

András INOTAI *

From the Association Agreements to Full Membership?
The Dynamics of Relations Between the Central and
Eastern European Countries and the European Union

* general director of the Institute for World Economics, Budapest

Paper presented at the Fourth Biennial International Conference of the European Community Studies Association, May 11-14, 1995, Charleston, South Caroline, USA

Introduction

It is more than surprising how much the professional political and economic literature dealing with the relations between the European Union (EU) and the Central and Eastern European countries (CEECs) is dominated by an evident imbalance. On the one hand, there is a rapidly growing number of publications on specific but not necessarily strategically important issues, from the impact of trade policy measures through special areas of cooperation to an overall assessment of the Association Agreements. On the other, there is rather few evidence of different strategic approaches to the future of the European pattern of security, political, economic and social cooperation. This imbalance is the more striking because the history of EU-CEECs relations in the last years have provided an unprecedented dynamism of bilateral relations which has definitely not come to an end by the signing of Association Agreements (AAs).

It was less than seven years ago that, after a decade of deadlock, the joint declaration between the European Communities and the late CMEA was signed. This document opened the way for trade and cooperation agreements, with very modest potential improvements in real terms. The dramatic transformation of CEECs made these agreements obsolete practically overnight. The granting of GSP treatment, the starting of the PHARE programme and the signing of an AA followed within the next two years. As a result, all CEECs have substantially upgraded their position on the pyramid of trade preferences granted by Brussels to third countries (Inotai, 1994a). Once the AA was ratified (February 1994), Hungary and Poland almost immediately applied for full membership (April 1994), and other transforming countries are expected to follow this way soon.

Moreover, substantial changes have characterized the attitude of the EU, as well. Still, the AA does not contain any EU commitment to future full membership of any of the associated countries. Just the opposite, and very much against the interests of the CEECs, the EU has clearly stated that there was no linkage between present association and future membership. One year later, the EU summit at Edinburgh, and even more, the next one in Copenhagen have acknowledged the effort of the CEECs to become full member, if and when basic political and economic criteria, to be set by Brussels, were fulfilled (Inotai, 1994). The German presidency (second half of 1994) qualified future membership of the CEECs as one of the main priorities. Therefore, clear criteria for joining, further opening of the EU markets and the intensification of political dialogue were considered the most important policy steps to be made. Only three years after the refusal of potential future membership, the Essen summit in December 1994 has already fully taken into account the Eastern enlargement of the EU. Any more the question was about membership of the CEECs in the EU but about when and how, "only". In the meantime, associate membership in the Western European Union (WEU), the political and security body of the integration could materialize, and a comprehensive network of "structured dialogue" has started in several integration-relevant areas (foreign and security policy, domestic and legal issues, education, environment, research, telecommunications, etc.).

Partly, this dynamism has been incorporated into the time schedule of the EU for the next years. Negotiations on membership may start after the EFTA enlargement (January 1995) and the Intergovernmental Conference (IGC, in 1996 and possible also in 1997). Although, except for Malta and Cyprus, clear EU commitment to start negotiation has not been made up to now, but some CEECs are firmly insisting on beginning with these talks in the second half of 1997 or in early 1998, in the worst case.

This is, however, only the in-built dynamism into the process of decision making and institutional reforming of the EU. Substantial impetus can also be expected both from the CEECs and the internal developments within the EU in the next years. One has to be blind not to recognize that the dramatic changes in Europe which started in 1989 did not come to an end by 1995. Just the opposite, it is now Western Europe where changes, both for domestic and external reasons, are expected to become more pronounced. Evidently, we do not know the exact volume and direction of changes which are expected to shape the future of Europe. It is, however, obvious that the Western European political, security, economic and social status quo, as established in the late fifties and early sixties and based on a firmly divided Europe cannot be maintained.

This paper focuses on some of the fundamental future issues. Thus it does not deal with achievements and shortcomings of EU-CEECs relations as reflected by bilateral developments in the last years. More importantly, it tries to address the dynamics of developments and some of the major challenges European integration is likely to face well before the end of the century. Divided into eight chapters, the analysis starts with the adjustment criteria preceding CEECs membership (chapter I), to be followed by developments and special interests in sensitive areas, including the question of financial transfers (chapters II and III). Chapter IV looks at intermediate or alternative proposals to full membership. Special chapters are dedicated to the timing of membership and to the question whether accession should happen individually or in a group approach (chapters V and VI). Chapter VII examines the future of intra-European balance, while the last chapter offers some conclusions.

I. The Development of Adjustment Criteria

1. The Copenhagen criteria

At least partially urged by the Central European associated countries (ex-Czechoslovakia, Hungary and Poland), the EU, at its Copenhagen summit in the summer of 1993, has formulated some conditions to be fulfilled by the would-be members. This list, including stabilization of democracy and law; readiness to adopt the *acquis communautaire*, the establishment of an effective market economy and the adoption and fulfilment of the convergence aims of the Maastricht treaty, covers a wide but rather "soft" range of political, legal and economic conditions.

For several reasons, this set of criteria is an unprecedented step of the EU in comparison with earlier enlargements. For the first time, specific conditions have been imposed on acceding countries. The Treaty of Rome laid down only one condition: the entrant nation must be European. So the Copenhagen decision, in fact, discriminates against the transitional countries (Inotai, 1994b). Of course, there were prerequisites in the previous enlargements, too, but these only affected the conditions of accession, not the starting of negotiations and the very chances of joining. In this context, the question can be formulated whether the system of criteria can be considered as an instrument to facilitate membership, or, on the contrary, as a substantial barrier to future accession. In other words, does this concept help sustain the dynamics of European developments or, on the opposite, it tries to slow down, and if possible, even stop the dynamic forces of European reorganization set free after the collapse of the Berlin wall and of communism in Europe?

The Copenhagen set of criteria indicates the EU's interest in shifting future enlargements from political pressures towards economic merits. In fact, both Mediterranean enlargements were predominantly characterized by political motives. Paradoxically, after the collapse of the Yalta-based European security system, Brussels does not experience any short-term political interest in favour of the Eastern

enlargement. On the contrary, in the absence of such pressure, it tends to concentrate on the economic performance of newcomers.

In addition, and for at least two reasons, the associated CEECs are in a worse initial position than former applicants. First, they have to adjust themselves to a flexible, or even more, to an unpredictable EU. In consequence all criteria may be changing according to the changing situation and interests of Brussels and the member countries. Second, the integration standard of the EU is much higher today than it was a decade ago when the Mediterranean enlargement occurred. As a result, less developed CEECs, burdened with burning transformation problems should carry out a successful adjustment to a new quality of integration.

Last but not least, there are serious questions regarding the measurement of "integration maturity" as well. Should this maturity level be measured on the basis of virtual economic performance (static survey) or, more importantly, on the basis of the speed and quality of the adjustment process (dynamic assessment)? And, even if the first, static criteria applies, should macroeconomic adjustment or microeconomic developments be considered as more important? How can third country performance be compared with that of member countries, if the latter enjoy a very special status, from free market access to substantial financial transfers, while the former are largely deprived of these opportunities until they become full members.

2. The enlargement capability of the EU

Although the enlargement capability of the EU is one of the Copenhagen criteria, it has to be dealt with separately because it is just this factor that may substantially influence the future shape of Europe.

It has to be stressed that the viability of the European integration does not only depend on an Eastern enlargement. The original architecture of the EU was created for six to ten countries, more or less on the same level of economic development and political culture. Its profound restructuring has been overdue even without any future Eastern enlargement. Therefore the new integration framework is not (only) a precondition for further enlargement but a pressing requirement of survival for the "European anchor" of the international economy.

First, the EU has to respond to serious international challenges, as changing pattern of competitiveness, regionalization and globalization trends and technological developments.

Second, Brussels has to find an adequate answer to the dynamics of European processes. This, however, does not mean a shift in emphasis or another mix of policy instruments. On the contrary, a fundamental rethinking of the whole concept of integration and Europe is required. The decades-long status quo mentality based on the protection of Western values against an imperialistic Soviet empire should give way to an active, offensive and future-oriented attitude (Weidenfeld, 1995).

Third, most of the member countries are plagued by an "European disease", characteristic of the ex-socialist transforming economies as well. Two-digit unemployment, exploding budget deficits and state debts, obsolete agricultural and industrial structures, serious limits to finance the already achieved level of social welfare and a rapidly aging population can be mentioned as some of the outstanding negative factors.

Fourth, and most unfortunately, these external and internal challenges affect the EU at a time where, mainly as a result of internal developments, the integration itself is facing new problems. The concept of integration developed in the Maastricht treaty seems to be outdated under the present conditions in Europe. More importantly, the integration pattern based on priorities of the fifties and sixties (e.g. iron and steel community, customs union and agricultural self-supply) cannot efficiently answer the challenges at the turn of the century. In addition, as recent referenda tell, popular support for a large Union, as conceived by Brussels and some politicians from member countries, is much less than desired ("democracy deficit").

Finally, for the first time in its history, the EU is facing an increasing balance-of-power crisis due to German reunification, EFTA enlargement, Central and Eastern European association and highly

unpredictable Russian developments, all of them part and parcel of the emerging dynamics of European politics and economics.

The capability of the EU to further enlargement has to be assessed in this framework. Key importance will be attached to the handling of new "fault lines", as the definition of the "finalité" of the European integration, the managing of the North-South conflict or the control of the internal balance of the Union (Dauderstädt and Lippert, 1995). The Intergovernmental Conference (IGC) is expected to deal with some of these issues. It is, however, unlikely that it will be able to develop a completely new pattern of European integration. It has to be noted that there is no contractually fixed linkage between its success and Eastern enlargement. The only link, at the moment, is that negotiations on further enlargement will not be initiated before the IGC.

3. The forthcoming White Book

Still under German presidency, Brussels has promised to produce a White Book containing more elaborated conditions of membership

for new applicants. This set of criteria is expected to be published shortly. Preliminary reports indicate that the experts will not be able to go beyond setting general and not binding conditions. For political and economic reasons, no recommendations will be provided how applicants should go from their present status towards full membership, and how the EU would support this process. Neither a clear timetable will be offered (Altmann, Andreff and Fink, 1995). Although the EU has already acknowledged the fundamental differences among CEECs, no "geographic sequencing" of an Eastern enlargement will be envisaged. In sum, the underlying philosophy of the White Book will remain the old one. It will contain adjustment requirements for applicants without taking into consideration the changing European dynamics and claim for a mutual adjustment process coupled with EU support during the period of preparation for accession (Inotai, 1995).

4. New obstacles to membership?

To be sure, none of the transforming economies is ready for full membership at the moment. However, most of them have made substantial progress in the last years, and their adjustment capability and transformation dynamics proved incomparably higher than that of Western Europe. In some areas they are at least on the level of some EU members (Altmann and Ochmann, 1995). In other, mainly economic areas their adjustment performance has been overshadowed by the transformation crisis. However, as the old problems fade away, a more competitive economic structure is emerging at least in the Central European countries. Industrial restructuring is on the way, the share of agriculture is decreasing, the service sector is rapidly progressing. Intra-industry trade is growing dynamically, and its share in the CEECs exports is already higher than in that of some member countries. Also their favourable human factor endowment is coming to the fore.

Looking at these trends, it may be increasingly difficult to argue against their membership because of major political or economic reasons. Such an attitude is being made even less acceptable as some of the CEECs seem to be more in line with adjustment to the EU principles than some of the member countries are. If, thus, Eastern enlargement should nevertheless be postponed, new ideas have to be found in order to explain why the CEECs would be still not able to join the EU.

These barriers are taking already shape in various forms. According to the most recent French position, new entrants should immediately cope with the prescriptions of the Social Charter and with the environmental rules. Other ideas include the examination of the exchange rate in the CEECs, the elimination of any major (even temporary) gap between productivity and wage growth, and a linkage between foreign direct investments and employment in the capital exporting countries.

It is not difficult to identify the common roots of all of these measures, which is a growing fear of competitiveness throughout Western Europe, but particularly in the less prepared member countries of the EU. In consequence, the impression of experts from the CEECs is getting support, that adjustment criteria have not been formulated in order to fulfil them but in order to maintain the doors of the Union closed to the transforming economies as long as possible.

II. Sensitive Issues on the Way to Full Membership

1. Free trade

Except for agriculture, the complete elimination of trade barriers is foreseen by the Association Agreements. In a ten year long and asymmetric process tariffs and non-tariff barriers have to be abolished on both sides. It is generally considered that free trade in industrial products belongs to the hard core of criteria for membership. At the same time, little attention has been paid how sensitive this issue may become as a consequence of economic and social developments that cannot be fully ruled out.

The associated countries may be challenged by two major adverse developments. First, the process of asymmetric elimination of trade barriers approaches its second stage, in which the CEECs will have to dismantle the still-existing restrictions. In other words, after 1995 to 1997 a "reversed asymmetry" will be built up, where the transforming economies will have to accelerate their process of trade liberalization, including most of the sensitive areas. For various reasons, this is a more difficult task for the transforming economies than for the EU. Average tariffs are generally higher in the CEECs than in the EU. Therefore the impact of tariff dismantling is expected to be more substantial for domestic production than in the case of the EU. In addition, and parallel to the global tariff reduction process, the EU developed a highly efficient "secondary wall of protection" consisting of a jungle of technical norms, environmental, veterinary and sanitary prescriptions, etc. Such a non-tariff protection hardly exists in any of the CEECs. Therefore, without taking quick and similar policy measures, the elimination of tariffs would result in a much more vulnerable situation for Central and Eastern European producers than for their EU counterparts. This vulnerability is further exacerbated by the fact that, as of 2001, free trade would cover 96 per cent of EU exports to the CEECs, but only about 70 to 80 per cent of the CEECs exports to the EU, for agricultural products are not included.

One has to be increasingly aware of the political and socio-psychological repercussions which have been emerging most recently. After the first years of overhasty trade liberalization in an extremely adverse economic situation plagued by the collapse of the Eastern markets and the dramatic shrinking of domestic demand, the transforming economies are now experiencing a growing pressure of protectionist lobbies consisting of domestic producers and foreign-owned firms located in the region as well (Inotai, 1994a).

Secondly, temporary asymmetry in bilateral trade relations was not able to produce a sustainable trade surplus for the CEECs. After an initial boom of exports, due to a number of domestic and external factors, imports from the EU started to grow much more dynamically than exports to the EU. Most importantly, the higher level of economic development, much stronger bargaining position, financial solidity, better marketing methods and generally the competitive strength of EU companies have more than compensated the initial(ly expected) impact of asymmetric trade liberalization. In other words, the "development asymmetry" proved stronger than temporary and rather selective "trade asymmetry". The Western European recession of 1993 has given a special impetus to this adverse development, as it boosted EU exports and slowed down imports.

The inevitable consequence was a rapidly growing trade deficit of all associated CEECs with the EU. While between 1989 and 1993 the EU has accumulated a five-year trade deficit of more than ECU 205 bn in its trade with non-EU countries, there were two bilateral trade relations in which the EU could register a trade surplus. Beside the Mediterranean, characterized by traditional EU surplus, it was the trade with the Visegrád Group which helped improve the EU's trade balance by more than ECU 7 bn between 1991 and 1993 only. As a result, the sustainability of trade liberalization crucially depends on the capacity of the transforming economies to finance growing trade deficits with the EU. Temporary or lasting balance-of-payments problems, at least partially caused by the growing imbalance of trade with the EU could slow down or even stop the process of trade liberalization stipulated in the Association Agreements. Under some circumstances, this could be interpreted by Brussels as a lack of "EU maturity" of some CEECs.

Simultaneously, sensitive areas of trade relations can also be identified on the EU side. The still very restrictive market access for agricultural products of the CEECs is just one example. It cannot be completely ruled out that the rapidly growing competitiveness of the CEECs in selected areas, would increase the protectionist pressure within the EU as well. Acute tensions on the labour market of several EU countries, or real or alleged implications of adverse economic developments on essential political processes can further reduce the EU's readiness for maintaining free trade with the transforming countries.

Another factor which may decrease the EU's interest in Eastern enlargement can be the temporary shrinking of the CEECs' import market as their balance-of-payments situation deteriorates. The sensitivity of future trade relations could substantially be reduced if the EU recognized the necessity of financing the natural "modernization deficit" at least in the more progressing CEECs. In the next years, all CEECs will require huge investments in order to create a modern production and export structure. A large part of the investment goods will be purchased abroad, and there is little doubt that the EU (and foreign companies located in the EU) will be the basic supplier. According to international experience, in the first years of economic modernization a rapidly widening trade gap can hardly be avoided. Restrictions on the exports of available (agricultural) commodities make this problem more serious. Assuming a high efficiency of investments and an export-oriented economic policy in the CEECs, this gap can be narrowed or even closed in the medium term. It is, however, by far not clear, how the emerging "modernization deficit" will be financed in some of the most critical years of transformation.

2. Adjustment to the *acquis communautaire*

The second hard core of future membership is the acceptance of a constantly increasing package of EU rules and regulations. Some of the CEECs have already started this adjustment process and have been integrating the EU rules into their national legislation. Nevertheless, legal adjustment, for several reasons, cannot be completed before membership.

First, none of the present member countries was able to prepare itself fully for membership before accession. In all cases, there were and still are important derogations which enabled both the new member and the EU to gradual adjustment. Taking into account the development gap between the EU and the CEECs, and the sensitivity threshold of the latter burdened with the unique tasks of transformation, the difficulties of the adjustment process become manifest. Therefore a clear medium-term strategy, elaborated jointly by the applicants and Brussels, would be needed.

Second: part of the *acquis communautaire*, the so-called primary laws, can only be implemented once a country has become member of the EU. The whole package of the common agricultural policy belongs to this area.

Third: the EU itself is in a constant change with unpredictable outcome. It would be a serious mistake to make a sometimes economically and socially costly adjustment to something which will be changed before the CEECs may become members of the Union.

3. Agriculture

While most experts do not devote special attention to the sensitivity of trade relations and of legal adjustment, there is a widespread consensus that agriculture will be one of, if not the most sensitive area which could hinder or substantially delay the Eastern enlargement of the EU. Of course, there are substantial differences among the individual CEECs. At the moment, only Poland and Hungary are meaningful exporters of agricultural goods, while agriculture is not a major negotiation issue for the Czech Republic.

For the first time after 1973 when Ireland joined the integration, the accession of most CEECs challenges the producers of continental commodities. These countries happen to be the most influential members of the EU who have not only largely benefitted from the common agricultural policy (CAP) but consider the maintenance of this system crucial for their domestic political balance as well.

Although it is generally acknowledged that the present system of agricultural support cannot be maintained, and both budgetary problems of the Union and international obligations deriving from the Uruguay Round documents make a reform of the CAP unavoidable. However, even the most radical transformation plans, vehemently opposed by influential lobbies within the EU, fall considerably short of the transformation which would be needed to absorb the expected impacts of an Eastern enlargement.

A further problem consists in the fundamental behaviour of the EU which, as some experts in the CEECs have always feared, has considered the CEECs as an additional market for highly subsidized EU agricultural goods and not as a low-cost supplier of EU markets. In fact, the most dramatic developments reflecting the most extensive "reversed asymmetry" took place in the agricultural trade between the EU and the CEECs in the last five years. At present, except for Hungary, all CEECs are net agricultural importers in their bilateral trade relations with the EU. Also Hungary's traditionally substantial trade surplus started to shrink rapidly. In addition, subsidized EU exports and food aid packages to the successor states of the Soviet Union have largely devastated traditional agricultural markets of the associated CEECs.

Looking at the present situation in the agriculture of the transforming economies, the EU's fear of "Eastern competition"

can hardly be justified. For several reasons, agriculture became the sickest sector in all CEECs. The share of agriculture in the generation of GDP fell dramatically, from about 15 to 20 per cent to less than 10 per cent, which is not higher than in the less developed EU countries. Similar tendencies can be observed in the pattern of the labour force. Of course, some CEECs, notably Poland and Hungary, still have a substantial production and export potential, but some of the basic preconditions, as efficient production structure, money, technology, marketing organizations are missing. Therefore, as seen today, the real problem of an Eastern enlargement is not so much how to integrate a highly competitive Eastern agriculture into the system of the CAP, but how to finance those regions which, as a consequence of declining or already eliminated agricultural production are becoming poorer and poorer.

Most experts are convinced that a sound and competitive Central and Eastern European agriculture would cost less to the EU than a devastated one. Calculations have to consider not only direct agricultural impacts but also the impact of agricultural production on several other areas (financing of imports from the EU, employment, regional development, political stability, etc.). Starting from such an assessment, a coordinated plan should be designed in order to combine the restructuring of agriculture in the EU with restructuring in selected CEECs. In this way, the costs of adjustment could be substantially reduced and some of the essential barriers to future membership cleared. In addition, the impact of an Eastern enlargement on the agricultural budget of the EU would be moderate.

4. Manpower

The highly sensitive issue of the free flow of labour has not been regulated by the Association Agreements, for this topic still belongs to the competence of the member countries. Therefore, the flow of labour has to be settled in bilateral negotiations with the individual EU countries. At the moment, only Germany (and the newcomer Austria) has signed such a document, and even in this case, the yearly quota of Central and Eastern European labour to be employed in Germany is decreasing. It can be predicted that the issue of free flow of labour will be one of the fundamental areas where the EU will apply a long period of derogation, as it was the case with the (second) Mediterranean enlargement, too. This restriction will, however, be differently felt in the individual CEECs. The problem is much more important for Poland and Romania than for the Czech Republic or Hungary.

There are two special aspects of this issue, however, which matter for all CEECs. On the one hand, the first stage of Eastern enlargement may occur at a time of two-digit Western (and also Eastern) European unemployment. On the other hand, labour problems are not confined to unskilled or low-skilled labour, as it was the case with the guest workers coming from Southern Europe in the sixties and seventies. More importantly, the real competitive pressure is expected to come from the (highly)

skilled labour with clear competitive advantages both in their wage level and, in several cases, also in their "skill flexibility".

It is not unlikely that EU restrictions on the free flow of labour will further strengthen the flow of capital to the CEECs not only in traditional but also in new, skill-intensive sectors, as the wage (and productivity) differences are becoming more manifest in the latter. This could contribute to accelerated economic development and quick adjustment to the EU more than the reinvention of a new "guest worker system". What is not yet clear is the future answer of EU governments and trade unions to the increasing flow of capital, and with it, the (alleged) "export of employment" to the CEECs. High social and environmental standards, as mentioned in the first chapter, are an early indication of the potential behaviour of some pressure groups which can cause some difficulties for the eastward enlargement of the EU.

III. Financial transfers

At least based on most recent literature on the possibilities of and the limits to an Eastern enlargement, all difficulties listed above are dwarfed by the financial needs of such a decision.

Beyond any doubt, all CEECs, in their present situation, would be net beneficiaries of the currently working EU transfer mechanism. Most of them would be entitled to get money for their agriculture, and all of them would be net receivers of the structural, cohesion and regional funds.

It can easily be understood that the present member countries who are net beneficiaries of the system strongly protest against any kind of enlargement which would deteriorate their present position and hurt any of their vested interests. They would oppose any enlargement which would lead to any kind of redistribution of the existing funds. There is nothing new in it, the same had happened with earlier enlargements as well.

The really new development is that the mechanisms which were able to remedy the above problems in earlier periods, do not seem very likely to work in the second half of the nineties. First, the net contributors to the EU budget are not ready to commit themselves to "recapitalize" the existing funds and create extra resources for the CEECs, without hurting the vested interests of other net beneficiaries of the system. Just the opposite is happening, for most of them would like to reduce their contribution, as they struggle with serious internal imbalances. Neither their high or even growing budgetary deficit and an exploding state debt, nor the strong adjustment criteria to be fulfilled in order to become member of Maastricht-Europe allow a meaningful scope of financial activities. The most important country which is strongly interested in Eastern enlargement has been struggling for years with the astronomical costs of German unification. Second, earlier enlargements were regularly accompanied by the creation of a new fund tailored to the applicant(s), in order to avoid conflicts which could have been caused by a major redistribution of previously committed resources. At present, no such an initiative seems to be financially feasible, even if it were not difficult to find a number of justified "labels" for it ("modernization fund", "pre-accession fund", "physical and human infrastructure fund", "stability fund", "regional development fund", etc.).

The situation is complicated by three additional factors, which may increase the total costs of Eastern enlargement. First, there is a widespread fear in the EU of the unexpectedly strong competitiveness of the CEECs in a wide range of commodity markets. At a time of high-level unemployment and substantial social and political resistance to structural changes in the EU, influential interest groups will do their best to get some kind of compensation as a consequence of Eastern enlargement. Second, also the currently net beneficiary member countries will present their bill, as they have already done it shortly after the signing of the Association Agreement and the coming into force of the PHARE programme. In fact, they have got several times more additional money than what has been envisaged for the financing of the transformation in the CEECs. Finally, the Essen meeting has provided a first indication of an emerging political struggle between advocates of an Eastern enlargement and those

preferring contacts with the (Southern) Mediterranean. The growing fear of Islamic fundamentalism and, more directly, the interest in maintaining the increasingly delicate balance between France and Germany may require substantial "political compensation" expressed in financial terms for North Africa in exchange for any Eastern enlargement. Summing up, the total costs of an Eastern enlargement may turn out much higher than the resources to be virtually directed towards the applicant countries.

But there is an extremely large gap also in the calculation of the direct costs themselves. Figures fluctuate from ECU 18 bn to over ECU 100 bn annually. It is not difficult to discover political considerations behind the calculations. The higher the amounts are, the more the experts try to point out why an Eastern enlargement is impossible or at least unwanted. Although most of the unreasonably high figures turn out to be the result of serious miscalculations, and they may be even withdrawn. However, once published they start their independent life, and will have a lasting impact on the mentality of policy makers. Both for economic and political reasons, and both in the interest of the EU and in that of the CEECs, it would be highly recommendable to rule out politically motivated "scientific approaches".

Any realistic assessment of the potential costs of an Eastern enlargement has to take into consideration the following elements.

First, all calculations based on the present transfer mechanism of the EU are exaggerated because none of the CEECs believes in the financial capability of the EU to extend this system without any major reform to the new entrants.

Second, an assessment of the economic performance of the CEECs cannot be realistically based on old figures, as it often happens with their agricultural potential based on the late eighties. Neither can all present figures considered realistic, because such an approach ignores the development which is expected to take place before full membership materializes. In this context, per capita GDP, as a key indicator of entitlement for transfers from the regional and the cohesion funds, has to be mentioned. To be sure, at present all CEECs are entitled to such transfers, but some of them may get out of this framework in a shorter than expected period, because GDP per capita, as expressed in ECU terms does not only depend on GDP growth rates but, sometimes to a larger extent, on the appreciation of the national currency, a general consequence of economic recovery and structural upgrading.

Third, there is no plan that would envisage a "bloc accession" of all CEECs to the EU. Therefore, all reliable calculations have to make it clear that the individual CEECs will be entitled to a substantially different amounts of net resource transfer from the EU budget. Therefore, any overall estimate or the frequently used "basket principle" is hurting the interests of the individual countries, in general, and the interests of those who are expected to become full members sooner, and would cause less resource diversion than others, in particular.

Fourth, no comparison can be made between the financial requirements of German unification and the resources to be needed by an Eastern enlargement. The CEECs did not become part of another country, they did not give up their national currency, and, most importantly, they very well know that they cannot reach West German living standard in the foreseeable future. For economic, political and psychological reasons, the financing of their modernization is much less expensive. Neither can the CEECs be compared with the financial requirements of Russia or the Ukraine.

According to realistic calculations, Poland would need an annual net transfer of about ECU 5 to 7 bn, the Czech Republic and Slovakia ECU 1.5 to 2 bn each, and Hungary ECU 2 to 3 bn. Thus the Visegrád Group would require EU financing of ECU 10 to 16 bn annually. This would increase the annual budget of the EU (about ECU 70 bn) by 15 to 23 per cent, provided that the Visegrád countries could join the EU at the same time. Between 1993 and 1997, the four less developed EU member countries, with the same level of population as the Visegrád Group (about 64 mn) get an annual transfer of ECU 18 bn from the structural and cohesion fund only (Nötzold, 1994). The calculated total transfer to the four Central European countries would be 60 to 90 per cent of this sum. Finally, a one-

percent growth of the EU means a GDP increase by about ECU 67 bn. In the next years, a rapid and sustainable growth of about 3 per cent can be predicted. The establishment of a special fund to be devoted to the financing of Central Europe's economic modernization would need less than a quarter of a one-percent economic growth within the EU.

The timing of the financial transfers is extremely important. The CEECs would need this money earlier than they may become members of the EU. The financing of the pre-accession period is crucial for several reasons. Such a mechanism could partially finance the emerging modernization costs and maintain the momentum of economic and social transformation and its political support. At the same time, it would be a clear sign that the EU is really committed in an Eastern enlargement. Most importantly, however, such a fund could contribute to the financing of those industrial and infrastructural investments which would substantially enhance the development level of the CEECs, a precondition for efficient membership on both sides. In addition, the financing of a successful preparation would decrease the amount of transfer that would be necessary following accession.

In order to implement such a policy, some basic strategic decisions have to be taken. The EU has to answer the fundamental question, whether the financing of modernization or that of constant instabilities would cost more. The first option has a better chance to create sustainable security and development, increase European competitiveness on the global scale, while, certainly, it would also strengthen adjustment pressure in Western Europe. In turn, a "strategy" based on repeated damage limitation requires much more money, without eliminating the roots of instability, and, more importantly, without creating the "grass-root cells" of modernization. The dynamics of European development will not allow to delay very much this decision between financing (painful) modernization or financing a minimum level of social welfare promising short-term stability. The EU's answer to this challenge will not only influence the future of Eastern enlargement but, at least to the same extent, the future of the EU as well.

IV. Transitory Concepts Between Association and Membership

The preceding chapters have pointed out some of the most sensitive areas of the adjustment and preparation process both in the transforming countries and within the EU. It is not surprising that, taking into account these difficulties, a wide range of suggestions has been developed in order to bridge over the time gap between the present status and future objectives. All of these recommendations are based on the common assumption that the European dynamics will not produce any dramatic and sudden shift in the current balance-of-power pattern, and, more importantly, Russian political developments will remain sufficiently predictable and under control. In other words, there will be no reason for an emergency access to the EU of the CEECs.

Practically all such suggestions have been formulated in the EU. In turn, the associated countries consider a direct linkage between association and full membership and treat the association agreements as a stepping stone towards future membership. Consequently, they are rather suspicious regarding plans splitting or threatening to split this linkage.

One of the general Western European argument is that the transforming economies have to reach the average level of the EU before becoming full member. This has, however, never been the case in any integration scheme, and particularly not in the EU. The argument has to be reversed. All applicants would like to become full member of a more developed and prosperous integration because they consider membership as an instrument to achieve a higher level of development. In the same line goes the concept of regional integration preceding membership in the EU (see Chapter VI in more detail). Also Baldwin's idea of an "Association of Association Agreements" (Baldwin, 1994) can be refuted on the same grounds.

The second set of transitory measures tries to split economic and security issues. This is particularly manifest in French approaches, including the Balladur stability pact. From a short-sighted Western

European point of view this concept is understandable, for the EU would like to achieve the highest level of security without the need to co-finance the economic modernization process in the CEECs. This attempt is based on the fatally erroneous assumption that stability in Europe can be sustained without fundamental economic modernization at least in Central Europe. As long as the latter fails to be achieved no lasting stability on the continent can be created (Inotai, 1994c).

The third approach offers full membership in some areas (mainly in those which are of key importance for the EU, as security and political cooperation), but exclude the new members from other areas which would be vitally important for them. Membership without participation in the common agricultural policy or membership without financial transfer are the two most important suggestions. It goes without saying that such an approach is unacceptable for the CEECs.

There are also plans which recognize the importance of economic issues for the CEECs but try to manage them in frameworks different from the EU. In this context, membership in the OECD, the creation of a new EFTA or the joining to the European Economic Area can be mentioned. Although some of these frameworks, mainly that of the OECD is an important policy issue, and may even be a precondition for EU membership, they do not substitute the EU in two basic areas: agricultural trade and financial transfer.

Finally, the CEECs do not share the idea which emphasizes the importance of the European cultural identity and a common value system without supporting the economic modernization in the transforming economies.

At least at the first glance, there is a more common view that the way from the present association status to full membership in all aspects will be a long period. It is, however, extremely important what section of this long preparation period will be implemented before membership, and what section will be carried out by the transforming economies as new members of the EU. All new entrants, including the highly developed ones, have got long derogation periods, and also the EU needs some time for adjustment to integrate the new members fully. It will not be different for the CEECs either. Even more, some adjustment tasks can only be implemented once a country is member of the EU (e.g. common agricultural policy).

One of the most widespread arguments covers the relation between deepening and widening. Those who give priority to deepening argue that only a strong and united EU can provide the necessary support for the transforming countries and could absorb the problems that are likely to arise as a result of Eastern enlargement. In addition, a premature Eastern enlargement could easily dilute the EU and threaten even the already achieved level of integration. This argument is based on the assumption that the dynamics of deepening is much stronger than the dynamics of European restructuring. Experience gathered in the last years does not prove this hypothesis. If the EU does not consider the new European dynamics adequately in its strategic plans, it can easily face tremendous challenges not only from outside but also from within the EU, mainly in the form of growing German dissatisfaction with the integration. The danger of - at least temporarily - diluting the integration is real, but so is the danger of disrupting the Union as well.

From the point of view of the CEECs, those plans of preparation for full membership seem to be convenient which are jointly designed by the individual CEECs and the EU. A clearcut pre-accession strategy is needed, for this can substantially decrease the costs of enlargement both for the applicant and for the old members of the Union. This plan should be gradual in three directions: time, geography and contents. In other words, it has to offer a clear timetable spreading from the present situation until full membership, integrate the individual CEECs step by step, and contain a list of derogations.

It cannot be ruled out that a feasible modernization plan to be financed by the EU could substantially reduce the present pressure on the EU for quick Eastern enlargement. The CEECs look at the EU as their economic modernization anchor. However, if they could get most of the resources needed for a medium-term modernization strategy (mainly free access to the EU's agricultural market and

substantial modernization transfers), perhaps the question of membership could be temporarily postponed by some years.

V. Is a clear timetable necessary?

As long as, however, such an approach lacks reality, the issue of setting a clear timetable for membership remains on the agenda.

EU officials have repeatedly refused to identify the exact date of Eastern enlargement. They were not ready to make any commitment which could not be fulfilled, either because of the low level of adjustment and performance of a CEEC or as a result of the EU's internal problems. In addition, the setting of a fixed date could cause political problems. If one date only will be set, there is a danger that no differentiation can be made among the CEECs, so that enlargement will only be feasible as a group accession. If, however, different dates were given to different countries of the region, the EU could easily contribute to further splitting the transforming region, which is definitely not Brussels objective. It is obvious that Brussels would like to avoid such traps.

On the other hand, there are powerful arguments in favour of establishing a fixed timetable for future membership. It would provide a fundamental political, economic and psychological support to the transforming economies, just in one of the most painful periods of transformation. In political terms, the consolidation of democracy and the control of nationalistic (and, to a much smaller extent, extremist) movements can be mentioned. In economic context, CEEC governments could get support against growing pressure by protectionist lobbies. In psychological terms, the way out of the transformation crisis badly needs a credible vision. Reaching EU membership could be such a vision.

Not less importantly, a clear timetable could substantially reduce the costs of adjustment to future membership on both sides. By establishing a final point, it would create adjustment and cooperation pressures on both sides in order to fulfil all necessary requirements before accession takes place. Costly and dangerous ex-post adaptations could be largely avoided. Also more room would be provided in influencing the reform process of the EU itself. Finally, and according to international experience, a fixed date could become a relevant factor of attracting strategic investors from different parts of the world. Once potential investors can be sure of the future status of a (small) country, its locational advantages will substantially increase. More foreign direct investment would decrease the importance of financial transfers from the EU to the CEECs, as the relevant part of the "modernization deficit" could be financed by foreign investors.

Once would-be members are well on the way to full membership, the relevance of the previously fixed date is likely to become secondary. The dynamics of the process will be more important than an eventual delay of some months or a year in the date of membership. Therefore, setting a date would not be counterproductive, if it can generate confidence in future membership and accelerate the process of adjustment.

VI. Individual or group accession?

Immediately after the unprecedented changes in Central and Eastern Europe, the EU tried to convince the transforming countries that they should cooperate first of all among themselves and consider (sub)regional integration as a stage in their way towards the EU. Although in a rather "soft" way, subregional cooperation has been considered as a precondition for EU membership.

For a number of reasons, the CEECs were unanimously against this approach. It was not only their rich and negative experience with the CMEA, the largely competitive and not complementary production and export structure, as well as similar macroeconomic problems of the transformation process that forced them to reverse the sequencing between subregional and EU integration. Most importantly, they

have seen the time coming where, after decades, they would be able to intensify economic relations with more developed countries from which a substantial contribution to their several times delayed modernization needs has been expected. Also, the pattern and sequencing of subregional and European integration has given rise to the not totally unfounded view according to which the EU wanted to limit the CEECs' competition in Western Europe by persuading them about the benefits of subregional cooperation.

Evidently, subregional cooperation among the CEECs is important. However, economic modernization and export-driven growth can only be achieved through a decisive orientation towards the main and more developed markets. Similar to experience with successful modernization in East Asia, and partly also in Latin America, integration into the EU was given priority over subregional cooperation. The latter was considered as an important element of enhancing exports after, and not before, and even less, instead of, membership in the EU. Also, intraindustrial trade with EU countries was considered as a precondition for the upgrading of subregional cooperation.

Evidently, the EU had justified reasons for treating the CEECs as a bloc, or, at least, as a unit. Its rather superficial knowledge of the region, sweeping changes everywhere, the survival of bloc mentality as a heritage of the cold war period and more recently, the EU's self interest in protecting the Western European markets against competitive CEECs products provide sufficient arguments in favour of such attitude. In a more positive sense, Brussels has also reckoned with the political sensitivity of any effort to divide the otherwise rather divided region more openly.

For several years, the EU has always avoided any clear statement on the diversity of Central and Eastern Europe. Even when entrepreneurs and politicians became fully aware of the huge differences among CEECs, the political rhetoric did not change at all. Today, Brussels is using a double pattern consisting of bloc mentality on the one hand, and of a very cautious distinctive approach, on the other. The EU very well knows that the region cannot be officially declared split. At the same time, any unification of the region would immediately produce harsh protests from those who, "fed up" with their experience with the CMEA, are unwilling to join a band wagon pattern in which the least developing country is determining the future and the integration maturity of the whole region. It is obvious that future Eastern enlargement, if it takes place, cannot be but gradual, both because of the rather different development level of the potential member countries and the highly different costs to be involved in enlargement of the individual countries. The economic requirements of modernizing Central and Eastern Europe cannot be financed at the same time on the same level even because of the financial limitations and the scope of virtual interests of Western Europe.

The most important reasons, however, for an individual treatment can be found in the rather diverging starting conditions of the specific transforming countries. First, and probably most importantly, the collapse of socialism and Soviet domination resulted in the emergence of historically developed economic, political and civilization patterns across the region. This first fault line roughly draws between the Visegrád countries of Central Europe and the other transforming economies. Second, also the Visegrád countries have achieved different levels of macroeconomic stability and, more importantly, microeconomic maturity (as a good test, see the rather different behaviour of foreign direct investments in the region). Third, the political vulnerability and sensitivity of the individual countries differs a lot. For instance, Slovenia and the Czech Republic have completely different security problems than Poland. In turn, both Poland and Hungary have a much bigger role to play as an East-West and North-South transit country than most of the other CEECs. Also the share of sensitive products is different, with relatively high role of industrial goods in the Czech and Slovak Republics, and of agricultural commodities in Hungary or Poland. Due to the level of development measured in GDP per capita, the structure of production and the size of the country, the financial requirements to be met by the EU are highly diverging, with the Czech and Slovak Republics, Hungary and Slovenia representing the group of countries with the lowest level of potential support. In addition, also the nature of support differs with different levels of development, mainly at the microeconomic level (e.g. more investment-oriented support in Hungary vis-à-vis the priority of technical assistance in some other countries).

Considering this complicated situation, the Realpolitik of the EU should focus on three major issues.

First, it has to provide a clear timetable of accession for each CEEC. A credible period of time should be identified within which all or most countries are expected to become members of the EU. Without specifying which country when is set to enter the Union, the definition of this time period does not produce any inconvenience either for the EU or for the CEECs.

Second, any gradual Eastern enlargement, as a high probability alternative against bloc enlargement, has to keep the new external borders of the EU as open as possible. This is both in the interest of the EU and certainly a vital interest of the joining CEECs, particularly, if their accession to the EU would, at least temporarily, mean the "sacrificing" of strong ethnic and nationality linkages (large minorities living in not-yet-EU member countries).

Third, any gradual Eastern enlargement should be preceded and accompanied by Brussels' regional support to the whole group of CEECs. This resource transfer should focus on regional infrastructure and the shaping of specialization patterns that can lay the ground for future intraindustry trade also among the CEECs.

Although current arguments are in favour of individual treatment and of a gradual Eastern enlargement, several questions remain open and dependent on the partly unpredictable European dynamics. Based on experience with previous enlargements, both for political and administrative reasons, it is likely that also the next enlargement will simultaneously involve various countries. However, negotiations on membership conditions will be carried out strictly on bilateral level, between representatives of the Commission and the would-be member country. However, neither a (partial or total) bloc accession, under specific conditions, can be ruled out. This could be the case if the CEECs, as a region would be vitally threatened by developments in Russia and the Ukraine, and/or regional instabilities would strongly challenge the EU, in general, and its most powerful and, at least in security terms, most vulnerable country, Germany, in particular. Much less attention has been paid to the not fully unlikely development that a (partial) bloc accession will be forced out by different EU members in order to sustain the real or perceived internal balance of the enlarging Union. In this context, German economic, security and political interests in integrating Poland, the Czech Republic and Hungary could be compensated for by overwhelmingly political interests of France in letting Romania join at the same time.

VII. Eastern enlargement and the future of European balance

This issue, however, is leading us to the outstanding external factor affecting the chances of Eastern enlargement in the next years (or even in the next decade).

The EU has been undergoing unique shifts in its internal and external balance-of-power pattern in the last years. Domestically, the French-German pillar had been the key stability and development factor of the integration, both in its periods of deepening and widening. French-German cooperation was needed not only in order to stabilize the integration process during some of its difficult stages (agricultural policy, monetary issues and exchange rate policies, industrial restructuring, budgetary and financial transfer framework, etc.) but also to provide the necessary impetus to push the integration undertaking forward (single market, political and military cooperation, Maastricht, etc.). In its external relations, potential French-German dissent remained rather limited by several factors. Primarily, the stable (or frozen) European balance of power pattern did not generate any major dispute among EU members, as the integration was considered a solid component of the post-1945/1948 global and European order. The security of Western Europe was adequately guaranteed by NATO. The EU's economic development was supported by achievements of the integration process, by strong, although slowly eroding transatlantic links, and by the global involvement of most national economies. Attempts at special ways in times of serious challenges (oil crises) or in the hope for rewarding

business (oil and gas contracts with the ex-Soviet Union) could be managed after initial problems. In addition, Germany, although a key economic player, practised a high level of self-restraint in order to avoid even the appearance of any unique way to go (Alleingang).

The spectacular changes on the map of Europe after 1989 have radically affected this "peace order". German unification in itself has shifted the internal balance of power of the EU, even if, in the first years and in economic terms, Germany became weaker and not stronger.

The double challenge of having a stronger influence in the shaping of the future of the Union and of responding to the changing European structure has led the EFTA countries to apply for membership. Having made use of the short period of Russian paralysis, formerly neutral countries have swept aside all kinds of political reservations and rushed to become EU members at the first convenient time. This, however, has resulted in a different integration pattern. On the one hand, the geographic and economic (philosophy) balance of the EU has clearly shifted towards the East and the North. Although the net contributory position of the EFTA countries to the EU budget may temporarily hide this fundamental difference, one has to be aware of the longer term impact of this change. On the other hand, the EU has got two, equally important "mare nostrum". The Mediterranean lobby has been complemented by a Baltic lobby, with clear impact on the future of German politics, for Germany is a Baltic country but is not a Mediterranean one. At the same time, the struggle for the redistribution of EU resources has started between the old and the new semi-periphery of the EU core. Until now, the achievements of the new semi-periphery (CEECs) are less manifest in any major restructuring of the EU budget. Nevertheless, they are increasingly obvious in micro-level developments represented by changes in market shares and in the geographic orientation of international capital and technology.

Association agreements with the CEECs have benefitted all EU countries, and, in some cases, Germany's relative share has been even decreasing in comparison with some EU countries. However, Germany's contribution to the structural modernization of the region, both by offering more competitive and open markets, by supplying more adequate commodities, and also by exporting direct capital to the region is unquestionable. The economic upswing in the new Bundesländer and the largely positive impact of tremendous investments in modern infrastructure will have a substantial spillover to some CEECs and will strengthen the modernization process in the associated countries of Central (and later also of Eastern) Europe. The political shift consisting in the reestablishment of Berlin as the capital of Germany will support this process. As a result, Germany's economic and political interests will be shifting towards the CEECs. More importantly and in contrast with most other EU countries, this shift is not only due to security reasons and a higher level of "damage limitation capabilities". On the contrary, this is a strong positive shift which is expected to make Germany the main beneficiary of the advantages the CEECs can offer. It is particularly this positive "expansion" and not "negative" security concerns which tend to strengthen the assumption that the unified Germany will not be tolerating for a long time to represent the Eastern border of the EU. Berlin itself will hardly accept to be located just 50 miles from the still dividing European border.

The emergence of Islamic fundamentalism, a new threat in the Southern Mediterranean can exacerbate this shift even more in the next years. In comparison with a militant Islamic ideology, Central Europe shares all traditional Western values, and even Eastern Europe seems to be much closer to the Western way of life than the emerging Islam. One can predict a situation in which the EU will be virtually "sandwiched" between two major external challenges. It is by far not clear whether member countries will perceive these threats in the same way, and, it is even less clear, whether the shaping of a united European strategy will follow from this situation.

At the moment, the strategic planning of the future of the EU does not go so far. Politicians are mostly engaged in trying to find adequate instruments to maintain the old internal equilibrium between France and Germany. Unfortunately, almost all concepts keep on moving within the old framework of "how to keep Germany down". These ideas might have worked under pre-1989 conditions, but they are not only unviable but sometimes virtually counterproductive in the nineties.

Mainly French plans have repeatedly insisted on binding the domestically changing Germany with a rapidly changing external environment into a traditional pattern of EU framework. For this purpose, France would be ready to sacrifice part of its sovereignty and tolerate the predominance of the German mark. The enforcement of Maastricht, a creation of the pre-1989 period, the "stability pact" conference designed by Balladur, political integration, several efforts to give priority to deepening against widening and the clear preference given to the Mediterranean area (partly with more German money, in other words a resource diversion from the CEECs towards francophone countries) are obvious elements of this endeavour. In most cases, Germany is not opposing this French effort. To some extent, it is even supporting it, as some elements of the rather controversial Schäuble paper indicate it. To be sure, at least as yet, there is no clear German message manifested on the highest political level that would take a substantially different position than that of France regarding the future of the EU. Most probably it would be unwise to threaten German-French relations, a cornerstone of European stability. It is, however, not less unwise to ignore the dynamics of European developments that could derail current cooperation patterns unless adequate answers will be found within a relatively short time.

In my view, Germany's binding into Europe, a common interest of Western, Central and Eastern Europe, and not less that of Germany itself, urgently needs the binding of Germany's Eastern neighbours into the EU. This is the decisive issue which should lead the EU and its member countries in the shaping of integration strategies. In fact, the EU's agricultural and financial transfer problems or generally weak arguments for postponing the Eastern enlargement are likely to be dwarfed by this key element of the sustainability of European balance.

Beyond the general(ly weak) arguments, two points have to be answered regarding this proposal. First, adversaries of such a plan may argue that Eastern enlargement would virtually consolidate already dominating German positions in the region. Second, any Eastern enlargement would definitely put Germany into a geographically central position in Europe.

Concerning the first point, it has to be underlined that German influence is likely to be relatively more important without integrating CEECs into the EU. Austria's economic history from the sixties to the early nineties clearly shows this trend. (Interestingly, in the mid sixties France has vetoed Austrian membership in the EEC with exactly the same arguments.) The CEECs' membership in the EU would provide better opportunities for strengthening cooperation with other EU countries, attract more foreign investors, including from outside Germany and the EU, and, most importantly, introduce a strong political, legal and economic control imposed by institutions of the Union.

The second argument is more difficult to be refuted. In fact, Germany will get a central geographic position in Europe, which is in accordance with changing realities on the continent and may hurt some Western European (mainly French) interests. If, however, this shift is adequately bound into the integration framework, most impacts could be favourable for European stability and cooperation, and compensate for eventual negative impacts. In consequence, a positive sum-game is easily attainable. In turn, Germany's prolonged "Eastern" position in the EU would create much more problems, without the positive impacts of integration.

In a nutshell: two basic scenarios can be forecast. The first scenario does not consider early Eastern enlargement as a realistic alternative. The consequences would be growing instability, deepening economic gap and the heavy concentration of EU-CEECs relations on German-CEECs cooperation. As the direct neighbour to some CEECs, Germany would be forced to pay more attention and, ultimately, also to divert more resources to its Eastern neighbours. Simultaneously, German firms will be increasingly using the comparative advantage of shifting part of their production to low-cost transforming countries well endowed with skilled labour. The EU would be damaged in two ways. On the one hand, part of German resources, a major component of the EU budget will be diverted for damage limiting and stabilizing purposes. On the other hand, Germany, making more extensive use of competitive production factors in the CEECs, will emerge as a more competitive economy within the EU. Both elements are likely to generate developments which may substantially affect the intra-EU balance.

The second scenario is based on quick Eastern enlargement and Germany's binding into a larger European framework. Most probably, instabilities on Germany's Eastern border can be eliminated (even if partly shifted to the new Eastern border of the EU), available resources could be dedicated to economic modernization of the transforming countries and all EU members would benefit from the rapid development and high import demand of the CEECs.

It has to be stressed that the choice between these two scenarios is not unlimited in time. The later the decision in favour of the second option will be taken, the lower will be the possibility of a stable and competitive European architecture based on the EU anchor.

VIII. Concluding remarks

The chain reaction of dramatic shifts in Europe did not come to an end with the collapse of the Warsaw Pact, the Soviet Union and of Eastern Germany. The process of political democratization and economic transformation in the CEECs is but one of the major elements of these changes. The EU is the obvious modernization anchor of the continent. However, it can play this role only if it can provide the right answers at the right time to the new challenges. Flight into earlier status quo attitude is definitely the wrong answer, even if it is described in "modern terms" (deepening, cautious enlargement if any, balancing between the Mediterranean and Eastern Europe, all-European stability contract, etc.). Also the EU's pursuit for unilateral adjustment of the CEECs is untimely. A new European pattern providing a sufficient level of security and a high level of economic integration requires substantial adjustment efforts on both sides. Economic and political adjustment should be accompanied by a more positive communication strategy. This strategy should emphasize the positive results that can be expected from the Eastern enlargement and not the high costs, which hinder the geographic extension of the EU, or the relevant threats that may force the EU to widen the integration but for reasons of damage limitation exclusively.

Beyond any doubt, gradual Eastern enlargement costs additional money, but much less than the financing of any non-membership alternative. Although the Association Agreements stipulate the creation of free trade in industrial products by the end of the century, and, thus, cope with the basic commercial interest of the EU. However, the market of the CEECs can only expand and offer sustainable dynamic demand for EU goods, if these economies recover, start a high, export- and investment-led growth, and will be able to finance their exploding trade deficit in the crucial years of economic modernization ("modernization deficit"). While Eastern enlargement is likely to enhance competition on Western European markets and increase pressure on the EU's industrial structure and labour markets, it can substantially contribute to higher levels of European competitiveness on the global scale. Both all-European restructuring and the integration of low-cost and highly-skilled labour into the international division of labour are expected to work in this direction. Finally, Western European stability and security cannot be sustained for a longer period without Eastern enlargement. The latter would not only provide a relevant support to a new security scheme but also strengthen European stability by creating a solid balance of power structure.

Time and again, the author of this paper has been meeting with Western European arguments which qualify the scenario of rapid Eastern enlargement as an illusion. What is, however, the very illusion? Is it a forecast that tries to follow the dynamics of European developments, or the stubborn insistence on an outdated pattern of Western European status quo?

Budapest, April 25, 1995

References

- Altmann, Franz Lothar, Wladimir Andreff and Gerhard Fink (1995), "Future Expansion of the European Union in Central Europe", January (manuscript)
- Altmann, Franz Lothar and Cornelius Ochmann (1995), "Mittel- und Osteuropa auf dem Weg in die EU", Europäische Rundschau, No. 1. pp. 41-61.
- Baldwin, Richard E. (1994), "Towards an Integrated Europe", Centre for Economic Policy Research, London.
- Dauderstädt, Michael and Barbara Lippert (1995), "Differenzieren beim Integrieren. Zur Strategie einer abgestuften Osterweiterung der EU", Friedrich Ebert Stiftung, Bonn, March
- Inotai, András (1994a), "Looking forward to full membership", Hungarian Economic Review, June-August, pp. 64-69.
- Inotai, András (1994b), "The System of Criteria for Hungary's Accession to the European Union", Institute for World Economics, Budapest (Trends in World Economy, no. 76.)
- Inotai, András (1994c), "Die Beziehungen zwischen der EU und den assoziierten Staaten Mittel- und Osteuropas", Europäische Rundschau, no. 3. pp. 19-36.
- Inotai, András (1995), "Die deutsche Präsidentschaft und das Essener Gipfeltreffen im Kontext des europäischen Integrationsprozesses", Budapest (manuscript)
- Nötzold, Jürgen (1994), "Wann werden die Staaten Ostmitteleuropas Mitglieder der EU?", Europäische Rundschau, no. 4. pp. 53-65.
- Weidenfeld, Werner (1995), "Ernstfall Europa", Internationale Politik, no. 1. pp. 11-19.