

# Floor Discussion of the Inotai Paper

## Conditions for Accession and the Adjustment Process

The comparison of Eastern enlargement with the previous Southern enlargement of Spain, Portugal and Greece provided the basis for a number of comments. Franz-Lothar Altmann began this part of the discussion by focusing on the financial flows. "If you compare the utilisation of these financial flows and the absorption of these flows to Portugal and Spain on the one side and Greece on the other, there is a substantial difference. It was clear that Greek import surpluses at the beginning of membership were in consumption, whereas for Portugal and Spain, the import surpluses clearly resulted in a high inflow of investment goods. The financial means, not only what was imported but what was transferred from other EU members into the new member states, was also very different in Greece. The major criticism was – and still is – that there was an enlargement of the state sector and that much of these financial means ended up there instead of in investment or in modernisation which could improve overall production capacity. The lesson is that one should also look at what happens with the expected inflow of means after accession in order to speed up the adaptation process."

Joan Pearce added two comments on this comparison. "András Inotai refers to the position of the applicant countries now and of Spain and Portugal when they were applying, but that is not the relevant comparison. The relevant comparison is Spain and Portugal in relation to the community as it was at the time of their application and the applicant countries in relation to the EU today. It is true that there is a greater degree of privatisation and demonopolisation in the applicant countries, but the Union has also progressed tremendously in this respect. The context in which Spain and Portugal were joining was quite different.

My second point concerns another lesson from the Spanish and Portuguese enlargement. The negotiation of accession for Spain took almost nine years. One of the reasons why negotiations took so long was that a lot of people thought that Greece had been brought into the community too quickly, and that this had caused a lot of problems. People were very wary about bringing in two more countries that might have similar problems. This is a lesson that we all need to keep in mind, particularly if the first-wave countries are concerned for the second-wave countries. This is one more reason why the first-wave enlargement has to be a success. If it

happens, but then generates all kinds of problems in the Union, there is going to be great reluctance to contemplate a second wave in a relatively short time span after the first wave.”

Zdeněk Drábek commented on the maturity of countries in Central and Eastern Europe. “Quite frankly, I think that András Inotai is overly optimistic in judging the adjustment ability of the countries themselves or the successes in adjustment so far. I was struck by his comments about substantially increased export competitiveness of the region. This may be the case in Hungary, but I doubt that this is the case in the Czech Republic where there is a very serious problem with the competitiveness of the tradable sector.

With regard to the adjustment process and the role of macroeconomic policy, you say that there has been a very successful adjustment, but in my view, adjustment has not been good enough in terms of an integration strategy toward the EU. How important is the maturity question? How mature do we have to be to become members of the EU? If this security question is the driving force of negotiations – and this would not surprise me – then the EU might even take a less mature member in order to increase stability in the region.”

Joan Pearce linked the issue of security with the question of financial transfers. “Security is the driving force in that the EU’s *raison d’être* for enlargement is seen mainly in security terms. On the whole, it is seen as a process that will bring security benefits at certain financial and economic costs. I agree, András, that is not an accurate assessment of the costs and benefits, but nevertheless, it is the perception. When considering what is meant by security, some would be sufficiently blunt and say, ‘enlargement is about Poland’. While this is an overly simplified expression, there is some truth in it. So when you say that there will be significant differences in financial transfers for the various applicant countries, this is certainly true if we look at the present arrangements for agriculture and structural funds. The big ticket item is going to be Poland, but Poland is also the country in which there is the most interest from a security perspective, so there you would expect to find a balance between the perceived costs and benefits. There are other countries where the security benefits are much less and the financial costs rather high – if not quite as high as Poland – and therefore the security argument would not be sufficient to outweigh the financial argument.”

Mark Allen expressed concern about the assessment of the benefits in the transition process. “There is this notion that because the EU was running a large trade surplus that the benefits have been asymmetrically distributed so far in the process. This is an incorrect analysis of the situation. The distribution of benefits cannot be judged separately from the move-

ment of trade balances or current account balances. Current account balances are going to depend on the savings investment balances in the individual countries, not on matters of trade policy. All that trade policy can do is change the distribution of items inside the balance of trade. What is more important is to determine whether exports have been behaving dynamically on the two sides as a sign of where the benefits are really occurring. What I find particularly disturbing about the argument that trade surplus on the EU side is a sign of the wrong distribution of benefits is that, at the same time, one is asking for substantially larger financial transfers from the community and, of course, the financial transfers are precisely the counterpart of the current account deficit. Thus, the bigger the financial transfers, the larger the current account deficit of these countries is going to be and, on this analysis, the more the transfers, the worse the distribution of benefits – which is clearly not the case. So an analysis of who has gained most from the trade liberalisation process so far has to be done on a different basis.”

## Negotiations

Franz-Lothar Altmann turned the discussion to the negotiations and the question of sequencing. “We should try to avoid making groups of countries because, groups entail the danger of erecting new borders between these countries. Groups are going to emerge in the process of accession anyway, but it is important from the start to avoid calling three or four countries a group. This could have a negative impact on all of the endeavours of these countries in the course of preparation and adaptation for new membership. Rather, we should use the baseline approach in which we begin negotiations with all of these countries at the same time, but with varying intensity and speed. Then, when one, two or three countries are ready and both sides agree, treaties can be signed. This country-by-<sup>15</sup> country approach would not entail the danger that there would be a long waiting period for successive groups while the EU is dealing with the problems of the first group. We must search for additional means and economic and political cooperation with these countries, but at the same time, we should not forget the other countries which are not one of the ten or eleven accession countries. Ultimately, countries like Croatia, Serbia, Montenegro, Albania, Macedonia or the Ukraine will probably also apply for associated status, so we have to think more in advance of these countries and prepare for the additional incorporation of these countries into the wider Europe.”

Joan Pearce responded to Franz-Lothar Altmann’s view on a case-by-case approach. “I am certainly in favour of beginning negotiations with all

the applicant countries and then maintaining as flexible an approach as possible which would permit some to accelerate. It would be case by case in the sense that negotiations would be bilateral. But, just as it is inconceivable that the Union would take in ten member states simultaneously, it is equally inconceivable that it would take them in one at a time. On pure institutional and administrative grounds, it takes about two years to absorb a new member state, and the idea that Europe would spend ten to twenty years taking in ten countries at the rate of one or two every two years would be incredibly disruptive to the Union. It is simply not in the cards. There will come a point when, whatever the shifting in the relative speeds during the process of negotiation, certain groups of countries are ready for accession and they will come in as the first wave and then groups of countries will form the second or third waves.”

Zdeněk Drábek emphasised the importance of distinguishing among the countries and suggested some specific negotiating issues. “For example, financial transfers will surely be less of an issue for the Czech Republic for some other countries. On the other hand, there will be some very sensitive topics to negotiate, and here are three suggestions which will become important on your list. One, certainly for the Czech Republic, is the issue of property ownership on border areas with the Austrians. Another one will be transport, particularly road transport. And a third one will be macroeconomic policy, my favourite topic. I can foresee a situation that the EU will be, by then presumably, an EMU and the extent to which these countries will be able to join will depend on their macroeconomic situation.”

Barbara Stallings made a comparison with the position of Mexico in the NAFTA negotiations. “If one takes Mexico and NAFTA as an example, Mexico has as much trade with the US as the CEFTA countries have with the EU, but in Latin America, this is seen as a problem. As a matter of fact, when Mexico was in the process of negotiating the NAFTA agreement, important people in the Mexican government publicly said their reasons for joining NAFTA was to make Mexico more attractive as an investment and trade partner for Asia and Europe. But this notion doesn’t seem to be part of the game plan of the CEE countries. What is your opinion on the notion that they would make themselves even more attractive to Europe if they were a bit more diversified? Their lack of bargaining power has been mentioned. Would it help their bargaining power if they had a more diversified economic base?”

Albrecht von der Heyden elaborated his view of the role of CEFTA both before and after accession. “It has a specific role in the preparatory process but also a key role after accession for those who are not in the first accession track. I have the impression that CEFTA has been reduced to a

tool for the bargaining position of the countries concerned. We should think about alternatives and procedures to guarantee that the accession process is not limited to those who have the best chances in terms of maturity, but make sure that the accession process for all ten countries is continued. No one has a sufficient solution for this, including those who have made specific proposals, such as the French and German foreign ministers who suggested a European conference. It is an expression of apprehension that if we don't find the special tools for guaranteeing that we see it as a process of accession as a whole, then we won't achieve our goals. I would like to take up the ideas mentioned with regard to the customs union and the EEA, and I would like to limit our task to finding some kind of procedure."

### **Response by András Inotai**

"The first issue I would like to comment on is the security issue. As it concerns enlargement to the East, the first-wave countries should definitely be interested in a strategic framework for further enlargement. Nobody who is thinking in strategic terms will want to become a member of the EU and then close it down. This would just transfer the security risks from the western border of these applicant countries to their eastern borders. Four kinds of countries may emerge. One is the country which is already an EU country, such as Germany and Austria. The second is the country which borders and is likely to join the EU. The third group includes those countries who are expected to become members later on. And the fourth group is made up of those countries who are not expected to become members, at least as the situation stands today – I would never use the word never. In our security perception, and this should be shared by the EU, we need a very different and very careful approach to these groups. I have discussed this issue in Hungary with some individuals who only look at the uncertainties, dangers, dilemmas and challenges arising from the accession of Hungary and the simultaneous non-accession of some countries with a large Hungarian minority. It is a first-rank security issue for the whole of Europe. It is a very important issue for using the potential Hungarian, Polish, Czech and other advantages in becoming a transit country and not a fortress country. And it is very important for our bilateral economic relations. Please do not forget that some of the most dynamic relations in our trade, and not only Hungarian trade, are with the neighbouring countries and they will remain so. Nobody is interested in finishing with the first enlargement. We are very interested in securing the framework for further enlargement, also for security reasons.

My second remark concerns speed. Joan Pearce has suggested some

ideas about why speed should not be considered so important. Of course speed is not the only component and a lot depends on other factors. However, it is difficult to compare the speed of negotiations of the CEE countries with that of Portugal and Spain for different reasons. The transformation process itself is much faster than has been envisaged and than any other adjustment process. It does not mean that transformation may not produce some setbacks, and that many questions remain regarding the next stage of transformation, in all of our countries. This might have repercussions on our preparation for membership, and it would be very interesting to analyse what the ideal sequencing of transformation on the one hand, and the ideal sequencing of adjusting to the EU would be, on the other. I am not sure that the sequencing is the same in all cases. What kind of compromises need to be made? What is the right policy mix? These are some of the biggest challenges we are facing. Europe is a very different place from when Spain and Portugal were negotiating. At that time, there was a divided but predictable Europe without too much unforeseen, unpredictable dynamism. It was reliable and there was time. Today, the time constraint may substantially influence the speed, and this is particularly the case if we consider intra-European dynamism which is also shifting. Berlin will be the future capital of Germany, and I don't think that it can remain just 60 kilometres from the eastern border of the EU. There are tremendous dynamic forces, and in order to maintain the internal balance and stability of the Union, enlargement is imperative probably earlier than many people think today.

I do fear the view that all those first-wave countries are responsible for the future of Europe and for the future of handling security and other issues in their neighbourhood. They must have a very specific role, not just as a member of the Union, but much more. I do agree with Lothar that groups should not be created artificially, but some groups have already been created. There are three OECD countries in the region; what is that if not a clear distinction? Is it possible that a non-OECD country could become a member of the EU? It has not been the case up to now. Will there be a change in EU policy or will these countries first become members of the OECD? There will probably also be some NATO members before enlargement. I think there is a linkage between NATO membership on the one hand and EU membership on the other. While I understand the fear regarding the creation of groups, there are also fears in the applicant countries in the other direction. The more developed applicant countries may fear that the non-creation of groups is practically equivalent to the postponement of enlargement, and this also contributes to paralysing sub-regional cooperation. They would be much more able and willing to enter a sub-regional cooperation arrangement if they knew that this was

the group that would join. They would consult each other in a much more intensive way.

As for the diversification mentioned by Barbara Stallings, you are absolutely right that our trade and other relations should be more diversified, and this is already the case regarding FDI. A number of US, Japanese and Korean companies have come to Central Europe to invest in the CEFTA countries – with one eye on the EU market. One problem for these countries, mainly the Far Eastern ones, is the 60 per cent share of domestic EU and CEFTA inputs. Especially in their first years, they would like to have their own inputs and parts to be imported and shipped to these countries. But if you look at Suzuki in Hungary, for instance, it managed to produce 70 per cent of its inputs in Hungary, EU and CEFTA countries. We are very much interested in capital from the global market, and since most of the available capital today is from non-European countries, we think that the speeding-up of the enlargement process will certainly contribute to convincing non-European investors to invest more heavily in this part of the world.

Finally, I would not like to be misunderstood with regard to the trade surplus of the EU. It was not meant as an indicator of the distribution of benefits toward the EU. It is just one factor, and no one has denied the favourable impact of the association agreement on the associated countries. The temporary trade asymmetry in our favour is unlikely to compensate for the historical development asymmetry between the two parts of Europe. In the case of Spain, Portugal and Greece, the trade deficits with the EU have been largely offset by EU transfers. In the case of Portugal, between 1986 and 1992, they have accumulated a trade deficit with the EU in the amount of about 30 billion dollars. Half of this can be accounted for by transportation and so on. The other half was unilateral transfers from Brussels to Lisbon.”