

EU Enlargement toward Eastern Europe:

Challenges and Issues

Introduction

When the European Union enlarged its membership southward to cover such countries as Greece, Portugal and Spain in the 1980s it altered EU's economic geography and budgetary structure some but the process was smooth and painless overall. These new partners, although struggling with their incomes, had more or less the same economic structures as most of the old EU members. When EU in the 1990s also took into its fold the Northern European countries – Austria, Finland and Sweden – it was even better. The economies of these three countries were in such great shape that their EU membership influenced an increase in the union's per capita income.

Following the launch of the euro as EU's common currency, the EU found it necessary to shift its attention to the East. The decision to enlarge EU membership to Eastern European countries was finalized in 2002 and its first phase would have been carried out between 2004 and 2006. Here, EU negotiates what analysts perceive as a bumpy road.

Almost all of the 10 prospective EU members from Eastern Europe

belonged to the former communist bloc which just emerged from half a century of Soviet domination. Throughout this long period, they operated on a planned economy and it is only now that they are moving in unison towards a market economy. As a lingering effect of a less efficient economic system, their incomes are much lower than those of existing EU members. This poses a problem to the process of harmonizing the entry of these countries into EU.

EU enlargement to Eastern Europe will boost the European common market from 320 million people to about 470 million. Unlike Switzerland, Norway and Iceland which joined only EU's free trade area, the Eastern European countries need to be full EU members or they will not enjoy the promised benefits. This entails huge costs on the part of the new members.

Eastern Europe is a low-income region of about 100 million people whose combined income will raise the GDP of EU by a mere 5 per cent. This is very much less than the result of previous EU expansions to the North and South. It is not only their low income levels that may bring deleterious effects to EU but also the fact that these countries are in the middle of a transition phase from a centrally planned to a market economy. In addition, the new members will have to cope with more EU regulations than before because of the recent creation of the Single European Market concept.

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Although many of the former communist bloc countries are convinced of the superiority of the free market, some have retained their faith in the socialist system and in the role of government in steering economic growth. Thus, many of them continue to bring up the rear on the list of world's freest economies. In the *2003 Economic Freedom of the World Report*, only Estonia made it to the 16th rung. Hungary was 35th, Czech 39th and Latvia 51st. At the bottom of the list were Bulgaria at 103rd place, Russia 112th, Romania 116th and Ukraine 117th. (Tupy, L., 2003)

Initially, liberalization of these economies pushed output down, but they gradually recovered. By 2002, their separate GDPs grew as foreign investment started to come in. During that year, the World Bank reported that Poland, Hungary, the Czech Republic and Slovakia led the pack with an average 2.3 per cent growth.

Poland is the largest of these former communist bloc countries and may prove to be of strategic importance to EU since it is the gateway of Western Europe into the large Eastern European countries of Belarus, Moldova and Ukraine. (Mind Your Business, 2004) The other big countries in the East that are slated to join EU are Russia, Bulgaria, the Czech Republic, Romania, Hungary, Slovenia and Slovakia.

Poland's Problems

Signs that Poland is a possible problem child for EU became evident as soon as the homeland of the beloved Pope John Paul II took the first step of joining the union in May 2004. Polish officials attending their first EU meeting in Brussels to discuss a new constitution insisted on their voting rights within the new enlarged EU. (Mind Your Business, 2004) This caused the collapse of the talks as Poland acted like the new kid on the block claiming an adult privilege for itself.

For Poland, an EU membership means further stability to its shaky political system as a fledgling democracy. Under EU, it is duty-bound to open up its economy and put in place a level playing field for business. This will attract much-needed foreign direct investment to modernize its infrastructures and industry, including new capital and new ideas. As a reward of sorts, it will also gain access to EU structural funds for infrastructure.

Poland has a manageable inflation rate of 1.9 per cent but it contends with a runaway unemployment rate of 18.4 per cent. It is primarily an agriculture-driven economy with agriculture accounting for 63 per cent to its GDP and the agriculture sector employing 20 per cent of the workforce. (Mind Your Business, 2004) If government statistics are accurate that 18.4 per cent of the Polish

population lives below the poverty line, then agricultural production leaves much to be desired.

The twin problems of unemployment problem and low agricultural productivity pose the biggest challenge to the EU enlargement process because of the perceived threat of large-scale labor migration and the stiff budgetary costs required to implement EU's agricultural and regional policies. On the part of Poland, it may have to cough up huge sums of money to comply with centralized EU regulations on labor and agriculture. This is the hardest part of joining up EU as they impose the most costs on new members. (Tupy, L., 2003)

By putting up the huge costs required for complying with stern EU labor laws, this could diminish the level of investment the new members sink into industry thus running the risk of losing whatever competitive edge they enjoy. Adverse effects are also expected on workers' productivity.

As for EU regulations on agriculture, these involve subsidies that are given to new member countries in place of strategic constraints to production. The idea is to "harmonize" the agricultural production of all EU members.

Migration

At the initial stages of the new members' entry into EU, cross-border movements of workers will be regulated but it is stipulated that this movement will

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be freed by 2010. This hews with the EU philosophy of promoting the free movement of trade, capital and people within the union. But there is a possibility that Polish workers would defy such regulations to escape poverty in their homeland.

Brenton, P. observed that with the accession, there is an incentive for Eastern European workers to migrate westward and for capital to move eastward. This means that workers from the Eastern European countries will be attracted to the richer EU members in the West, while capital will take the reverse course.

Fears from such large-scale labor migration were however scotched by Brenton, P. who finds no historical basis for that trend. The same fear was expressed in 1998 when EU accessed relatively poor members. What happened was legal migrant workers accounted for only 0.2 per cent of total EU employment, and 80 per cent of the total number of migrant workers were concentrated in Germany and Austria which were capable of absorbing them.

Even if the temporary suspension of labor movement is lifted by 2010, the inflow of migrants from the East are estimated to come to less than 1 per cent of the working population of the 15 EU members in 2009. (Brenton, P.)

Agriculture

The EU Common Agricultural Policy is the thorniest issue in the enlargement process because of its potential to throw a new member country into bankruptcy. EU spends on this program 46 per cent of its total annual budget of 100 billion euros.

Under the accession arrangement, the 10 Eastern European countries will get 5.1 billion euros between 2004 and 2006 as a direct CAP subsidy. This amount represents 25 per cent of what the current EU members received in 2004, 30 per cent in 2005 and 35 per cent in 2006. The new members from Eastern Europe will have to come up with a counterpart fund to top off these amounts, specified at 55 per cent in 2004, 60 per cent in 2005 and 65 per cent in 2006. Governments hard put to co-finance the project may access the EU Rural Development Funds in the meantime. But after 2007, only the national budgets of the new members can top off the CAP funds. (Tupy, L., 2003)

The CAP was initially a food security mechanism that evolved into a system that supports inflated prices of agricultural products. Such a deliberate distortion is designed to ensure that farmers keep their income levels that are centrally determined. An inevitable result of this policy is prices that are constantly above market levels. This also leads to overproduction and a glut in agricultural produce.

Agricultural subsidies are common throughout the world but EU “spends almost twice as much as the US to subsidize its farmers (Tupy, M., 2003).” With the imposition of production quotas, Slovakian negotiators in the enlargement proceedings earlier fought with their EU counterparts over every sheep and liter of milk. Slovakia wanted to produce 1.2 billion liters of milk and 400,000 heads of sheep yearly but EU set the limits to 950 million liters of milk and 400,000 heads of sheep.

EU’s agricultural policy goes beyond CAP. The union even intrude into such activities as marketing of potato and vegetable seeds, peas and poultry. One EU regulation even seeks to increase the production of an exotic type of honey on a tiny Aegean island by subsidizing the beekeepers.

Al in al , there are fears that the stringent EU policies on agriculture and food safety would make Eastern European countries less competitive. Seen as a possible protectionist measure that could dampen the growth of the new members is the power given to EU to limit the flow into the internal market of current members of agricultural products from Eastern Europe for three years, the transition period for their full EU accession. The avowed purpose of this policy was to prevent unsafe food products from getting into the EU common market. But many see it as a policy meant for genetically modified foods from the US.

At the outset, EU promised to remove existing quotas and tariffs on agricultural products coming from East European countries but the union has yet to make good its word. Meanwhile, EU continues to dump its subsidized agricultural products from existing members into the Eastern European applicants, thus increasing the pains of the transformation process.

Conclusion

When the Eastern European countries led by Poland decided to join EU, the assumption was that they wanted to share the blessings of the free market being enjoyed by existing EU members. What can the old EU members show them in the way of stimulating the growth of their own economies?

For the most part, the standard of living in Eastern Europe is low. In Slovakia and Slovenia, for example, average per capita income are \$3,700 and \$10,070, respectively. But still Slovakia managed to grow by 4.4 per cent in 2002. In contrast, the old-time EU member Germany grew only by .2 per cent, France by a measly 1.45 per cent and UK by 2.58 per cent. Tupy, M. (2003) asks: "So how could the EU economic model be appropriate for the future prosperity of Eastern European countries?"

Most EU economies also exhibit deep structural problems, reeling from the high cost of complying with restrictive EU regulations on environmental and safety standards, high taxes and rigid labor markets.

Even in employment, EU lags behind. In the past decade, the unemployment rates in Germany and France were hitting double figures, as against an average only 5 per cent in the US. Since 1970, the US created 57 million new jobs in both the public and private sectors while EU, with a larger population, has not come up with any in the private sector, only in government.

For these reasons, the Eastern European countries are not exactly beating a path to EU's door. In 2002, EU itself conducted a survey on how the Eastern Europeans view their admission into EU. Only 32 per cent of the Estonians said it was a good thing. In Latvia, Slovenia, Czech Republic and Lithuania, the figure was 35 per cent, 43 per cent and 48 per cent, respectively. Which means that majority of these countries' population want to keep out of EU.

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