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Politics and Governance
2024 • Volume 12 • Article 7449
https://doi.org/10.17645/pag.7449

ARTICLE

Open Access Journal

The "EU-Leash": Growth Model Resilience and Change in the EU's Eastern Periphery

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Submitted: 28 July 2023 **Accepted:** 24 November 2023 **Published:** 12 February 2024

Issue: This article is part of the issue "From New to Indispensable? How Has the 2004 'Big Bang' Enlargement Reshaped EU's Power Balance" edited by Matej Navrátil (Comenius University) and Marko Lovec (University of Ljubljana), fully open access at https://doi.org/10.17645/pag.i376

Abstract

Although the EU's Eastern periphery has been afflicted by a series of crises over the past two decades, the region's dependent market economies have shown puzzling resilience. Since the global financial crisis, the FDI-led, export-oriented growth models of the Visegrád countries have been reinforced. Meanwhile, the debt-based, consumption-oriented capitalism of the Baltic states has not experienced dramatic shifts either, despite a strengthening of its export component. Scholarly accounts from a comparative political economy perspective explain this resilience as the product of country-specific factors and tend to downplay the role of external influence. Instead, we aim to bridge these approaches with international political economy scholarship by arguing that European integration, in general, and the EU's transnational regulatory influence, in particular, serves as an external anchoring mechanism for both semi-peripheral growth models. In addition to the region's structural characteristics, such as deep embeddedness in global value chains, high exposure to trade with the EU, and dependence on external sources of finance, which already limit domestic agency in changing national growth models, we argue that European transnational regulatory integration involves an "EU-leash" that sets the boundaries for domestic economic policies, thereby influencing growth model trajectories. This ensures institutional continuity and prevents sudden and radical changes in semi-peripheral growth models. We demonstrate these mechanisms through two country studies (Estonia and Hungary).

Keywords

Baltic states; dependent market economies; Eastern periphery; economic governance; EU; growth models; Visegrád countries

1. Introduction

In an informal, non-public, meeting with foreign journalists in December 2022, Hungarian Prime Minister Viktor Orbán is said to have replied with a definitive "no" to a question about Hungary's future EU membership. However, he immediately added that his hands were tied because 85% of the country's exports go to the EU (Csonka, 2023). With this remark, Orbán—inadvertently—addressed one of the most pressing questions in contemporary political economy, namely how the interaction of external constraints and domestic agency contributes to the resilience or change of political-economic systems. In the context of the dependent market economies (DMEs) across Central and Eastern Europe (CEE), this topic is even more salient. Since the Visegrád countries (Czechia, Hungary, Poland, and Slovakia; referred to as the V4) and the Baltic states (Estonia, Latvia, and Lithuania) joined the EU in 2004, there have been no substantial changes to their growth models (GMs) even though they have been hit by a series of political and economic crises (cf. Ban & Adăscăliței, 2022).

This article aims to contribute to the scholarly debate on the resilience and change of these semi-peripheral GMs by addressing the following puzzle: Even though multiple crises and the rise of right-wing populist leaders in CEE have challenged the region's political economies, the consumption-led GMs in the Baltics and the export-led GMs in the V4 have exhibited remarkable stability and only limited change. Complementing existing comparative political economy (CPE) and international political economy (IPE) accounts, we argue that the systemic stability of these GMs can be partly attributed to specific regulatory channels of European integration that constrain the economic policies of semi-peripheral member states and thereby affect the evolution of dependent GMs. We refer to these channels as the "EU-leash," which is tightest for consumption-led GMs in the European Monetary Union (EMU) and loosest for export-led GMs outside the eurozone. Our concept of the EU-leash differs from the widely used notion of policy transfer (Dolowitz & Marsh, 2000) because it does not involve any concrete regulatory imprints that the member states can adopt. For the same reason, our concept differs from the process of Europeanization (Schimmelfennig & Sedelmeier, 2005) because it involves neither coercive top-down transnational rule transfer nor voluntary "downloading" of EU regulations. The EU-leash indirectly influences economic policy choices in member states, and, overall, it pulls the GMs in a direction that contributes to their stability and minimal change. Our dependent variable is, therefore, the resilience and change of national GMs. We investigate how the EU can influence the trajectory of GMs, an approach that contrasts with IPE accounts that examine how the heterogeneity of GMs across member states affects European integration (Höpner & Schäfer, 2014).

In exploring GM resilience and change in CEE, CPE scholars generally emphasize domestic factors as explanatory variables. For instance, Bohle and Greskovits (2012) argue that political commitments to preserving industrial legacies have been a key driver of the export-led GMs in the V4, while decisions to pursue a comprehensive break from Russian economic influence have ostensibly contributed to the consumption-oriented GMs in the Baltics. Similarly, recent attempts to move away from the dependent GM have been explained by domestic political and ideational factors in the case of Poland (Naczyk, 2022) and Hungary (Scheiring, 2020; Sebők & Simons, 2022). Existing CPE scholarship thus either neglects the role of EU integration as an explanatory variable (e.g., Ban & Adăscăliței, 2022) or does not consider its influence as a systemic feature in CEE (e.g., Bohle, 2018; Toplíšek, 2020). In contrast, IPE scholars identify several transnational factors that may have contributed to the evolution of CEE GMs. First, through regulatory and normative influence, the EU promoted the birth of DMEs (Bandelj, 2010; Jacoby, 2010). However, in the post-accession context, this line of scholarship only establishes that the EU's economic impact on CEE has been greater than its political influence, without assessing the subsequent EU impact on these GMs (Epstein & Jacoby, 2014). Although some scholars show how the EU has extended post-accession development resources for upgrading CEE economies (Bruszt & Vukov, 2017), they do not discuss the implications on GMs. IPE scholars only recently began to link GMs with the EU's regulatory influence. Johnston and Matthijs (2022) argue that the EU's post-2008 institutional architecture and macroeconomic governance have penalized domestic consumption-led growth strategies and promoted export-led growth. However, the consequences of this external pressure on consumption-driven GMs have so far only been studied in the case of Southern Europe (Johnston & Regan, 2016) and not in the Baltics. Conversely, the domestic drive in Hungary and Poland to move away from the dependent model has not been addressed by IPE scholarship that examines the EU pressures and constraints that may limit the scope of domestic agency in transforming their GMs (see Vukov, 2023, for a notable exception). Consequently, there is a need to bridge CPE and IPE approaches in explaining the evolution of CEE growth regimes.

The contribution of this article is threefold. First, we aim to combine the CPE and IPE approaches to stress the importance of EU regulatory channels for resilience and change in CEE capitalism. Second, we identify several mechanisms through which the EU disciplines domestic policy that seeks alternative trajectories for dependent GMs. This EU-leash defines the limits within which national GMs can be compatible with the institutional architecture of the EU. The strength of the leash (or its tightness) depends on the respective country's specific GM and its membership in the EMU. The EU-leash for EMU member states, such as the Baltics and Slovakia, is thus tighter than in non-EMU members. Furthermore, it is looser for export-led than consumption-led GMs. Third, we demonstrate how the EU-leash interacts with domestic politics through two country cases: Estonia, a least likely case to shift its consumption-led GM, and Hungary, a most likely case to move away from its FDI-dependent export-led GM. We show that in Estonia, the EU-leash contributed to a slight shift in its consumption-led model despite a firm domestic political commitment to the status quo, whereas in Hungary the fundamental features of the export-led GM have not changed despite the government's ambitions. We, therefore, argue that there is a need to account for the EU's transnational regulatory influence to explain the failure of the politicization of economic dependence in some CEE countries (cf. Baccaro & Pontusson, 2022).

This article is structured as follows: The next section provides an overview of the evolution of the Baltic and V4 GMs since EU accession. This is followed by an identification of the mechanisms through which the EU-leash limits deviation from the dependent GM trajectory in the CEE region. Subsequently, we demonstrate the politics of the EU-leash on two country cases. The final section presents key conclusions.

2. Evolution of the Dependent GMs in CEE

Following the fall of the "shortage economy" in the late 1980s, financial deregulation and liberalization of capital flows met EU conditionality and generated massive FDI inflows into CEE, mainly from Western Europe (Holzner, 2017). Foreign capital was mostly attracted by the combination of low labor costs, skilled labor, and pro-FDI policies, as well as the prospective integration of the countries into the EU single market, resulting in sui generis FDI-dependent capitalist diversity (Myant & Drahokoupil, 2011; Nölke & Vliegenthart, 2009). While the V4 mostly attracted export-oriented manufacturing investors linked to the German complex industries, FDI into the Baltic states predominantly came from Scandinavia and was service-oriented (mainly in finance, insurance, and real estate), thereby stimulating domestic consumption (Bohle & Greskovits, 2012; see Figure

A1 in the Supplementary File). This resulted in significantly higher manufacturing value added in the V4 than in the Baltic states (see Table A1 in the Supplementary File) and led to the rise of an export-led GM in the V4 and a consumption-led GM in the Baltics (Kohler & Stockhammer, 2022).

Figure 1 shows the import-adjusted growth contributions of the main GDP components in the V4 and the Baltics between 1995 and 2018. The figure reveals that, apart from Poland, the V4 economies were

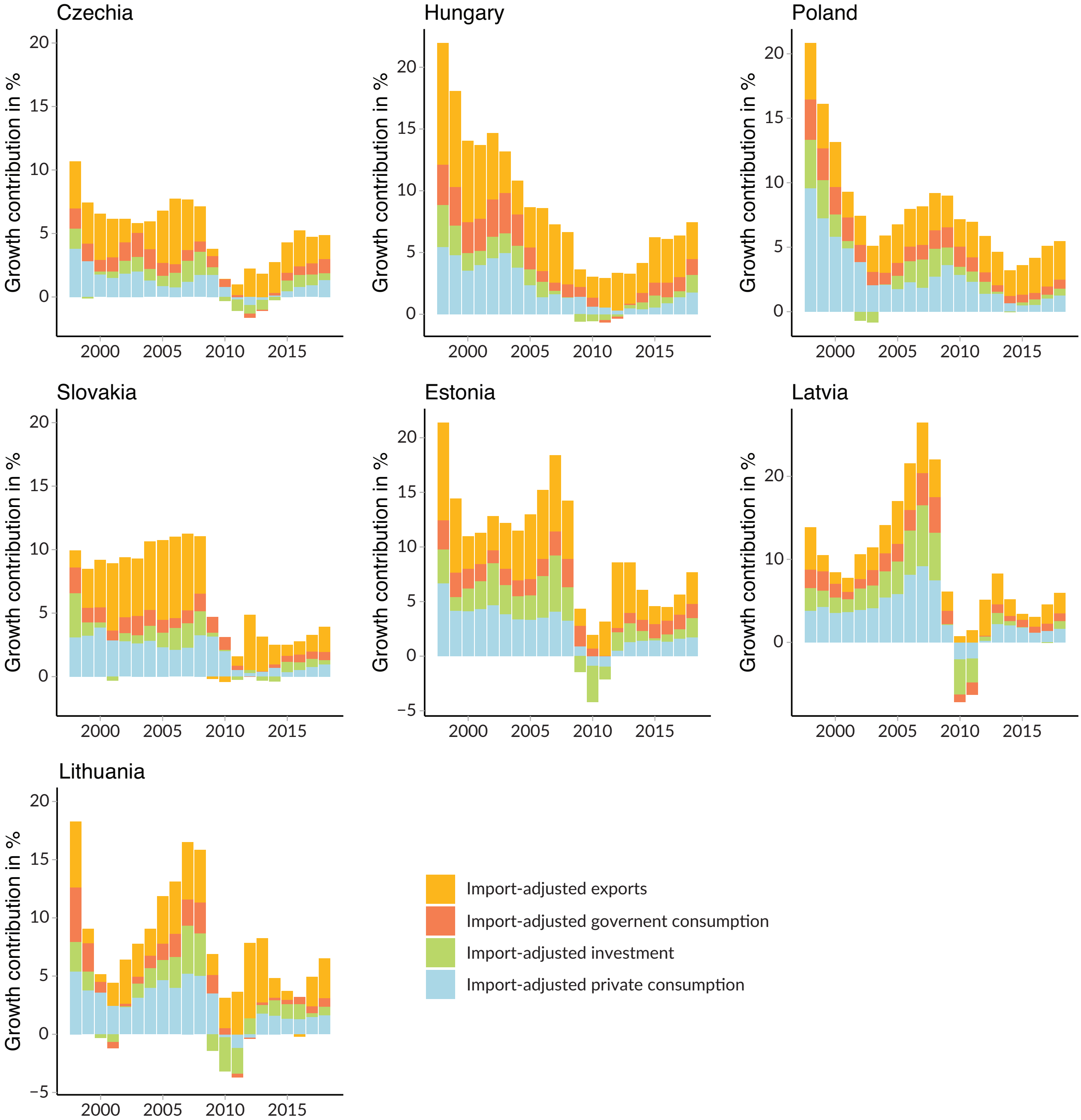

Figure 1. Import-adjusted growth contributions in the V4 and the Baltic states in 1995–2018 (3-year moving averages). Note: Values at basic prices. Sources: Authors' elaboration based on OECD Input-Output Tables 2021 (OECD, 2021); data, methodology, and R code are available at the GitHub repository (https://github.com/Jszabo16/IMadj_growth).

primarily export-led throughout the entire period. Poland exhibited a more balanced GM, though the relative contribution of private consumption to Polish GDP halved following EU accession. Especially after the global financial crisis (GFC), all V4 GMs can be characterized as "strongly export-led," with the relative contribution of their import-adjusted exports to economic growth exceeding 50% (cf. Baccaro & Hadziabdic, 2023, p. 11). The Baltic states followed a slightly different trajectory, with their import-adjusted growth contributions tilting towards consumption-led (and credit-based) GMs before the GFC. After the GFC, the Baltic GMs appear to have rebalanced, with exports taking on a more prominent role. The Baltic trajectory is in line with broader trends apparent across major European economies (see Table A2 in the Supplementary File) and confirms that there has been a recent push towards an export-led GM in the EU. While the export-led model was strengthened in the V4 after the GFC, the Baltic states have slightly retreated from their consumption-oriented GM and shifted to a more balanced path (cf. Baccaro & Hadziabdic, 2023, pp. 20–23).

However, it would be misleading to argue that the rise in the contribution of (import-adjusted) exports to aggregate demand alone provides solid empirical evidence of changing GMs in the Baltics. To understand the nuances of CEE capitalism, it is necessary to take into account the countries' positions in global value chains, their trade relations, and the structure of the balance of payments. Accordingly, Figure 2 reveals important structural differences in trade across the two regions. While 80% to 90% of the V4's exports are still based on manufactured goods, in the Baltics the same figure has consistently been 20% to 30% lower, even after

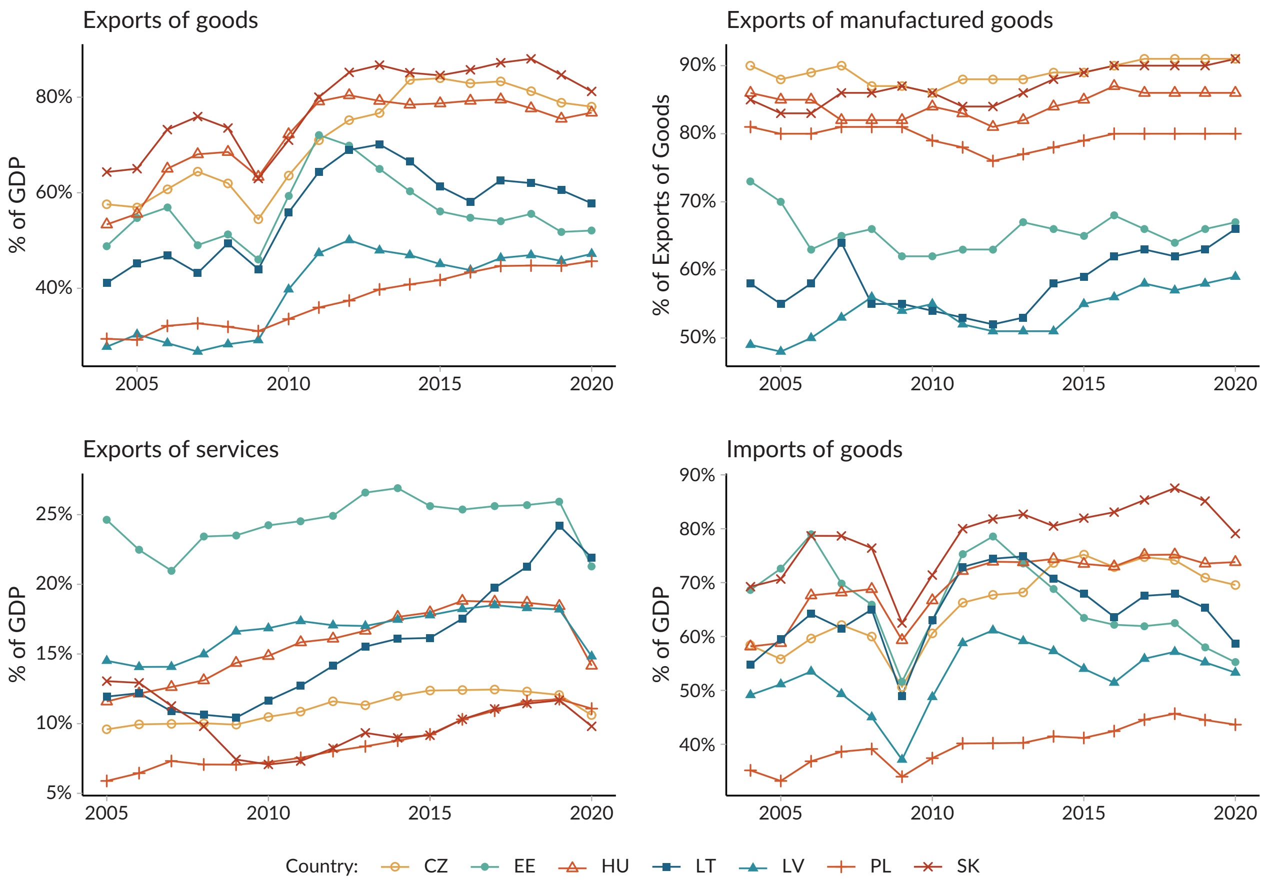

Figure 2. Trade in the V4 and the Baltic states in 2004–2020. Source: Authors' calculations based on UNCTAD international merchandise trade (United Nations Conference on Trade and Development, 2023a) and international trade in services data (United Nations Conference on Trade and Development, 2023b).

the GFC. This suggests that the post-GFC export drivers in the Baltics are non-manufactured goods, such as agricultural and forestry products, but most importantly service exports (cf. Bohle & Regan, 2022). The relative decline of imports as a share of GDP in the Baltic states also confirms the slight shift from a consumption-based model to a more balanced arrangement where exports are becoming more important drivers of growth.

The dynamics of the financial balances of the main macroeconomic sectors before and after the GFC provide additional support for the above observations (see Table 1). Financial balances reveal that none of the CEE countries followed a purely export-led trajectory before the GFC as they experienced a "foreign-financed boom" (Holzner, 2017, p. 60), with domestic sectors becoming net borrowers. This is a consequence of the combination of decades of suppressed demand prior to 1990 and the availability of cheap credit in the early 2000s. At the same time, the private sector in the V4 and the Baltic states failed to generate surpluses in the 2000s (see Figure A2 in the Supplementary File), which can be attributed to the massive inflow of FDI (Kattel, 2010). While the consumption boom in the Baltics was associated with growing household indebtedness, household sectors in the V4 enjoyed a surplus, for the most part, before the GFC. However, these surpluses were later consumed by the corporate sector and the governments seeking to increase productive capacity, which also explains the lower level of external debt compared to the Baltic states (Holzner, 2017). Nevertheless, all these countries suffered from recurrent current account deficits that reached unsustainable levels prior to the 2008 crisis (Figure A3 in the Supplementary File), making CEE countries vulnerable to capital outflows.

The GFC was, therefore, a defining moment for CEE and the Baltics in particular. As a large part of their pre-GFC FDI went to their banking sectors leading to an excessive level of foreign-owned banking assets in

Table 1. Financial balance by sector in % GDP in 1995–2018.

		Private sector	Public sector	Household sector	External sector
CZ	pre-GFC	−1.92%	−4.18%	2.24%	3.86%
	post-GFC	−0.90%	−1.71%	2.03%	0.57%
HU	pre-GFC	−3.16%	−6.20%	2.38%	6.98%
	post-GFC	2.09%	−3.04%	4.33%	−3.39%
PL	pre-GFC	−2.27%	−4.10%	2.90%	3.47%
	post-GFC	4.03%	−3.82%	−1.52%	1.31%
SK	pre-GFC	−2.62%	−5.47%	1.99%	6.10%
	post-GFC	3.24%	−3.75%	0.98%	−0.47%
EE	pre-GFC	−7.70%	0.53%	−1.01%	8.83%
	post-GFC	2.19%	−0.16%	1.43%	−3.45%
LV	pre-GFC	−3.13%	−1.41%	−5.01%	9.55%
	post-GFC	5.50%	−2.97%	−0.29%	−2.24%
LT	pre-GFC	−5.91%	−2.73%	0.10%	8.54%
	post-GFC	7.08%	−3.05%	−1.38%	−2.65%
DE	pre-GFC	0.02%	−2.90%	4.52%	−1.66%
	post-GFC	1.06%	−0.24%	5.27%	−7.15%

Notes: Share of net lending/net borrowing (B9) as % of GDP at current prices in million units of national currency; the private sector includes both non-financial corporations (S11) as well as financial corporations (S12); and pre-GFC period average values for years 1995–2008 and post-GFC period for years 2009–2018. Source: Authors' calculation based on Eurostat (2023) data.

the region, it is not surprising that the Baltics were hit hard by the drying up of foreign capital inflows and witnessed their economies go into free fall. The abrupt freezing of credit markets also triggered asset price volatility in the housing sector and contributed to the accumulation of non-performing loans often denominated in foreign currencies, bursting the housing bubble and prompting a subsequent banking crisis (Bohle, 2014). Aiming to complete the adoption of the euro, the Baltic countries opted for painful internal adjustments rather than currency devaluations to regain competitiveness (Kattel & Raudla, 2013). The V4, for their part, experienced a non-uniform recovery from the GFC. For example, Poland, boasting a relatively large, industrialized, and diversified economy, managed to avoid recession owing to the very low exposure of its financial sector to subprime-related assets and stable export performance stemming from the sharp depreciation of the real exchange rate (Matysek-Jędrych et al., 2021). Although the export-led GM contributed to Poland's resilience during the GFC, domestic managerial discontent with its heavy dependence on FDI led to a subsequent political backlash against this model (Naczyk, 2022). Falling external demand in export markets was responsible for the economic slowdown in Czechia and Slovakia, but as global trade rebounded, these economies also recovered. In Hungary, however, the presence of foreign-owned banks, combined with a boom in foreign currency loans, exposed the entire financial sector to capital fluctuations and exchange rate risk. The devaluation of the Hungarian currency placed a heavy burden on mortgage holders while growing public debt, associated with an unsustainable welfare state, led to Hungary's dubious distinction as the only V4 country to turn to the IMF and the EU for financial support (Ban & Bohle, 2021).

3. Features of the EU-leash: EU Influence Over CEE GMs

The evidence from the previous section suggests that while export-led GMs in the V4 remained stable even after the GFC, the consumption-led regimes in the Baltics weakened (Dünhaupt & Hein, 2019) and have shifted to a more balanced model, where exports constitute a larger relative contribution to economic growth. Yet, one should be careful about inferring the convergence of these two growth regimes (cf. Pataccini et al., 2019). While the V4 still relies on manufacturing, the shift of the Baltics to export-led growth has "occurred by default rather than design" (Bohle & Regan, 2022, p. 344) and represents the result of weaker import demand in the context of stagnant growth (Kohler & Stockhammer, 2022) as well as repressive fiscal adjustments. This implies that it was not deliberate domestic action alone shaping changes in the Baltic GMs. Similarly, the strengthening of the V4 model seems to have had an external stimulus. We claim both changes were significantly influenced by the EU-leash, which in itself varies by member state and is also subject to repositioning depending on the regulatory developments at the EU level following a crisis. The "leash" is, therefore, dynamic and context-specific. However, it is possible to identify some key transnational regulatory channels through which it has indirectly influenced member state GMs, particularly in CEE.

Although far from an exhaustive account, we highlight three types of mechanisms through which European integration has promoted dependent growth in CEE and, more recently, favored export-led growth at the expense of consumption-driven strategies, thereby limiting the discretion of domestic policy-makers in shaping the trajectories of semi-peripheral GMs: soft conditionality linked to macroeconomic governance rules, state aid regulations, and the EU's Structural and Cohesion Funds.

In the pre-accession period, the EU exerted immense influence over the economic trajectories of CEE countries through the promotion of structural reforms. Apart from the mandatory adoption of the *acquis* *communautaire* and its strict conditionality as the backbone of Europeanization, the EU applied quasi-legal practices to accelerate FDI inflows into the region (Medve-Bálint, 2014), which contributed to the emergence of DMEs. After enlargement, conditionality weakened in most fields (Epstein & Sedelmeier, 2008) but it returned at least in a soft form against the backdrop of the euro crisis (Jacoby & Hopkin, 2020). During the crisis, the EU emerged as a pro-austerity advocate (Lütz & Kranke, 2014), limiting fiscal policy space for governments in consumption-led economies, thereby indirectly pushing them towards export-led models. The implicit threat from the EU that the Baltic states might be excluded from joining the EMU reinforced fiscal discipline in these countries (Dandashly & Verdun, 2020), acting as an indirect nudge towards export-led growth.

The EU-leash appears most tangibly in the EU's macroeconomic governance rules that incorporate soft conditionality. Pushed through by Germany as a precondition for the creation of the EMU, the Stability and Growth Pact with its preventive and corrective arms (i.e., Excessive Deficit Procedure; EDP) and the post-crisis macroeconomic governance rules (for a detailed account, see Fabbrini, 2022) have created growing constraints on member states' fiscal policies, thereby indirectly narrowing GM diversity within the EU. The European Semester's Macroeconomic Imbalance Procedure (MIP), which aims to regulate external imbalances produced by the private sector, is an emblematic example of this (cf. Johnston & Matthijs, 2022; Johnston & Regan, 2018). Among other effects, the MIP's scorecard limits current account balances and the net international investment position of member states, but does not place a limit on the external assets that a country can acquire abroad (Johnston & Matthijs, 2022, p. 129). Therefore, it renders fiscal expansion and excessive foreign borrowing unviable while promoting surplus savings, which export-led GMs tend to produce. Moreover, the country reports prepared under the MIP tend to downplay sustainability concerns when a large share of external liabilities stem from FDI. The different MIP thresholds for the euro and non-euro member states also demonstrate that the EU-leash is much tighter for EMU members. However, even though the EU macroeconomic rules mostly apply to EMU member states (at least their corrective features), their influence is not confined exclusively to the EMU as the MIP scoreboard is used for country-specific recommendations and often generates peer pressure on all member states, especially those suffering from imbalances (Zeilinger, 2021).

The EU's state aid regulations constitute another element of the EU-leash, although less restrictive than the macroeconomic rules. In principle, the granting of state aid violates free market principles, but the EU Treaties allow for the provision of state aid under certain circumstances. In particular, Article 107(3) of the Treaty on the Functioning of the European Union stipulates that state aid may be compatible with the EU's internal market if it is granted in backward regions to promote investments and regional development. According to the European Commission's regularly revised regional aid guidelines, the more backward a region, the higher the regional aid intensity permitted. Consequently, governments in less economically developed member states, such as those in CEE, enjoy greater discretion over providing aid to investors. Although state aid rules curb the ability of governments to promote investment through aid, in the context of FDI-dependent economies, regional aid has become a tool for attracting FDI within the parameters set by EU rules, thus indirectly contributing to the persistence of FDI-dependent GMs.

The EU-leash also exerts both direct and indirect influence on the GMs in CEE through the allocation of EU funds. Although these funds come with strings attached, they increase the pool of fiscal resources available for member states. Since CEE countries are among the biggest beneficiaries, receiving EU funding of up to

4% of their GDP, this effect is far from negligible in their case. EU funding acts as partial compensation for tight fiscal control imposed by economic governance rules. Throughout their two decades of EU membership, the size of EU funds has become comparable to FDI inflows and remittances in the V4 and Baltic regions (see Figure B1 in the Supplementary File). More recently, however, EU funds, or rather the lack thereof, have had an indirect stimulatory effect on the export-led GM in some CEE countries. Due to their ongoing disputes with the EU over rule of law violations, the European Commission has suspended payments in the current programming period (2021–2027) to Hungary and Poland, compelling these two member states to seek out alternative sources of external finance, in particular, FDI (Szumski, 2023). These developments suggest that the suspension of EU funding in CEE countries running afoul of the rule of law has triggered more extensive efforts to attract foreign capital, thus indirectly reinforcing the export-led, FDI-based GMs.

4. Domestic Politics of Dependent GMs in CEE

In the previous section, we argued that the EU-leash structurally anchors CEE GMs. However, these transnational constraints leave some room for domestic agency, depending on the specific country context. To better explore these mechanisms, in this section, we focus on the politics of the EU-leash in two CEE countries, Estonia and Hungary. While Estonia is a consumption-led Baltic country that has been a member of the EMU since 2011, Hungary is an export-led V4 country that retains monetary sovereignty. Hungary's right-wing populist government, in power since 2010, has openly questioned the FDI-dependent GM, while the politicization of the consumption-led model has never gained political salience in Estonia. In this respect, Estonia is the least likely case to experience a shift away from its GM, while Hungary can be considered the most likely case to see its FDI-based, export-led model change. By examining these two country cases, we aim to explore how dependency can be politicized in CEE countries and what role the interaction between domestic politics and structural constraints imposed by the EU may play in this process.

4.1. Embracing Dependency in the Baltic Region: The Case of Estonia

Ever since restoring its independence in the early 1990s, the commitment to participate in European integration was a driving force behind Estonia's willingness to introduce neoliberal reforms that were necessary to qualify for EU accession. This unconditional commitment led to the mass privatization and liberalization of the financial sector, in turn contributing to the expansion of dependent financialization. By the early 2000s, 90% of all banking assets in Estonia belonged to four foreign-owned banking groups (Swedbank, SEB, Sampo, and Nordea), with Swedbank alone owning almost half the total assets in the sector (Directorate General for Economic and Financial Affairs, 2010).

With a negligible exchange rate risk due to the currency board, Swedish-owned banks began to provide cheap credit, mostly denominated in euros (Bohle, 2014). Although Estonia's credit-driven growth averaged 8% per year, it came at the cost of rampant inflation, a housing boom, and the accumulation of net foreign liabilities. After the foreign credit-driven bubble burst in 2008, Estonia suffered a severe double-digit GDP decline. However, in contrast to other CEE countries, the Estonian government committed itself to excessive austerity measures amounting to 9% of GDP, despite low pre-crisis debt (Raudla & Kattel, 2011) and losing its parliamentary majority in the process (Jõgiste et al., 2012). The main impetus for fiscal retrenchment was the prospect of EMU membership, long a primary goal of Estonian policymakers. Adopting the euro was seen as one more step deeper into Europe and "away from Russia" ("Baltic bet," 2010), and thus compliance with EU conditionality gained political priority. As the inflationary nature of Estonia's GM made it difficult to meet the inflation convergence criterion, the government hoped to capitalize on the EMU's deflationary pressures. To facilitate EMU entry, the government decided not to abandon the currency board and not to devaluate, which could have mitigated some of the social costs of the post-crisis adjustment (Dandashly & Verdun, 2020).

Despite the high social costs of its commitment to austerity, Estonia stands out for a lack of social discontent and politicization of economic dependency. Apart from limited protests, austerity measures were largely accepted, and the neoliberal governing parties were able to form a government even in the aftermath of the crisis. There are several domestic and external reasons for that. Most importantly, Estonia's political system is divided along ethnic cleavages where the main political conflict plays out between parties backed by ethnic Russians (around 30% of the population) and parties supported by ethnic Estonians. Citizenship restrictions have politically sterilized the Russian-speaking minority, effectively silencing an important potential source of opposition to austerity (Bohle & Greskovits, 2012), whereas all major Estonian parties essentially converged on socioeconomic issues (Rohrschneider & Whitefield, 2009). Furthermore, this ethnic cleavage has been intensified by moves of the dominant Reform Party in recent years, which has participated in most post-transition governments, securing neoliberal continuity. The party has interpreted national neoliberalism as intrinsic to every "Estonian-minded person" (Saarts & Saar, 2022, p. 14). In this environment, every collective action voicing socioeconomic dissatisfaction has often been framed as reminiscent of the Soviet past and thus politically unviable. Therefore, the Estonian population has generally opted for exit to the EU labor market instead (Sippola, 2014). The Estonian GM was only at risk of a challenge for a brief window after the eurosceptic, anti-migrant Conservative People's Party of Estonia entered a coalition government in 2015 (Raik & Rikmann, 2021). Even though the party attempted to politicize socioeconomic disparities stemming from the consumption-led GM, its impact remained relatively limited, and two years later the party returned to the opposition benches after the fall of the government.

Apart from domestic political factors, geopolitical considerations also play an important role in constraining the politicization of the Estonian GM, with the pair often reinforcing one another. Estonia is one of the most Europhile EU member states and is exemplary in transposing EU directives into national legislation (Gudžinskas & Bekišas, 2018). According to Estonian policy-makers, their attempts to defend the country's status as an EU stalwart has become excessive, with most of the country's state capacity going to implement EU law, leaving little room for autonomous policies (Raudla et al., 2019). Estonia obediently accepted the macroeconomic governance rules, often going beyond the required minimum regulatory standards, even though it placed an additional fiscal straitjacket on its inflationary GM (Raudla et al., 2018). In some cases, Estonia even backed Germany in supporting measures that would further limit the fiscal space of member states (see appendix in Wasserfallen et al., 2019). The unshakable support for the EU is linked to geopolitical constraints, namely the perceived threat posed by neighboring Russia, which has pulled Estonia closer to the EU.

The Estonian case findings point to the presence of a politically uncontested EU-leash, with a firm political commitment to consumption-led GM. Ironically, this has shifted the Estonian GM from its original consumption-led stature to a more balanced weakly export-led orientation (see Table A3 in the Supplementary File) because of the export-led bias built into the EU-leash. The country's austerity policy and strict adherence to the EU's economic governance rules entailed an internal devaluation, which increased cost competitiveness while reducing the role of private consumption in GDP growth. As a result of the above processes, exports increased, especially in knowledge-intensive services (Kalanta, 2023).

4.2. The EU-Leash Reinforcing an FDI-Led GM: The Case of Hungary

Since the late 1990s, Hungary's GM has been export-led, primarily based on the performance of foreign companies active in manufacturing. This model remained unchallenged by Hungarian governments until the populist right-wing Fidesz party and PM Viktor Orbán won a constitutional majority in the 2010 elections. Since then, the government's rhetoric has been characterized by an increasing anti-FDI stance and economic nationalism, manifested in concrete measures of renationalization, especially in the banking and finance sectors, which were dominated by foreign companies (Karas, 2022; Sebők & Simons, 2022). Moreover, foreign firms have been subjected to unfair treatment by the Orbán government, including special sectoral taxes (Sallai et al., 2023).

The literature suggests that the EU played an enabling role in the process of this unfolding economic nationalism, without much leverage over Hungary, as long as the Orbán government kept the budget deficit and public debt under control (until the coronavirus crisis; Johnson & Barnes, 2015). However, no deep, transformative changes in Hungary's GM have occurred: It remains an export-led, FDI-dependent economy (Ban & Adăscăliței, 2022), with renationalization and the expulsion of foreign companies confined to sectors that are structurally less relevant to the country's GM (Scheiring, 2020). Thus, despite the government's political commitment to changing the FDI-dependent, export-led trajectory, this has not materialized (cf. Bohle & Greskovits, 2019).

The literature explains this systemic continuity as the product of the country's deep embeddedness in global value chains, so the pursuit of anti-FDI policies could easily have backfired (Vukov, 2023). Others argue that the mutually beneficial relationship between transnational capital and the political elite may have cemented the country's GM (Bohle & Regan, 2021). Complementing these views, we argue that, contrary to the international enabler thesis, the EU has contained the economic nationalist agenda by indirectly pulling the Orbán government towards the preservation of the FDI-led GM. As we show in the paragraphs below, three mechanisms of the EU-leash have performed this role: the EDP, state aid rules, and, more recently, the suspension of EU funds to Hungary.

Immediately after joining the EU, Hungary was placed under the EDP because its budget deficit exceeded 3% of GDP and its debt-to-GDP ratio was well above the 60% reference value. Hungary's public finances have often been characterized by overspending (Benczes, 2014), with the EDP at times requiring the government to introduce corrective measures, limiting its fiscal maneuvering space. Facing fiscal distress during the GFC in 2008, the country was the first EU member to turn to the IMF and the EU for a bailout agreement in that period, which imposed further constraints on the government's fiscal policy (Ban & Bohle, 2021). In line with its economic nationalist agenda, the government sought to exit both the EDP and the bailout agreement to increase its fiscal autonomy. Following the introduction of measures that nationalized the private pension system and imposed special sectoral taxes, mainly on multinational companies in the financial, energy, telecommunications, and retail sectors, the budget deficit fell to below 3% and public debt also began to decline (Győrffy, 2018), allowing the country to exit both the EDP and the bailout agreement in 2013. However, the commitment to fiscal discipline also meant that the government had to rely on

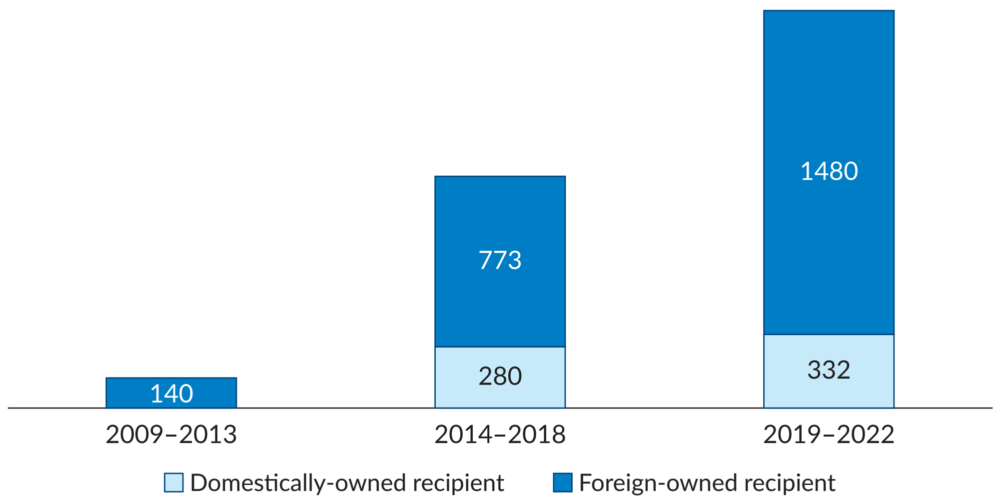

Figure 3. Regional investment aid granted by individual government decisions to domestic and foreign companies in Hungary (in millions of constant 2010 €). Source: Authors' calculation based on Ministry of Foreign Affairs and Trade (2023).

sources of external finance that did not add to the country's deficit or incur debt. In addition to EU funds, FDI remained such a source. Thus, fiscal discipline required the government to continue the FDI-based model to avoid direct EU fiscal interference. The EDP, consequently, indirectly ensured the continuity of FDI inflows, which are fundamental to Hungary's export-led growth.

European state aid rules also contributed to the stability of the FDI-based GM. As almost all Hungarian regions qualify for a regional aid intensity of up to 40%, it gives the government considerable leeway in granting regional investment aid to investors. Taking advantage of this opportunity, the Orbán government intensified the granting of regional investment aid through individual government decisions after 2013 (Figure 3). The vast majority of these grants (78%) went to foreign-owned companies, making regional investment aid a tool for the government to reinforce FDI-led growth and accelerate the inflow of foreign capital.

Meanwhile, the debate between the EU and the Orbán government over the deterioration of the rule of law in Hungary intensified, and the European Council adopted a regulation to protect the EU budget (Kölling, 2022), establishing the rule of law conditionality based on which the European Commission suspended all cohesion policy payments to Hungary. The Minister for Economic Development, articulating the government's response, argued that EU funds could be "easily replaceable by FDI" (Szumski, 2023). This suggests that the Hungarian government will continue to intensify the promotion of FDI in sectors where it welcomes foreign investors, which also implies that the suspension of EU funds has indirectly contributed to the further strengthening of the FDI-based export-led GM in Hungary.

5. Conclusions

Aiming to bridge CPE and IPE approaches in the analysis of semi-peripheral capitalism in the EU, we argued that the GMs in CEE are tied to the transnational influence of the EU, which we labeled as the EU-leash. We have shown that certain European regulatory mechanisms (soft conditionality through economic governance, state aid rules, and EU funding) set the limits within which institutional change in the respective

GMs is possible. Through two country case studies, we have demonstrated that the EU-leash has contributed to outcomes that were contrary to the aims the central governments sought to achieve: an incremental shift towards a weakly export-led GM in Estonia and the reinforcement of FDI-based export-led growth in Hungary. In both cases, the EU leash has softly limited the economic policy space of central governments although in the Baltics this has been almost voluntary because of the governments' strong commitments to comply with European economic governance rules. By exploring the dynamics between domestic politics and European influences, we have contributed to the literature on how the EU may accommodate GM heterogeneity across member states (e.g., Johnston & Regan, 2018; Johnston & Matthijs, 2022).

Despite the export-led bias of the EU-leash, the GM of the Baltics as a whole has remained highly inflationary due to a lack of wage repression and housing price increases, suggesting an enduring orientation toward domestic consumption (Bohle, 2018) and signaling potential problems with their long-term export competitiveness (Kalanta, 2023). The dutiful adoption of austerity measures and pro-forma export-support policies have resulted in high socio-economic costs, generating significant out-migration from the Baltics (Kattel & Raudla, 2013) despite attempts to mitigate these negative distributional consequences by ramping up social investment (Avlijaš, 2020). Overall, this outcome suggests protracted cycles of inflationary periods followed by excessive austerity, severely disempowering domestic democratic agency. All this, however, remains within the limits set by the EU-leash. Equally concerning are the potential socio-economic and political consequences of the continuation of the FDI-based, export-led GM in the V4. This model entails asymmetrical power relations with foreign investors and has adverse distributional consequences, such as rising income inequality and insecure labor markets, which fuel illiberal politics (Epstein, 2020).

It is important to note that the EU-leash does not downgrade domestic political agency in CEE countries, but limits room for maneuver to varying degrees. EMU membership, for instance, poses much tighter constraints than "simple" membership in the single market. The EU-leash may therefore exert a disciplining influence in the case of Slovakia, which recently experienced the comeback of national-populists with Róbert Fico in government, who has long advocated for replicating some of the policies implemented by Orbán in Hungary (e.g., sectoral taxes). Due to the country's EMU membership, the Fico government will face a narrower space for economic policy than Hungary, thus the EU-leash may prevent the adoption of certain measures, as suggested by the tied hands of national populists among the Southern EMU members (e.g., Vampa, 2023). Although the EU's influence on the GMs of its member states extends beyond the CEE countries, our concept of the EU-leash applies primarily to small and open economies that are heavily dependent on external sources of finance. Thus, it is the nature of dependent growth that allows for the EU's enhanced influence on GM trajectories in CEE. The analysis of the politics of semi-peripheral GMs should, therefore, incorporate the EU's role as a decisive stakeholder contributing to institutional stability and change.

Acknowledgments

The authors wish to thank the academic editors and the three anonymous reviewers for their most helpful comments on earlier drafts of the article.

Funding

This work was supported by the Slovak Research and Development Agency under the Contract No. APVV-21–0237 and by the National Research, Development and Innovation Office, Hungary (Contract

No. NKFIH-FK135342). Gergő Medve-Bálint is a recipient of the János Bolyai Research Scholarship of the Hungarian Academy of Sciences.

Conflict of Interests

The authors declare no conflict of interests.

Supplementary Material

Supplementary material for this article is available online in the format provided by the authors (unedited).

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