Towards greater economic integration

The European Union's financial assistance, trade policy and investments for central and eastern Europe

Introduction

The central and eastern European countries (CEECs) are now in their eighth year of transition from the planned economy to the market economy.

The European Union is supporting the multi-faceted transformation process through a wide variety of measures, aiming at, above all, a sounder integration of the CEECs into the international economic system. In particular, the enlargement process will help to promote economic and political reform. The ten countries of Central Europe which have applied for membership will be able to join the EU when they satisfy the required economic and political conditions. To support the process of integration, the European Council in Essen agreed a pre-accession strategy that sets out practical ways to help the candidate countries to adapt to EU norms and rules.

Figures and facts help in understanding the role of the EU in the CEECs. The European Commission has therefore decided to update its previous publication on the European Union's commercial policy and assistance towards the countries of central and eastern Europe, including a new chapter on foreign direct investment in the region.

As the data in this brochure show, the European Union has become the CEECs' main trading partner in an extremely short period of time. The European Union is, by far, their main provider of bilateral assistance. Foreign direct investment is growing in many of the CEECs, with strategic investors originating in the European Union playing a vital role in upgrading the central and eastern European economies.

It is the aim of the European Commission to carry these policies further forward with a particular emphasis on opening markets, promoting trade and investment and enhancing assistance.

Note: The figures in this document were finalised in December 1996.

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Executive summary

Bilateral economic relations between the European Union and central and eastern European countries (CEECs) are based on three main pillars: trade policy, assistance and foreign direct investment. On all three counts the European Union and its Member States are the most important partner of the CEECs. The European Union is the CEECs' main customer and main supplier. Together with its Member States, the European Union provides by far the largest share of assistance to the countries of central and eastern Europe. Foreign direct investment originating in the Member States of the European Union plays an important part in the overall inflows into the region.

For reasons of statistical consistency, all figures in this document concerning the European Union refer to the European Union of the fifteen, including Austria, Sweden and Finland, even before 1995.

The summary term of 'central and eastern European countries' (CEECs) used in this document refers to a geographical region, encompassing altogether 15 countries(*): Bulgaria, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, Slovakia, Slovenia, Albania, Bosnia-Herzegovina, Croatia, FYROM and FRY. Figures and charts have to be read carefully, always paying attention to the group of CEECs referred to.

European Union trade with the countries of central and eastern Europe

The European Union has become the main trading partner of the countries of central and eastern Europe, accounting for more than ECU 47 billion of imports from the 15 CEECs in 1995. It is also their main supplier, exporting to them more than ECU 58 billion in the same year. Growth in EU imports from CEECs has soared by 273.5 per cent in the case of Poland from 1989 to 1995. EU exports to the CEECs rose in some cases by more than 400 per cent (Romania and former Czechoslovakia).

For the six CEECs for which we have figures for 1989 (i.e. Hungary, Poland, Czechoslovakia-Czech Republic/Slovakia, Bulgaria and Romania), the EU's share of exports soared to 63 per cent in 1995.

From the point of view of the European Union, the CEECs have become increasingly important trading partners, too. The six CEECs plus Slovenia and Croatia accounted for 7.9 per cent of total imports into the European Union in 1995.

The trade deficit of the CEECs with the European Union is the normal consequence of a transitional situation, preliminary to a period of growth. The important thing is that the deficit should be sustainable - which means to say that it should not cause excessive debt - and that it goes along with growing trade, which has been the case up to now.

The criticisms aimed at European commercial policy in the sensitive sectors are unfounded, in so much as in 1995, for example, quota utilisation for imports of textiles from the CEECs was in general low.

The trade policy which the European Union has pursued is one of total and asymmetric liberalisation of non-agricultural trade. Since the beginning of 1995, all industrial exports from the CEECs have had virtually free access to the European Union market. This makes an important, enduring and clearly mapped out contribution to the dynamic development of trade which is vital for the CEECs' economic reconstruction.

The pre-accession strategy agreed at the Essen European Council in December 1994, represents a further important step in this direction and emphasises the position taken previously while establishing the process for integration with the CEECs.

Assistance to the countries of central and eastern Europe

Between 1990 and 1995, the European Union and its Members States provided 70 per cent of all western bilateral aid to the CEECs. Just in terms of grants, which play a crucial role during the initial phase of economic reconstruction, the European Union provided over the same period ECU 16.8 billion out of a total ECU 25.6 billion from the west as a whole. But not only from the point of view of quantity the EU is playing the leading role. The European Union is constantly developing and adapting its assistance according to needs. Fulfilling the new role as the financial instrument of the pre-accesion strategy, the EU's Phare Programme spending is set to rise from ECU 1.1 billion in 1995 to an estimated ECU 1.6 billion in 1999. Main targets will be investment, infrastructure and integration (legal harmonisation, public administration reform, etc).

(*) of which ten have already signed Association Agreements

Foreign direct investment in the countries of central and eastern Europe

Foreign direct investment (FDI) is a major vehicle for developing a strong, dynamic private sector. It is essential to ensure successful transition to a market-based economic system and integration into the world market. In 1995, FDI inflows into the region grew significantly. Strategic investors originating in the Member States of the European Union play a major role in upgrading the CEECs economies, accounting for at least 60 per cent of total FDI inflows. However, the major part of FDI goes to Hungary, Czech Republic and Poland. In general, FDI inflows have been below the level required to sustain growth.

European Union trade with the countries of central and eastern Europe

From the Council for Mutual Economic Assistance to integration in the world markets

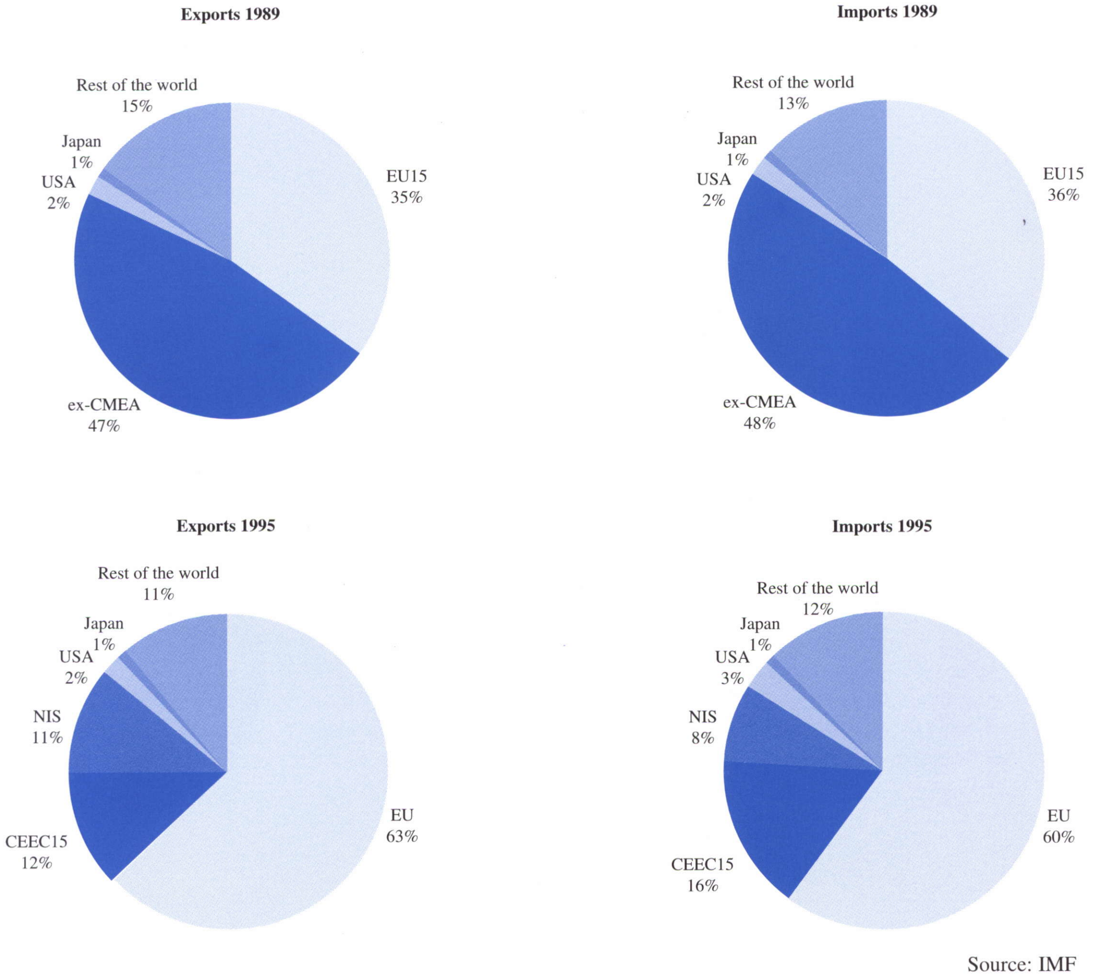
The European Union is far and away the main trading partner of the countries of central and eastern Europe.

In the aftermath of the demise of the CMEA, all CEECs swiftly redirected their trade flows towards the European Union. In a very short space of time the European Union has become the CEECs' main trading partner, replacing trade with their former partners in the Council for Mutual Economic Assistance (CMEA).

From 1989 to 1995, the European Union's share in the external trade of the six CEECs for which we have figures for 1989 - Hungary, Poland, former Czechoslovakia, Bulgaria, Romania (CEEC6) - has nearly doubled and now accounts for 63 per cent of exports and 60 per cent of imports, making the EU by far their main trading partner.

In 1989, exports to the European Union represented only 35 per cent of their total exports against 47 per cent within the CMEA. Imports from the European Union stood only at 36 per cent of their total imports against 48 per cent from CMEA countries.[1]

Role of different partners in the external trade of the CEEC6 1989 to 1995 (%)



Source: IMF

[1] The figures should be regarded as indicators of general trends rather than precise information about trade flows. There is uncertainty about (1) the value in convertible currency of 1989 trade between the members of the CMEA, which was conducted in "transferrable roubles", (2) understatement of trade flows with some members of the NIS in 1995, (3) possible misclassification of trade with East Germany in 1989.

Share of different partners in the external trade of Czech Republic, Hungary, Poland, Slovakia, Bulgaria and Romania from 1989 to 1995 (%)

	Exports to		Imports from	
	1989	1995	1989	1995
EU 15	35	60	36	59
ex-CMEA CEECs	46	12	48	16
NIS		11		8
USA	2	3	2	3
Japan	1	0	1	1
Rest of the world	15	15	14	13

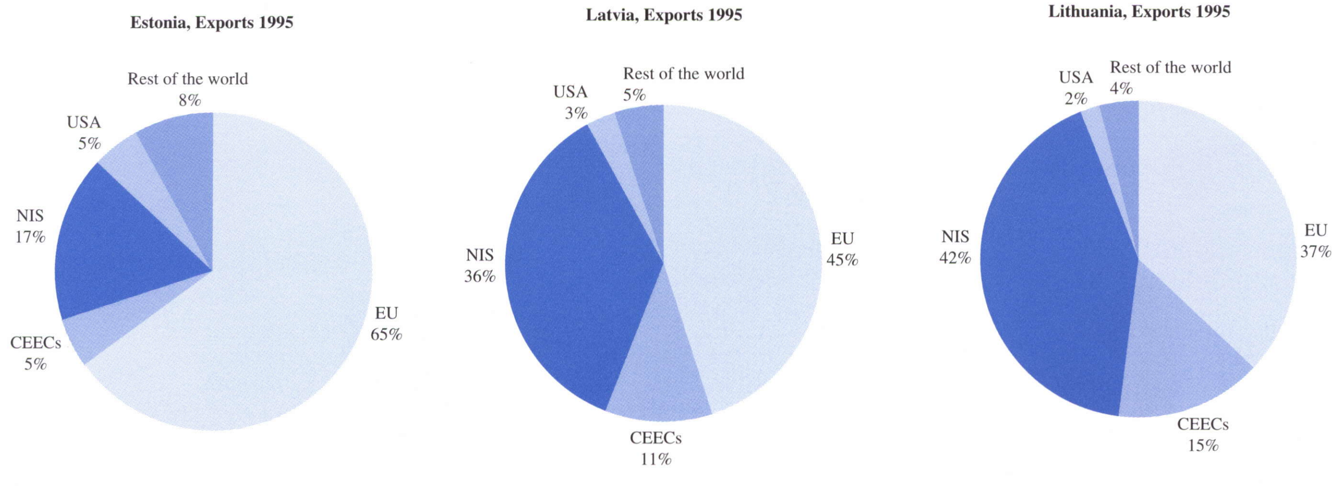
Sources : IMF

Trade between the CEECs and the EU expanded dramatically. The European Union's imports from the Czech Republic, Slovakia, Poland, Hungary, Bulgaria and Romania (CEEC6) rose on average by 156.4 per cent from 1989 to 1995. The exports of the European Union swelled by 226.3 per cent.

The four Visegrad countries (Poland, Czech Republic, Slovakia, Hungary), especially, experienced extremely high growth rates in trade with the European Union. The picture is more mixed for Bulgaria and Romania, where we can also observe high but asymmetric trade growth as regards imports and exports. Bulgaria has seen a tremendous increase in exports to the EU whereas imports from the EU are only growing slowly. The case of Romania is the opposite and growth in EU imports outpaces that of exports to the EU.

The three Baltic states Lithuania, Latvia and Estonia follow a similar pattern of geographical reorientation. All three registered a high export growth in sales to the EU, which accelerated for the third year in 1995. Estonian exports to the EU for example rose by 50 per cent in 1995 over the 1994 level, imports from the EU have grown by 31.9 per cent. Exports to the EU now account for between 46 per cent (Latvia) and 64 per cent (Estonia) of total exports.

Role of different partners in the external trade of the three Baltic states from 1993 to 1995 (%)



Role of different partners in the external trade of the three Baltic states from 1993 to 1995 (%)

	Estonia				Latvia				Lithuania			
	Exports to		Imports from		Exports to		Imports from		Exports to		Imports from	
	1993	1995	1993	1995	1993	1995	1993	1995	1993	1995	1993	1995
EU	68	64.8	64	65.6	43.3	46	70.2	59.9	51	36.9	67.6	51.6
CEECs	5.2	5.2	12.6	8.6	17.1	10.5	7.2	6.6	10.3	14.7	17.8	10
NIS	15.6	16.6	15.6	18.2	26	35.5	16	23.7	31.4	43.2	6.7	29.5
USA	5.6	5	2.9	3.7	8.3	3.4	2	4.2	4.7	1.5	1.3	1.1
Japan	0.7	0.3	1	0.7	0	0	1.5	0.2	0	0	1.5	0.2
Rest of the world	4.9	8.1	3.9	3.2	5.3	4.6	3.1	5.4	2.6	3.7	5.1	7.6

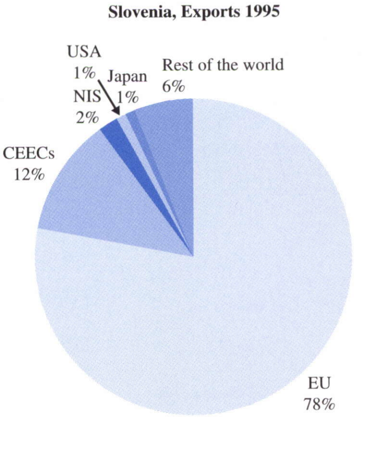
Source: Eurostat, based on IMF trade statistics

Slovenia has the greatest share of exports going to the EU among all CEECs. They now account for 78.8 per cent of total exports, while imports from the EU stand at 70 per cent of total imports. Growth of trade between Slovenia and the EU is continuing to develop dynamically, reaching an annual growth rate of 11.7 per cent in exports and 19.3 per cent in imports in 1995.

External trade of Slovenia

	Exports to		Imports from	
	1993	1995	1993	1995
EU	76.9	78.8	71.6	70.2
CEECs	15.1	11.9	16.2	15.3
NIS	3.1	1.7	4.6	4.8
USA	1.8	1.4	4.7	4
Japan	0.5	0.5	0.7	0.4
Rest of the world	2.6	5.7	2.2	5.3

Source: Eurostat, based on IMF DOTS



The other four successor countries of former Yugoslavia - Croatia, Bosnia-Herzegovina, FRY (Serbia-Montenegro) and FYROM[1]- face stagnating trade with the EU due to the political situation in the region. After 1995 however in particular as a consequence of the lifting of the UN embargo, EU trade with the area has seen an increase.

Albania's trade with the EU is developing dynamically. Imports from the EU have risen by 300 per cent in 1995 over the 1989 level. Exports to the EU are growing, too, albeit at a slower rate.

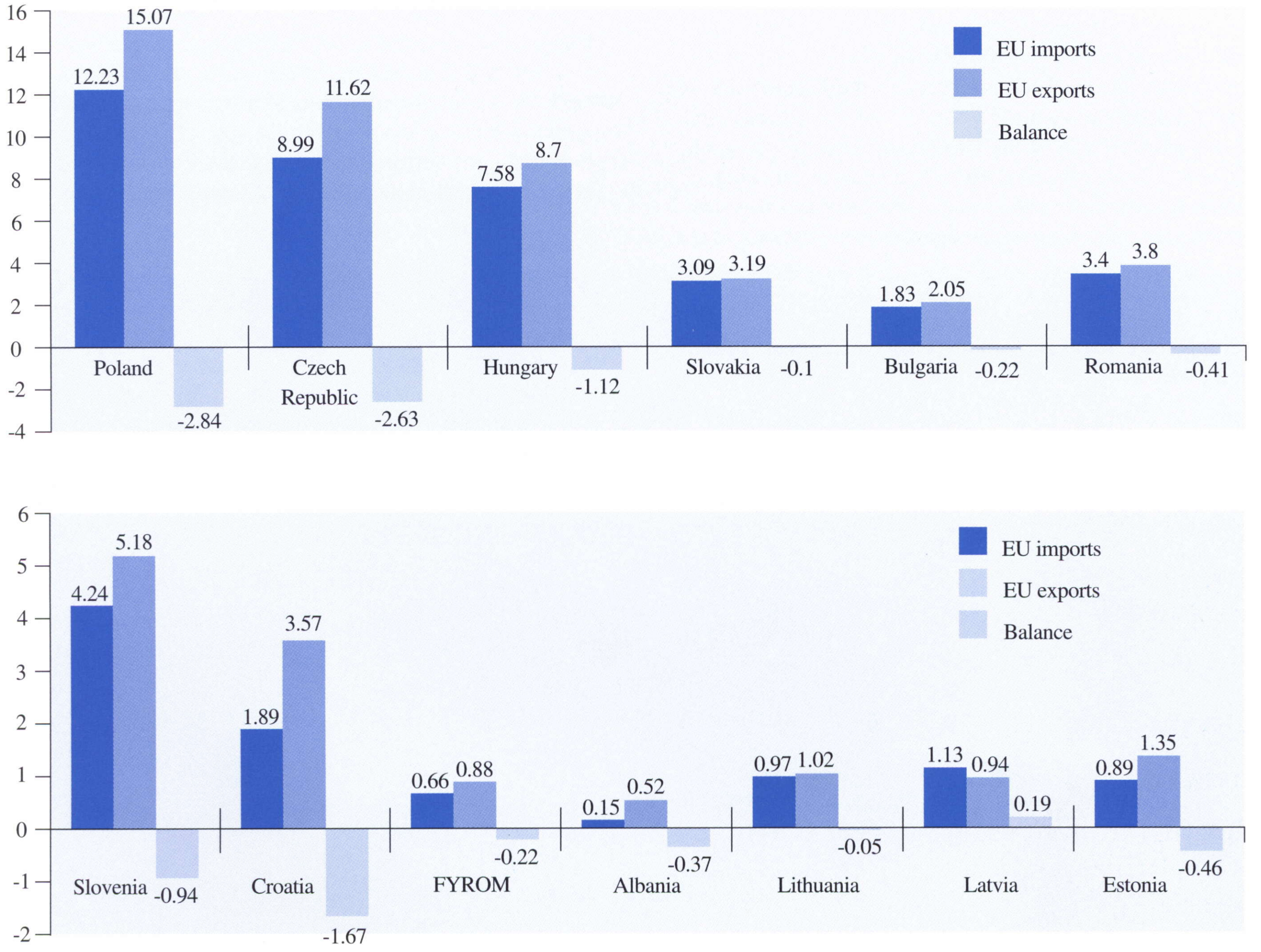
Trends in trade between the European Union (15) and the central and eastern European countries 1989-1995 (ECU billion)

	EU Imports from				EU Exports to				Balance EU imports - EU exports		
	1989	1994	1995	% increase 1989 1995	1989	1994	1995	% increase 1989 1995	1989	1994	1995
Poland	4.66	10.13	12.23	162.6	4.55	12.16	15.07	231.4	0.11	-2.03	2.84
Hungary	3.33	6.05	7.58	127.6	3.75	8.06	8.7	132	-0.42	-2	-1.12
Czech Republic	3.23*	7.38	8.99	273.5	2.88*	9.2	11.62	414.2	0.35**	-1.83	-2.63
Slovakia		2.24	3.09			2.19	3.19			0.05	-0.1
Bulgaria	0.59	1.42	1.83	212.3	1.7	1.75	2.05	20.8	-1.11	-0.33	-0.22
Romania	2.67	2.64	3.39	27.2	0.74	2.8	3.8	411.3	1.92	-0.16	-0.41
Lithuania		0.84	0.97			0.85	1.02			-0.01	-0.05
Latvia		0.96	1.13			0.71	0.94			0.25	0.19
Estonia		0.59	0.89			1.02	1.35			-0.43	-0.46
Albania	0.11	0.13	0.15	36.3	0.13	0.43	0.52	294.3	-0.02	-0.31	-0.37
Slovenia		3.8	4.24			4.34	5.18			-0.55	-0.94
Croatia		2.07	1.89			3.26	3.57			-1.19	-1.67
Bosnia-Herzegovina		0.01	0.02			0.11	0.16			-0.1	-0.14
FRY (Serbia+Montenegro)		0.01	0.03			0.15	0.19			-0.15	-0.16
FYROM		0.68	0.66			0.81	0.88			-0.13	-0.22
Total		**38.95**	**47.09**			**47.84**	**58.24**				

Source: Eurostat-Comext
Since EU trade with FRY and Bosnia-Herzegovina is too small, it has not been included.
(*) Czechoslovakia

[1] FYROM = Former Yougoslav Republic of Macedonia

Balance of trade of the central and eastern European countries with the European Union in 1995 (ECU billion)



Source: Eurostat-Comext

Since imports continued to grow more quickly than exports, the foreign trade deficit increased, especially in the high growth countries such as the Czech Republic, Poland, Slovakia and Slovenia in 1995. The negative trade balance should be seen against the background of particularly high growth rates, and especially the fact that the CEECs' economies are just getting off the ground. The economies have an immense need for modernising and adjusting (import of investment goods). As the CEECs are net capital importers enjoying a high influx of capital, a trade deficit is neither surprising nor, per se, dangerous. If the CEECs utilise capital inflows increasingly for investment in education/training and technology and thus upgrade their industrial base, they will eventually achieve competitiveness and, as a corollary, push up exports.

From the sectoral point of view there has been no major shift in the make-up of the European Union's trade with the Visegrad countries (the only ones for which we have a historical perspective following the entry into force of the Interim Agreements, followed by the Association Agreements), but there has been a shift from consumption goods to investment goods. "Sensitive" products such as agricultural products, textiles and steel account for around 50 per cent of total exports from Poland and Hungary to the European Union and around 35 per cent of total exports from former Czechoslovakia. Imports of those products from the Visegrad group into the European Union have forged ahead since 1991.

Intraregional trade

After the liquidation of the CMEA the close economic ties forged among its members unravelled to a considerable extent. This process was encouraged by the transition to the market - especially by the shift to trade at world market prices and in convertible currencies - and by the political will of the CEECs to reorientate towards the West and join the EU. Trade between Poland, Hungary, former Czechoslovakia, Bulgaria and Romania plummeted on average by 70 per cent from 1989 to 1993.

Since 1994, however, the trend has turned to positive growth. Trade between the central European countries is increasing. In Poland and Hungary trade with the CEEC6 has already overtaken the level of 1989. Former Czechoslovakia's exports to the CEEC6 have passed their 1990 level and imports the 1991 level. Trade flows between the Czech Republic and Slovakia are especially high and accounted for over 50 per cent of total intra-CEEC6 trade. In comparison, Bulgaria and Romania have experienced a more modest growth of intra-CEEC6 trade.

Change in trade flows among CEEC6 between 1993 and 1995

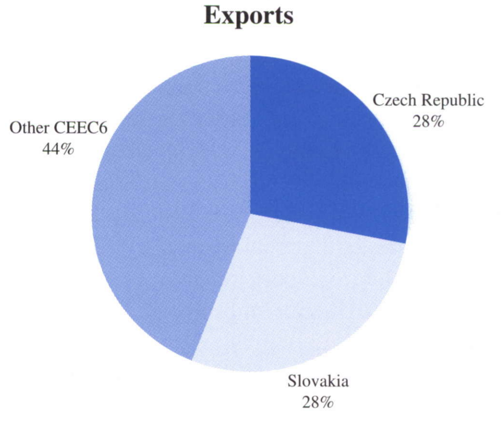
	Exports in %	Imports in %
Poland	+130	+201
Hungary	+132	+147
Czech Republic	+40	+45
Slovakia	+90	+59
Romania	+18	+54
Bulgaria	+6	+11
Total	**+71**	**+72**

Source: IMF

Trade between Czech Republic and Slovakia as % of total intra-CEEC6 trade in 1995

	Exports in %	Imports in %
Czech Republic	28	27
Slovakia	28	30
Total	**56**	**57**

Source: IMF



The Baltic States' trade with other central and eastern European countries is still small, though growing fast in the case of Latvia and Estonia. Taking the three Baltic states jointly as a group, exports to CEECs account only for 3.9 per cent and imports for 4.7 per cent of total intra-CEECs foreign trade.

Trade between these three is growing. On average, imports from the Baltic neighbours make up 6.2 per cent of total imports, ranging between 5.7 per cent (Lithuania) and 10.8 (Latvia) per cent. Exports to the Baltic region stood at 10.2 per cent, rising by 17.7 per cent over the 1994 level. With the exception of Estonia, exports to the NIS are stagnant. Trade between the Baltic States and the NIS now account for between 20 per cent (Estonia) to 40 (Lithuania) per cent of their total external trade.

In general, the central and eastern European countries and Russia remain important trading partners. Trade cooperation between CEECs and Russia fell sharply after the liquidation of the CMEA. Yet trade with Russia still takes an important place in the external trade of the CEECs, ranging from 6 per cent for Poland to 24 per cent for Bulgaria. However, there is no return to the high degree of integration which was obtained under the CMEA.

Poland and Slovakia have experienced the highest growth in trade cooperation with Russia. In the first half of 1996, total Polish exports rose by 4 per cent, while exports to Russia soared by 53 per cent. Russia is Poland's second largest export customer behind Germany. Slovakian-Russian trade has grown more strongly than with any other CEECs in the last two years. Russia ranks second place in Slovakia's import structure and seventh in its export structure.

The CEECs are running a significant trade deficit with Russia, but one which is however shrinking due to the fact that growth in CEECs exports is faster than growth of Russian exports to central and eastern Europe which consist to a large extent of energy.

Trade and other agreements

Facilitating access to the European Union market has been a crucial instrument for supporting the political and economic reform processes in central and eastern Europe. The European Union has progressively accelerated its trade concessions. As a result, almost all industrial products from the CEEC6 have entered the Union free of duties and quantitative restrictions since 1 January 1995.

Agreements have been drawn up between the European Union and all the countries of central and eastern Europe (except the three countries of former Yugoslavia which have been until recently involved in the Bosnia conflict).(*)

Europe Agreements have been signed with 10 CEECs, covering trade and trade-related issues, political, economic and cultural cooperation as well as financial assistance. The Europe Agreements with Hungary and Poland came into force in February 1994, the Europe Agreements with the Czech Republic, Slovakia, Romania and Bulgaria entered into force in February 1995. The Europe Agreements with the Baltic States were signed in June 1995. The Europe Agreement with Slovenia was signed in June 1996.

As a result of the Interim(**) and Europe Agreements, and of decisions following the Copenhagen (1993) and Essen (1994) European Councils, almost all industrial products from the CEEC6 have entered the Union free of duties and quantitative restrictions since 1 January 1995. This is a result of a progressive acceleration of trade concessions by the European Union.

The few remaining exceptions include textiles and garments, for which the European Union phased out duties on 1 January 1997. Quantitative restrictions are to be abolished by 1 January 1998. However, the largest proportion of textile and garment imports into the Union is already free.

Trade in agricultural and processed agricultural goods and fisheries products is subject to preferential treatment. Beyond the binding of GSP advantages, the parties agreed to grant each other concessions on a reciprocal basis. Special provisions were made for fishery products.

The Baltic countries enjoy a similar treatment based on the Free trade agreement which entered into force on 1 January 1995.

All associated countries are reciprocating these measures, but are given more time to implement their trade concessions. This is called the "asymmetry" of the agreements, favouring the central and eastern European economies. The aims of this asymmetry were to give the countries in question rapid free access to the European Union market, and to allow them time to restructure their economies before they have to face full competition by European Union goods.

The Interim and Europe Agreements also provide for the usual trade policy instruments and a number of trade-related matters. They include a standstill clause and thus

(*) See table page 14

(**) Interim Agreements comprise the commercial aspects of Europe Agreements do not allow for introducing new trade restricting measures. However, some exceptions might be considered under specific circumstances. Thus the associated countries - and only they - may under certain circumstances take temporary trade measures to protect their infant industries, sectors in restructuring or facing serious difficulties. They may also take temporary trade measures in case of serious balance of payments problems. On the other hand, general safeguard measures, anti-dumping provisions and export restrictions can be invoked by both parties. Special safeguard measures can apply for agricultural and steel products.

Competition rules, protection of intellectual, commercial and industrial property as well as liberalisation of payments and capital transfers in respect of trade in goods and services and of investments are among the trade-related matters included in the Agreements.

With the exception of the EFTA countries, which have also concluded free trade agreements with the ten countries of central and eastern Europe similar to those concluded with the European Union, none of the other western countries has negotiated agreements with the ten CEECs as far-reaching as the Europe Agreements.

Albania concluded a non-preferential Trade and Cooperation agreement with the EU as early as 1992. An evolutionary clause refers to the objective of an association agreement as soon as conditions are met. A preferential Cooperation agreement with FYROM was initialled in 1996.

Pre-accession strategy

The Essen European Council of December 1994 reinforced the orientations made up to then by adopting a pre-accession strategy which consists of preparing the ten associated CEECs for accession to the EU and progressively integrating them into the internal market of the European Union.

Key elements are the harmonisation of the CEEC's legislation to that of the European Union, the Phare Programme as financial instrument of the strategy, the structured dialogue and the Europe Agreements.

In order to help the associated countries to prepare as rapidly and efficiently as possible for integration into the internal market of the Union, the European Commission adopted a White Paper explaining the technical aspects of pre-accession.

The Phare Programme has in addition been further reoriented towards financing investment in infrastructure, institution building and assistance to the accession in line with the "acquis communautaire".

The so-called "structured dialogue" between the associated states and the European Union provides for a particular framework created to discuss issues of common interest, such as economic and monetary policy, justice and home affairs or education. The dialogue is essential to familiarise the associated countries with the decision-making and institutional set-up of the EU and should, above all, enhance the good working relationships which are crucial for the process of European integration.

Enlargement

In 1993 in Copenhagen, the European Council stated that "the associated countries in Central and Eastern Europe that so desire shall become members of the Union. Accession will take place as soon as a country is able to assume the obligations of membership by satisfying the economic and political conditions". These conditions include the existence of stable institutions guaranteeing democracy, the rule of law, human rights and respect for and protection of minorities as well as the existence of a functioning market economy.

The associated countries which have applied for membership of the Union are (order by date of application):

Hungary	31 March 1994
Poland	8 April 1994
Romania	22 June 1995
Slovakia	28 June 1995
Latvia	13 October 1995
Estonia	28 November 1995
Lithuania	11 December 1995
Bulgaria	16 December 1995
Czech Republic	23 January 1996
Slovenia	10 June 1996

The European Council has asked the Commission to prepare an Opinion for each of the candidate countries on their preparedness to join the EU. The Opinion is an in-depth analysis of the economic, political and legal situation of the applicant country, designed to assist the Council in its decision whether or not to open negotiations for accession. The ten Opinions will be sent to the Council after the end of the Intergovernmental Conference (IGC). Accession negotiations with candidate countries could start within six months of the conclusion of the IGC.

Trade policy

The textiles and clothing sector shows how the European Union has liberalised a generally sensitive sector.

The European Union will have phased out duties by 1 January 1997. Quotas are to be eliminated on 1 January 1998. Therefore, the phasing out of quotas is to take place over a time period which is half that agreed in the Uruguay Round.

The CEECs have benefited from significant increases in quotas in recent years. For most of the restricted categories of textile products the quota utilisation for direct imports in 1995 by the CEECs was low, which implies that for most of these categories the CEECs cannot be considered as constrained suppliers. Even if we consider more disaggregated statistics, the picture does not change substantially. The following table demonstrates this: OPT refers to the export of Community origin textile products to be processed in a third country for subsequent re-importation into the Community under specific OPT quotas. These OPT quotas are additional to the normal quotas for clothing products and are aimed at encouraging industrial co-operation.

As a result of the review of the Additional Protocols to the Europe Agreements, the CEECs benefited from significant increases of the OPT quotas in 1995.

Duties on OPT imports were abolished before the abolition of textile duties.

Quota utilisation in textiles and clothing in 1995
(in % terms)

	Direct quotas	OPT quotas
Poland	33	62
Hungary	34	34
Czech Republic	53	79
Slovakia	28	47
Romania	44	71
Bulgaria	49	72

Source: Commission Services

The European Union's trade cooperation with the central and eastern European countries

	MFN/GSP	Agreement in force	Official application for EU membership
Hungary	superseded by bilateral free trade agreement	Europe Agreement in force 1.2.1994	March 1994
Poland	superseded by bilateral free trade agreement	Europe Agreement in force 1.2.1994	April 1994
Czech Republic	superseded by bilateral free trade agreement	Europe Agreement in force 1.2.1995	January 1996
Slovakia	superseded by bilateral free trade agreement	Europe Agreement in force 1.2.1995	June 1995
Romania	superseded by bilateral free trade agreement	Europe Agreement in force 1.2.1995	June 1995
Bulgaria	superseded by bilateral free trade agreement	Europe Agreement in force 1.2.1995	December 1995
Estonia	superseded by bilateral free trade agreement	Free trade agreement Europe Agreement signed	November 1995
Latvia	superseded by bilateral free trade agreement	Free trade agreement Europe Agreement signed	October 1995
Lithuania	superseded by bilateral free trade agreement	Free trade agreement Europe Agreement signed	December 1995
Slovenia	non-reciprocal preferential agreement	Interim agreement Europe Agreement signed	June 1996
Albania	Yes	Trade and cooperation agreement	
FYROM	preferential import regime, GSP for agricultural products only	Cooperation agreement initialled	
Croatia	preferential import regime, GSP for agricultural products only		
Bosnia-Herzegovina	preferential import regime, GSP for agricultural products only		
FRY (Serbia + Montenegro)	No		

The future outlook

The CEECs have continously increased their market share in the European Union. The effects of a slight contraction in the external trade of the European Union did not stop the expansion of CEECs' trade with the EU.

Today, the CEEC6 plus Slovenia's and Croatia's market share in the EU has reached 7.9 per cent. Poland ranks in the 7th place behind the USA, Japan, Switzerland, China, Norway and Russia. The Czech Republic's rank is 14, ahead of Singapore, Saudi Arabia and India.

Ranks and shares of the CEECs in the EU's imports (%)

Rank 1995	Origin	1992	1994	1995
1	USA	20.1	19.3	19.0
2	Japan	12.2	10.4	10.0
7	Poland	1.7	2.0	2.2
14	Czech Republic		1.4	1.7
19	Hungary	1.1	1.2	1.4
28	Slovenia	0.4	0.7	0.8
32	Romania	0.3	0.5	0.6
36	Slovakia		0.4	0.6
44	Croatia	0.2	0.4	0.3
45	Bulgaria	0.2	0.3	0.3

Source: EUROSTAT

Both imports and exports of the EU have probably grown only at half of the rate of 1995. These developments have a direct impact on the CEECs, for whom the European Union has become the major trading partner. If the exports of the CEECs towards the European Union have not risen in volume in 1996 as much as one could have hoped, it is above all due to the disappointing economic situation which prevailed in the European Union and not due to any measures taken by the Member States of the European Union.

The economic estimates of the external trade of the European Union for 1997, which are currently in our possession, indicate a difficult economic climate after a slow-down in world trade in 1996.

However, according to forecasts, growth in trade for the EU is already expected for 1997. It is estimated that demand in the EU will strengthen. The CEECs should be able to take direct profit and experience stronger growth in exports in 1997.

Growth in international trade (volume in %)

		1995	1996 (estimates)	1997 (predictions)
Imports	of the EU	6.2	3	5.3
	of the rest of the world (-EU)	11	8.1	8.1
	of the CEECs	19.8	10.7	9.3
Exports	of the EU	7.3	3.8	6
	of the rest of the world (-EU)	10.9	6.9	8
	of the CEECs	12.6	5.8	7.3

Source: Services of the Commission

Financial assistance to the countries of central and eastern Europe

The European Union and its Member States are by far the greatest source of assistance to the central and eastern European countries[1]. The European Union coordinates western aid in the G-24 and has generally provided the lion's share of assistance to the CEECs.

The accession of the three new members increased the European Union's share of the burden to 70 per cent of the overall assistance to the region (excluding International Finance Institutions (IFIs)).

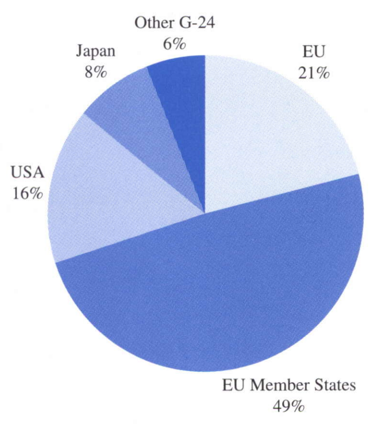
In the period 1 January 1990 to 1 January 1996 the European Union and its member states provided ECU 45.9 billion for central and eastern Europe (ECU 13.3 billion from the European Union as such), while Japan provided ECU 5.0 billion and the United States ECU 10.1 billion. The G-24 countries and the IFIs together provided a total of ECU 86.5 billion in that period. When the ECU 21.4 billion from the IFIs is subtracted, the European Union and its Member States accounted for the lion's share of 70 per cent of the west's bilateral aid to central and eastern Europe during this period.

Grant finance

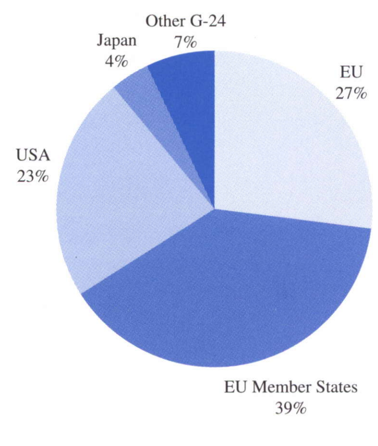
Taking only grants into account, the European Union and its Member States gave the CEECs ECU 16.8 billion in the period from 1 January 1990 to 1 January 1996. Japan granted ECU 1.1 billion and the United States ECU 5.8 billion.

This type of aid is crucial because it does not increase debt. Given that the G-24 as a whole contributed ECU 25.6 billion, the European Union and its Member States once again emerge as the CEECs' principal source of funding. The European Union and the Member States alone account for 66 per cent of the bilateral grant aid received by the CEECs.

Overall assistance (excluding IFIs) 1990-1995



... of which grants



Source: G-24 Scoreboard

[1] All 15 central and eastern European countries

Total assistance from the G-24 countries to the 15 countries of central and eastern Europe in the period 1 January 1990 to 1 January 1996 (ECU billion)

	overall assistance	of which grants
EU	13.3	6.9
EU-Member States	32.6	9.9
USA	10.1	5.8
Japan	5	1.1
IFI	21.4	–
Other G-24	4	1.9
G-24 total (excluding IFIs)	65.2	25.6
G-24 total (including IFIs)	86.5	25.6

Source: G-24 Scoreboard

Different types of assistance

From the very beginning the European Union reacted promptly and continuously adapted its assistance according to needs.

In the first years of transition, the European Union and its Member States provided more than 70 per cent of all emergency non-food aid received by the CEECs[1]; the United States provided 21 per cent.

As regards technical assistance, the European Union and its Member States have also provided 68.5 per cent of the non–IFI technical assistance received by central and eastern Europe; the United States has provided a little more than 27 per cent.

The European Union alone (i.e. as distinct from its Member States) has provided more than 46 per cent of all non-IFI technical assistance to central and eastern Europe, primarily through its Phare Programme. In 1995, Phare again increased its budget by 19 per cent over 1994 and began to function as the financial instrument of the European Union's pre-accession strategy. Phare now devotes up to 25 per cent of its funds to cross-border cooperation and the co-financing of infrastructure.

Following the Dayton peace agreement reached in December 1995 and on the basis of a multilateral plan, the Commission prepared a new programme for Bosnia-Herzegovina. A first tranche of the Phare Essential Aid programme (of a total of 125 Mecu) was launched in January 1996 and a second tranche in the summer.

The CEECs have practically no old debt to the European Union awaiting rescheduling. The Member States, which do have considerable claims, account for a considerable share of the restructured debt and certainly more than the United States. Official export credits are also mainly in the province of the Member States, so that the European Union operates almost exclusively through them. The Member States have provided more than 73 per cent of all the official export credits received by the CEECs, whereas the United States has provided just over 17 per cent. Lastly, the Member States have provided over 81 per cent of official assistance for private-sector investment, an area also beyond the scope of the European Union as such. The United States have provided just over 17 per cent of the non-IFI total.

[1] including all 15 CEECs

Breakdown of G-24 assistance to central and eastern Europe in the period 1 January 1990 to 1 January 1996 (ECU million)

	Food aid	Emergency non food aid	Restructured debt	Technical assistance	Official exports credits	Official assistance for private investment
EU and Member States	1,394.35	1,411.46	9,320.1	5,784.83	12,926	2,664.2
(European Union alone)	(854.4)	(1,012.2)	–	(3,872.57)	–	–
USA	1,427.4	418.1	2,046.6	2,288.58	3,011.7	579.6
Japan	23.6	–	477.6	39.81	–	–
IFI						
G-24 total (excluding IFIs)	2,974.2	1,988.2	13,164.2	8,447.12	17,539.5	3,259.8
G-24 total (including IFIs)	2,974.2	1,988.2	13,164.2	8,447.12	17,539.5	3,259.8

Source: G-24 Scoreboard

Foreign investment in the countries of central and eastern Europe

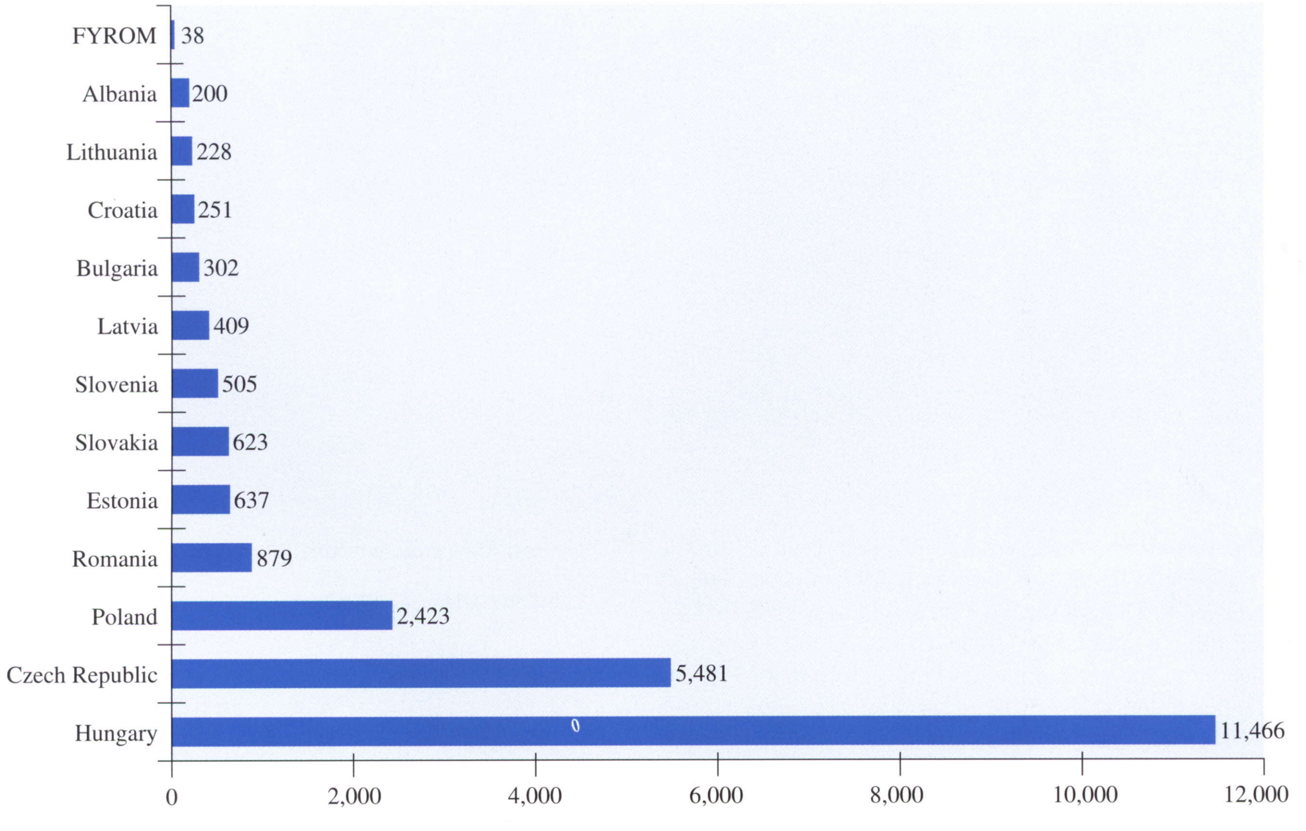
The CEECs need significant levels of foreign investment to continue the upgrading of their economies.

Foreign direct investment (FDI) is a major vehicle for developing a strong, dynamic private sector. It is essential to ensure successful transition to a market-based economic system and integration into the world market. Strategic foreign investors do not only bring debt-free capital but also know-how, technology and access to foreign markets.

Under the socialist planned economy foreign investment was viewed with suspicion. Thus, only with the opening-up of the central and eastern European economies in 1989 did FDI start to enter the region.

Though figures on FDI inflows vary widely, they demonstrate that many foreign investors are still hesitating about entering the region with production facilities. So far, the inflows have met neither expectations nor needs. The cumulative stock of FDI in the 13 CEECs stood at US$ 23.4 bn by the end of 1995. Total inflows in 1995 did not even account for 10 per cent of all FDI flows to developing countries.

Stock of FDI in US$ million at the end of 1995



Source: EBRD Transition Report 1995 and 1996

FDI stock and flows in CEECs 1990-1995

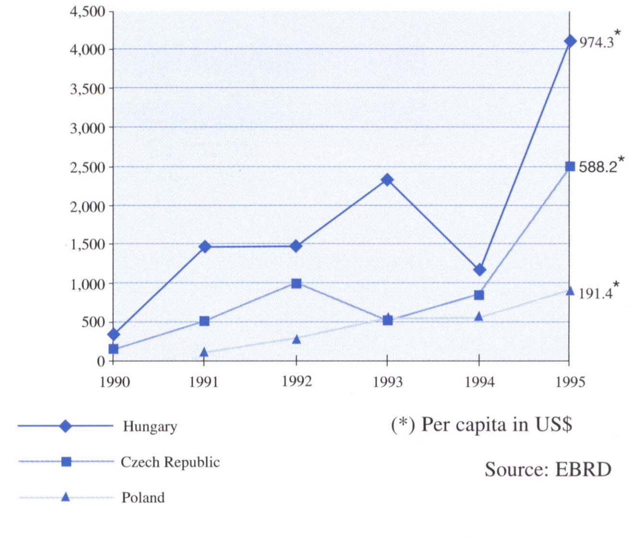
	Inflows in 1995 in US$ million	per capita in US$	Stock 31/12/95 in US$ million	per capita in US$
Hungary	4,100	432	11,466	1,113
Czech Republic	2,500	243	5,481	532
Poland	900	23	2,423	63
Slovakia	180	34	623	117
Slovenia	150	75	505	253
Romania	367	16	879	39
Bulgaria	100	12	302	36
Estonia	193	132	637	413
Latvia	160	64	409	164
Lithuania	55	15	228	61
Albania	70	22	200	63
FYROM	14	7	38	18
Croatia	68	14	251	53
Total	**8,857**		**23,442**	

Source: EBRD

The year 1995, however, was the first year of rapidly accelerated FDI growth. Inflows in 1995 almost doubled over 1994. Though the huge increase has been helped by sell-offs of stakes in Czech telecoms and Hungarian electricity and gas utilities, it could well be that 1995 saw the beginning of a picking-up of inflows of FDI into the region. Preliminary data forecast a further increase for 1996.

Hungary, the Czech Republic and Poland do not only account for the largest increase in 1995, but are generally the spearheads, attracting almost 83 per cent of total investment into the region.

Foreign direct investment flows 1990 - 1995



(*) Per capita in US$

Source: EBRD

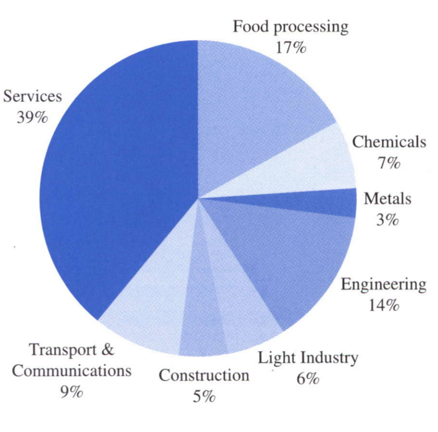
Inflows into particular sectors depend very much on the national privatisation strategy, structure of industry etc. Thus, the Czech republic experienced major inflows into its telecommunications and engineering industry, the former as a result of privatisation, the latter being a traditionally strong sector of the economy. Hungary has opened up its economy the quickest and allowed foreign investors to enter the banking, utilities and telecommunications sector at an early stage. FDI in these sectors was particularly encouraged. However, the breakdown by sector will probably change in the future both according to the nationality of the investor and the economic health of the sector concerned.

Sectoral breakdown of FDI as of 1 January 1995 (%)

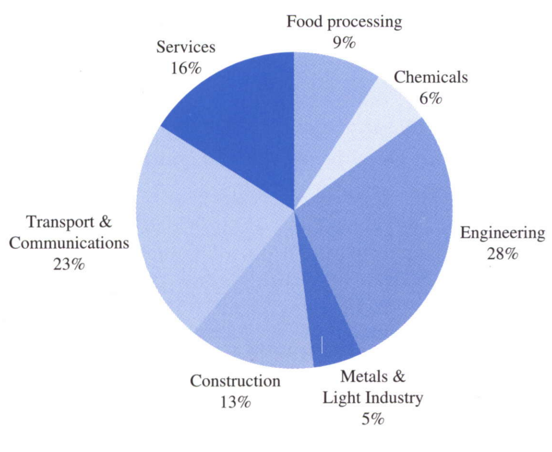
	Industry total	Food processing	Chemicals	Metals	Engineering	Light industry	Construction	Transport & Communications	Services	Total
Hungary	49.9	16.3	6.5	3.1	13.2	6	4.7	8.2	35.5	**100**
Czech Republic	47.6*	9.3	5.7		27.5		12.7	23.3*	16.4	**100**
Poland	64.1	18.3	10	4	17.4*	2.7	3.3	4.1	28.2	**100**
Slovakia	47	2.1	17.7	1.8	19.5	2.3	1.4	0.5	50.9	**100**
Slovenia	49.7	3.3	7.6	1.1	23.7	0	0.2	1	23.8	**100**
Romania		32.6	1.4		26.5		17.6			**100**
Bulgaria	45.2						1.1	24.3	53.7	**100**
Estonia	52.2	8.7	27.9	0.8	2.5	2.1	0.5	9.9	36.3	**100**
Latvia	24.9	11.9	1	0.9	3.3	2.7	1.4	31.6	41.3	**100**

Source: UN/ECE Economic Survey for Europe 1995-1996
* Business Central Europe

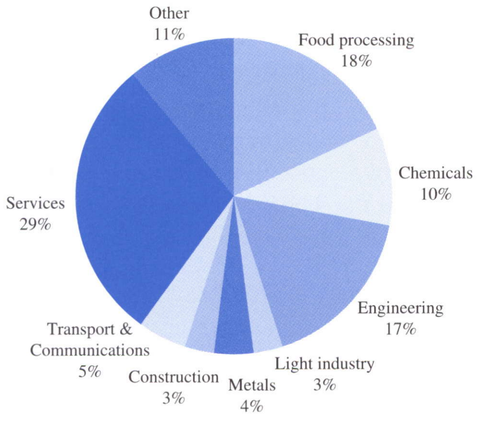
Hungary



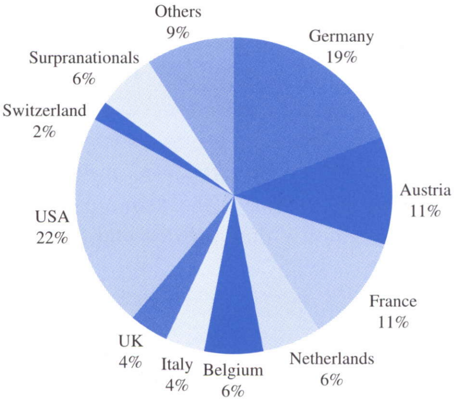
Czech Republic



Poland



FDI by origin in the Visegrad countries

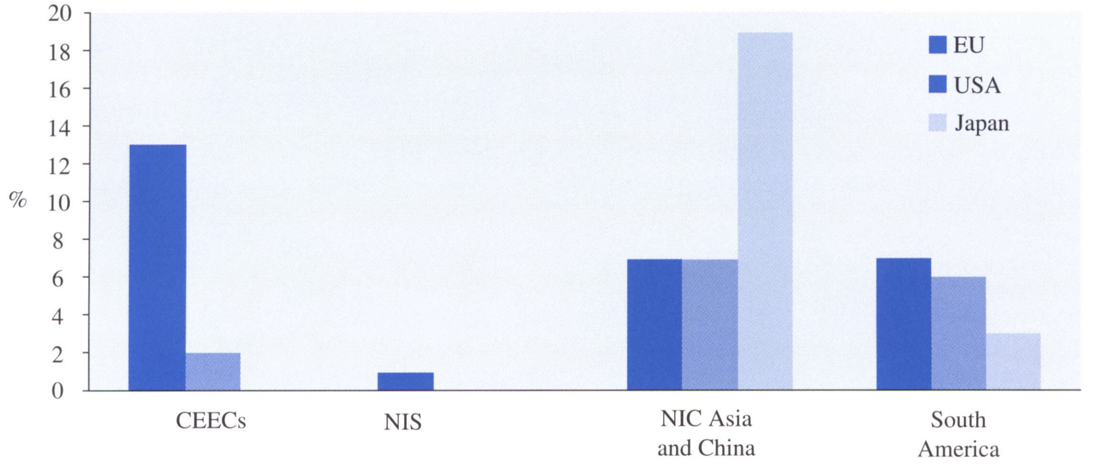


Sources: CzechInvest, CSO, PAIZ,SNAFID

Enterprises originating in the European Union are by far the strongest investors in CEECs. In the four Visegrad countries, investors originating in the EU accounted for at least 60 per cent of total investment at the end of 1994. The USA are the second largest investor, accounting for 20 per cent, whereas there are only a few Japanese investors.

EU enterprises invested 13 per cent of total EU FDI outflows in the central and eastern European economies in 1992-1994. This equals total EU FDI in South America (7 per cent) plus newly-industrialised countries of Asia together with China (7 per cent). In contrast, CEECs received only 2 per cent of total USA FDI and less than 1 per cent of Japan's.

Share of selected regions in total EU, US and Japan FDI outflows (%)



Japanese investors prefer their own region. 19 per cent of total Japanese FDI went to the NIC of Asia and China, only 3 per cent to South America. US companies are inclined to prefer their neighbouring regions as investment locations, too. 9 per cent of US FDI goes to the NAFTA members Canada and Mexico, whereas these countries attracted only 2 per cent of total EU FDI and 3 per cent of Japanese outflows.

Investment promotion and infrastructure investment

The European Union is supporting foreign investment in the CEECs in various ways.

In recognition of the importance of foreign investment, the European Union has made investment promotion a priority area in its pre-accession strategy.

At the European Council of Cannes in 1995, the European Union authorised allocation of up to 25 per cent of the total Phare budget for support of infrastructure investment.

Within the framework of Phare, the EU has helped to set up and run investment promotion agencies in ten Central and Eastern European countries altogether: Hungary, Poland, Czech Republic, Slovakia, Estonia, Latvia, Lithuania, Romania, Slovenia and Bulgaria. Since experience in setting goals and selecting target sectors for attracting FDI was lacking, the EU provided assistance with the much needed strategy and policy formulation. Further services provided for by Phare include institutional assessment, help with marketing and research, training and supply of equipment. Implementing the pre-accession strategy, Phare has increased its support for the autonomous government bodies and provided help for harmonisation of fiscal and other legislation.

The Phare - Joint Venture Programme's (JOP) aim is to facilitate productive European Union investment in the CEECs, especially through the creation of joint ventures. By encouraging cooperation between partners located in the EU with partners in the CEECs, the EU contributes to the efforts of the CEECs to develop productive investment and a market economy.

Last but not least there are plenty of initiatives by the Member states providing for instruments which help to promote investment in CEECs, including bilateral agreements on promoting investment and avoiding double taxation.

However, one should keep in mind that the possibilities for investment promotion by international institutions are limited. According to surveys among foreign investors, the crucial role in encouraging FDI lies with the central and eastern European governments. Unless national governments guarantee a sufficiently stable legal framework and provide for a favourable business climate, foreign investors cannot be persuaded to invest and remain put off by uncertainty and high risk.

The CEECs have already made considerable progress in removing trade and investment obstacles. The European Union is supporting these endeavours in every respect.

This document has been prepared by Anne Ev Enzmann with Maurice Guyader, Manlio Condemi and Michèle Barth.

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