development a national priority.

The end of a model, the return of dualism

On a territorial level, the combined impact of opening borders and confronting markets on the one hand, and the radical transformation of the Soviet development model on the other, translated into a serious crisis for formerly privileged sectors—mining, steel manufacturing, energy and mechanics—which few investors, if any, wanted to take over. In that time of rapid transformation, it was imagined that catching up could be achieved not by fitting out the missing technological cycles in sectors affected by radical changes due to exposure to Western capitalist practices, but by liquidating them. Thus, the industrial colossuses of the Soviet era soon became industrial wastelands. The weight of such decrepitude was all the heavier to bear on a local scale since these industries had contributed to shaping entire regions. Simultaneously with this collapse, which caused large pockets of unemployment, a trend developed of starting companies in the vicinity of the large complexes. Tiny family businesses came into being, only a handful of which eventually converted into service providers for business. At the same time, the gap widened between the major regional cities or capitals, certainly hit by the crunch but having their own alternative resources available, and the rural milieus, dotted with small and medium-size towns. These small urban areas were the ones that had to bear the most dramatic effects of the post-1989 transition, first because they had been the first beneficiaries of industrialization in the 1960s and 1970s, when they acted as subsidiaries of major groups which themselves had remained in the large cities; next, because in the wake of this wave of industrialization, they benefited from the creation of major government service agencies, to the extent that some of them became "regional capitals". The severe crisis in the 1990s drove them into an impasse, not only because the industrial subsidiaries were the first to be dismantled, but also because state reforms very often led to the liquidation of their administrative prerogatives, and lastly, because of the collapse of the large community farms.

Very soon, the idea prevailed that the agricultural model now had to conform to the West's, dominated by average-sized family farms. Two public policies gave concrete backing to this model, which had never really existed in the Eastern European countryside: the restitution of land to its former owners (prior to collectivization) and privatization of collective property. The first policy led to a scattering of land ownership and its extreme fragmentation; in many places it was ineffective because of the incapacity of landowners to make their way in the new economic landscape, owing to age or merely incompetence. The second policy, land privatization, was conducted in a highly disorganized fashion in the name of ideological principles: for some, the guiding principle was to obliterate the legacy of collectivism; for others, the main thing was to preserve jobs and local traditions. In this incessant conflict, the state often retained a large share of land ownership, particularly in Romania. These two dynamics resulted in a considerable diversification of rural areas, whether in the practice of leaving large stretches of land fallow, or the reappearance of very large industrial farms managed by former engineers and technicians who managed to rent land that was not cultivated by the new owners, or the emergence of a large number of small farms, often under 10 ha in size. Finally, the dualism historically very present in this part of Europe underwent a revival after 1989, although it did not bring in its tow either the anticipated efficiency or a real privatization of farming activity comparable to that in Western Europe. Thus, contrary to expectations, large estates with often more than 1,000 hectares continued to predominate in the eastern part of Germany and the Czech Republic, while in Estonia, Lithuania, Poland, Bulgaria and Romania, all countries with a strong farming population, farms did not exceed nine hectares on average (3.5 hectares in Romania, 8.6 hectares in Poland) in 2006.

Foreign direct investment

FDI has had a considerable impact on the territorial level, and for this reason largely accounts for new forms of polarization in this part of Europe. Not only

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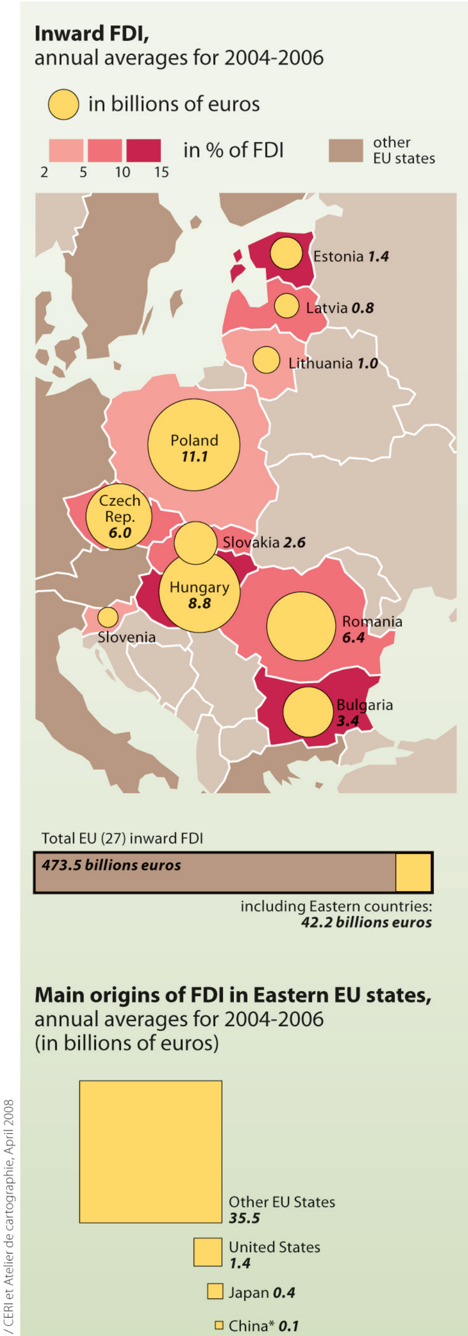
has it buoyed up macroeconomic development by boosting exports and stimulating the territories through financial funds and technology, but it has also largely contributed to the employment crisis by drastically reducing the exorbitant number of workers employed in the companies taken over. It was only from the 2000s that greenfield investments replaced brownfield investments and created the anticipated jobs.

First, and throughout the whole 1990 decade, FDI was concentrated on the four countries of Central Europe and there was hardly any, or none at all, in the Baltic countries or the Balkans. In terms of per capita amounts invested, Hungary and the Czech Republic, Slovakia and finally Poland together concentrated nearly 80% of the investment. This superiority was not reduced until the 1990s when foreign investors moved north and especially south towards more politically stable countries certain to join the EU in the long run, even if they were taking a little longer than the first group to enter.

Within each country, FDI created a large gap between cities and rural areas. Several agribusiness industries certainly benefited from large investments, particular in Hungary, Poland (the second largest producer of red fruit in the European Union), and Bulgaria (in the milk products sector). But FDI nevertheless shifted massively to urban areas where the effects of agglomeration were the most palpable, opportunities most obvious and services most developed. The capitals and major regional cities were the first to benefit from FDI, as opposed to medium-sized and especially small towns. It was not uncommon to see more than half of foreign investments localized in capital regions. This explains the importance of another disparity that came to overlap the first: the gap between west and east. Given that the most developed cities were always located in the west (with the notable

figure 52: **FDI to some Eastern EU states, 2006**



*Including Hong Kong

Source: Compiled by Dorian RYSER, From Eurostat.

Sciences Po / CERI et Atelier de cartographie, April 2008 exception of Warsaw), territorial development was much more apparent in this part of Central and Eastern Europe. Added to that is the fact that the western regions of some countries are adjacent to highly developed countries (Germany and Austria), whereas on the other hand, the eastern regions border poor or even very poor regions (Ukraine, Belarus, Moldova and Russia). The latter moreover do not have the benefit of decentralized governments, unlike the Polish, Hungarian and Slovakian regions. The concentration of FDI in the countries of Central Europe, and, within them, in developed urban areas adjacent to the territories of the EU-15 states led to the polarizing of growth and development in the quadrilateral represented by the cities of Prague, Bratislava, Vienna and Budapest, with the hope that development would spread to the surrounding areas. It is in this quadrilateral that all the automobile manufacturers of Western Europe, the United States, Japan and Korea have located along with their suppliers. Connected with the developing EU territories, the western regions of the ten countries that recently joined the EU thus stand clearly apart from their largely peripheralized eastern counterparts.

Main lines of development: metropolization, clusters and cross-border cooperation

Under the impact of these various factors, identified early on in the first decade of post-communism, three main lines of endogenous development, largely sustained by European financial aid, have been identified as the structural pillars of the 2000s. The first, on which the "new" member states are massively wagering, is metropolization. Unlike the West, where this term refers to urban units of over one million inhabitants, in the East, although it also refers to capitals of comparable size, these are part of a much looser urban network. With the exception of Poland, in no country does the second largest city exceed 500,000 inhabitants, scarcely 300,000 in Bulgaria and 200,000 in Slovakia or Hungary. Only Poland can actually claim to have a strong urban network with eight large cities—Warsaw, Lodz, Kraków, Katowice, Wroclaw, Poznan, Szczecin, and Gdansk—to which should be added two cities in the Eastern region, Bialystok and Lublin. In any event, the concept of metropolization is used to conceive a type of development concentrated around large cities, due to transport infrastructure capable of supporting worker mobility by fostering the link between urban peripheries and city centres as well as between the centre and its regional hinterland. The prevailing notion here is one of polycentric territorial development organized around cities viewed as regional capitals that are purveyors of services, particularly in terms of the job market and community facilities. And so, associated with the idea of metropolization are the notions of free zones and "industrial parks".

The second main line of endogenous development relates to the notion of cluster which, in the field of sectoral production, is supposed to illustrate the decisive factors for the economic catching-up process, the concentration of

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resources (material and human), and the potential for diffusion to surrounding areas. Here again, the term is employed in the East in a different sense from the way it is used in the West, where it refers to a central factor of "social capital" in economic geography analyses. This term refers in theory to relations of mutual trust at the basis of local production systems that constitute informal networks in which various employment, innovation and export services are exchanged. Borrowed directly from Putnam, this approach emphasizes the importance of informal relations, the anticipatory capacity of actors and collective initiative in building local milieus. In practice, the term "social capital" refers to the French "local systems," the "second Italy" or "Silicon Valley"—all examples that highlight the innovative capacity of local milieus, largely based on family relations or relations of proximity, which rely more on the "community" than on "society", to use the standard dichotomy.

After nearly a half-century of communist-style organization based on the liquidation of family production, it seems to make little sense to talk about local heritage in the East. What heritage could possibly have been preserved that could revive local production networks, alumni associations, family relations or industrial traditions? Moreover, development deficiencies attest to a glaring lack of cooperation among private and public actors. Everywhere the low level of government commitment to industrial policy can be noted. Despite that, there is a great diversity of clusters on the basis of a very high degree of territorial concentration in certain industrial branches, the development of their innovative capacities and the networking of certain services, particular commercial services. The pre-1989 territorial organization can play a role when it is linked with the introduction of FDI. Rarely are local operators alone responsible for tapping "hidden resources", to use Hirschmann's term, even if such cases do exist, for instance the "Aviation Valley" in southeastern Poland. More generally speaking, Eastern European development since 1989 seems more like a combination—some speak of a hybridization—of local resources and foreign capital, more exactly as the recomposition of an industrial heritage (with strong cultural traditions) that fits with Western development norms.

This is for instance the case in the automobile sector wherever it has developed (particularly in the above mentioned quadrilateral), as well as the pharmaceutical and electronics sectors, particularly in Poland—in Lodz, Warsaw and Kraków—but also in Hungary, and in the region of Ljubljana in Slovenia, in the metallurgical and energy sectors in Moravia, and in the lumber sector in the Baltic countries, Poland and Hungary. Certain clusters have arisen out of the initiative of a few SMEs that have set up in the same location and have generated a regional concentration. Others have been created by cooperatives in reaction against supermarkets. Still others, more rarely, have a specifically agricultural focus, such as the food production cluster in the Polish region of Lubelski.

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Sometimes these clusters are located within "special economic zones" that were created after 1990 in declining industrial areas. The aim was to attract both foreign and domestic investors by setting up fiscal incentives on the condition that a minimum amount was invested (from 500,000 to one million euros in Poland), jobs were created, new technology introduced, etc. Given their importance in these regions undergoing conversion, the European Union tolerated them beyond 2004, and some of the zones today have turned out to be major actors in Eastern European development. This is true of the "economic zone" of Wallbrzych in Lower Silesia, Poland, hard hit by the mining crisis in the 1990s, which in 2007 constituted one of the most dynamic regions in Poland. Spread over 18 sites and 14,000 ha, the zone can boast of having attracted some 30 major international corporations, including Toyota, KPMG and Italmetal, for a cumulative amount of 1,505,000 million euros invested and 22,980 jobs created.

The third main line of development has to do with cross-border cooperation, to which the European Union since 2006 has devoted a new development instrument. Border areas represent a major development stake owing to the number of inhabitants in such areas, particularly those in the East adjacent to Russia, Belarus, Ukraine and Turkey, and the backwardness affecting them. Several phenomena have come together to reinforce the peripheral nature of these regions since 1989: the collapse of agricultural complexes, the lack of FDI, the emergence of a vast informal economy, large trade asymmetries due to the centralized nature of the Russian, Belarusian and Ukrainian economies, and the introduction of the neighbourhood policy which deprives states bordering the EU of any hope of membership in the short term. Yet Poland, Slovakia and Hungary are all keen to link their eastern regions to their central poles of development and to do so have implemented assistance programmes all based on the same principles: the strengthening of transport infrastructure between regional cities and border areas, support for local economies, particularly SMEs, and aid for cross-border cooperation in the educational and cultural sectors. The fact nevertheless remains that to attract foreign investment, many of the so-called peripheral regions still rely essentially on the low cost of their labour. In this context, the relevance of certain programmes that seek to enhance innovation where there exists no scientific community is questionable, as is the wisdom of favouring the metropolization process where urban networks are extremely loose.

Are these development characteristics of Central and Eastern Europe likely to provide outlines for an Eastern European "model"? Beyond the differences stemming from their industrial, agricultural and territorial legacies, the ambitions of the political authorities on the whole or the instruments used to further them do not seem very different from what can be observed in the West. EU recommendations regarding economic, social and territorial cohesion have been accepted by all. They constitute the basis for national development programmes, all oriented towards

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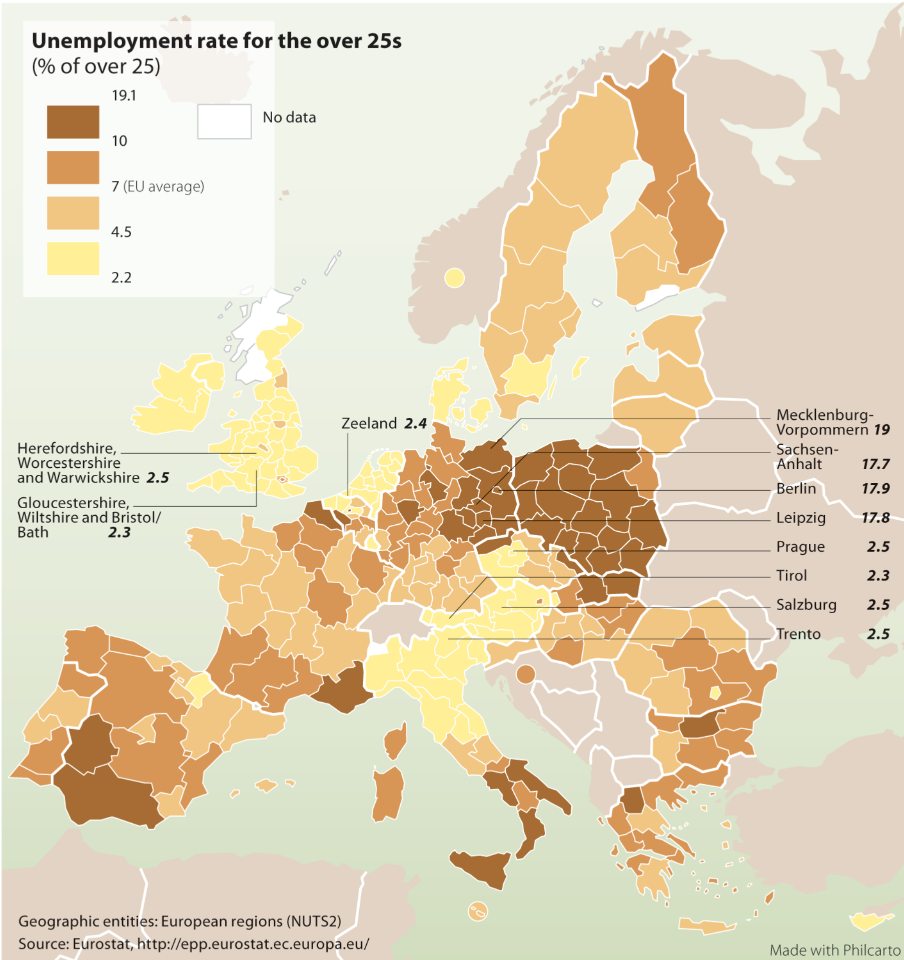
figure 53: **Unemployment rate for the over 25s, 2006**



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promoting growth, reducing unemployment and reducing the growing territorial disparities due to the rapid growth all these countries are experiencing.

In all the operational programmes established for the 2007-13 period, regional development is at the top of the list of allocated amounts, ranging from 25% to 30% of the total aid. At the national level, the consolidation of regional and local governance is cited as the mainspring of territorial development in the future. Infrastructure is the primary budget item and the notions of metropolization, cluster and cross-border cooperation are considered as the foundations for development. Lastly, the West's fundamental concerns over energy supply and environmental protection are all the more shared by the East because the dependence of these countries on Russia is much greater than the West's (except for Germany), and the weaknesses inherited from the former regime are immense in this particular area.

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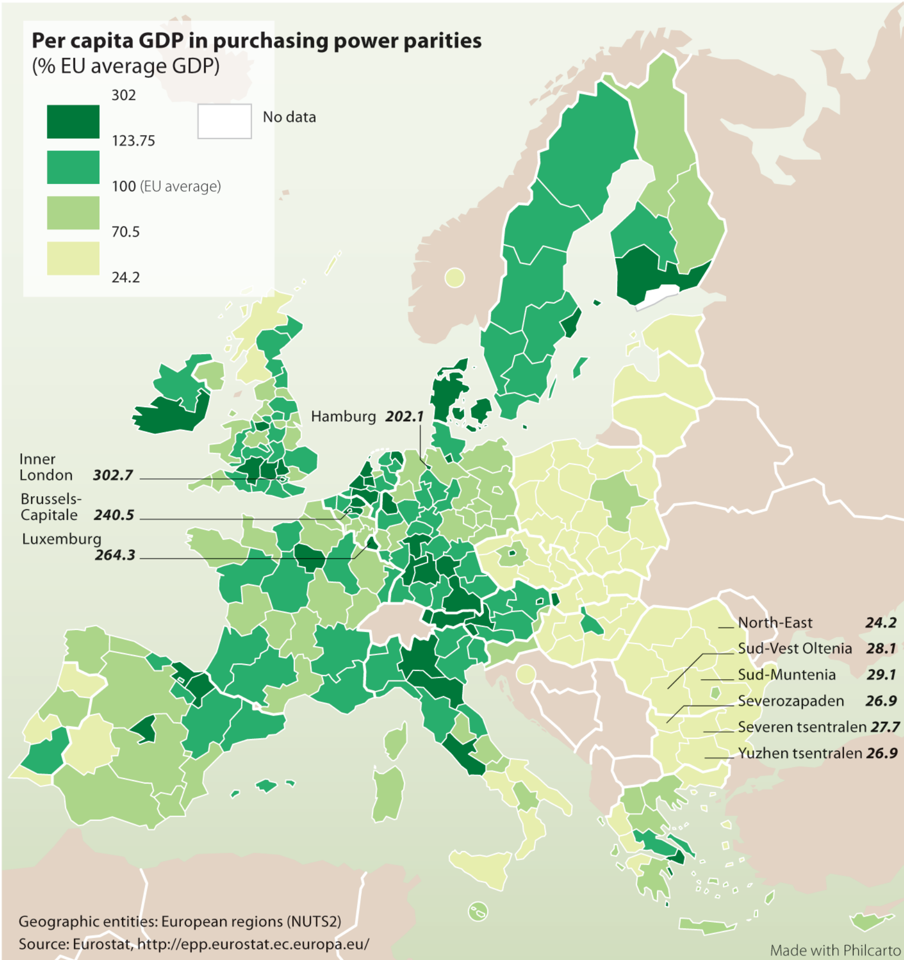
figure 54: **Per capita GDP, 2006**



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The conditions for a balanced development

Nearly 20 years after the fall of communism in Central and Eastern Europe, several development patterns have come to light. These are characterized by polarization and concentration of resources on one hand, and slower development and a low rate of FDI in certain territories marked by rural decline and their peripheral situation, on the other. A dual phenomenon results: growth in the territories taken as a whole with respect to the European average—in other words catching up with the West, evidenced by annual GDP growth rates of more than 6% since 2004 in all the countries—and increasing differences with developed areas.

In these conditions, it is nearly impossible to ensure balanced development, and one that would combine economic growth and territorial cohesion, even if the

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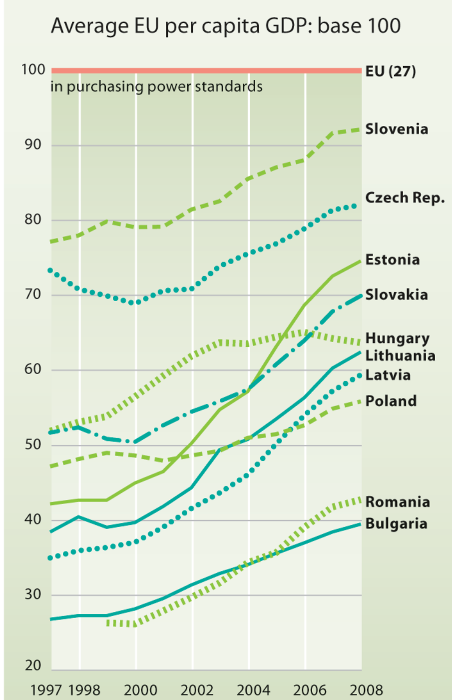
territorial disparities are not as marked in the East as they are in the West. Actually, between growth and solidarity, national development programmes have opted for the former, hoping that growth will have a domino effect powerful enough to prevent the gulf between regions from widening. In Hungary, differences in regional GDP between Budapest, the capital, and north-eastern Borszöls were on a scale of 1:2 in 1988; 20 years later, it was more than 1:3. The territories of northeastern Romania or the central Bulgarian plain show a regional GDP of about one-quarter of the European Union average, and the poorest Polish regions, the Carpathians and Podlasie, about one-third. This is the feature highlighted in the third report on cohesion in 2005 for the member countries of the former EU of 15, when the Commission had identified both a dynamic of convergence of national GDPs and growing disparities within certain countries at the regional level.

Yet, the fourth report published in the spring of 2007 emphasizes the lack of homogeneity of territorial developments in Central Europe with respect to the west of the EU. This points to the major role of structural aids in reinforcing growth by favouring the concentration of funds and preventing territories from going adrift under the effect of growing inequalities.

figure 55: **Per capita GDP of some Eastern European states compared to the EU per capita average, 1997-2008**



Source: Compiled by Dorian RYSER, from Eurostat, http://epp.eurostat.ec.europa.eu/

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