



Center for Social and Economic Research

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**Participation in the EU Internal
Market: the experience of NMS
and its relevance to the ENP**

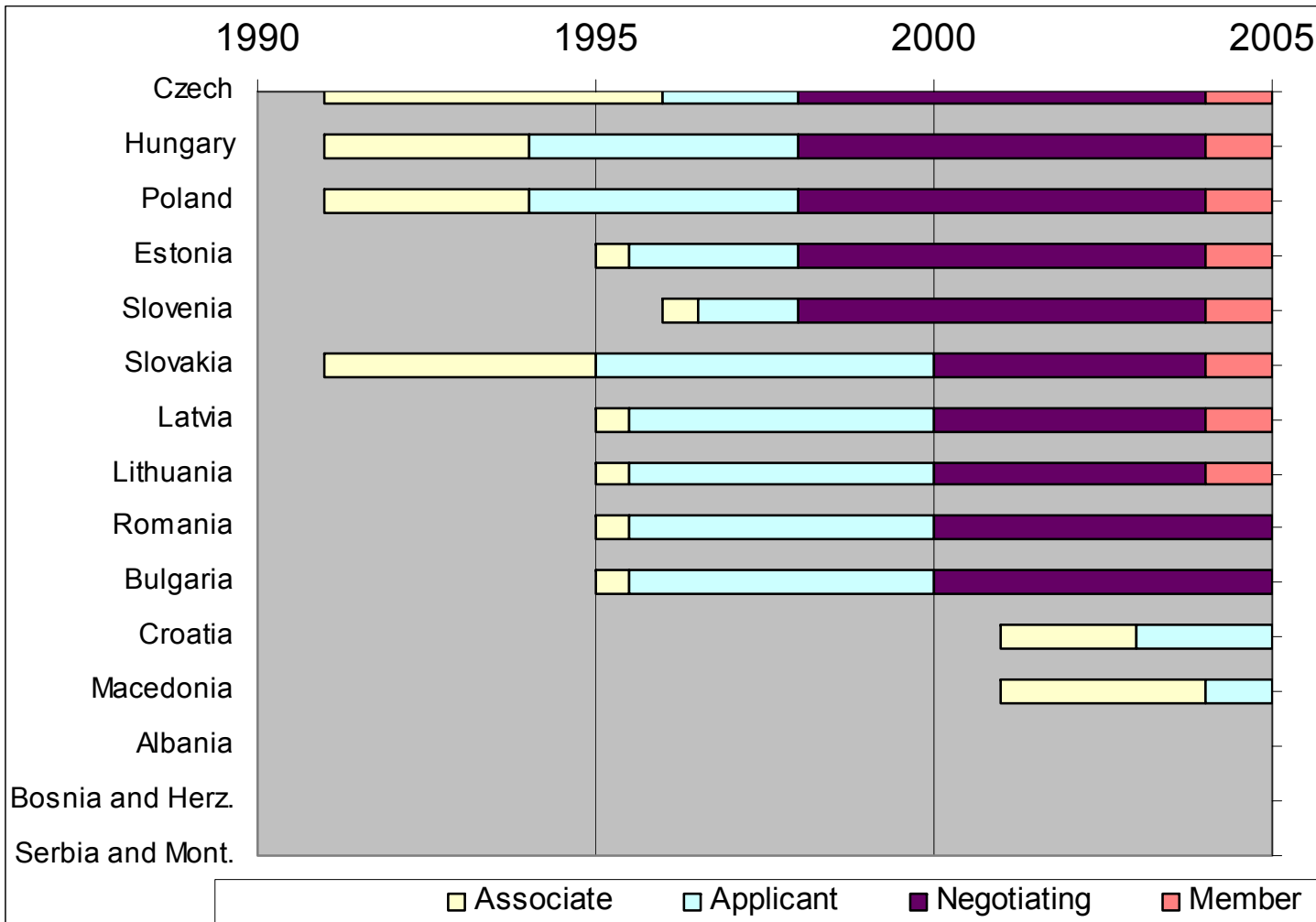
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Merchandise Trade of Eastern Europe, by direction

	1980	1990	2004
World	100.0	100.0	100.0
Eastern Europe and the CIS	48.5	38.1	23.2
CIS	27.1	22.3	4.7
Eastern Europe	21.4	15.8	18.5
Developed market economies	35.7	49.5	71.0
Developing economies	15.8	12.4	5.8

Source: UNECE *Economic Survey of Europe, 2005 No. 2, Appendix Table B14*

EU integration process (embracing Balkans)



NMS – unfinished integration with the EU Internal Market

- Transition arrangements related to free movement of labor
- Transition arrangements related to some services
- Transition arrangements related to land purchase
- Indirectly: EMU and Schengen

Directions of Exports of Goods, 2004, World=100%

	EU-25	Acceding/ Candidate Countries	CIS	MENA
EU-25	68.3	2.4	2.2	3.8
Belgium	77.8	1.3	0.9	3.1
Czech Republic	83.8	3.0	2.4	1.6
Denmark	68.5	1.0	1.8	2.5
Germany	64.6	2.7	2.8	3.0
Estonia	74.6	0.6	11.5	0.5
Greece	60.1	15.6	3.3	7.0
Spain	75.2	2.5	0.9	5.2
France	67.1	2.0	1.4	6.8
Ireland	63.2	0.5	0.3	1.3
Italy	60.4	4.8	2.6	6.3
Cyprus	64.9	2.8	2.8	17.6
Latvia	75.9	0.1	7.8	1.0
Lithuania	61.3	2.1	15.2	0.1
Luxembourg	90.4	0.7	0.8	1.0
Hungary	80.7	6.0	3.2	2.2
Malta	44.5	2.4	0.1	5.2
Netherlands	81.0	1.4	1.6	2.3
Austria	72.4	4.2	2.4	1.8
Poland	79.1	3.1	7.9	1.2
Portugal	80.8	0.9	0.3	1.8
Slovenia	73.3	11.1	5.1	2.1
Slovakia	85.7	2.9	2.8	0.5
Finland	58.3	1.1	9.9	4.7
Sweden	59.1	1.3	2.1	3.2
United Kingdom	57.0	1.6	1.3	5.0

Source: European Economy 2005, No. 5, Table 57

Sources of integration success of NMS

- Clear perspective of EU membership
 - Strong incentives to conduct reforms and open the economy
 - Guidelines how to reform (*acquis*) \Rightarrow mass-scale institutional import
 - Package solutions (loses in one area could be compensated in another area)
- Generous EU offer at the association stage
 - Asymmetric trade liberalization
 - TAA before or parallelly to WTO accession
 - Early abolishing of visa regime
 - Substantial aid package

The magnetism of EU membership

- Political ('club') membership
- Historical links and cultural proximity
- Geopolitics and security
- Four basic freedoms (goods, services, capital, labor)
- Prospects of prosperity
- Structural funds

Σ = the magnetism of a Western European prosperity, freedom and lifestyle

Limited relevance of NMS experience

- The ENP offer does not include the EU membership perspective
- The ENP is unlikely to provide a fast-track full participation of neighbors in the EU internal market (particularly for CIS); more realistic option: selective participation in some segments of EU internal market ⇒ selective institutional harmonization with *acquis*
- Integration “fatigue” in Western Europe
- Institutional problems in neighborhood countries are different comparing to those of NMS in 1990s and early 2000s (particularly in the case of Southern neighbors)

**Possibly more similarities
to the current and future
EU accession process of
Turkey and Western
Balkans**

Consequences of differences

- Weaker incentives to domestic reforms and integration
- Weaker enforcement mechanism
- Lack of package effect \Rightarrow sectoral negotiations driven by narrow sectoral interests on both sides
- Bilateral agendas of ENP Action Plans
- Domestically: weaker reinforcement effect (integration progress helps to build a pro-integration constituency)

Limited market integration with neighbors

- Southern neighbors: association agreements with long implementation period (up to 12 years); asymmetric liberalization for manufactured goods; important sectors (like agriculture or services) only partly covered or excluded
- CIS: only PCAs so far; postponing start of trade liberalization negotiations after WTO accession process will be completed (difference with NMS and Balkans)
- Restriction on movement of people (visa regimes)
- Various degree of liberalization of capital movement in neighboring countries but limited real flows due to poor investment climate

Integration obstacles (neighbors side)

- Failure to meet Copenhagen criteria
 - Deficit of democracy, human rights and rule of law
 - Poor business climate, excessive protectionism, government interventionism and etatism
 - Weak institutions
- Limited interest in advanced forms of European integration (due to historical and cultural differences) with some exceptions like Moldova and Ukraine

Integration obstacles (EU side)

- Integration ‘fatigue’
- Cultural differences/ prejudices
- Income differences
- Migration/ security fears
- Unreformed CAP, welfare state and other structural rigidities
- Limited economic potential of neighbors

Arguments in favor of closer integration of neighbors with the EU

- Geopolitics and regional security
- Window of opportunity for economic, social and political modernization of ‘neighbors’
- Energy supply and transit
- Transport routes
- Controlling migration flows
- Economic, cultural and ‘historical’ interests of ‘frontier’ EU member states

Arguments in favor of package approach:

1. Trade expansion will depend not only on trade liberalization *per se* but also on neighbors' investment climate, speed of institutional harmonization and, to some extent, on liberalization of movement of people.
2. Intensification of foreign investment inflow to neighbors will depend not only on improvement of domestic investment climates (determined by a speed of institutional harmonization) but also on trade liberalization (market access).

Arguments in favor of package approach (cont.):

3. Intensification of trade and FDI and the resulting diminishing of the income gap can weaken the income motive of labor migration and make freer movement of people less politically controversial in the EU. To some extent, free movement of goods and capital may serve as a substitute to the free movement of labor.
4. Free movement of people is important for balancing national labor markets, current accounts, development of the domestic SME sector and learning experience of more mature market economies and democratic societies, therefore strengthening pro-reform constituencies in 'origin' countries.

Arguments in favor of package approach (cont.):

5. Institutional harmonization involves substantial costs. The traditional pay-off offered by the EU (modest improvement of trade access and technical assistance) is insufficient. A stronger set of incentives should include a faster pace of trade liberalization and liberalization of movement of people. For countries, which are interested in EU membership, such a perspective should not be ruled out *a priori*.