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Communication from the Commission  
to the Council

implications of recent changes  
in central and eastern Europe  
for the Community's relations with the countries concerned

Explanatory Memorandum

This Communication examines the implications of recent developments in central and eastern Europe for the Community's relations with the countries concerned.

### The Present Situation

The new authorities which have recently taken office in the countries of central and east Europe have expressed their wish that the Community should play an important role in reinforcing the process of political reform and economic liberalization which is underway and in enabling their countries to participate more fully in European affairs and the wider international economic system. For these countries, the Community offers an attractive framework for overcoming the division of Europe and encouraging a peaceful transition to democracy and market oriented economies.

While progress achieved in the different countries varies considerably, only Poland thus far having a predominantly non-communist government resulting from elections, free elections have been announced for the first half of this year throughout central and east Europe.

Democratic forces opposing the present governments generally seek more time to organize, better access to the media and sufficient funding from sources within their respective countries. In some cases these forces have indicated their concern to ensure that the elections are organized fairly and have raised the question of international supervision. If these concerns become formal requests, institutions in the Community, notably the European Parliament, should be ready to respond appropriately.

Meanwhile governments are acutely aware of their provisional status and, with varying degrees of effectiveness and conviction, are seeking to establish the necessary legal framework for a peaceful transition to democracy. There is a general commitment to ending constitutional provisions establishing the leading role of the Communist Party but, in some cases, lingering ambiguity over provisions establishing a "socialist" system. While such ambiguities remain and pending the formation of stable governments resulting from free and fair elections, the process of reform remains fragile. Affirmations of its irreversibility are convincing in most cases although the possibility of set-backs remains, notably in Romania.

The goal of economic liberalisation and progress towards market economies has been proclaimed in all countries. In some cases this goal is qualified by an attachment to the concept of a socialist market economy; in most, however, the goal is unambiguous. Legislation is being introduced establishing new property rights, permitting private enterprises to enter trade and commerce, and relaxing restrictions on direct foreign investment. There is a strong desire to obtain western technology and managerial skills; foreign capital is welcomed, although rules governing shares in joint venture companies vary. Particular stress is placed on the need for management and vocational training and the need to create a modern services infrastructure.

The point of departure for liberalisation is uneven, with some economies, notably the Czechoslovak, in overall internal equilibrium, and others with severe imbalances. In every case fundamental distortions exist as a result of centrally imposed planning requirements and subsidies which amount to a considerable proportion of government expenditure and national income. Liberalisation implies fundamental restructuring in which full employment may not be guaranteed and further inflationary pressures may develop. Some authorities, notably in Poland, have responded to this challenge by making a dash towards market economies, through the freeing of prices and deregulation, while others prefer a graduated approach to the same objective.

All are convinced that the conditions for currency convertibility must be met as rapidly as possible and that trade with free market economies must be stepped up. This implies major efforts to improve the quality of manufactured goods so that they can find outlets in the markets of industrialised countries. Until hard currency earnings from these sources build up, there is a reluctant recognition that the Comecon countries, and notably the USSR, will continue to account for a high proportion of trade. This is reinforced by dependence on energy imports from the USSR.

Nonetheless it is widely felt that Comecon as presently constituted fails to provide a useful framework for external economic relations. The outspoken position of the Czechoslovak delegation at the Comecon meeting in Sofia on 9 January envisaging a dismantling of the organisation if it proved resistant to reform, was not, however, followed closely by other delegations. The general preference appears to be for a fundamental restructuring of Comecon, eliminating all unequal requirements governing trade with the USSR and allowing each country to pursue its trade relations bilaterally on the basis of comparative advantage and normal competitive conditions. Soviet proposals for rapid movement towards trade in hard currency at world prices on selected items are, however, viewed with suspicion as the selectivity proposed would limit the capacity of individual countries and enterprises to earn and retain hard currency for use according to their own priorities.

Under these circumstances, the members of Comecon in central and east Europe look to the Community to take a prudent position, avoiding action which might reinforce outmoded structures while strengthening bilateral links with Comecon members.

Closer commercial and economic links with the Community are welcomed both for their inherent value and as steps towards the open international trade system. Countries which have not already concluded trade and economic cooperation agreements with the Community look forward to doing so in the first half of this year on terms at least as favourable as those negotiated with Hungary, Poland and the Soviet Union. Although these agreements do not themselves include provisions for financial support or food assistance, a number of measures have already been taken in favour of Poland, Hungary and Romania. With differences of emphasis and with the apparent exception of Czechoslovakia, all countries concerned look to the Community for appropriate forms of financial cooperation. Poland and Romania urgently require additional food supplies and requests for food have been made by Bulgaria.

The declaration of the Group of 24 at the Ministerial Meeting in Brussels on 13 December confirming their commitment to this programme as well as their willingness to respond positively to other countries in east Europe at the time they put into place political and economic reforms, has been duly noted by the countries concerned. The authorities in Prague, Sofia and Bucharest are preparing requests to the Group of 24 to become beneficiaries of its programmes of coordinated assistance. In general, the priorities established by the 24, notably training, investment and the environment, correspond with their own needs.

The launching of the negotiations on the European Bank for Reconstruction and Development is welcomed, as witnessed by the participation of the countries concerned in recent preparatory meetings. They have also expressed an interest in the European Training Foundation and the Community's proposed scheme for youth exchanges which will be presented to the General Affairs Council in February.

Within the wider multilateral framework of the CSCE, the authorities in central and eastern Europe expect decisions to be taken which will create a positive environment for their own peaceful transition to systems based on fundamental political and economic freedoms. The Helsinki process is expected to assist in overcoming the divisions in Europe which prevented the development of normal political and economic links with the Community, its Member States and other western countries.

### New Community Initiatives

The pace of change in east Europe, the expectations of the peoples concerned and of their governments as well as the Community's own interests in the political and economic future of Europe now require the Community to take further initiatives.

These should provide support for reform and should complete the Community's network of agreements with the countries concerned. As democracy and economic liberalisation take root, the agreements can be applied flexibly, as with the acceleration of the dismantling of quantitative restrictions applying to Poland and Hungary. Already the Community has concluded trade and cooperation agreements with Hungary, Poland and the Soviet Union in addition to more limited agreements with Romania (1980) and Czechoslovakia (1988).

In December, the Council authorised the Commission to open negotiations for a trade and cooperation agreement with the German Democratic Republic; it is expected that these negotiations will be completed within the first half of this year. The Commission fully subscribed to the declaration of the Strasbourg European Council on the self-determination of the German people. This principle is enshrined in the German Basic Law of 23 May 1949 and is reflected in the protocol to the Treaty of Rome on Inner-German trade. Meanwhile the German Democratic Republic is to be viewed by the Community and as a specific case.

The development of bilateral relations with the countries of central and eastern Europe should take place within the framework of an overall Community policy. Once the first generation of agreements is complete, the Community should respond positively to aspirations for closer links with the Community by means of a form of association. Association agreements with the countries of central and east Europe would have common elements covering trade, cooperation and financial support, modulated according to the needs and the capacities of each country as well as its progress towards open political and economic systems. With respect to trade, such agreements would aim at attaining free trade when the conditions for this were right. In this way the countries concerned could eventually be linked to the wider European framework which the Community and EFTA are now in the process of developing.

There is a common interest on the part of the Community, its neighbours and all states sharing its fundamental values in ensuring that reform in east Europe does not founder. This will require further financial efforts by the Community to support economic restructuring in east Europe. As demonstrated in the case of Poland and Hungary, Community funding acts as a catalyst, bringing forward contributions from other sources with added cumulative effect.

The Community must now equip itself with the budgetary instruments needed to ensure an adequate response to the needs and the requests of our neighbours. New policy instruments should also be developed in such areas as export credit and investment promotion and protection.

Winter has now set in and the Community should also be ready to respond rapidly to urgent requests from Poland and Romania for food assistance. Such assistance helps to satisfy immediate needs and contributes to restructuring by freeing resources for investment.



Against this background and bearing in mind requests from the countries concerned, the Commission will present to the Council shortly proposals along the following lines :

- with respect to Czechoslovakia, the Commission will complete exploratory conversations and present draft directives for the negotiation of a trade and economic cooperation agreement, which will replace the more limited agreement on trade in industrial products now in force; the new agreement should in principle be signed within the first half of this year;
- now that the Bulgarian authorities have repealed measures which undermined the human rights of a significant part of the population, negotiations for a trade and economic cooperation agreement should be brought to a satisfactory conclusion; the agreement should, in principle, be ready for signature during the first half of this year;
- with respect to Romania, the Community should respond positively to the Romanian authorities' decision to lift their country's reserves on the CSCE Vienna concluding document and to their request to establish diplomatic relations with the Community; the Joint Committee, provided for by the 1980 agreement, should be rapidly convened; this will provide a forum both to review existing trade relations and to discuss their extension; if necessary, the Commission will bring forward proposals to modify the 1980 negotiating directives to permit the negotiation of a trade and cooperation agreement similar to those concluded with other countries in central and eastern Europe; in principle the new agreement should be signed during the first half of this year; on the basis of commitments that Romanian food exports, notably to the USSR, will remain blocked, the Community should be ready rapidly to respond to Romania's request for food assistance;

- With respect to Poland, the Community should consider favourably requests for additional food assistance and should be ready to provide the necessary supplies rapidly; other aspects of cooperation underway with Poland should be maintained and strengthened;
- within the framework of the Group of 24, sympathetic consideration should be given to requests from the Czechoslovak, Bulgarian, and Romanian authorities that coordinated assistance should be extended to their countries; following the declaration of Ministers of the Group of 24 of 13 December, the Commission will put forward arrangements for strengthened cooperation to ensure that the beneficiaries obtain full additional value from the efforts of the 24. Such coordination will be all the more necessary with the extension of the actions of the 24 to other countries in east Europe.
- the Council should consider favourably proposals from the Commission for adequate multiannual budgetary provisions to enable the Community to contribute significantly to bilateral and multilateral assistance for the countries of central and eastern Europe; the Council should also consider favourably proposals for Community action in the areas of export credit, investment promotion and protection;
- by lending its full support to the Helsinki process, while at the same time strengthening links with all its participants, the Community can help maintain stability and confidence which are essential conditions for peace and prosperity throughout Europe. This implies closer Community coordination within the framework of the CSCE. The Twelve should defend with determination and imagination a common position within the CSCE on issues in the second and third baskets regarding economic and industrial cooperation and human rights. This common approach should have an impact both at the forthcoming economic conference in Bonn and at the CSCE summit proposed by Mr. Gorbachev.