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EUROPE DIVIDED? CAN WARSAW BECOME THE REGIONAL LEADER OF THE CENTRAL AND EASTERN EUROPEAN REGION?[1]

ABSTRACT This paper investigates the long-term problems of capital accumulation in the context of centre and periphery and dependency models, the systemic and geo-economic features of the integration of post-socialist transition countries in the context of dependent market economy (DME) model characterized by high dependency on foreign direct investment channelled by foreign MNCs into the CEE and the restructuring of the centres in Central and Eastern Europe. It argues that the global economic crisis has been exposed the systemic vulnerability of the post-socialist neo-liberal transition model characterized by foreign investment-led growth which is failed to generate domestic capital accumulation and decrease the relative development gap between the 'old' and 'new' EU members. We would like to use the principles of geoeconomics in order to analyse the Central and Eastern European region and the role of the Foregin Direct Investment and its special role in financial sector in transformation and the question of the problem of Central and Eastern European financial centres focusing on the position of Warsaw.

Key words: geoecenomics, financial centre, transformation

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When the Berlin Wall fell, the peoples of Eastern Europe were told that privatisation and the market would bring them economic efficiency and freedom. They were also told that as soon as they set up democratic regimes they could join the 'civilised, normal world'. In other words, go 'back to Europe'.[2]

INTRODUCTION, THE MEANING OF GEO-ECONOMICS APPROACH

The importance of geoeconomics lies in the importance of this method in the globalised world. As a discipline, geoeconomics is associated with American strategist Edward Luttwak who emphasized the importance of trade and finance among nations over military strength and ideological competition.[3] Geoeconomics is also understood as the use of economic tools to advance geopolitical objectives or as the interplay of international economies, geopolitics and strategy.[4] According to Edward Luttwak following the Cold War the importance of military power is giving way to geoeconomic power. Geoeconomics has gradually replaced geopolitics in the era of globalisation. The discipline of geoeconomics is different from that of geopolitics in two fundamental ways. First, with respect to *topic*, it is not primarily concerned with political and military activities, but with economic activities. Secondly, with respect to *actors*, the activities are not undertaken chiefly by individuals representing the nation state, but by employees of private-sector organizations, whose loyalties are first and foremost to the owners of those organizations. Geoeconomics, like geopolitics, is studied first of all with the interests of the nation state in mind, or from the macro perspective. This makes it more complex than the study of geopolitics, where the State itself is the primary actor. In contrast with geopolitics, it focuses not primarly on the state and its role, but rather on the private enterprises.[5] Their focus is on networks not blocks, connections not iron curtains, transborder ties instead of national territories. The logic of geoeconomics is a process which the nation state does not control in the Western world, since it is moved forward chiefly by private-sector economic initiatives on an interna-

[2] C. Samary, "The EU's Eastward Expansion", *International Viewpoint*, 28 June 1997, at <http://www.internationalviewpoint.org/spip.php?article758>.

[3] See M.J. Munoz, *Advances in Geoeconomics*, London–New York 2017, p. 1.

[4] M. Petsinger, *What is Geoeconomics?*, at <https://www.chathamhouse.org/system/files/publications/twt/WiB%20YQA%20Geoeconomics.pdf>.

[5] See K.S. Søilen, *Geoeconomics*, London 2012, p. 302.

tional scale. In other parts of the world the State is more actively in charge of economic activities.

Geoeconomic visionaries tend as a result to anticipate capitalist inclusion rather than the expulsion or containment of evil others. Their focus is on networks not blocs, connections not iron curtains, and transborder ties instead of national territories. They focus on what can link and not what to separate as the most important is the business and economic netwoeks. And rather than reproduce geopolitical understandings of 'us' and 'them' that fetishize place, they tend instead to fantasize about connectivity and pace. To connect this contrast to two big names, this is how Halford Mackinder[6]) – who originally imagined a modern geopolitical condition of competing empires and 'post-Columbian closed space' – differs geo-discursively from Thomas Friedman – the *New York Times* columnist who like many other geoeconomic gurus of globalization enframes a post-Cold War world and, indeed, post-post-Columbian epoch of globally flat and level space.[7]

ECONOMIC TRANSFORMATION IN CENTRAL AND EASTERN EUROPE

Economic transformation in Central Europe has mainly followed a development path based on Foreign Direct Investment, which has reinvigorated short-term competitiveness, but now faces the need to go beyond low costs, and counteract the unfavourable effects of external capital and export dependency. The economic transition fuelled by a neoliberal approach through economic liberalization, marketization, privatization overlapping with excessive 'foreignization' which created the legal and structural frameworks for the dependent mode of re-integration into the EU, and at the same time, into the global division of labour (Sachs,[8] Gowan,[9] Sokol,[10] Smith[11]). The most important *historical dependencies* of the CEE region, such as financial, technological and market ones, remain constant. This is complemented with the large energy dependency of CEECs on Russia. This not only further strengthens the external vulnerability of the

6 I. Szilágyi, "A földrajz a történelem kulcsa", *Magyar Tudomány*, no. 11 (2011).

7 M. Sparke, "Geopolitical Fears, Geoeconomic Hopes, and the Responsibilities of Geography", *Annals of the Association of American Geographers*, vol. 97, no. 2 (2007), at <https://doi.org/10.1111/j.1467-8306.2007.00540.x>.

8 J. Sachs, "What Is to Be Done?", *The Economist*, 13 January 1990, pp. 23-28.

9 P. Gowan, "Neo-liberal Theory and Practice for Eastern Europe", *New Left Review*, no. 213 (1995), pp. 3-60.

10 M. Sokol, "Central and Eastern Europe a Decade after the Fall of State-socialism: Regional Dimensions of Transition Processes", *Regional Studies*, vol. 35, no. 7 (2001), at <https://doi.org/10.1080/00343400120075911>, pp. 645-655.

11 A. Smith, "Imagining Geographies of the 'New Europe': Geo-economic Power and the New European Architecture of Integration", *Political Geography*, vol. 21, no. 5 (2002), pp. 647-670, at <https://doi.org/10.1016/S0962-6298(02)00011-2>.

region, but also makes re-interpretable the geopolitical and geoeconomic features of the former buffer zone situated between the German and Russian spheres of interest.

Global financial capital has played an important role in all transition economies. Foreign Direct Investment (FDI) in the banking and insurance, as well as manufacturing sectors is closely connected to the transition process in Central and Eastern Europe (CEE) and has received considerable attention from both a theoretical and an empirical perspective[12] much less attention has been devoted to the post-transition period and the impact of the crisis despite the crisis have shown the limits of externally financed and dependent transition models in Central and Eastern Europe.

Central and Eastern Europe can be identified as a special type of transitional and civilisational zone. According to Wallerstein's approach it can be described as semi-periphery – states that are located between the core and the periphery. They catch influence from the core area, but there are characteristic features that make them similar to periphery, too. This division survived for centuries, this historic heritage remained in Europe as a dual structure. The difference can be caught in the following issues: nation state versus global governance, representation of the local or global interest, federalism or strong nation state.[13]

Most of the literature studying transition process has seen the transformation and the (re)-integration of the region into the global capitalist system as a linear convergence with the advanced market economies, following the path of liberalization and privatization. However, there are considerable diversity among Central and Eastern European countries, due to the varieties of implemented transformation models and economic policies.[14] The crisis further strengthened these different developmental trends resulting in diverging economies and regions within Central and Eastern Europe.

Due to the legacies of state socialism, but also long-term historical dilemmas of catching-up and capital accumulation, the development prospects of the CEE countries require additional scrutiny. While the protagonists of post-socialist transition and EU integration expected that this semi-peripheral region would experience significant development over the following decades, fundamental problems of convergence and integration remain unanswered.

Dependencies and semi-peripheral situation are the direct consequences of relative scarcities in capital and technology. The roots of these scarcities lie in the unfavourable conditions of specialization in the international division of labour. This is character-

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12 S. Estrin (ed.), *Privatization in Central and Eastern Europe*, London 1994; A. Bevan, S. Estrin, "The Determinants of Foreign Direct Investment into European Transition Economies", *Journal of Comparative Economics*, vol. 32, no. 4 (2004), pp. 775-787, at <https://doi.org/10.1016/j.jce.2004.08.006>.

13 See in: A. Schmidt, "International Political Economy, the V4 States and the Economic Transformation", University of Pecs 2015, pp. 9-10, quotes I. Wallerstein, *A modern világgazdasági rendszer kialakulása. A tőkés mezőgazdaság és az európai világgazdaság eredete a XVI. században*, Budapest 1983.

14 Martin Sokol ("Central and Eastern Europe...") puts the CEE transition into the context of the centre-periphery model and divides the regions by different subregions: 'super-periphery A' (ECE nd Baltic sates) have a more solid economic structure, legacy of modernization and more experince with market and politica democracy. In 'super-periphery B' (former Soviet Union) liberal-capitalist economic and political structures were relatively underdeveloped.

ized by the limited access to resources in the process of capital accumulation, and at the same time, semi peripheral regions experienced significant outflows of resources, which make semi-peripheries unable to follow autonomous growth. As a result, there is a heavy dependence on external resources for both investment and consumption.

Nölke and Vliegenthart[15] present the CEECs as a new dependent variety of capitalism, based on strong capital dependency developed during the course economic transition and integration with the advanced countries of Western Europe through foreign ownership of industrial capacity and much of the financial sector. We argue that the FDI-led development path in the CEECs followed the pattern of the dependent market economy (DME) type of capitalism and the semi-peripheral dependent development (see e.g. Raviv,[16] Nölke and Vliegenthart,[17] or Myant and Drahokoupil[18]) and also fits to the world-system model which consider CEE as a perpetual semi-periphery. This is characterized by the limited access to resources in the process of capital accumulation, and, semiperipheral regions experiencing significant outflows of resources unabling them to follow autonomous growth.

THE BORDERS OF CENTRAL AND EASTERN EUROPE AND THEIR PERFORMANCE

Thanks to its location CEE region was always the target zone of the great powers from the West and the East. The German concept composed in the programme of Neumann called Mitteleuropa plan from 1915 was the similar attempt of political subordination of Germany and the economic exploitation of the Central and Eastern Euroean region during the first World Was such as the forced economic and political dependence that appeared in the political programme of the Nazi party and was involved with the ideology of Lebensraum. Befoore 1945 Germany was the main international trade partner among the Central and Eastern European states that was replaced by the Soviet Union from the late 1940s and extended with the founding of Comecon. By the early 1950s the share of foreign trade among the satellite states increased from 10-20% to 60-75%.[19] Energy dependency was a determining problem thanks to the rapid and forced industrialisation that was forced by the Soviet Union. Bilateral agrements between the Soviet Union and the satelite states also guaranteed the energy and raw material supply for the

15 A. Nölke, A. Vliegenthart, "Enlarging the Varieties of Capitalism: The Emergence of Dependent Market Economies in East Central Europe", *World Politics*, vol. 61, no. 4 (2009), pp. 670-702, at <https://doi.org/10.1017/S0043887109990098>.

16 O. Raviv, "Chasing the Dragon East: Exploring the Frontiers of Western European Finance", *Contemporary Politics*, vol. 14, no. 3 (2008), pp. 297-314, at <https://doi.org/10.1080/13569770802396345>.

17 A. Nölke, A. Vliegenthart, "Enlarging the Varieties of Capitalism...".

18 M. Myant, J. Drahokoupil, "International Integration, Varieties of Capitalism, and Resilience to Crisis in Transition Economies", *Europe-Asia Studies*, vol. 64, no. 1 (2012), pp. 1-33, at <https://doi.org/10.1080/09668136.2012.635478>.

19 A. Schmidt, "International Political Economy...".

small Central and eastern European states from the Soviet Union while they mostly paid by industrial products. However idustrial deliveries for the huge and undermanding Soviet market also helped the rapid industrialisation of the mostly agrarian countries of the region.

The trajectory of Central and Eastern Europe differed significantly from that of the West and it was characterized by historical dependencies and perpetual attempts of catching up. The CEE region within the system of capitalist division of labour became semi-periphery of a transforming West during the early modern age. The 19th and 20th centuries were characterized by three major waves of catching up with the West.

(1) Turn of the 19th and 20th centuries experienced the most successful catching up even within the framework of empires. According to our calculations based on Angus Maddison's dataset the per capita GDP of the broader CEE region (with the West Balkans countries) in comparison with the 12 most developed Western European countries[20] 49% in 1910.

(2) Modernization under the centrally planned economy with its heavy industrialization and forced capital accumulation policy resulted in surprisingly rapid convergence of the region during the 1960s. Its per capita GDP reached 44% of the West by 1975, and started declined to 41% by 1980.

(3) Post-communist transformation and a fast privatization led to a tragic 20-25% decline of the GDP, and 20% to 30% decline of industrial output. The GDP per capita level of CEE reached its lowest point in 1992 (27%) and entered the period of half decade of transformation crisis and stagnation.

The deep transformation crisis followed the transition from a command to market economy reflected the collapse of eastern markets, economic decline, unemployment, inflation, doubtful results of privatization and a general decline in living standards. With the return 4-5% per year growth between 1994 and 2003 per capita GDP reached 35% of the West European level of development in 2005 (virtually the same level as in 1989) and 44% in 2008. This short term catching-up was halted by the 2008 crisis. Our calculations reflect that less than half (40%) of the Western level was achieved in Central and Eastern European countries in 2011. It seems that the development gap between the so-called 'old' and 'new' member states of the EU has not narrowed, but in fact has increased since the early 20th century.

In our interpretation the form of access to international capital is tied to a certain geopolitical situation and also to the changing geoeconomic framework conditions due to the course of globalization. In the case of CEE three major processes have resulted in the region's geopolitical and geoeconomic repositioning.[21]

First, the *transition and economic transformation* with its neoliberal marketization (and foreignization) strategy was accompanied by trade liberalization and inflows of

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[20] Austria, Belgium, Denmark, Finland, France, Germany, Italy, Netherlands, Norway, Sweden, Switzerland and United Kingdom.

[21] A. Smith, "Europe and an Inter-dependent World: Uneven Geo-economic and Geo-political Developments", *European Urban and Regional Studies*, vol. 20, no. 1 (2013), pp. 3-13, at <https://doi.org/10.1177/0969776412463309>; idem, "Imagining Geographies...", pp. 647-670.

FDI. Trade liberalization produced a significant market pressures on transition countries, even if a few Central European countries had some capacity to compete in Western markets, their export ability paradoxically restrained by protective measures of the EU, particularly in those sectors that were important to CEE recovery.[22]

Post-socialist transformation was a top-down driven process conducted by the CEE governments and externally assisted by the neoliberal financialization project and by international institutions (IMF, WB, EBRD, G7, EU, NATO), which made the institutional aspects of financial market integration to be part of an inherently political project of transition.[23] From the very beginning a broadly accepted set of criteria for the reform programme, the so-called Washington Consensus of 1989 was offered as a blueprint for the process of CEE economic transformation. The transformation as Bohle and Gerskovits remark[24] can generate conflicts in market economy and social cohesion and can determine the political legitimacy took part in a problem burdened region that was one of the least developed regions of Europe. The incorporation of the huge market with its natural and human resources offered several advantages for them. They could increase economies of scale and to exploit a low-wage and relatively well-educated labour force, and rearrange their production networks with a new kind of division of labour.[25]

Second, the international environment in which transformation took place in CEE was shaped by two major interrelated processes; the *economic and financial globalization*. The economic and political transformation of the 1990s across the CEE region was simultaneous with the faster expansion of globalisation. Apart from the fall of the Soviet bloc these developments contributed to the geographical extension of globalised integration that was accompanied by the relocation of industrial (later service) production of MNCs from the developed countries to emerging economies. It was the time when financial capital with the re-emergence of its unfettered mobility in the course of financialization left the US and EU for seeking new investment opportunities elsewhere. As Berend writes: *When the Berlin Wall collapsed, multinational companies from Asia, the United States of America, and most of all from Europe turned to the new hunting ground in Central and Eastern Europe*.[26]

The external pressure came from the intertwined virtue of foreign capital and the powerful intervention of international institutions. During the early transition foreign investment-led growth strategy was continuously backed up by a steady flow of studies and reports, emanating from the various international financial institutions as well as academia, supporting neoliberal solution and depicting foreign investment, driven by

22 See P. Gowan, "Neo-liberal Theory..." and M. Sokol, "Central and Eastern Europe...".

23 O. Raviv, "Chasing the Dragon East...", pp. 297-314.

24 D. Bohle, B. Gerskovits, *Capitalist Diversity in Europe's Periphery*, Ithaca 2012.

25 A. Schmidt, "International Political Economy...".

26 I. Berend, *From the Soviet Bloc to the European Union. The Economic and Social Transformation of Central and Eastern Europe since 1973*, Cambridge 2009.

large MNCs, as a panacea to the problems of the transition economies.[27] They created rather strict economic conditions for post-communist countries for their reintegration into the international market economy. As Gowan[28] argued the neoliberal way of economic transformation designed to allow foreign (Western) capital to conquer Easter European markets and to integrate there captured cheap production lines into the 'hub & spoke' West-East economic relations.

Third, the enlargement of the European Union in 2004 and 2007, besides being a political project, committed to the neoliberal, externally dependent investment-led growth strategies and the marketization process. As EBRD Report acknowledges *The requirements for accession to the EU are very similar to the requirements of transition*.[29] The structural power of EU financial capital (like in the US and UK) has been on the rise, mostly the result on EU policies. This capital flew towards Central and Eastern Europe mainly in the form of foreign direct investment (FDI) even before its accession. Eastern enlargement was accompanied by the expansion of multinational enterprises in the new member states, particularly in the 'Visegrad Group' countries.[30] The third dimension of relating to the geographical shift of industrial and services production within Europe of certain parts of the value chain in order to make EU (German) companies globally more competitive.

A key part of the EU's internal inter-dependencies aims to restructure its global geo-economic position, creating interdependent trajectories within the EU with the relocation of the more labour intensive or efficiency seeking industrial and services value chains to CEE. This internal geoecononomic restructuring within the enlarged EU created new core-periphery relationships that primarily benefit the core, often at the expense of the peripheries. This process that hollowed out not only the Mediterranean but also even more the Eastern periphery of the EU was caused by the resurgence and the growing the supremacy of the German capital. The Eastward expansion of German capital largely contributed to the geoeconomic supremacy of Germany over the European Union.[31]

It is generally accepted that the transition countries of the post socialist region remained dependent on foreign investment. These weaknesses did not slow down the re-

[27] Literature also suggests that only large enterprises capture economic of scale and scope, and larger banks enjoy significantly greater market power than their smaller peers. See A. Rugman, J. D'Cruz, *Multinationals as Flagship Firms. Regional Business Networks*, Oxford 2003. Others, like, Jeffrey D. Sachs and Andrew Warner argue that openness, measured partially by the investments of foreign owned companies, contributes to growth and economomic convergence. See J. Sachs, A. Warner, "The Course of Natural Resources", *European Economic Review*, vol. 45, no. 4-6 (2001), pp. 827-838.

[28] P. Gowan, "Neo-liberal Theory…".

[29] European Bank for Reconstruction and Development, *Transition Report 1998. Financial Sector in Transition*, London 1998.

[30] Czech Republic, Hungary, Poland and Slovakia.

[31] K. van der Pijl, O. Holman, O. Raviv, "The Resurgence of German Capital in Europe: EU Integration and the Restructuring of Atlantic Networks of Interlocking Directorates after 1991", *Review of International Political Economy*, vol. 18, no. 3 (2011), pp. 384-408, at <http://dx.doi.org/10.1080/09692290.2010.488454>.

gion's transformation and adjustment to the market requirements, but instead created limitations on further changes of transformation to catch up with the advanced West.

As a result, the chief characteristics of this blend of 'imported capitalism' included a relatively fast recovery from economic crisis but also the dominant role of foreign capital in the process of stabilisation. However, foreign investments not only contributed to the modernisation of the economy, but also increased its structural and spatial segmentation.[32]

THE ROLE OF FDI IN CEECS

Via economic liberalization and market-oriented institutional building, the post-socialist countries have also integrated into the system of production, commerce and finance of global and European capital and became the parts of a broader regional integration project. European and US assistance in reconstruction of the post-socialist region resulted the appearance of not just foreign capital, but controversal aid programmes foreign advisors sometimes with contentious proposals paving the way for foreign private investors.[33] In 1989 there was an G7 initiative to assist and help financially the CEE transitional economies by establishing European Bank of Reconstruction and Development[34] and the EU also generated a special aid called PHARE programme.[35] The main difference between the post-WII Marshall aid for Western Europe and the support coming from the EBRD for CEECs was that former was a non-refundable financial aid while the loan the EBRD had to be repaid. However, both IMF and EU aid programmes using their instruments to create the desired al of open indebted CEECs to FDI.

Foreign investments fundamentally helped the post-socialist countries in the shaping the region's diverse development paths. International (mainly US and German) capital was seeking market opportunities in Europe at the same time when CEECs started to privatize their state-owned enterprises and the European integration was also preceded. The European Union's decision to start entry negotiations with selected candidates greatly increased the region's attraction for FDI. It also resulted that the Viseg-

32 G. Eyal, I. Szelenyi, E. Townsley, *Making Capitalism without Capitalists. Class Formation and Elite Struggle in Post-Communist Central Europe*, London–New York 1998.

33 One of the most influential advisors was Jeffrey Sachs and the idea on 'instant capitalism' that concentrated on the following radical reforms: free trade, tax reform, deregulation and privatisation.

34 Despite of being aware of the economic conditions of the potential beneficiary states the original amount of the money for the investment in the economic reconstruction reached only 20 Bn USD, The Marshall aid accounted 13 Bln USD (130 Bln in 2015 August prices).

35 PHARE = Poland and Hungary: Assistance for Restructuring their Economies that is the abbreviation of the first beneficient countries; Poland and Hungary were the first target countires. This programme later covered the entire CEE region. PHARE programme was focusing on the promotion of economic and social cohesion and the in the last phase it concentrated mostly on strengthening the institutional convergence towards the European Union.

rad states became the most important target locations for investors, offering generous subsidy package to transnational strategic investors. During the period of privatization in the indebted countries of CEE there was a far greater cumulative need for external capital than the actual supply of foreign direct investments in these economies.

Foreign financial inflows and especially FDI have resulted in dramatic changes of ownership structures. In 1994, in the wake of the early transition crises, an overwhelming majority of banks in the post-communist countries were still state-owned. There was a double shift of ownership from public to private sector and at the same time from domestic to foreign owners through privatisation. In contrast, in 2007 private foreign ownership already accounted for about 80% of banks' assets in the CEE region.[36] Hungarian financial markets similarly to other CEE counterparts remained rather bank-centered, and security markets played only a limited role. The only exception in the region is revival of Warsaw securities market since the mid-2000s.

One of the most important targets of the FDI was the financial sector and in particularly the banks. Foreign financial inflows have resulted in dramatic changes of ownership structures throughout the region. In 1994, in the wake of the early transition crises, an overwhelming majority of financial intermediaries in the post-communist countries were still publicly owned. By contrast, in 2007, more than a decade later, private foreign ownership already accounted for about 80% of financial intermediaries' assets in the CEE region.

FDI inflows into CEE economies have been a vital factor in privatisation, and FDI became the predominant type of incoming capital investment in the first stage of the economic transition.[37] This process not only was to facilitate the restructuring and transformation of centrally planned economies but also the privatization process, i.e. the increase of the share of private ownership at the expense of state-ownership. CEECs lacked domestic private capitalists with financial resources to by these enterprises; therefore these opportunities were transferred to foreign investors. The banking sector and manufacturing became the primary targets of strategic foreign investors, resulting in significant inflows of FDI in these sectors, connected mainly to the privatisation of state-owned enterprises. Similarly to global processes foreign investors' entry has been geographically and sectorally concentrated (high tech manufacturing, food processing, retailing and financial services), and the main investors have come from traditional economic and trading partner countries (mainly Eurozone countries) of the host countries.

Foreign capital was expected to be the engine of transition bringing new capital, new technology, efficient management, jobs and economic growth to Eastern Europe.

36 These figures are especially striking when we compare them with the average level for EU-25, where the share of foreign owned banking assets in total is less than one quarter. In the Euro area this figure is equal to 15.5%. Even the average for non-OECD countries is 50%. Z. Gál, "Role of Financial Sector FDI in Regional Imbalances in Central and Eastern Europe", in A. Gostyńska et al. (eds.), *Eurozone Enlargement in Times of Crisis. Challenges for the V4 Countries*, Warszawa 2014, pp. 27-35.

37 D. Holland et al., "The Determinants and Impact of FDI in Central and Eastern Europe: A Comparison of Survey and Econometric Evidence", *Transnational Corporations*, vol. 9, no. 3 (2000), pp. 163--212.

FDI is still can be seen as a key driver for economic modernization and convergence of the low and middle-size income countries in Eastern Europe. However, the effects of FDI depend fundamentally on the initial condition of the host country, therefore FDI in the region were very unevenly distributed. Investors have clearly preferred the more stable and economically relatively more advanced countries within the region.

Privatization became the cornerstone of economic transition since it shaped the property rights and the corporate government systems. Privatization period is considered to be a take-off in FDI inflows into transition countries. It was also important for establishing the future rules of the game with regards to the competition. It also generated the ever-largest FDI booms during the 1990s in CEECs and in the world.[38]

FDI inflows have resulted in dramatic changes of ownership structures first in the banking and insurance sector being a forerunner in privatization process, and quickly followed by manufacturing. In 1994, in the wake of the early transition crises, an overwhelming majority of financial intermediaries in the post-communist countries were still publicly owned. In contrast, in 2007, more than a decade later, private foreign ownership already accounted for about 80% of financial intermediaries' assets in the CEE region. The high importance of foreign ownership in the banking sector is indicated by the share of foreign ownership as a percentage of total banking sector assets.[39]

The overall share of FDI in the GDP is the highest in Hungary (52%), Czech Republic (48%) indicating not only the strongest integration of these economies the EU/global economy but the largest (external) dependencies on MNCs' value chains as well. The share of FDI was lower in Slovakia (32%) and much lower in Poland (25%), which is comparable of the Austrian figure (23%). The transition to market economy helped the growth of services sector with the increased amount of foreign direct investment (FDI). From the 2000s, the largest part of this FDI reached was committed to the business and IT services sector. The share of foreign affiliates in production value in the non-financial sectors is highest in Slovakia and Hungary, with over 57%, followed by Czech Republic but it is below 30% in the case of Poland and around 20% in Slovenia.[40] Foreign shares in manufacturing production in CEE are dominated by multinational corporations (MNCs). Their share in manufacturing is even higher than in the economy as a whole, reaching 80% in Slovakia, almost 70% in Hungary, and 67% and

[38] Average purchase prices were minimal in CEE: avarege amount of foreign equity invested in developed countries were 18 million USD, and in developing country subsidiaries avareged 4 million USD, while in CEE it has been only 380 thousands USD. P. Gowan, "Neo-liberal Theory...".

[39] A significant part of the post-crisis external adjustment is followed by the increasing role of state intervention through tightening regulations and increased taxation on banking (for example in Hungary and in Slovakia). The Hungarian government launched a major re-nationalization program in the banking sector in 2010 in line with the plans to strengthen local financial structures. The share of foreign ownership dropped to 49% by 2015 in Hungary and also decreased to lower level in Poland and Slovenia with the lowest foreign presence.

[40] G. Hunya, "Mapping Flows and Patterns of Foreign Direct Investment in Central and Eastern Europe, Greece, Portugal during the Crisis", in B. Galgoczi, J. Drahokoupil, M. Bernaciak (eds.), *Foreign Direct Investment in Eastern and Southern Europe after 2008. Still a Lever of Growth?*, Brussels 2015, pp. 37-70.

in Czech Republic, whereas it is only 42% in Poland and 30% in Slovenia, demonstrating a smaller exposure and dependence on the foreign owned MNCs.

In terms of the fundamental motives for FDI in the region it followed first the market-seeking, and later efficiency-seeking strategies. *Market-seeking investments* concentrated on searching new market to buy important raw materials and sell products or services of the multinational company, without investment into processing or production. The risk of this strategy was that the extracting industry remained an enclave in the host country without generating spillover effect. The main investors in Central and Eastern Europe concentrated in building shopping malls, tobacco factories, sometimes in order to monopolize the markets.[41]

The second type of investment can be called *efficiency (labour) seeking investment*, which exploited the great differences in wages in particular in labour-intensive production branches. Low wage levels in the Central and Eastern European countries were combined with a relatively well-trained and educated workforce, as well as the proximity to Western Europe. Foreign investors in medium-high tech sectors such as the car industry prefer this combination.This is partciularly true for business services offshoring, which led to the mushrooming of shared services centres throughout the region.

The external capital dependency of the region is exacerbated by its manufacturing export dependencies on Western Europe. Industrial relocation of EU-based (mainly German) companies relying upon assembly production, accelerating in car manufacturing and in electronics, integrated CEECs into their global value chains and to the global division of labour. At the same time, they provided capital in the form of FDI the industrial upgrading towards high-tech manufacturing production.[42] In this respect, CEE played a significant role in the consolidation of the German (car) manufacturing industries and contributed to their globally compeptitive position.[43] However, high levels of international economic openness created vulnerability to economic decline in their markets during the economic crisis. The capital and export dependencies of CEE further aggravated by the energy dependency on Russia. The risisng cost of energy has increased both the trade and the balance of payment deficits.

GROWING IMBALANCES AND THE CRISIS IN CENTRAL AND EASTERN EUROPE

A large foreign capital inflow was also noticeable the standards of livings were also increasing temporarily. The new democracies of CEE were looking forwards to joining

41 A. Schmidt, "International Political Economy...".

42 P. Pavlínek, B. Domański, R. Guzik, "Industrial Upgrading Through Foreign Direct Investment in Central European Automotive", *European Urban and Regional Studies*, vol. 16, no. 1 (2009), pp. 43--63, at <https://doi.org/10.1177/0969776408098932>.

43 CEE region plays as significant role in the increasing competitivness of German manufacturing industries as the Single European Area, which is an instrument for protetcting the interests of German manufacturers.

European Union with great expectations. In CEECs catching up in the first half of the 2000s was generally accompanied by macroeconomic stability, but most countries of the region became increasingly vulnerable due to the unsustainable trajectories of huge credit,[44] housing and consumption booms, high current-account deficits and quickly rising external debt. The large proportion of household as well as corporate debt was denominated in foreign currencies. Consequently the debt risk and the unsustainable credit-fuelled growth risk is accompanied by excessive exchange rate risk as a result of foreign currency denominated lending. This latter risk transferred to underbanked CEE clients in the form of FX loans. This increasing dependence on foreign capital led to growing imbalances resulting in transmittance of contagion into CEE and the deepening crisis.

The financial crisis in 2008 ended the optimism in the European Union among the new member states. The attempt of creating an economically balanced structures with the accession of the postsocialist states was failed. In the run-up to the global crisis, the countries in Central Eastern and South-eastern Europe attracted large capital inflows and some of them built up large external imbalances. However, the crisis years caused not only a deterioration of capital inflows but also a deterioration of domestic and foreign demand, which led to a deep economic depression in much of the region.

The direction of shock transmissions and potential contagion affected the most fragile countries. In 2008 the crisis transmitted to the CEE region too and a year later the previously prospering countries had to experience a double digit decline in GDP while the average decline of the entire region was around 6%. Households with foreign currency debts began to feel the real weight of their indebtedness after the outbreak of the crisis as a consequence of continuous currency depreciation. They began to reduce their consumption due to the sudden increase of their debt. This decrease in consumption triggered a major contraction of investment.

The economic transformation (with dramatic transfer of ownership and the reallocation of factors of productions in favour of foreign investors) and integration model (joining the Single European Markets in a dependent semi-peripheral position), as well as the internationalization pursued during the transition to financialized capitalism (ended-up in short term boom on the expenses of indebtedness) created systemic vulnerabilities to wider economic crisis and to the long-term economic convergence of Central and Eastern Europe. The systemic vulnerabilities generated by the transition model of CEE is exacerbated by geo-economic problems, both by the predominant external capital & export dependence on Western Europe in the form of this uneqal semi-peripheral division of labour and energy dependency on Russia. The Atlantic system of financialised capitalist model was trasmitted into the CEE region in the form of dependent market economies (and dependent financilaization or credit-debtor) model, which further strenghtened the western control over Central and Eastern Europe.

[44] The amount of the loans granted is considerable everywhere, on the scale of the countries concerned: thus, the Austrian and Swedish banking networks cover with their loans the equivalent of 20% of the GDP of the Czech Republic, Hungary and Slovakia and of 90% in the Baltic States.

The financially and industrially integrated debtor countries of the region had become locked-in the growth trajectories of the core EU countries.

External dependency poses *long-term disadvantages for the accumulation of financial, human, and even social capital*. Dependent market economies are heavily reliant on external capital, a problem that can be considered a 'historical' weakness of Central and Eastern Europe, especially after periodic 'transformation losses' caused by frequent regime changes and the accompanying transformation losses.[45] Low and middle income competitiveness leads to a development trap in CEE: it hinders the formation of new, well-capitalised domestic enterprises, while encouraging skilled workers to move westwards in pursuit of higher wages – leading to long-term human capital loss and faster aging in Central Europe, and undermining the potential sources of catching-up to the West.[46]

Financial markets in the region remained rather bank-centred as a consequence of slowly developing capital markets. The share of banks in the financial sector assets is still around 70%. The depth of banking measured by assets per GDP was the highest in the Czech Republic (101 and 135% respectively) and the lowest in Poland (62.4 and 86%). Hungary with its figures ranked in the middle. As for the banking sector, measured by operational efficiency and profit indicators the Hungarian banking system proved to be the most and the least efficient at the beginning and at the end of our research period.

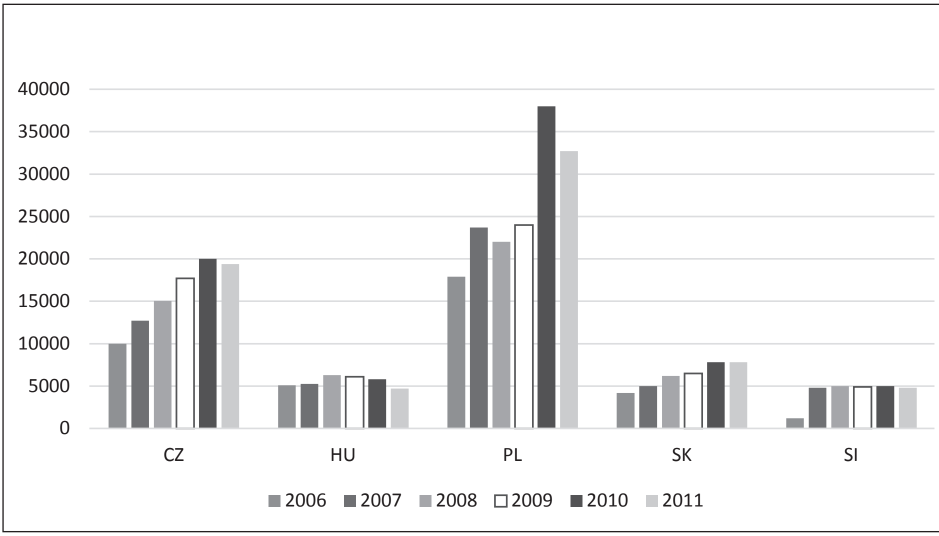
Operational efficiency of the banking sector has improved significantly in the region after a relatively short transition crisis. However, prior to the recent 2008 crisis, banking sectors in Central and Eastern Europe has become a major target of credit-fuelled growth. Foreign banks (parent to subsidiary) played a significant role in the transmission of contagion to transition economies.

There are significant cross-border transactions channelled through the networks of the West European parent banks and their local (CEE) subsidiaries. About 50-70% of corporate lending and 60% of interbank lending in 2009 was the subject of cross-border transactions, which has an implication not only for increasing international integration of CEE financial markets by strengthening connectivity to the European IFCs but this links also generated imbalances in the banking system during crisis time since the CEE remained largely reliant on cross-border lending. Hungary is experienced higher cross-border lending, which is expected on the basis of economic fundamentals and it had developed significant vulnerabilities in the pre-crisis period. This resulted in the largest drop in cross border lending (Contrary to Poland which almost managed to maintain its international position and Czech Republic where demand for cross border lending remained low). Cross border bank flows demonstrate that Poland has leading position of attracting banking flows, while Hungary shows larger fluctuation in this sense.

45 Z. Gál, "Role of Financial Sector FDI…", pp. 27-35.

46 G. Lux, "Can We Build Location Advantages? Local Policies for Industrial Competitiveness", in D. Vuković, H. Hanić (eds.), *Regional Development Policy. Scientific Basic and Empirical Evidence*, Belgrade 2015, pp. 42-51.

Figure 1. FDI stock in financial services, 2006-2011 (million Euros)



Source: national banks.

Concerning the crisis transmission in CEE, there are two distinct approaches in the transition literature. According to Myant and Drahokupil[47] the financial crisis was an external shock to CEE region and affected countries in different ways, where financial inflows and export flows were the transmission channels of the contagion. The other arguments emphasize that the crisis cannot be simply understood as internal adjustments to an external shocks, and rather the global financial and economic crisis exposed the weaknesses of the post-socialist neo-liberal economic development model in CEE. Focus on the dependent models and uneven forms of transition to capitalism and internationalizatiotion of the financial sector in CEE. They argue that this model of transition has contributed to systemic vulnerabilities exacerbated by the crisis in CEE region.

In a few CEE countries catching up in the first half of the 2000s was generally accompanied by macroeconomic stability (Czech Republic, Slovakia and partially Poland), but most countries of the region became increasingly vulnerable due to the unsustainable trajectories of credit-fuelled housing and consumption booms, high current-account deficits and quickly rising external debt (large proportion of it denominated in foreign currencies). The impact of the crisis has been highly uneven within the European Union and not only increased the gap between the core countries and the peripheries but resulted in growing diversity within CEE.[48] Poland has avoided recession by not having expanded huge debt and benefiting from its large internal markets. The

[47] M. Myant, J. Drahokoupil, "International Integration…".

[48] Hungary's external funding exposure was the highest (while Czech Republic had the lowest), reaching one third of total liabilities in 2009.

excessive burden of debt repayment resulted in severe decline both in investments and consumption. This was the case in some countries that experienced negative or zero growth in 2008 and 2009 (Latvia, Hungary, Romania).

GROWING ECONOMIC SIGNIFICANCE OF WARSAW WITHIN CEE

DMEs are not only characterised by an unequal power relation between the home countries and CEECs through parent-subsidiary networks of TNCs but created a 'dual banking system' models, which is characterized by the dominance of foreign-owned commercial.[49] Dual-economies literature argues that FDI generates typical core-periphery disparities between old and new Member States, which suffer from a 'de-nationalised dual-banking system'. That model, consisting of large foreign banks and small local/indigenous banks, displays strong dependence on foreign banks and their resources (external liabilities vs. local savings). These power relations mediate strong command & control functions over CEE countries within the international financial centre network, from where these investments are controlled. Asymmetric power relations also play a significant role in international financial centre function of Budapest, Warsaw and Prague and provide certain unfavourable preconditions.

As Central and Eastern European countries are largely dependent on foreign investors in finance, explicit attention is directed at determining which CEE financial centres attract multinational financial firms, and it is empirically assessed from which international financial centres these investments are controlled. The banking sector in the CEE region is predominantly commanded from the financial hubs of the neighbouring 'old' EU Member States. Vienna, Stockholm and Athens, among others, became gateways to the East and host the headquarters of large investors in the CEE, Baltics and South-eastern Europe, respectively. The largest concentration of parent-subsidiary connections forms bridgehead centres (Moscow, Warsaw, Budapest) in the CEE. Prague, Warsaw and Budapest were major centres in at least one category of high-order services. According to Taylor who examined the global network connectivity of banking firms, Warsaw ranked the 9th place in Europe followed by Prague (17th) and Budapest (19th).[50]

Csomós compared these capital cities on the basis of their economic strength measured by GDP (PPS). In 2008 Warsaw with 68 Bn USD ranked 85th (followed by Hamburg), Budapest with 53 Bn USD was 100th and Prague was the 106th. Functions of coordination and control can be measured by the number of corporate headquarters

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49 Z. Gál, "The Development and the Polarised Spatian Structure of the Hungarian Banking System in a Transforming Economy", in G. Barta et al. (eds.), *Hungarian Spaces and Places: Patterns of Transition*, Pécs 2005, pp. 197-219.

50 Warsaw was the 25th most connetcted IFC worldwide according to the banking network connectivity in 2003. See P. Taylor, *World City Network. A Global Urban Analysis*, London–New York 2004.

of domestic companies located in these capitals.[51] Multinational companies and banks prefer to hierarchically control local subsidiaries from the headquarters of their parent banks located in the centres outside CEE region. From the emerging international financial centre (IFC) functions point of view headquarters of locally based multinational companies matters more as they concentrate their own control functions in a Central and Eastern European IFCs.[52]

The spatial concentration of foreign banks is an important indicator of global integration of the financial center of the region. However, the clear indicator of a thriving international financial center is the increasing presence of private investment banks. Despite the relatively low level of overall presence at that time Warsaw proved to be the most attractive location where seven investment banks had their representation, while only four such offices were opened in Budapest. A relatively large and crisis-resilient Polish economy attracted more investment banks than all their counterparts put together. In 2011 Goldman Sachs opened its Warsaw investment banking office, considering Warsaw as an important financial hub with huge development potential for the whole region

Hungary lost its attractiveness even before the financial crisis. In terms of the stock of FDI in the sector, Poland stood out in 2007 with more than 20 billion Euros foreign investment demonstrating the bigger potential to attract new strategic investments in the Polish financial sector. Changes in FDI flows during the crisis period were substantial. While there was a smaller fall of FDI in the Czech Republic and a larger one in Poland in 2009, FDI stock in financial services was mainly characterised by growth, while in Hungary this indicator slightly decreased in that period of the crisis.

Studies focused on global cities draw attention to the fact that the dominant feature of these leading cities is the considerable concentration off financial capital not only in banking but also in stock markets. Data on total market capitalisation and the number of companies listed of stock exchanges, therefore, serves as an ideal index for measuring financial centre development. It has to be noted that stock exchanges in the CEE countries has taken a fairly short period of time to reach their recent potential.

There are no large companies in the region with longer stock market experience and none of the institutional investors has long history of presence in the region. All CEE stock exchanges were launched as late as in the early 1990s, after the change of the

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51 According to the Forbes Global 2000 database in 2010 the world's 135th largest HQ city in CEE is Budapest with 26 Bn USD aggregate turnover of the companies located there. Budapest is followed by Warsaw only ranked 227th and Prague with 238th place (with 11 and 10 Bn USD turnover respectively). It has to be noted, that while both Hungary and Czech Republic are represented by single capital cities with a very high geographical concentration of HQ function, Poland is represented by three additional cities (Płock, Gdańsk and Lublin). G. Csomós, "A közép-európai régió nagyvárosainak gazdaságirányító szerepe", *Tér és Társadalom*, vol. 25, no. 3 (2011), pp. 129-140.

52 Budapest is a peculiar IFC in this sense as it is the only centre which developed its own control functions due to the fact that the only Eastern European regionally based multinational bank (outside Russia and to some extent Slovenia), the OTP Bank has its headquarters in Budapest. Z. Gál, G. Lux, *ET2050. Territorial Scenarios and Visions for Europe. Project 2013/1/19. Rinal Report, 30/06/2014*, vol. 8: *Territorial Scenarios and Visions for Central and Eastern Europe*, Luxembourg 2014, p. 22.

political and economic regime. Budapest Stock Exchange was founded in 1990. As the fast economic uplift in the countries of the Visegrad Group was substantially driven by FDI, the contribution of domestic companies to the GDP of the national economy remained rather small. Since primarily domestic companies are listed at the regional stock exchanges it is not surprising that the value for domestic market capitalization is low.[53] The market capitalization of the new EU Member States accounted for only 2% of market capitalization of the EU in 2004. The aggregated size of the Warsaw (WSE) and Prague (PSE) and the Budapest Stock Exchange (BSE) was equal to only 13% of capitalization of the Deutsche Börse at a time. Due to the relatively strong banking sector and the non-organic development of capital markets in the region, firms were allowed to seek affordable bank loans rather than to endeavour attracting investments through less mature stock exchanges. I addition, the propensity of the households to raise funds in the capital market is still low.

Table 1. Key indicators for the stock exchanges of Central and Eastern Europe in 1999-2013

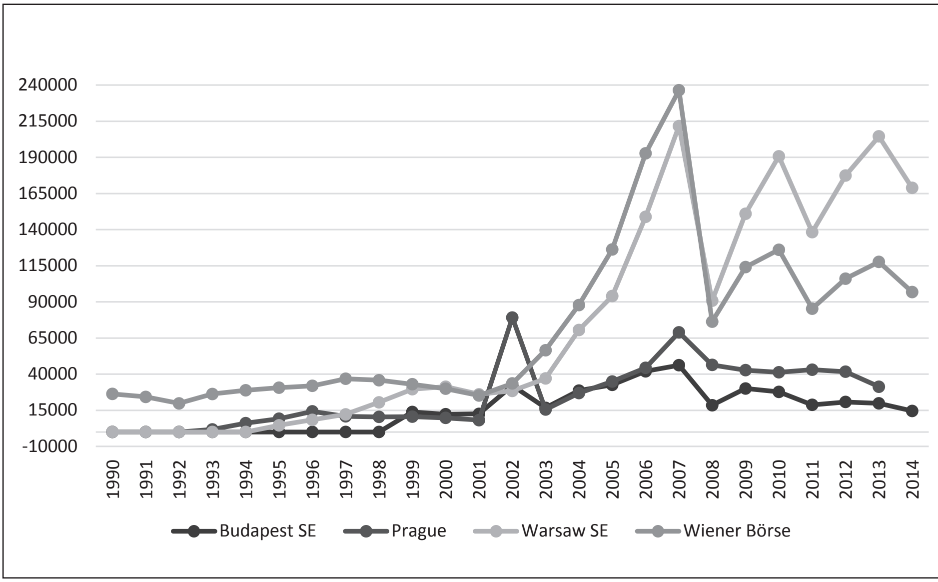
	Market capitalization				Number of listed companies							
	1999	2005	2009	2013	1999		2005		2009		2013	
		Million USD			Domestic	Foreign	Domestic	Foreign	Domestic	Foreign	Domestic	Foreign
Budapest SE	13 811	32 575	30 037	19 797	64	2	44	0	42	4	50	0
Prague SE	10 582	34 886	75 022	31 260	74	0	23	4	18	8	13*	10*
Warsaw SE	29 577	94 028	150 962	117 541	221	0	234	7	470	16	869	26
Wiener Börze	33 023	126 251	114 076	204 677	97	14	92	19	97	18	82	20

Source: World Federation of Exchanges, Annual reports and statistics.

* 2014

[53] G. Csomos, "A közép-európai régió…".

Figure 2. Total market capitalisation in Million USD



Source: edited by the authors, World Federation of Exchanges, Annual reports and statistics.

Despite its slow start, the Warsaw stock exchange rapidly increased its capitalization from early 2000s and attracted more companies for listing than the neighbouring stock exchanges (Budapest, Prague, Vienna). The effect of financial crisis was visible in both 2008 and 2011, although Warsaw seemed to recover faster than the other financial centres. The development of stock market in Budapest, being once a forerunner in the region, has been rather weak, with the current level of market capitalisation being comparable to the pre-EU accession period level, despite steady increase of GDP. The number of companies listed in Warsaw in 2013 doubled since 2009 and reached 895, out of which 26 are foreign. This level is significantly higher than that of Vienna – 102 companies with 20 foreign; Prague (23 with 10 foreign) in Prague, and Budapest (50, none foreign).[54]

By the mid-2000s the Warsaw Stock Exchange, due to its larger capitalisation, poses serious competition to the Budapest Stock Exchange. Warsaw Stock Exchange became the leading stock exchange of the region and that is why the Wiener Börse intends to compete with it by acquiring control over the smaller stock exchanges in CEE region. The rearrangement of the ownership structure of these stock exchanges suggests that Vienna and Warsaw are strengthening their leadership roles in CEE region, while the roles of Budapest and Prague are diminishing. As far as foreign listing is concerned Budapest does no longer seem to be strong international capital market centre.[55]

[54] Federation of European Securities Exchanges, 2015.

[55] In 2011, Poland's stock market ranked fourth in the amount of capital raised. At the WSE, 38 new companies were listed in 2011 and 25 of these were foreign ones.

The stake of the ongoing race among metropolises in Eastern and Central Europe at the beginning of 2000s partially was whether Budapest, with the relatively most developed financial markets at that time, can become a regional business and financial centre of Central and Eastern Europe. Nevertheless, contradicting former optimistic expectations, Budapest has not yet become such a regional financial and business (gateway) centre, the envisaged 'Singapore of Central Europe',[56] rather as a result of the crisis and the recently committed unorthodox economic policy, Budapest seems to have exited from the regional competition of international financial centres located in the region.[57]

Budapest's previous competitive advantage in the financial sector and capital-attracting potential has gradually decreased due to the deteriorating macro-economic position of the country prior to the crisis. The competitive advantage of Budapest was also weakened by organizational transformations of the BSE in 2004. This allowed the Wiener Börse following a policy of expansion in the framework of takeovers to acquire majority shares in the Hungarian and Czech stock exchanges. Budapest's position, concerning its independent decision making functions was adversely affected by the acquisition of the Vienna Stock Exchange.[58]

A plan to compete against Warsaw and Prague as the regional business centre was introduced in 2001. This plan seemed to have correctly identified Budapest's comparative advantages vis-à-vis 'western' cities (e.g. Munich, Vienna), but it was short in explaining the vision for the identity of Budapest vis-à-vis Prague and Warsaw as financial centres. Nevertheless, it should be noted that rise and fall of Budapest as a prominent regional financial centre could belargely explained by the actions and the successes achieved by other financial centres.

The crisis has also altered the future growth prospects of these CEE countries, while monetary and fiscal policies are on a tightening course for several years and there is little room for powerful countercyclical policy responses. External capital inflows suddenly and significantly stopped despite the relatively fast recovery in the region. After the ambitious start of Budapest thanks to the seemingly successful gradual transition model now it is losing competition to other CEE capitals in the race for become the international financial centre in CEE region.

Rapid decline of Prague as a financial centre in the late 1990s and Budapest in the second half of 2000s was accompanied by not only a less spectacular recovery, but also the rise of Warsaw, especially after 2008 financial crisis. Despite the fact that recent financial crisis had visible effect on Warsaw in 2008 and 2011, it recovered faster than

56 In the period of dynamic growth in Hungary the first Orban government had made attempts in 2000 to develop Budapest as CEE regional business and financial centre.

57 Z. Gal, "Development of International Financial Centres in Central and Eastern Europe during Transition Period and Crisis: The Case of Budapest", *Studia Regionalne i Lokalne*, no. 2 (2015), pp. 53-80, at <http://dx.doi.org/10.7366/1509499526003>.

58 Since the Wiener Börse has acquired control over the Budapest stock exchange, series of debates generated between the Austrian management and the handful dometstic blue chip companies (OTP, MOL, Richter) in strategically issues, which hinders the development of a long-term strategic vision for the BSE.

other financial centres in the region. In this regard there are two effects in play – the country' effect and the financial centre effect. Poland not only was able to avoid the recession but well-timed regulations managed to prevent the burst of housing bubble. Foreign capital inflow was not significantly affected. Warsaw experienced tremendous scale of public and private investments and the large domestic market generated huge demand. Poland does not rely heavily on export (it accounted for only 40% of GDP, half of the percentage of Czech Republic and Slovakia). The EU funds also contributed to the mitigation of the crisis effects.

Besides its crisis resilience there are important factors which make *Warsaw* suitable for the functions of IFC with strong regional focus, i.e. the high-standard of financial regulations in the Polish financial market in general, and the wise and active strategy which made the Warsaw Stock Exchange the largest player in the CEE region. This strategy is accompanied by the active marketing, and by an active engagement in multilateral trading platform, which helped linking the WSE with London.[59] Warsaw was the only city out of the tree, which managed to attract many foreign investors and influential market players even during crisis time. With its global presence, WSE successfully maintained its independence from Vienna unlike its larger regional counterparts (Budapest, Prague).

Contrary to Warsaw the development of financial markets in *Budapest* has been rather weak, reflecting to the deteriorating macroeconomic situation, characterised by with the lack of strategic-minded long-term economic policies in Hungary started much before the crisis. Paradoxically, its financial integration once being the engine of transformation and growth, became the source of relatively large accumulated private and public debt, and contributed to the crisis. Hungary's public debt, although it is below the EU average, had increased rapidly from 54% in 2000 to 80% in 2010. Foreign currency indebtedness of the private sector resulted in he largest risk for macroeconomic imbalances. The capital inflows to the financial sector recovered somewhat since the outbreak of the crisis in 2008 and the stock has increased substantially in the Czech Republic and Poland, while decreased in Hungary. The seemingly successful stabilization programme in Hungary could not take the advantage of counter-cyclical measures until recently due to the huge burden of public and private indebtedness. (Transfer of foreign currency debt to local currency decided in late 2014 could cost 8% of GDP). The right-wing government launched a major re-nationalization program after 2010, primarily in the energy and banking sectors. It aims to increase of the domestic/state share of banking sector, which reached more than 50% by 2015 at the expense of purchased foreign owned subsidiaries. Hungarian government 'levied' foreign-owned banks in the past years and therefore the Hungarian financial market is considered lacking 'shareholder value' for foreign financial players. Nationalist approach strongly discourages the internationalisation of Budapest as a financial centre and as it looks now it left the competition for becoming international financial centre of CEE region.

59 D. Wójcik, "Geography and Future of Stock Exchanges: Between Real and Virtual Space", *Growth and Change*, vol. 38, no. 2 (2007), pp. 200-223, at <http://dx.doi.org/10.1111/j.1468-2257.2007.000364.x>.

The rise of Orbán's government and his campaign against foreign-owned banks in Budapest characterize the challenges Budapest's international position faces today. On one hand, the foreign capital inflow has stabilised the Hungarian economy and even developed it to the highest level in the region by 2004. On the other hand, the recent financial crisis has shown the possibility of reverse capital flow as capital inflows suddenly stopped in 2009 and was accompanied by outflows. In other words, the high volatility of capital flow in Budapest signals a certain degree of financial exploitation by other financial centres in the region, namely Vienna, Munich and Frankfurt. Although the Hungarian 'gradual' transition model is characterized by some degree of stability, at the same time, foreign investment and takeovers seemed to have strengthened the fundamentals in Budapest, the lack of consistent and long-term economic policies and weaknesses of regulations made the Hungarian financial markets unstable during the crisis and further weakened Budapest's international positions.

Renationalization policy of banking sector characterising both Hungary and Poland after the crisis may help to find a more optimal balance between the predominant position of foreign ownership in banking and the local economic needs of the countries. However, the maneauvering pace and benefits of these policies are much more limited in Hungary due to the much higher dependence and exposure of the country to foreign capital.

With its increasing global presence, Warsaw Stock Exchange seems to continuously maintain its independence from Vienna unlike its regional counterparts (Budapest, Prague), which lost their control over their stock exchanges. Budapest Stock Exchange was recently purchased by the Hungarian Central Bank.

CONCLUSION

Both financial and economic crisis demonstrated the vulnerability of the CEE region and their controversial position within the European Union. Apart from this question further dilemmas lie in the institutional systems of Central European states and the problem of the role of the state, the debate among the followers of centralisation versus decentralisation in planning and decision-making. The region has long traditions of centralisation and top-down bureaucratic control, with weak bottom-up organisation and development cooperation – although Poland has developed a relatively competent planning system on the regional level.[60] With weak local governance, there is instead a 'planning vacuum' which is filled by actors from central governments or the European Union, who in turn develop plans according to their own ideas and interests. There are new challenges in front of the CEE region.

Consequently, endogenous development is a strategy to achieve a reintegrated space economy: the building of strong local networks (mostly clusters, industrial districts and

60 C. Mezei, A. Schmidt, "A lengyel regionális politika és intézményei", *Tér és Társadalom*, vol. 27, no. 3 (2013), pp. 109-126.

innovation systems), which can provide sufficient added value for both TNCs and domestic enterprises. The key of these networks is the density and diverse directions of their connections, which can break one-sided dependent relationships, and help to establish these regions as competitive players in the European and global context.

Altogether, endogenous development and the reintegration of space achieve three different, but closely connected goals:

– It encourages re-specialisation in industrial regions which have lost their previous focus;
– It makes it possible to transcend the limitations of FDI-based competitiveness and the DME development model;
– There is no guarantee that endogenous development can prevent the emergence of 'the disappearing middle' problem, or offer full protection from global competitive pressures: but, hopefully, it can help us learn to adapt – that is, to learn better learning.[61]

Central and Eastern European countries had to face various challenges at economic and political transformation. As a consequence of their economic condition and the lack of internal capital for destructuralisation they definitely needed the presence of foreign assistance. As it can be proven by statistical data this support had sometimes ambiguous consequences as the aims of foreign investors were also various. The financial and economic crisis in 2008 showed the vulnerability of the transforming economies of the Central and Eastern European states and the reaction to these challenges demonstrated the importance of a relatively more developed national capital in these countries. As at the beginning of the 1990s Prague, Budapest and Warsaw had similar opportunities and by the early 2000s Warsaw and Poland could develop as a regional leader in the CEE region. The aim of this paper was to demonstrate the challenges and the process through which Warsaw strengthened its position as a regional leader. However, keeping its status is strongly determined by internal policy and external international factors.

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[61] G. Lux, "The Institutional Conditions of Reindustrialisation in Post-crisis Central Europe", *Journal of Economics and Management*, vol. 19 (2015), pp. 16-33.

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