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# Post-Socialist States and the World Economy: The Impact of Global Economic Crisis

David Lane \*

**Abstract:** »Post-sozialistische Staaten und Weltwirtschaft: Die Auswirkungen der globalen Wirtschaftskrise«. The impact of the world financial crisis on the post-communist European states is predicated on their position in the world economic system. The first part of the paper considers the changing position of the European state socialist societies in the world system. The second part analyses the impact of the economic financial crisis. Since 1989, the post-socialist states have pursued different trajectories. The new member states of the European Union (EU) have followed a neoliberal course and have entered the world economy formally as members of the 'core' (the EU). The Commonwealth of Independent States (CIS) constitutes a 'hybrid' social formation containing elements of state coordination, national and global capitalist interests – characteristics of 'semi-peripheral' states. The exposure (through trade and finance) of all the post-communist states to the world system has opened up their economies making them liable to external shocks. This is illustrated by the effects of financial stress caused by the world economic crisis of 2007-2009. Reactions and adaptations to the crisis are discussed: the post-socialist members of the EU have been more affected by the crisis than the CIS states. It is contended that the legitimacy of neoliberal policies has been undermined and state regulation enhanced. It is argued that the semi-periphery is not a transitional formation in the world-economy. In a world system perspective, the 'semi-periphery' has to be differentiated between potential 'counterpoints' (Russia and China), which have a capacity for autonomy and renewal, and countries that are more dependent on the capitalist economic core states.

**Keywords:** world system, post-socialist states, financial crises, globalisation.

## The world system approach

The world system orientation attempts to combine a Marxist capitalist paradigm with a political-military state system. World system writers divide the *world-economy* into three sectors: the hegemonic core (the dominant 'Western' capitalist countries), the periphery (developing countries of the South) and the semi-periphery – countries with industrial capacity and national capital but not part of the capitalist core. Analytically, the 'core' is constituted of capitalist countries which, through their transnational corporations (secured through their

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political hegemony and military power) accumulate capital at the expense of the peripheral countries. The peripheral countries are sources of profit through the supply of primary sector materials or of products at the lower end of the production chain. The 'semi-periphery' includes states which are in an intermediary stage: they are agents of economic exploitation as well as subjects of it. Finally, there are external areas that remain outside the world-economy (self-sufficient herding and gathering societies, which are not our concern here).

For world system theorists, state socialist countries were part of the semi-periphery. There were no 'socialist economies'. Wallerstein claims that the world-economy included the 'entire world, including those states ideologically committed to socialism' (1979, 271). State socialist systems, it is contended, were not socialist modes of production, but interacted with the capitalist world economy. The socialist state, which exhibited some features of socialism (e.g. employment security, comprehensive welfare provision, the absence of a capitalist owning class), nevertheless became a major player in capitalist accumulation, which in turn provided a basis for reintegration into the world capitalist system. Wallerstein makes it clear that there is a unitary capitalist *world-economy* (ibid., 13).

This approach, which has many valuable insights, is contested in this paper. First, it is contended that the 'core' states should be differentiated into hegemonic powers and a semi-core or 'satellites': the latter share the dominant values of the core and are components of its political institutions and participate in its military alliances, but they lack economic and military power and have marginal membership of the world capitalist class. Second, we should consider a 'world economy'<sup>1</sup> constituted of interacting economies, of regional blocs and 'counterpoints' to the dominant capitalist world economy. The 'semi-periphery' is not locked into the core; it exchanges with it and has possibilities for autonomous development – for movement into the core or periphery or to become a 'counterpoint'. Third, by counterpoint I mean a social system that can operate independently from, and in harmony with, the core. Such counterpoints are not integrated into the hegemonic socio-economic system of the core states, though they have forms of exchange with it. They have the capacity for different ideologies, forms of class structure and resulting capital accumulation; they are not part of the world capitalist class formation and its military expression.

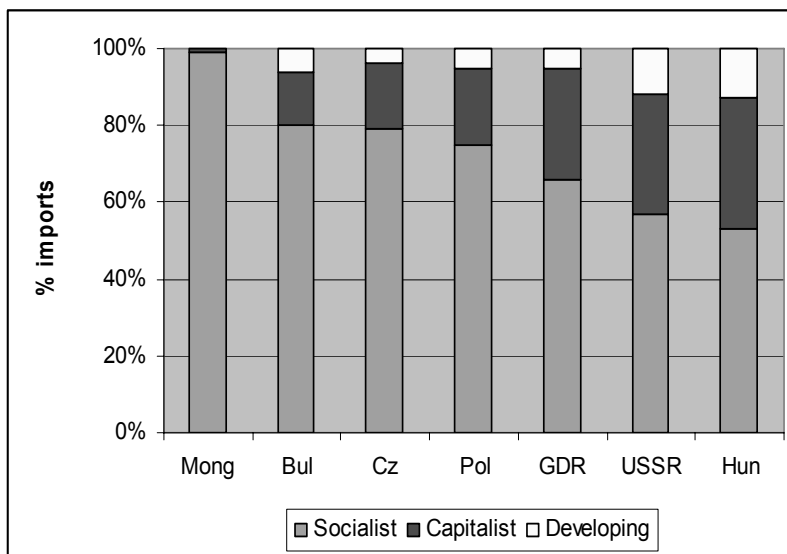
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<sup>1</sup> A world economy (pluralistic) may be distinguished from Wallerstein's 'world-economy' (unitary).

## The Soviet block: a counterpoint in the world economy

The Soviet block before Gorbachev's reforms of the 1980s was a relatively independent autonomous economic entity. Study of developments before 1985 shows that inflows and outflows of investment capital were small in scale. Outward investment from the state socialist countries was relatively meagre. Even relatively small transnational companies (TNCs) like Pepsi Cola (55th in world rank) had a greater share in the world stock of foreign investment than did all the state socialist countries combined. Trade with capitalist countries played a relatively minor role<sup>2</sup>.

Figure 1: Imports of selected SEV\* countries, 1983.



Source: Statisticheski ezhegodnik stranchelenov SEV. 1984, 297

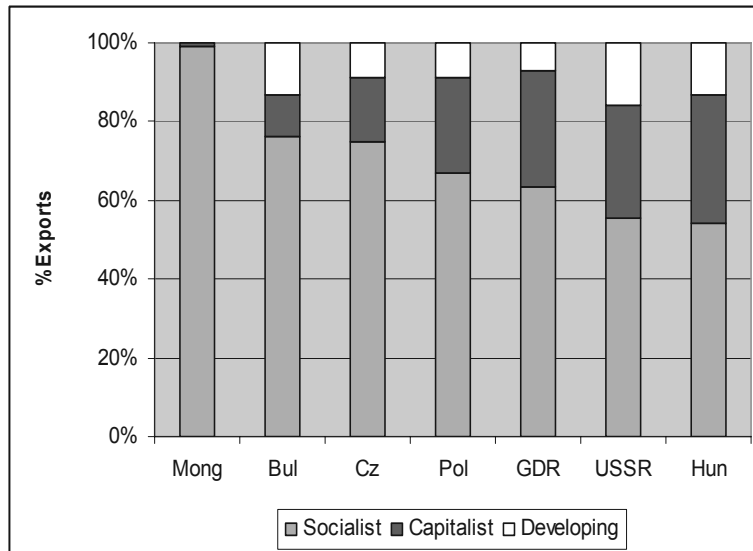
\*Council of Economic Cooperation, sometimes referred to as Comecon.

As illustrated in Figure 1, the scale of import from developed capitalist countries was small: only the USSR, Hungary and the GDR had any significant levels, and by far the greatest trade was with the socialist bloc. Expressed as a proportion of GDP, we can estimate the significance of this trade: in 1983, imports from non-socialist countries were only 1.39 per cent of gross national

<sup>2</sup> Even for the highest traders with the capitalist world (Hungary, USSR, and the GDR) turnover was a third or under and for Comecon members it was under 20 per cent.

product for the USSR, 4.2 per cent and 2.1 per cent for Hungary and Poland<sup>3</sup>. We witness a similar picture for exports, as shown in Figure 2.

Figure 2: Exports of Selected SEV\* Countries, 1983.



\*Council of Economic Cooperation  
Source: As for figure 1.

China, by comparison, had entered the world market earlier: even in 1975, the figure for exports was 5 per cent, rising to 11 per cent in 1980 and 19 per cent in 1990; the relative figures for imports were 5 per cent, 11 per cent, and 16 per cent (World Bank data base, accessed 1 May 2009). In 1985, the socialist countries (excluding China) accounted for only between 0.1 and 0.2 per cent of the world stock of foreign direct investment; whereas IBM alone accounted for 3.32 per cent (CTC Reporter, 1987). The state socialist countries' foreign holdings were low in capital value. Differences between the central European countries and the USSR, however, were to become more prominent in the post-socialist period<sup>4</sup>.

<sup>3</sup> GNP data from CIA 1986, 227.

<sup>4</sup> The dollar values of imports expressed as an average per capital of the population were only \$97.7 for USSR, though a more considerable \$307.2 for Hungary. Value of commodities expressed in 1975 dollar prices (Economic Bulletin for Europe, 1985. Population data, Statisticheski ezhegodnik 1985, 16). GNP data derived from CIA 1986. CIA calculations for per capita income in 1984 are: Hungary, \$7,200; Poland, \$6,190; USSR, 7\$, 120.

Foreign direct inward investment involved small companies; there was negligible penetration by transnationals. The financial consequences of foreign debt were not particularly serious for the Soviet bloc as a whole. By 1973, gross indebtedness was some \$17.6 billion<sup>5</sup> and by 1985 had risen to \$48.8 billion (Economic Commission for Europe 1986, 255-6). These were unevenly distributed with Poland particularly having a high level of indebtedness. However, Central East Europe and the USSR's total export earnings covered imports, with a large positive trade balance in 1984 and only a 2 per cent deficit in 1985 (Wilczynsky 1969, 382-383; Frank 1980, 194-202). Crucial here was the revenue received from the USSR's foreign export earnings, mainly from energy sales. One could not argue that before the Gorbachev reforms state socialism was in a financial crisis which precipitated the transformation entailed by perestroika. There were important differences, moreover, in the levels of exposure to international economic influence in the different socialist countries: as indicated above in Figures 1 and 2, those adjacent to the European Economic Community (particularly Hungary and Poland) already had stronger links.

Hence in terms of levels of investments and imports as well as consequent levels of foreign debt, and impact of communist transnational corporations, the state socialist countries could not be considered to be in any way integrated into the world-economy, as contended by world system writers (Wallerstein 1979, 271; Boswell and Chase-Dunn 2000, 135). Also one must take into account the political factors. The socialist economic enterprises were controlled by home governments; they did not operate with the freedom of capitalist firms and they certainly did not 'control' the state in the way that multi-national companies can influence host country governments. The global capitalist class, as actors, had no presence in the state socialist societies. Money supply was directly controlled by the government and could not be created by national or international banks. Only after the fall of communism did the central European countries enter the world economy.

Crises in the market economies had little influence on the Soviet bloc: the great economic depression of the 1930s for example did not adversely affect the Soviet Union, which experienced extensive economic growth. The socialist bloc after the Second World War became a counterpoint, a unit that exchanges with, but is not part of, the 'core' capitalist states. The context in which capital accumulation occurred was quite different from that of modern capitalism. A qualitative shock, a transformation, was required to push the state socialist societies into the world system. This came with the reform programme of Gorbachev who recognised the importance of the world economy and considered that exclusion from the global economy had a detrimental effect on the devel-

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<sup>5</sup> Data refer to USSR and Eastern Europe. See 'The European Economy of Europe in 1975' (United Nations 1975, 144).

opment of the USSR and the socialist bloc<sup>6</sup>. Here he follows writers such as Castells (1998, 9), who contended that the exclusion of the USSR from world developments in information technology led to stagnation. Gorbachev had no doubts that the USSR would join the 'core' nations of capitalism; would return to its European home. In this he was to be mistaken.

### The consequences of reform: The shift to a global economy

After 1989, the move to markets and private property strongly impacted on the shape of foreign trade, foreign investment and the place of the post-communist countries in the world global order. The global dimension of change is usually regarded positively as part of the victory of liberalism and democracy, globalisation in this perspective empowers people through the development of wealth, communications (travel, networks) and culture. Others contest this judgment and contend that globalisation has negative connotations. Global corporations and political organisations remove control from individuals and weaken the responsibility of states because the processes of government, previously at least answerable to public interests, have been superseded by global (and non-accountable) decision-making by transnational organisations. Asymmetric relationships develop between the core industrialised and militarised countries and the periphery; statist and socialist countries seeking to form a counterpoint are subject to political and economic sanctions. Moreover, the cyclical crises of capitalism, such as those of the 1930s and 2007-2009, derived from incompatibilities between demand and production, and imbalances in the financial system also detrimentally affect the peripheral countries.

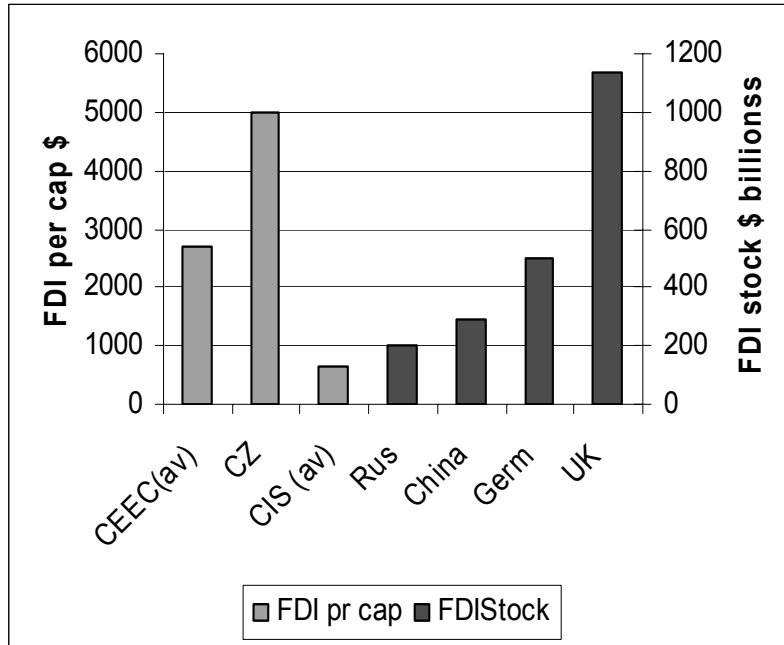
Following the collapse of Comecon and the opening of markets to the West, capital flowed to the former state socialist societies. This had the important effect of linking them through ownership of companies to the global class system. However, in comparison with advanced countries of the West such flows were relatively small. The average inflow for the whole period of transformation (1989 to 2005) for the CEECs was \$2,714 per capita; the largest, for the Czech Republic, came to \$5000 (EBRD 2006, 32; 38). For the CIS states, the average was only \$643 per head. The FDI stock in 2006 for Russia came to 197.6 billion dollars, by comparison, in China it was 292.6 billion; Russia is just above Ireland which had a stock of 179.0 billion, and China just below Italy which had 294.8 billion. As shown in figure 3, West European countries are in a different league: the comparable figure for Germany is 502.3 and UK 1,135.3 (UNCTAD 2007, 255-7). These figures represent purchases of assets in the host countries as well as capital investments in private companies. While the conditions in which assets were purchased led to their under-evaluation, the

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<sup>6</sup> M. Gorbachev, Adress to the United Nations, 1988. Cited by Castells 1998, 5.

figures, nevertheless, show a qualitative difference between the CIS states and the advanced capitalist states, as well as the new post-socialist members of the European Union.

Figure 3: FDI per capita and FDI stock selected countries



FDI US \$ per capita 1989-2005 (average), left side axis, FDI stock, \$bills 2006, right side axis.

Source: EBRD 2006, 32; 38.

### Penetration of foreign companies

The intentions of the economic reforms of the early 1990s were to bring the post-socialist societies into the world economy, optimistically to enhance their economic performance. However, their different geographical locations, factor endowments and level of competitiveness have led to differential effects. We consider here the presence of foreign affiliates of companies and the levels of imports and exports as measures of global interdependence.

Foreign affiliates play a significant role in the economies of the post-communist countries, but again there are significant differences between the new member states of the EU and the former republics of the USSR. The level of foreign company penetration reflects the level of investment in a host coun-



try, which in turn has important consequences for the commitment of the global political class.

Table 1. Number of foreign affiliates<sup>7</sup> in post-communist countries with comparisons to other countries (2007 or latest available year). *Full reference given below.*

New EU members	
Czech Republic (1999)	71,385*
Hungary	26,019
Poland	14,469
Slovakia	2,780
Slovenia (2000)	1,617
Lithuania	3,240
Latvia	665
Estonia	2,858
Other former communist countries	
Bulgaria (2000)	7,153
Albania	20
Croatia	2,532
CIS Total	10,782
Of which:	
Belarus	54
Ukraine	367
Russia	1,176
Kazakhstan	2,267
Kyrgyzstan (1998)	4,004
Moldova	2,670
Comparisons	
USA (2002)	24,607
Turkey	14,955
UK	13,667
Brazil	3,712
China (excluding Hong Kong)	280,000
World Total	794,894

\*The high figure for parent corporations in Czech Republic probably accounted for by splitting of former Czechoslovakia; of this figure 53,775 are fully-owned foreign affiliates.

Source: UNCTAD 2008, 211-213. Data based on national sources.

<sup>7</sup> Number of foreign affiliates in the economy shown. 'An equity capital stake of 10 per cent or more of the ordinary shares or voting power for an incorporated enterprise is usually considered as the threshold for the control of assets. A foreign affiliate is an enterprise in which an investor, who is a resident in another economy, owns a stake that permits a lasting interest in the management of that enterprise'. The threshold is 10 per cent of equity state or equivalent. Definition cited from the 2005 Report, 297-8. (UNCTAD 2005)

The post-communist countries in the European Union host an exceedingly high number of foreign based firms (see Table 1). There were over 26 thousand in Hungary alone. As one would expect given the much lower level of foreign direct investment in the CIS countries, foreign ownership is much less: of the 10,782 firms operating in the CIS, Russia in 2004 had 1,176, Belarus – 52 affiliates, and Ukraine, only a few hundred. In the central Asian economies, Kyrgyzstan (data only available for 1998) and Kazakhstan had thousands of foreign companies though Uzbekistan had only 50. China is a special case, hosting approximately a third of all foreign affiliates of TNCs on a world scale. As China had a small share of world inward investment (2% in 2006), these foreign affiliates are very small in size.

These data show that the expectations of those reformers who conceived of integration into the world economy have been fulfilled to some extent. The new EU members and China have certainly attracted investment from foreign corporations and have an even larger number of foreign affiliates than many established Western capitalist countries. The large numbers of take-overs have led to a growing preponderance of foreign companies in some of the central European states, though not so in the CIS. In all the post-communist countries, there has been a lack of capacity to form large national capitalist companies able to compete in the world economic system. The only exception is a small number of Russian companies exploiting natural resources<sup>8</sup> (Lane 2009, 102-110).

While the new EU member states have been integrated into the world economic system and have become integrated into its political and military (NATO) apparatuses, they are not equal members of the dominant 'core' nations. One should then distinguish between a hegemonic bloc (USA, Japan, Germany and UK) among the core countries and others (the new members of the EU among them), which constitute a subordinate group. Some have referred to a semi-core, but I prefer the term satellite. This indicates the independent political identity and the state's subordination to institutional and value configuration shaped by the fulfilment of the conditions of the EU's *Acquis Communautaire*. The CIS countries have remained on its semi-periphery. This becomes clearer when we consider the exposure of the post-socialist countries to global influence.

## Globalisation of the post-socialist countries

The transnationality index for a country (TNI) is calculated as the average of four ratios: FDI inflows as a percentage of gross fixed capital formation for the past three years, FDI inward stocks as a percentage of GDP in a given year, value added of foreign affiliates as a percentage of GDP in a given year, em-

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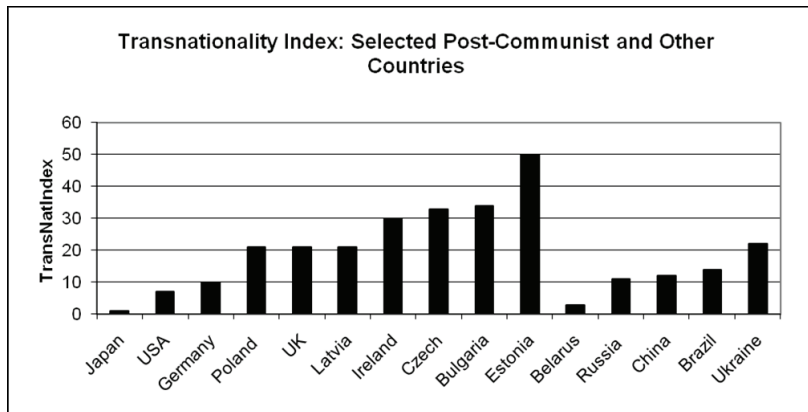
<sup>8</sup> These include Gazprom, Lukoil and a major bank, Sberbank.

ployment of foreign affiliates as a percentage of total employment in a given year. A high index indicates that a country is largely dependent on foreign companies for employment and wealth creation. A low index implies that a country, which may have many small foreign affiliates, nevertheless has a great deal of its national wealth generated by domestic production.

In 2005, the weighted average for developed countries was 12 and that for developing countries 14. There is a great range between the exposure of developed economies: lowest was Japan with 1, the USA had a low index (7) and UK 21. Figure 4 illustrates the differences between three advanced Western countries, new members of the EU, and a number of other countries (including Belarus, China, Russia, Ukraine, and Brazil). As one might expect from the earlier discussion, the new post-communist members of the EU had very high exposures: Estonia (50), Bulgaria (40), and Hungary (34), Czech Republic (33). Russia had a fairly average exposure (11) (though for 2002 it was 18 due to the disproportionate contribution of FDI as a percentage of GDP); Ukraine 22 (though only 14 in 2004) and Belarus (3) – one of the lowest in the world. China also had a fairly average ratio – 12 (though it was only 8 in 2004) (UNCTAD 2008, 12).

The implications here are that, despite exposure to the global system, the post-socialist states of the CIS, as well as China, still have a large domestic economic base, which is lacking in the new EU countries. They are less integrated economically into the world economy. As their companies have relatively low levels of foreign ownership they are not penetrated by the world capitalist class; to the extent that a capitalist class exists, it is largely national in character. Politically, they are not members of the hegemonic military political core.

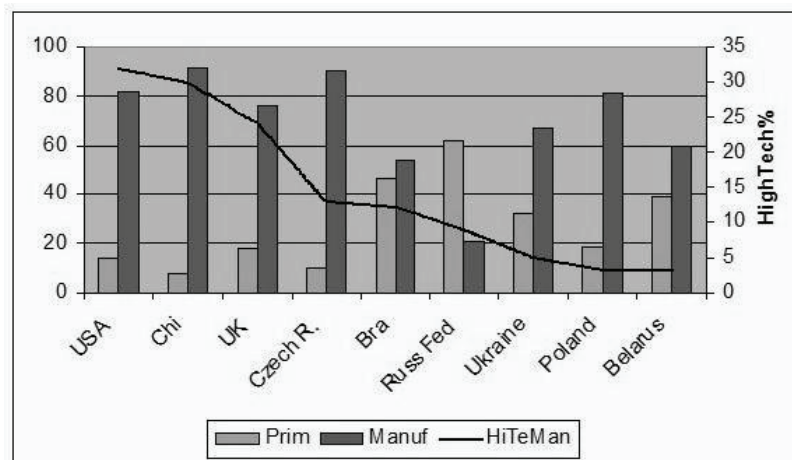
Figure 4: Transnationality Indexes: Selected Post-Communist and Other Countries



Source: UNCTAD 2008, 12 (Data for 2005 or latest date available).

One would expect that countries with a low exposure would be less affected by a major financial crisis in the world economy. Of course, a country with very large export earnings can be financially dependent on the level and price of its foreign exports – especially if it has few internal resources. The pattern and type of foreign trade is therefore also indicative of the position of countries in the world system. We consider then a) the structure of exports by types of commodity and b) the extent to which different countries are dependent on trade. Figure 5 depicts the commodities forming the exports of two advanced countries, (UK and USA) a third World country (Brazil), China, and a number of post-socialist countries.

Figure 5: Structure of exports, selected countries, by sector 2004



Primary and manufacturing measured on left axis (per cent of exports), high-tech exports (% of manufactured exports) measured on right axis.

Study of Figure 5 illustrates the significantly different trading profiles of the post-socialist countries compared to those of the leading capitalist states. It brings out the asymmetric relationship of the type of exports between the post-communist countries and UK and USA<sup>9</sup>. Russia has a particularly skewed distribution of exports, its energy sector exports accounting for 62 per cent of

<sup>9</sup> The United States had the following top exports: transistors (6.5%), aircraft (6%), motor vehicle parts (4%), special transactions (3.2%), and passenger motors (3.1%) (The low figures indicate a much more diverse range of export products); for the UK, the leading exports were passenger motor vehicles (5.6%), pharmaceutical products (5.6%), telecom equipment (5%), crude petroleum (5%), engines and motors (3.7%).

merchandise exports in 2004<sup>10</sup>. Russia provided 9 per cent of the world's crude petroleum, and 18 per cent of the world's gas; Ukraine exported 7.6 per cent of the world's iron and steel in primary form and 5.2 per cent in steel shapes.

The 'high-tech' component in manufactured exports is extremely low for all the central and east European countries, except for Hungary. By value in the period 2002-3, Hungary's top exports were in the commodity groups of telecom equipment (12.1%), combustion piston engines 9.3 (%), automatic data processing equipment (5.6%), and motor vehicles (3.9%). These derived mainly from foreign companies hosted in Hungary and were relatively small in scale: its telecom equipment, for example, only accounted for some 2.13 per cent of world output (UNCTAD 2005, 168). By comparison, the USA's production was in high-tech commodities: 17 per cent of the world's transistors and valves and 36 per cent of aircraft; the UK produced 4.7 per cent of the world's passenger vehicles and 9 per cent of pharmaceutical products. The only major industrial power in the post-socialist world is China. Eight per cent of exports are in automatic data processing equipment, 6.3 per cent in telecom equipment, 4.5 per cent in office machinery, 3.53 in toys and sporting goods and 3.3 per cent in footwear. Importantly, automatic data processing equipment came to 15.56 per cent of world exports, and telecom equipment 11 per cent (ibid, 163).

A second component of dependency is captured by the extent to which countries are reliant on exports and imports. Here we measure exports and imports as a proportion of GNP: a low figure will indicate high self-sufficiency, and a high one a great dependency on foreign trade.

Figure 6 shows the different export/import profiles of a selection of post-socialist and other states. The figures confirm some of the points made earlier. The post-socialist European countries (Estonia, Hungary and Czech Republic) have almost a complete dependence on foreign trade, as does Turkmenistan, which is dependent on natural gas exports. The United States and Japan have relatively low levels due to the size of their own domestic production and consumption. The other countries – China, Russia, United Kingdom – although important trading nations, have a considerable home market.

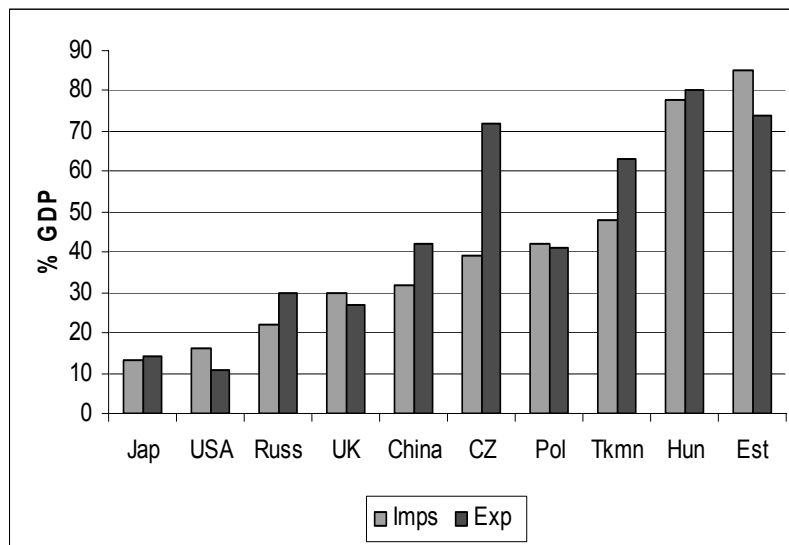
The conclusion to be drawn is that the post-socialist societies have entered the global system. But they have done so in different degrees. The new post-socialist members of the European Union have adopted a more open neoliberal economic model: they have a very large presence of Western capital and Western firms, they are highly dependent on the world market both for exports and imports – Hungary and Estonia remarkably so. Their trading pattern, however,

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<sup>10</sup> The top five traded products for Russia (value traded 2002-03) were: crude petroleum (27%), natural gas (14%), 'special transactions' (arms), (12%), petroleum products (11%), aluminium (3%); for Ukraine, iron steel (primary forms) (12%), iron (steel shapes) (7%), petroleum products (refined) (5.7%), wheat (unmilled) (3.8%).

is not analogue to the core industrial countries: with the exception of Hungary (which largely exports high-tech manufactures of foreign firms), they are at the low value added and low technology place in the world production chain. While the European members of the Commonwealth of Independent States are less dependent on the world economy and retain many companies in national ownership, their exports are not only in low-tech manufacturing, but in primary products – timber, ores, minerals and particularly energy. A group of countries here are distinguished by their energy exports – Russia, Turkmenistan, Azerbaijan and Kazakhstan. The post-socialist countries become part of the lower end of the world production chain.

Figure 6: Exports and imports as proportion of GDP: Selected countries, 2007.



Source: World Bank, Key Development Data and Statistics. (May 1, 2009), <<http://ddp-ext.worldbank.org.ext>>. Data are sum of exports and imports of goods and services expressed as % of GDP. They refer to 2007 or latest date available.

Another implication is that the CIS countries are less exposed to the global capitalist class and have a potential for internally led economic development. This explains why Putin and Medvedev can adopt a more independent policy in international and internal affairs. The European Union new member states are closely integrated by ownership of their assets by foreign companies, many of them multinationals. This binds closely their elites politically, militarily and economically to the hegemonic world powers; they are highly dependent on trade with them, though perhaps ironically, this trade is of low value added commodities.

The notion of a 'core' of Western states possessing intellectual, political and economic capital needs to take account of a political and economic cluster (USA, UK, Germany, Japan) forming a hegemonic bloc; and dependent satellites (new EU member states) (Pickles 2008, 23)<sup>11</sup>. Russia and China, usually considered 'semi-periphery' have a greater independence from the core. They interact with it, but its elites are not (yet) part of the world political class and they are not agents of economic exploitation by a global capitalist class. Moreover, they have the potential to form a countervailing power.

### Effects of the world economic crisis on the post-Soviet societies

A world financial crisis was precipitated in August 2007 consequent on the collapse of the sub prime housing market in the USA. In the following year, it impacted on the global financial system: many major banks had liquidity problems requiring government assistance, and confidence in the financial system collapsed, leading to a severe reduction in credit. The consequences of failures in the financial system have been economic contraction, a rise in unemployment, and falls in interest rates and commodity prices. States have been required to intervene to restore the financial market. Not only have states (sometimes aided by the IMF and European Union) financed failing financial companies, but they have also taken some leading ones into public ownership. In its January 2009 update to its World Economic Outlook, the IMF noted that the growth of world output had fallen from 5.2 per cent in 2007 to 3.4 in 2008 and it forecast that it would fall further to 0.5 in 2009 (IMF website, accessed 17 April 2009). The decline, however, is divided unevenly between different groups of countries. While all countries suffer adverse effects, the advanced ones (at least initially) are more affected than the emerging and developing ones; and the post-communist countries have had less dramatic falls.

Figure 7 illustrates the drop in production in three years: 2007, 2008 and 2009. Note the sharp decline in the leading developed economies (USA, Germany, Japan, UK) and negative projections for 2009. The post-socialist European countries started with higher growth rates in 2007, and maintained positive rates (3%) in 2008. The CIS states, when Russia is excluded, even have a predicted small positive economic growth for 2009, and China has a rate of nearly 7 per cent – though this represents a considerable fall.

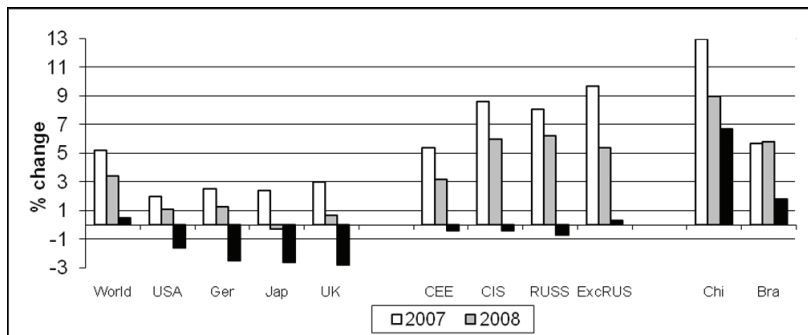
All economies are affected by contagion from the financial crises or 'stress' (IMF 2009, 140) stemming from the advanced economies. Clearly transmission will be greater to economies having stronger financial and commercial links. Economies with high levels of trade, dependency on capital investments and

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<sup>11</sup> Bela Greskovits uses the term 'semi-core' to define the Visegrad states.

bank credit will be adversely affected. There will then be direct effects (shortage and withdrawal of credit) of the financial crisis originating in the advanced countries and indirect effects of economic slowdown (fall in demand for exports and reduction of employment).

Figure 7: Falls in economic output of post-socialist and other countries: 2007, 2008, 2009



Data derived from: IMF website, January 2009 update to World Economic Outlook (accessed 17 April, 2009). Projection for 2009.

The direct effect of linkage to the global financial system is dependent on the level of penetration and indebtedness of economies to Western banks. Foreign banks' claims on 'emerging Europe'<sup>12</sup> are particularly high (on average in these countries over 60 per cent of GDP in 2007). Latin American countries are much lower (on average around 30 per cent), and 'emerging Asia' (which includes China and India) are around 40 per cent (ibid, 141). Russia<sup>13</sup> is even lower on the scale than the Latin American countries, being below 20 per cent. Russia as well as Latin America and the emerging Asian countries have all had financial crises in the recent past and have subsequently pursued a more cautious financial policy.

Exposure to foreign bank ownership increases the likelihood of reductions in credit in the host country. Such banks cut back on lending and withdraw funds from host countries. The post-socialist countries of central Europe are dependent on foreign banks. Foreign bank ownership has increased greatly in the post-communist countries. The CEE countries are almost completely dependent on foreign banks. As illustrated on Figure 8, in the new member EU states in 2004 on average over 70 per cent of the assets of banks are foreign

<sup>12</sup> Here defined as Bulgaria, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, Slovak Republic, Slovenia and Turkey. Russia is listed in the source, but this is an error – personal communication from IMF.

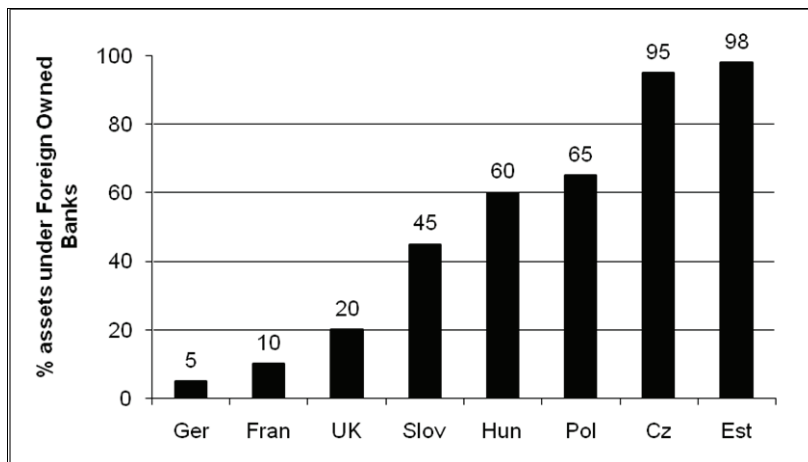
<sup>13</sup> IMF data. I am indebted to Staphan Danninger of the IMF for detailed information.



owned (in Estonia the figure was 98 per cent, Czech republic 95 per cent); in the old member states, foreign ownership in the Euro area zone was less than 20 per cent on average, with countries like Germany and France having less than ten per cent. UK's foreign ownership was 20 per cent (Cihak and Fonteyne 2009, 6).

With the worsening of the economic climate, banks in CEE became exposed: a large number of speculative loans had been made and failed in the economic downturn and the number of non-performing loans increased. The undercapitalised banks in the Baltic countries had a very large number of foreign currency denominated loans (ibid, 29).

Figure 8: Share of foreign owned banks (in per cent of total assets, 2004).



Source: Cihak and Fonteyne (2009, 6).

The new member EU states are more vulnerable than the CIS to the external bank crisis. The CIS states have far fewer foreign banks and are less dependent on them. Russian banks are in a better position than the banks in the new member states of the EU. According to a study by Zuzana Fungáčová and Laura Solanko, based on data between 1999 to 2007, Russian banks have lower risk levels than those in central and Eastern Europe. State owned banks have less insolvency risk than private banks, while foreign banks in Russia have higher insolvency risk. Russia has a large number of banks (1,243 by the end of 2007) but most are extremely small (in 2007 only some 900 banks had the right to attract household deposits and only 300 banks had a general banking licence). No comprehensive privatisation of the banking sector has taken place, making it difficult for foreigners to buy bank assets (though some small foreign banks have been set up). Consequently, ownership by foreign banks is small – 202 banks had some foreign ownership at the end of 2007, and only 62 of them

were fully foreign-owned. The operations of foreign banks in Russia are ‘dramatically different’ from those in central Europe (Fungáčová and Solanko 2008, 13). The asset share of foreign owned banks at the end of 2007 was 17% of total sector assets<sup>14</sup>. Russia would appear to be in a stronger position than the new member states of the EU, being less dependent on foreign banks and having greater regulation and more cautious state owned and controlled banks.

Dependence on foreign finance made the post-socialist European Union states more volatile; they have nearly all suffered considerable devaluation between 2008 and January 2009: the value of currency in Estonia, Lithuania and Bulgaria declined by nearly 20 per cent; Belarus 23 by per cent; in Czech Republic by 32 per cent, Poland by 41 per cent, Ukraine by 42 per cent; by comparison, the UK’s pound fell 29 per cent and the Euro 19 per cent<sup>15</sup>.

The finances of Russia, Kazakhstan and Turkmenistan were all significantly diminished by the severe falls in the prices of their energy exports. Russia suffered a major devaluation of 30 per cent. Foreign investors sold their stocks and precipitated falls on the stock exchanges. Such devaluations have made imports much more expensive and have boosted domestic industry. However, the enormous reserves amassed by Russia have mitigated many of the negative effects.

Other losses accrue in the post-communist countries through decline of value of their investments in the advanced economies following falls in the stock exchanges. More indirect consequences follow from the actual and expected slowdown of the advanced economies, and the decline in exports and earnings. The fall in the price of oil is one notable indicator. Hence, countries with a high proportion of exports as percent of GDP are likely to be more affected by the economic crisis.

A consequence of economic restructuring has been high levels of unemployment in the post-socialist countries, which have been made worse by the economic crisis. While registered unemployment statistics understate the real rate of unemployment, they are useful to illustrate the changes taking place. Even in the period between August 2008 and March 2009, unemployment increased considerably in all member states of OECD: the European Union from 7 per cent to 8.3 per cent – a rise of 18.5 per cent. Details are shown on Figure 9, the left hand axis shows the proportion unemployed in each country (the digits shown refer to the proportion unemployed in March 2009); the figures on the right show the proportionate increase in unemployment – the impact of the monetary recession. Data are not available for all the post-communist members. However, the unemployment rate in Czech Republic rose from 4.3 to 5.5 per cent of the work force – a rise of 28 per cent in the numbers

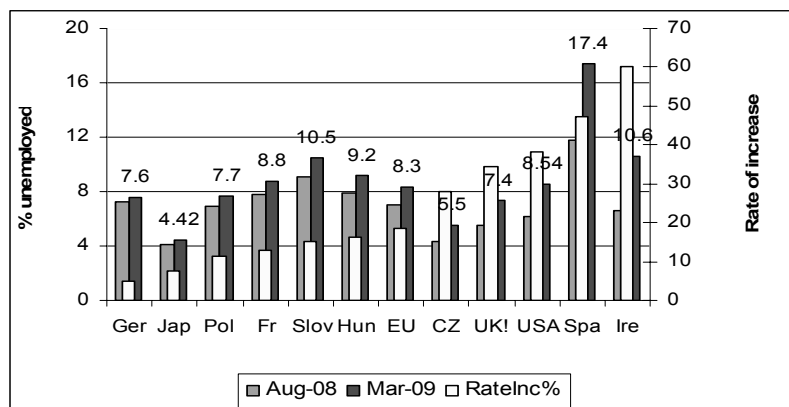
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<sup>14</sup> Based on the EBRD data, Laura Solanko, Email communication, April 2009.

<sup>15</sup> Vedomosti, 2 February 2009. Cited by Julian Cooper (Birmingham University) circulated paper, April 2009.

unemployed. For comparison, in the USA the rise was even greater – from 6.17 per cent to 8.54 per cent, an increase of 38.4 per cent. For Russia, the total number of unemployed rose from 1.39 millions (average for 2008) to 2.04 millions in March 2009, a rise of 46.7 per cent (OECD statistics 2009)<sup>16</sup>. The more corporatist economies – Germany, Japan and France – had the lowest percentage rises, whereas Ireland, UK, Spain and USA all had very high increases.

Figure 9: Unemployment rates: Post-socialist countries with comparisons: August 2008, March 2009



Source: OECD statistics. (accessed 5 May, 2009) <<http://webnet.oecd.org/wbos>>. UK rates for 2008 and 2009. IMF, World Economic Outlook, Chapter 2. p.65, May 2009.

The slowdown in the advanced countries also effects migrant labour. Countries with large numbers of citizens working abroad suffer falls in foreign remittances. This is particularly important for high unemployment countries such as many of the new EU member states and non-energy exporting countries of the CIS, such as Kyrgyzstan, Tajikistan and Uzbekistan. The shrinkage of the labour market leads to return migration of labour, both between countries, but also between more industrialized areas of countries and the rural hinterland.

This brief survey of the effects of the financial crisis indicates that while all countries have suffered, some have suffered more than others. Some post-socialist countries have advantages which enable them to cope with the externally generated downturn. Both Russia and China are countries with potentially large internal markets which could be stimulated to replace export losses. Both have accrued considerable financial reserves. The relatively low country transnationality index minimizes the effects of exit by foreign companies. The new

<sup>16</sup> Not all OECD countries are shown in this table.

member states of the EU have been hit by particularly negative consequences of credit reduction and foreign FDI. Their major compensating asset is a pool of low-cost and poorly protected labour. They have lower unemployment compensation and fewer restraints on dismissal of labour. They remain low-cost producers and are therefore favoured by international companies. However, such practices further instability and social unrest in the core countries when labour is confronted with unemployment.

## Conclusions and implications

The state socialist societies before 1986 were not part of the world-economy as defined by Wallerstein (1979, 13). The state socialist societies were a counterpoint to, rather than a semi-peripheral part of, the world capitalist system. Unlike Wallerstein, who conceives of a single capitalist world-economy, I consider the world economy to be composed of separate interconnecting units each with different qualities of sovereignty. At best, only two European countries (Poland and Hungary) had significant links with it but were not dependent on it. While fractions of the incumbent political elites in the socialist societies sought membership of the transnational political class, the latter had no economic base in the European socialist countries.

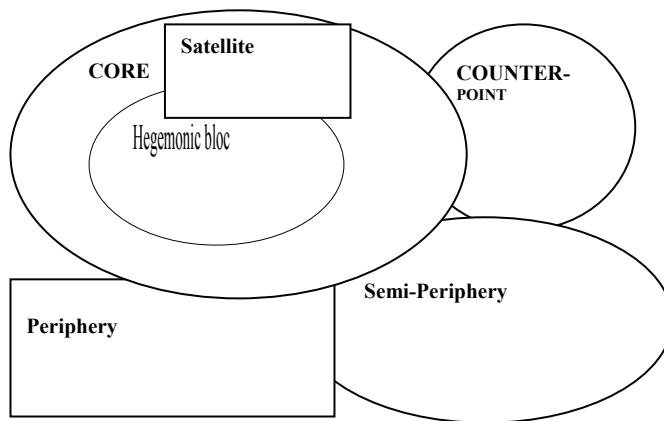
Following the fall of the socialist system, the former state socialist societies have developed along different trajectories to become part of, or to exchange with, the capitalist world system. In all the new European Union post-socialist states, integration into the world economy has occurred. These countries are much more closely integrated into the world system of commerce and production and have become part of the global division of labour. They have become integrated into the economies of neighbouring old EU states on the terms of the latter. While they have become integrated with the 'core' member states, foreign investment has entailed large scale foreign ownership of their financial, commercial and industrial assets giving a high level of dependency on foreign companies. Foreign ownership of financial and non-financial companies and tight links with the financial systems of the old European Union member states have led to contagion following the economic crisis of 2007. They remain economically dependent members of the European Union, exporting services and products at the lower end of the production chain. Additionally, they provide a pool of reserve labour for the old member states. The effects of the global economic crisis have led to economic decline as well as rising unemployment and return migration. One compensating strength is the weak organisation of labour and low-cost production.

How then may one theorise these post-socialist EU states in the world system? Some commentators, while agreeing with the general trends described above, come to different conclusions concerning their place in the world system. Bela Greskovits (2008, 23) uses the term 'semi-core' to define the

Visegrad states. Jan Drahokoupil (2009, 112) considers that ‘neo-liberal transition strategies in the Visegrad 4 led to the peripheral integration of the region into the world economy’; Arjan Vliegthart (2009, 14) concludes that the economic structure of the region ‘can best [be] captured under the heading of the semiperiphery’.

Some of the ambiguity may be overcome if one acknowledges a ‘hegemonic bloc’ among the core states dominated economically, politically and militarily by the United States. Around this bloc are a number of ‘satellites’ which include the new post-socialist EU states. These have separate state formations but are almost completely dependent on the hegemonic states for political and economic sustenance. The semi-periphery is constituted by countries which are both exposed to the core states and offer surplus value to them, but also have their own national forms of economic accumulation and may not be integrated politically and militarily into the core. Peripheral countries not only lack nationally based forms of capital accumulation but also are not part of the economic-political bloc of the core countries. The pattern is illustrated in Diagram 1.

Diagram 1. World System: Core (Hegemonic and Satellite), Semi-Periphery, Periphery and Counter-Point



The world economic crisis has exacerbated the differences between the neo-liberal, coordinated and statist forms of capitalism. Neo-liberal ideology, which has driven the movement for membership of the European Union, has experienced a legitimacy crisis consequent on the impact of the financial crash. The continental EU states – France, Germany and Italy – have revived the ‘social model’ of coordination. It is likely that ‘scepticism’ in the member states about the integrity of the European Union will intensify. Concepts of national identity are strengthened, leading to calls for national solidarity and national sover-

eignty. The severe economic difficulties of the New Member states will sharpen divisions in the European Union, especially if any of the new member states become financially bankrupt and require significant EU financial assistance (in addition to the sums already provided by the EU and IMF).

The Commonwealth of Independent States is far less integrated into the world economic system. Its largest economy, Russia, is a hybrid economic system: the energy sector is integrated into the world economy and significant transnational companies are emerging. These, however, have relatively low penetration by foreign capital, domestic capitalists ('oligarchs') and state ownership is dominant. But manufacturing and agriculture are local in character and are in decline. The CIS countries have a low component of high-tech products and a large primary sector share in their export profiles. The transnational capitalist class seeks a place in these economies through ownership and control of the primary sector exporting industries, which provide a firm link with the hegemonic countries of the core. However, their penetration is much weaker than in the EU new member states; foreign ownership of banks is particularly low. The state remains an important economic and financial actor in all these countries; many have a statist form of coordination. Nevertheless, contagion has spread: the world economic depression has led to a severe decline in earnings from the energy sector: economic growth has fallen and unemployment has risen.

Overall, the non European Union post-socialist countries remain on the semi-periphery of the world system. The economy largest in size, Russia, is the only one with any global economic presence. In terms of its companies, it is restricted mainly to a small number of energy companies whose products are sold abroad. In many respects, the CIS is not fully incorporated into the world capitalist system, as the economies have a high level of state ownership and state direction, and foreign companies have relatively little penetration. Whereas the central European countries have experienced considerable foreign ownership of their banks, the relative isolation of Russia in this regard may prove beneficial. Even with the falling value of energy exports, the world recession will have less impact because their economies are less integrated into the world system. However, this should not deflect attention from the severe problems, derived from the ways transformation has been implemented – deindustrialisation, high levels of unemployment and poverty. Economic decline in the industrial western countries impacts on demand for their primary and low value added products, and unemployment in (foreign) host countries leads to return migration of immigrant workers.

In all the post-socialist states the negative impact of the economic depression is weakening the ideological and economic attraction of globalisation in general and the neoliberal market model of coordination on which it is currently based. Even the hegemonic states (UK and USA) have fallen back on state coordination of the financial system – at least in the short term. National

sovereignty, national distinctiveness and state identity are becoming more important organising principles. This has led to an anti-nation back-lash fuelled by the economic liberalism of the global elites.

The global recession brings into question the role of the core hegemonic states, particularly the USA, in the world system. There are two main reactions to the underlying causes of the current economic crisis: first, strengthening the power and legitimacy of global institutions of world capitalism – organisations such as the International Monetary Fund, the World Bank and the World Trade Organisation. One consequence of the global financial crisis is the greater participation of non G8 countries in global decision making. Countries like China, India and Brazil have benefited politically and the G20, which became a forum for a global economic response, incorporates countries from the semi-periphery. It is likely that China and Japan will increase their powers in the global institutions of world capitalism at the expense of the European countries. In world system terms, this strategy diminishes the possibilities of alternative policies in the semi-peripheral countries. The second reaction involves a move towards national sovereignty, concurrent with a rejection of neoliberal globalisation. This entails a shift to, and a strengthening of, a more regulated type of capitalism (as in Germany and France). Even in leading neoliberal economies, such as the USA and UK, the state has taken strategic stakes in leading financial and non-financial companies.

A third scenario involves a reconfiguration of the relationships between the core and semi-periphery of the world economy: the development of regional blocs which exchange with, but are not part of, the core presently dominated by American capitalism. Critics of the global system envisage a polarisation of interests between core and periphery. The core countries extend their economic power, which is constitutive of their political hegemony and military power. The peripheral states provide out-sourcing as well as the provision of primary and secondary products. The 'semi-periphery' is considered to be a transient category destined to slip into the periphery or, exceptionally (as in the case of South Korea) to join the core.

This position is overdetermined and underestimates the potentiality of the 'semi-periphery'. It is true that many nations on the periphery, when confronted with the economic, political and military power of the core states, have little alternative than to accede to their policies. Others (Russia, China, India, and Brazil) of the 'semi-periphery' have more options than assumed by world system theorists. Global capitalism is as inherently unstable as national capitalisms and incompatibilities may arise between a neoliberal world economy and institutional regulation as proposed by the IMF.

The 'semi-periphery' is a site for major changes in the world economy. It may lead to the rise of alternative groupings of states which interact with the core but are not part of it – analogous to the state socialist societies before their collapse. These might form economic and political counterpoints to the capital-

ist world system. The economies of many countries have production that is local in character and could be developed, if given protection. Regional companies and political actors have considerable scope for action independent of the global economy (Kitschelt et al. 1999, 427-460). In the post-socialist countries, developments such as the formation of the Shanghai Cooperation Organisation<sup>17</sup>, the Collective Security Treaty Organisation<sup>18</sup>, the Eurasian Economic Community<sup>19</sup> and the Organisation of Central Asian Cooperation<sup>20</sup>, are evidence of the rise of regional economic and political blocs.

Such tendencies may be accelerated by the impact of the global depression which is severely weakening the neo-liberal model of development and change. Some Latin American countries, such as Brazil and Venezuela, might well follow the example of Russia and China and constitute a more state-led trading bloc having less dependency on the hegemonic capitalist world system. Such a grouping would be able to develop an alternative value system to that of global capitalism, with a greater emphasis put on economic and social security – the provision of employment, more equal distribution of income and wealth, less poverty, and the expansion of local and regional industries. Rather than a focus on monetary regulation and market coordination, as entailed in the neo-liberal model, an alternative is an emphasis on prioritising economic development and employment and the utilisation of Keynesian models of state economic stimulation. In this context there is an option for a type of national corporatist capitalism, or even a revival of traditional socialism, – as a ‘counterpoint’ – an alternative to participation in the global economy on the terms of neo-liberalism.

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<sup>17</sup> Composed of China, Kazakhstan, Kyrgyzstan, Russian Federation, Tajikistan and Uzbekistan.

<sup>18</sup> Armenia, Belarus, Kazakhstan, Kyrgyzstan, Russia, Tajikistan and Uzbekistan.

<sup>19</sup> Russia, Kazakhstan and Belarus.

<sup>20</sup> Russia, Turkmenistan, Tajikistan, Kazakhstan, Uzbekistan and Kyrgyzstan.



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