[Introduction to] Transnational Capitalism in East Central Europe's Heavy Industry: From Flagship Enterprises to Subsidiaries

Aleksandra Sznajder Lee
University of Richmond, asznajde@richmond.edu

TRANSNATIONAL CAPITALISM IN EAST CENTRAL EUROPE'S HEAVY INDUSTRY

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Aleksandra Sznajder Lee

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Introduction

From Flagship Enterprises to Subsidiaries

> The steel sector is a concrete exemplification of all the difficulties connected to democratization and economic reform in Poland.
>
> —Former Polish Deputy Minister of Economy

Introduction

Twenty years after the fall of communism in East Central Europe (ECE), the centrally planned economies in the region have given way to a capitalist system marked by the strong presence of foreign direct investment (FDI). Increased transnationalism, as evidenced by increasing trade flows and exchanges of capital, with inward investment consistently far exceeding outward investment, is an outcome of globalization in ECE countries. As a result, these countries are dependent on the decisions of foreign investors who base their investment calculus and business plan on the global interests of their corporations. The powerful role of foreign investors in the region has even led to the identification of the ECE economies as "dependent market economies."[1]

Heavy industry, and the steel industry more specifically, was among the numerous sectors in the ECE economies dominated by foreign investors. The transformation of the steel industry was highly symbolic and represented one of the most striking features of the transition. The behemoths of yesteryear, the once-proud standard bearers of the communist industrial prowess, became modest and significantly scaled-down subsidiaries of large multinational corporations fighting for meager profits on a hugely competitive world market. This book explains that treacherous journey.

Heavy industry restructuring—defined as actions by management intended to bring about greater efficiency within a company—is challenging, irrespective of geographical region. In ECE, the difficulty of restructuring and privatizing the steel sector was compounded by several factors. First, the industry enjoyed a very privileged position during communism. Second, it inherited pervasive overcapacity, which was a legacy of measuring economic success and prestige in terms of production volume. Third, the postcommunist transition coincided with dramatic changes in the steel industry globally. The transition began after more than a decade of fundamental steel-sector restructuring and capacity cuts in the West, and it coincided with a period of enterprise mergers and fierce competition from new, powerful market players from newly industrializing countries. Given these obstacles, the emergence of transnational capitalism begs the question of how these communist-era flagship enterprises, filled with purportedly nefarious vested interests, not only survived the transition but became profitable subsidiaries of leading multinational corporations. This common outcome is all the more intriguing in that it holds equally for the countries with the best and the worst political and economic reform records.

This book examines the emergence of transnational capitalism in the steel sector, a critical sector of the postcommunist economy, in the four biggest steel-producing countries in ECE: Poland, Czech Republic, Romania, and Slovakia. The analysis focuses on a long-neglected actor in the transition, the state, and on the tension it confronted between domestic vested interests and external pressures. I show that these countries followed different pathways to a common outcome of transnational capitalism and that state capacity played a crucial role in determining which pathway each country followed. Surprisingly, my findings demonstrate that relatively high state capacity is a double-edged sword. Although institutional strength and sophistication can be employed to discipline firms into engaging in market-oriented behavior, it may also enable political actors to shield enterprises from market pressures and promote political and personal preferences that are potentially inefficient. This finding has clear implications for designing economic reform packages not just in postcommunist countries but also in other parts of the world.

The Puzzle

The steel sector was a political hot potato. On one hand, because steelworks were often located in geographically concentrated, mono-industrial towns whose survival depended on them, a great deal hinged on the fate of the steel industry. Moreover, the governments in the region faced workers and managers who had become habituated to privilege under communism. Allowing the steelworks to go under, no matter how economically efficient, was tantamount to political suicide. On the other hand, the ECE governments faced a clear endgame: due to the provisions of the Europe Agreements they had signed with the European Community (EC) in the early 1990s, they were expected to cease state assistance, preferably by 1996/1997 or by the time of accession, at the latest. In other words, after about ten years, the state could no longer assist the steel sector if the candidate country wished to become a member of the European Union (EU).

The EU was not bluffing for two reasons. First, the EU underwent an extremely painful and costly restructuring process of its own sector during the 1980s and 1990s. Second, the EU steel producers found themselves under increasing pressure from global competitors originating in emerging markets, most notably, Ispat International (predecessor of ArcelorMittal). The EU, therefore, had a keen interest in the steel industry, and its member states were extremely wary of any potential largesse being actively or passively bestowed upon steelmakers by candidate states.[2] Beyond the restrictions on state aid, however, the EU played a more indirect role as well; membership became a prized political goal that helped strengthen the other external pressures vis-à-vis the transition governments.

Thus, the key challenge for companies in EU candidate states was access both to the investment capital necessary for restructuring and to a vehicle to help them integrate into the international production networks. The governments' choices for facilitating this process were limited by the paltry financial resources at their disposal and by the lack of a domestic capitalist class with sufficient wealth. Thus, restructuring required strategic foreign investors. As the cases discussed in the subsequent chapters illustrate, being a foreign buyer was no guarantee of quality or of having sufficient financial resources to undertake the restructuring task. Foreign adventurers were more than willing to make a quick buck at the expense of the companies they were claiming to save, with dire consequences for the workers. By contrast, strategic foreign investors had both the intent and the wherewithal to restructure companies. (For the sake of brevity, I refer to "strategic foreign investors" simply as "foreign investors," with the understanding that *investor* implies an ability to generate funds and to lead the restructuring process.)

Sales to foreign investors were certainly not easy; discussion of such sales prompted allegations of trying to sell the "family silver," and the overgrown mills were not exactly hot commodities. Furthermore, separating the working assets from nonworking assets, not to mention company housing units, day-care facilities, local medical clinics, and cultural and recreation centers, to name a few, demanded substantial state involvement. All in all, it was a buyer's market that offered several advantages to prospective investors. Most importantly, the region had an inexpensive and well-qualified workforce with substantial local market opportunities in construction, infrastructure upgrading, and manufacturing, especially in automobile and appliance production. In addition, the region's proximity to Western Europe was attractive due to both relatively low transportation costs and the impending free trade of steel products with the EU.[3]

These investment opportunities became more obvious as the transition process unfolded and economic outlooks became more optimistic. However, the courtship continued throughout the transition process. By the early 1990s, Czech steel producers had already received substantial interest in forming joint ventures from reputable foreign steel producers, such as Krupp, Mannesman, Thyssen, Voest-Alpine, and Usinor Sacilor. In Poland, the Italian Lucchini Group actually purchased the relatively small Warsaw Steelworks in 1992. In the mid-to-late 1990s, several well-known foreign investors, such as Voest-Alpine, Hoogovens, British Steel, and, later, Corus, engaged in far-reaching, albeit failed, privatization negotiations with the government.

Interest by foreign investors in the steel sectors of these two countries is consistent with the received wisdom that FDI tends to flow to countries that have a positive reform record.[4] The reason is straightforward: a better reform record signals greater political stability and results in better legal infrastructure and a predictable legal and administrative climate. When one compares the ratings of economic reform of the four countries in 1999, the Czech Republic emerges as the leader, closely followed by Poland, then by Slovakia, and finally by Romania.[5] As expected, investors' money was correlated with the reform record in each. Between 1989 and 1999, the comparably more populous Poland had attracted a total of over $20 billion in FDI, followed by the Czech Republic with nearly $15 billion. By contrast, Romania attracted $5.6 billion and Slovakia $2.1 billion.[6]

Given the initial foreign interest in the steel sectors of the Czech Republic and Poland and the political and economic difficulties of restructuring the industry, one would have expected the biggest steelworks in these two countries to attract foreign capital sooner than either Slovakia or Romania. After all, the Czech Republic and Poland, as the top reformers, were already attracting more FDI and would have been expected to have the ability to overcome the resistance to sales to foreign investors by vested interests, such as managers, unions, or state agents, interested in blocking reform. Second, the Czech Republic and Poland had more developed market institutions, which were needed to run such sophisticated industrial operations effectively.

However, in the steel sector, Slovakia and Romania became the pathbreakers in selling their biggest steel producers to international corporations. Slovakia sold its largest steelworks, Východoslovenské Železiarne (Eastern Slovak Steelworks [VSŽ]), to U.S. Steel in 2000 while Romania sold its major producer, Sidex Galaţi, to LNM Holdings, now ArcelorMittal, in 2001.

Lagging behind these two countries, considered at the time to be the "laggards" of transition, the Czech Republic and Poland eventually followed suit. The Czechs sold Nova Hut' to LNM Holdings in 2002, and Poland sold Polskie Huty Stali (Polish Steelworks) in 2003. Moreover, unlike in the Slovak and Romanian sales, EU pressure was dominant and direct in the Polish and Czech privatizations.

In Slovakia, the EU was conspicuously absent from the privatization discussions and considerations, even though EU accession was a central goal of the reform-minded post-Mečiar administration. In Romania, a civil servant at the European Commission lauded the Sidex privatization as a "huge achievement" by the government, which "has been clear as to the goals and desire to bring about change."[7] However, at the time of privatization, the closure of EU negotiations was a prospect very much in the future, and it was the World Bank that exerted the pressure to privatize Sidex. By contrast, the privatizations in Poland and the Czech Republic would likely have taken even longer, if they had taken place at all, had it not been for the pressure from the EU in the run-up to the closure of the accession negotiations.

To finish the accession negotiations with the European Commission—itself under pressure from EU steel producers to cut the EU candidate countries no slack—the accession country governments had no realistic alternative to negotiating the permissible amount of state aid with the European Commission. Given the accumulated enterprise debts, at that point, state aid had to be retroactive in nature, granted only once, and contingent upon restructuring and privatization measures assuring sectoral viability on the free market without subsequent aid. The other option available to candidate countries was to provide no aid to the sector whatsoever, which would have meant bankruptcy—and possible liquidation—of their biggest steel producers, an ordeal no government wanted to face. It would have also produced a political drama in which "Brussels" wanted no role, and certainly not that of the culprit. Hence, it was in both sides' interest to reach an agreement prior to accession.

The EU was adamant about the need to solve the state-aid question in the run-up to the closure of accession negotiations. The Czechs were being prodded by European Commission officials to develop a solution to their steel-sector woes. As one Commission official sternly told the Czech government, "This is your problem. If you want to solve it, you better get cracking . . . but time is running very short. . . . If you don't make up your mind over the next few weeks, it will be too late [to grant state aid]."[8] In Poland, the government engaged in elaborate brinkmanship to delay privatization, and the lack of a solution for the steel sector endangered the timely closure of Poland's EU accession negotiations. By the Polish civil servants' own admission, EU entry was "a pistol held to our head" as the government decided how to deal with the privatization of the steel sector in the summer of 2003.[9]

Eventually, the largest steelworks in all four countries were sold to foreign investors, exactly as the dependent capitalist model posits. This common outcome, however, obscures the differences in the trajectories the four countries followed in arriving at this point. As table 1 indicates, by the mid-1990s, the Czech Republic and Slovakia had begun creating a class of domestic capitalists whereas Poland and Romania maintained state ownership.[10] By mid-2005, the sector ownership structures in all four countries were dominated by foreign investors.

Thus, the reform trajectory of the steel sector in each country was marked by differences not only in the type of external pressure that was dominant in the sale to foreign investors but also in the initial policies adopted in the aftermath of the collapse of communism.

TABLE 1. Change in the Steel-Sector Ownership Structure, 1996–2005: Number of Enterprises

	1996			2005			Diff. (2005–1996)		
Country	SOE	DPO	FI	SOE	DPO	FI	SOE	DPO	FI
Czech Republic[a]	1	3	0	0	1	2	−1	−2	+2
Poland[b]	7	2	1	1	0	8	−6	−2	+7
Slovakia[c]	0	2	0	0	1	1	—	−1	+1
Romania	11	0	0	0	0	11	−11	—	+11

SOE, state-owned enterprise; DPO, domestic private ownership; FI, foreign investors.

[a]Vítkovice (VS), remained under state ownership in 1996, although a privatization contract was signed with the management and the state devolved responsibility for its oversight to the management. One of the companies, Poldi, was liquidated prior to 2005.

[b]One of the Polish companies, Baildon Steelworks, was liquidated prior to 2005.

[c]VSŽ (foreign-owned) is responsible for more than 93% of Slovak steel production.

Simply observing the similar outcomes reveals little about the transformation of the steel sectors of these four countries because the *process* through which the observed outcome was attained could be attributed to any number of causes. For example, the observed convergence in the steel sector could result from differences in partisan politics and reform proclivities, the economic significance of the enterprises, variations in labor and managerial organization and pressure, or disparity in country wealth. One could also reach for demand-side arguments and focus on enterprise attractiveness to investors. Finally, one could turn to external pressures, which usually entail the requirements of EU membership. The same outcome could also result from different combinations of any of these potentially causal factors. Thus, understanding the mechanics of the reform process helps to answer the questions of what domestic and external actors want, when, and under what conditions—all of which are important for tailoring future reform policies to local conditions. From the point of view of external actors, examining the reform process can help rectify the much-criticized, one-size-fits-all reform prescriptions and correct misleading assumptions about the preferences of domestic actors.

The task at hand, therefore, is to identify the determinants of the political decision to sell the enterprises to foreign investors in the steel sector. Since the mechanisms responsible for the outcomes may entail complex interaction effects that could easily be missed in statistical analysis, methodologically, these determinants are best isolated through process tracing the restructuring and privatization trajectories of each country.

Summary of the Argument and Definitions

In this book, which traces the process of reform between 1989 and 2009, I explain the convergence on transnational capitalism and show that different causal mechanisms were at play in the four countries. These diverse pathways resulted from the interactions of domestic institutions and external pressures. In a nutshell, the differing levels of state capacity associated with domestic institutions determined the extent and fiscal consequences of restructuring. These, in turn, shaped the converging trajectories of each country by determining which of the various external pressures, such as international financial institutions (IFIs), international financial markets, or the EU, proved *dominant* in which country.

I define "state capacity" as the ability of formal state institutions to implement policy and enforce legal sanctions.[11] Thus, state capacity rests on the infrastructural power of the state, defined by Michael Mann as the capacity of the state to penetrate civil society and implement political decisions throughout the territory. It is especially important in capitalist societies, where the state apparatus needs to regulate the economic processes.[12] Even though the communist states resembled leviathans that needed to undergo significant adjustment to the tasks of capitalist systems, they nonetheless possessed different levels of capacity at the outset of the transition process.[13] As the subsequent chapter shows, communist legacies left the transitioning states with bureaucracies that differed as far as training and access to technocratic resources were concerned. Thus, the different institutional endowment at the outset of transition, in part, explains the diversity of economic performance throughout the postcommunist world.

Communist legacies were key to understanding the disparate models employed in the challenging reform context of the steel industry. Facing the exigencies of economic transition, politicians needed to reform the steel sector. Initially, however, they secured their political and personal interests by opting for politically safer incomplete reform, epitomized by continued state ownership or privatization to nonstrategic, generally domestic, investors. As chapter 2 explains in greater detail, and as chapter 3 demonstrates empirically, the initial policy choice depended on the governing coalition's commitment to privatization and on the strength and preferences of managers and unions. All three variables were rooted in the political context shaped by the communist experience of the given country. The implementation of the initial policy choice at the enterprise and sectoral levels varied based on the capacity of a given state, and it determined the degree of restructuring and the resulting market adjustment that took place, including the consequences for the public purse.

At the enterprise level, developed in chapter 4, the analysis focuses on the relationship between state actors and the managers of the individual enterprises, with labor playing a secondary role. Here, the question is whether state actors were able to rein in managerial investment ambitions and rationalize production while checking their own impulse to seek rent. At the level of the sector, explored in chapter 5, the analysis turns to the institutional framework of social dialogue and the implications this has for restructuring.

Figure 1 summarizes the causal chain developed in chapters 4, 5, and 6, as it shows the relationship between the level of state capacity, the resulting domestic features of restructuring, and the dominant reasons for a sale to foreign investors. Given the overarching goal of "return to Europe," the figure also summarizes the role EU membership considerations played in the decision to sell the enterprises to foreign owners.

As figure 1 indicates, states with relatively low capacity, such as Romania,

State Capacity	Domestic Features of Restructuring	Dominant Reason for Sale to Foreign Investors	Role of EU Pressure in Sale to Foreign Investors
Low	State unable to introduce hard budget constraint, curb rent-seeking and managerial prestige maximizing; Lack of institutional capacity for quasi-market intervention; Captured unions and weak and dysfunctional social dialogue.	***International Financial Institutions*** Difficulty maintaining macroeconomic stability gives the IFISs leverage over the government and forces targeted sales.	***Indirect*** EU membership as primary political goal strengthens the hand of IFIs who need to "certify" the functioning market economy status for EU accession.
Medium	State able to curb some rent-seeking behavior (medium soft budget constraint) and managerial prestige maximizing; Lack of institutional capacity and funds for quasi-market intervention; Captured unions and weak and dysfunctional social dialogue.	***International Financial Markets*** Difficulty repaying loans to foreign lenders and severely limited state ability to bail out enterprises leads to a sell-to-FDI-or-perish scenario.	***Indirect*** EU membership as primary political goal strengthens the bargaining position of international market players vis-à-vis the government.
High	State able to introduce relatively hard budget constraint, curb significant rent seeking, and contain some managerial prestige-maximizing; State-led restructuring episodes and intervention to prop up failing enterprises using quasi-market means; Autonomous unions and functioning social dialogue.	***European Union*** Ban on state aid to the sector eliminates the use of quasi-market tools of intervention and forces sales for long-term survival.	***Direct*** EU greatly restricts the options available to the government due to the strict state aid provisions. ***Indirect*** Government desire for EU membership strengthens the bargaining power of foreign investors.

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Fig 1. State Capacity, Domestic Features of Restructuring, and the Dominant Reasons for Sale to Foreign Investors

were unable to curb rent-seeking behavior and managerial prestige maximizing. Social dialogue was poorly institutionalized and dysfunctional and marked by captured, rather than autonomous, unions. Endemic rent seeking made it difficult to maintain macroeconomic stability, which triggered the pressure from the IFIs to sell to foreign investors. IFI conditionality was strengthened further by the EU's requirement that Romania be considered a functioning market economy by the IFIs as a prerequisite to membership.

Medium-capacity states, like Slovakia, were more successful in their restructuring endeavors, as they were able to harden the budget constraint somewhat by limiting some rent-seeking behavior and managerial prestige maximizing. In Slovakia, social dialogue was also poorly institutionalized and dysfunctional and marked by captured, rather than autonomous, unions. Moreover, the Slovak state did not have the trust of the international lenders, and it also lacked quasi-market intervention instruments for propping up failing enterprises. As a result, although it was able to deflect the IFI pressures, it could not withstand the pressures of the international financial markets and banks that pressed for sales to foreign investors able to pay back the loans taken out on the international financial markets. The EU played an indirect role as well, as it provided an overarching reform trajectory for the government, but it did not need to intervene directly to press for privatization to foreign owners. The international banks had already done so.

States with higher capacity, such as the Czech Republic and Poland, were better positioned to restructure, and they did so, in part, by constraining excessive rent-seeking distributional coalitions and some managerial prestige maximizing that threatened reform. At the sectoral level, both states also had autonomous unions and a functioning social dialogue. Critically for their ability to deflect external pressures, they were able to maintain macroeconomic stability, and they had the quasi-market tools to intervene in ailing (and failing) enterprises. Paradoxically, higher state capacity became a double-edged sword that obstructed attempts to reform the sensitive steel sector, because it enabled states to maintain politically convenient status quos by staving off external pressures through the deployment of targeted market-based tools. These tools included debt workouts and parastatal entities that supported the embattled enterprises. In other words, the higher capacity of the Czech and Polish states allowed their governments to deflect the IFI and international financial market pressures to which their Slovak and Romanian counterparts had succumbed. The initial reform efforts were incomplete and would not be completed until these states were constrained by the requirements of EU accession, and specifically, the EU ban on state aid. Thus, the EU played a direct role in the decision to sell to foreign investors: the requirements of accession gave the governments no viable alternative to seeking strategic investors to ensure long-term survival. At the same time, the EU also played an indirect role in the process, as it strengthened the bargaining power of foreign investors interested in acquiring the enterprises.

Implications

This book draws on and contributes to a number of scholarly literatures. First, it adds to the literature on the political economy of reform—specifically, to the studies on the role of the state in economic reform, industrial restructuring, and industrial relations. Second, because of its focus on how the state mediated domestic pressures, on the one hand, and external ones, on the other, in the context of postcommunist economic reform, the book brings together and contributes to three distinct literatures: postcommunist transition, varieties of capitalism, and European integration studies.

First, although the role of the state and the importance of state capacity for development have been increasingly recognized by the IFIs, most notably by the World Bank,[14] I demonstrate that the relationship between higher state capacity and reform is more complex than these entities and the scholarly literature tend to recognize. The institutional sophistication indicative of higher state capacity is a double-edged sword that can be used to discipline firms into engaging in market-oriented behavior or, by contrast, to shield enterprises from market pressures and otherwise promote the inefficient preferences of political actors.

The dual nature of state capacity travels to other settings in both developing and developed countries. It sheds new light on why some countries are more likely to succumb to external constraints, such as IMF conditionality, than others. Differences in state capacity can also explain the variations in degree of economic reform among advanced market economies, such as the most recent bout of reforms in Greece and Spain, on the one hand, and the lack of reform in France, on the other. It also clarifies seeming contradictions, such as why some avid market reformers, such as Chile, manage to maintain public ownership over certain sectors of industry, as exemplified by the Codelco copper mining company.[15] In short, I illuminate the political determinants of economic reform more broadly, and privatization specifically, including the resources used to resist it, by focusing on the deployment of state resources by politicians.[16]

Second, the analysis also clarifies the potential range of developmental consequences resulting from privatization. At a basic level, the present study of the initial policy choice corroborates Hector Schamis's argument that far from being a silver bullet, privatization may be a gateway to enrichment for the governing coalition's allies.[17] However, unlike Schamis's approach to the state as the dependent variable, this study treats the state as an intervening variable that leads to privatization and, more generally, to reform outcomes. At the same time, this study addresses the criticism of treating the state as a unitary actor by explicitly recognizing the complex and often contradictory network of state agencies and institutions.[18]

Third, the book's systematic and central focus on the role of state capacity in mediating industrial restructuring fills an important void in the literature on the political economy of postcommunist transition. For a long time, this particular literature has ignored the state as an important actor, and existing studies of the state have tended to treat it as the dependent variable.[19] As my account makes clear, the state plays a central role in restructuring due to its interaction with the domestic actors. In other words, how well the state is able to rein in rent seeking and managerial ambitions and build an institutionalized relationship with the trade unions also determines its susceptibility to different types of external pressures. The sources of state capacity are deeply rooted in these countries' communist and precommunist legacies; thus, they are thoroughly domestic.[20] The analysis of the implementation of the initial policy choice in the four countries makes clear that the level of state capacity rather than ownership type—whether domestic private ownership or continued state ownership—accounts for better or worse restructuring outcomes.

Fourth, the book supports two propositions concerning effective restructuring in the context of market reform. First, neither abandoning the sector to the nascent market forces nor using the preexisting industrial networks for restructuring will foster significant restructuring without a transparent policy and sufficient state capacity to intervene and rein in managerial investment ambitions.[21] Second, contrary to the arguments for insulating decision makers from social actors, I show that, far from hindering the restructuring process, engaging unions in sectoral-level social dialogue is conducive to restructuring and can lead to unions becoming the agents of restructuring.[22]

Fifth, the book bridges the literatures on the varieties of capitalism and EU integration studies by illuminating the role of the EU and other external pressures in the convergence on transnational capitalism in the region. The type of capitalism emerging in the transition economies became a subject of considerable scholarly debate in the field of political economy of postcommunism. The proliferation of categories into which the countries are divided stems from the realization that the categories of liberal and coordinated market economies, originally developed by Peter Hall and David Soskice for the most advanced industrialized countries, are of limited applicability to the institutionally fluid postcommunist economies.[23] However, whether the categories center on the main institutional coordinating mechanism, insertion into the world production networks, or social forces and domestic institutions, there is a growing recognition of the central role played by foreign capital in the region.[24] Seeking to add to the Hall and Soskice framework, Nölke and Vliegenthart explicitly refer to the economies of the Central European region as "dependent market economies," in which external dependency is the principal coordinating mechanism in the economy. Thus, foreign capital plays a paramount role.[25]

This book addresses the understudied political process through which the outcome of transnational capitalism was achieved.[26] The few existing accounts that have tackled the complex process leading to the emergence of transnational capitalism have tended to emphasize either the active role of state elites and institutions in attracting FDI or, at least, their complicity.[27] The present study moves beyond these accounts by demonstrating that the entry of foreign investors into the steel sector not only lacked the active support of the elites but was resisted in an effort to retain the status quo. Rather, it focuses on the coercive pressures exerted by international actors in a sector in which the domestic actors did not unfold the welcome mat, even in those states, such as Poland, that have historically been relatively foreign-capital friendly in other sectors, such as banking. Thus, this book explains why and when the process of convergence holds even if the elites are not enthusiastic about internationalization and try to resist it.

This book adds to the EU studies literature through its examination of the EU's role in the emergence of transnational capitalism in the region.[28] The EU's transformative role in ECE has generated an impressive literature and sometimes contradictory conclusions, many of which depend on the sector and policy examined.[29] Most often, the EU effect is the focus of analysis, and other external pressures are treated as complements in the liberalization/market transformation project.[30] However, the relationship among these external pressures, and the conditions under which each of them plays a significant role, have not been given sufficient attention, and this is precisely the gap that this book addresses. Certainly, the EU set the parameters of reform for all accession countries in the wide-ranging *acquis communautaire*, or the body of all of EU's rules, regulations, treaty obligations, and court rulings.[31] However, in the case of this challenging sector, the EU had to exert direct pressure on the transition and enlargement leaders (Poland and the Czech Republic) to force compliance with EU regulations.[32] Even though the EU was avowedly neutral as to ownership type, the requirements of EU membership left the countries little leeway in choosing to sell to foreign investors. At the same time, due to the differences in domestic institutions, in the case of the transition "laggards" (Romania and Slovakia), the EU's *direct* pressure was preempted by other external pressures: IFIs and the financial markets.

Case Selection and Data

The book is comparative on several dimensions: it process traces the restructuring and privatization of a critical and difficult-to-reform sector across three levels of analysis in four countries over twenty years. The nested research design, progressing from the enterprise level to the sector level and on to the national-international nexus, creates an opportunity for making across- and within-case comparisons and for examining the salience and interactions of domestic and external variables over time. Such a research design complements prior work by linking the macro and micro levels. By examining a single sector, the analysis is broad enough to embed the sector within the overarching country-reform trajectories and narrow enough to engage in a systematic comparison at the level of the enterprise.

Steel Sector

Steel, a particularly sensitive sector in communist countries, is the ideal sector for examining the relationship between successive governments, the state, and managerial and labor interests during the transition process. The steel sector under communism operated in an ideologically loaded context, and a country's performance was measured by its annual steel output. The steelworkers were seen as the epitome of the proletariat, and their work was remunerated handsomely compared with other industrial sectors. It is, therefore, not surprising that at the outset of transition, the steel sector was expected to be filled with vested interests inimical to reform.[33] The heightened challenge of reforming sectors characterized by high capital intensity and overcapacity was only exacerbated by the steel sector's formerly privileged status and great symbolic value as a communist-nationalist project; it was in the steel mills that the new communist man was to be forged.

The construction of the Lenin Steelworks in 1949 at the outskirts of Kraków, Poland, was accompanied by the building of a model socialist-realist city, Nowa Huta, literally "New Foundry." In Romania, the construction of Sidex, the country's largest steelworks, in the eastern Romanian city of Galați, became central to the 1960 feud between the Romanian communist leader, Gheorghe Gheorghiu-Dej, and the Soviet leader, Nikita Khrushchev, over Romania's role in the Council for Mutual Economic Assistance (CMEA). With Gheorghiu-Dej rejecting the vision of Romania as the communist bloc's breadbasket, Sidex came to symbolize Romania's national communism.[34] Similarly, in Slovakia, the 1958 decision to build Eastern Slovak Steelworks (VSŽ) as part of the Second Five-Year Plan, was essential for meeting the developmental objective of putting the Czech and Slovak lands on an equal economic footing; VSŽ became Slovakia's flagship enterprise.[35] Even in the Czech lands, with their long history of steelmaking, the 1952 construction of Nová Huť Klementa Gottwalda (Klement Gottwald New Steelworks), named after the Czechoslovak Stalinist leader, was intended to represent a new era in Czech industrial development.[36] These legacies, combined with the sector's economic importance and global market pressures, shed light on the political economy of reform and the region's convergence on transnational capitalism.

Beyond its ideological and political legacies, the steel sector held an important position in the economies of the Czech Republic, Poland, Romania, and Slovakia. At the outset of transition, the share of total manufacturing industry (in current prices) held by the basic metals and fabricated metal products branch, of which the steel sector is the core, ranged from the 19.0% in Slovakia to 14.7% in Romania. In addition, the steel sector was similarly positioned in the economies of the four countries—a key comparative point because, following the insights of Shafer's sectoral analysis, dominant sectors can shape the restructuring of the national economy and affect the state itself. Sectors marked by high capital intensity, high economies of scale, and high production and asset/factor inflexibility are particularly influential.[37] In Slovakia, the metals branch was the biggest industrial sector; in the Czech Republic (17.2%), Poland (16.2%), and Romania, it was the second-largest branch.[38]

The branch was also an important employer. At the outset of transition, the basic metals and fabricated metal products branch was the biggest industrial employer in the Czech Republic, with a 17.6% share of total employment in manufacturing. In Romania (12.7%), the branch was the third-largest industrial employer, and the metals branch was the fourth-largest industrial employer in both Poland (11.5%) and Slovakia (9.9%).[39] Thus, the fate of the steel sector had important implications for the economy and the labor force in all four countries.

In this analysis, I use the biggest companies in the individual countries to identify different causal pathways, to present a theory of convergence, and to test initial hypotheses concerning external effects. I then test the claims about the role of state capacity in restructuring against the evidence garnered in the other big and medium-size enterprises in the steel sector of these countries. In the final chapter, I demonstrate that the other countries in the region also fit the pattern flowing from the theoretical expectations identified in this chapter. Thus, I test the theory of convergence within and across country cases, using the enterprises as units of analysis. I compare sectoral-level labor dynamics and managerial competition at the country level.

Country Cases

The choice of country cases follows the most similar research design. Given that the outcome to be explained is the difference in the converging trajectories, the countries selected are similar on several crucial variables. First, they have all faced the task of postcommunist transition and the simultaneous drastic political, economic, and social change it entails. Second, as the previous section has shown, the four selected country cases had steel sectors of similar political and economic domestic stature and salience. Third, none of the countries relied on natural resource wealth for export earnings. In 1999, during the mid-transition period, fuel exports as a percentage of merchandise exports equaled 2.8% in the Czech Republic, 4.7% in Slovakia, and 4.9% in Poland and Romania. By contrast, in Russia, this number stood at 41.8% in 1999.[40]

Finally, as noted earlier, all four countries took part in the EU accession process. Given the sensitivity of the steel sector in the EU, these states needed to reach the same standard as already established EU member states—namely, the viability on the market without state aid. Because the four countries represented the biggest steel producers among the EU accession states, the EU would have been expected to take a close interest in all four countries' production potential and restructuring process. Due to the importance of the EU in setting the broader parameters of reforms and because of its close attention to the developments in the steel sector, the universe of cases for this study is limited to the EU applicants.

The one key variable on which these countries differ, as the next chapter will show, is the level of state capacity. As the similarities in the ultimate trajectories of Poland and the Czech Republic demonstrate, it was the level of state capacity, rather than the differences in the initial policy choices, that drove the process of convergence.

Data

The following chapters process trace restructuring and privatization of the enterprises in the steel sector in the four countries over the entire transition period, 1989 to 2009. I used a wealth of local sources in Czech, Polish, Slovak, and Romanian, including government documents, policy papers, and publications by labor unions and by employer and industrial associations. I relied on hundreds of newspaper accounts of restructuring and privatization events from over fifty local newspaper sources, including those drawn from enterprise newspapers located in labor union archives. In addition, I conducted more than 125 open-ended interviews, listed in Appendix A, with various actors involved in the restructuring and privatization process in each country.

Chapter 2 provides the theoretical framework for the empirical analysis presented in subsequent chapters. It examines in greater detail the political economy of restructuring and privatization at the three levels of analysis and discusses the central role of state capacity in the reform process.