

EUROPEAN PARLIAMENT



DIRECTORATE GENERAL FOR RESEARCH

WORKING DOCUMENT

**TRADING BY THE NEW GERMAN LÄNDER WITH
THE FORMER COMECON COUNTRIES IN EUROPE**

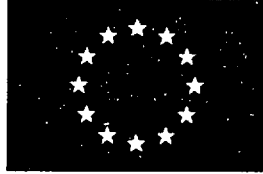
DEVELOPMENT, PROBLEMS AND PROSPECTS

EXTERNAL ECONOMIC RELATIONS SERIES

W 2

EN - 3 - 1992

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BY THE

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FOREWORD

In May 1992, in Dresden, the European Parliament is organizing a conference to discuss the impact of the economic and social situation in the five new German Länder on the Community's policies.

That prompted the European Parliament's Directorate-General for Research, in line with the wishes of the Committee on External Economic Relations, to commission this study on the external trade aspects of the conference from the Halle Economic Research Institute.

The study aims to provide an analysis of trading by the new German Länder, following German unification, with the former COMECON countries in Europe. It aims to portray the key problems and discuss the consequences thereof, in particular any impact of the Community's commercial policy and corresponding effect of investment from other EC countries on that trade, together with an examination of any competitive advantages for the new Länder because of their earlier trading relations with the former COMECON countries.

The study also aims to describe the prospects for that trade, the examination focusing on the scope for development and on recommended action to be taken as part of EC trade policy towards the group of countries referred to.

Luxembourg, March 1992

DIRECTORATE-GENERAL FOR RESEARCH

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Overview

Within two years, trading by the new German Länder with the states of Central and Eastern Europe has fallen to one third of its original level. The decisive factor in this has been the fundamental change that has taken place in East Germany's regulatory environment as a result of monetary union and German reunification. Political and economic transformation in Eastern Europe, together with the disbanding of COMECON, has speeded up this process.

Contrary to expectations, East Germany has not become the hub of intensifying trade relations between East and West. Very few traditional economic links have been maintained, with the result that a completely fresh start is having to be made in most areas. The headlong decline in trade has not been checked by the transitional arrangements adopted, for the adjustment period, by the European Community and the Federal Government; were it not for those arrangements, however, matters would have been worse.

To judge from the prospects for trading by the new Länder with the East in the short and medium terms, no more than a gradual recovery - at a modest level - is likely. More effective forms of European Community support for the revitalization of trade with the East would appear imperative.

1. Introduction

When German reunification took effect on 3 October 1990, East Germany (the former GDR) was formally incorporated into the European Community. German economic and monetary union - three months previously - had been the vital step in that direction. For the European Community, the incorporation of East Germany was an historically unique event made possible only because East Germany had taken over virtually the entire regulatory environment, as it stood, from the old Federal Republic's market economy and political system.

A sweeping and complex process of structural change began for the East German economy, throwing up inconsistencies as it proceeded. It extended to external trade, too; in the former GDR, this was characterized by its bias towards the COMECON states - its role in the international division of labour being modest overall - and by a product structure that was inappropriate for highly industrialized countries. Initially, it appeared desirable to maintain many of the external trade links of the new German Länder with their Central and Eastern European partners, since, in spite of the distortions and structural weaknesses caused by the system, considerable business was done with Eastern Europe in terms of both quality and quantity. In 1989 the GDR's exports to the European COMECON area were the equivalent of a little more than half the exports of all EC countries combined to Eastern Europe. The equivalent figure for imports was about 47%. After the new German Länder had been incorporated, therefore, the potential opportunities afforded by intensifying economic cooperation between the Community and the former COMECON had grown. The Community's declared political objective was to capitalize on them in spite of the warranted assumption that, for market reasons, trade flows between the new Länder and Eastern Europe would initially decline considerably. The transitional arrangements adopted were therefore geared to bringing traditional trading structures into line with the fact of East Germany's incorporation - in legal, political and economic terms - into the Community. Expectations were even voiced that the external trade obligations of the new Länder might become a catalyst for pan-European economic cooperation¹.

This study provides an analysis of how trade involving Eastern Europe has actually developed since German unification, describes the key factors and problems in this connection, and examines the medium-term prospects for the new trade relations, which are based on the market economy.

¹ The Community and German Unification, COM(90) 400 final, Volume 1, p. 49

2. Quantitative and structural change in trading by the new German Länder with the countries of Central and Eastern Europe since 1989

2.1. A new environment and overall trends

Over the last two years there has been considerable change, in both quantitative and qualitative terms, in trade with the East by the new German Länder. This is the result of the entirely new conditions - in the domestic economy and in external trade - which have emerged for East German enterprises. Although certain processes of radical change had already been set in train, the institution of economic and monetary union on 1 July 1990 was the vital turning point. That was the beginning of what was a rigorous and irreversible transition for the East German economy from centralized planned economy to social market economy. That was also the point when the economy began to be cut free from the Eastern European economic association and integrated into the all-German and hence Western European economic area. That led to shock - because of the structural change and transformation - the scale of which was initially underestimated; that shock has not yet been overcome; because of it, a completely fresh start has been necessary in most areas of economic activity. The immediate opening up of the economy to world markets, accompanied by substantial revaluation of the currency, was the most significant change in external trade conditions.

At the same time as the economy was being reformed in East Germany, major political and economic changes were taking place in all Central and Eastern European states which largely removed the basis for trade among the former COMECON countries. As a result, COMECON was disbanded and its pricing, financial and clearing system done away with, which had a considerable impact on trade relations with East Germany.

It is now certain that initial expectations as to the ability of the East German Länder to hold their own as the hub for Germany's trade with the East (or even Western Europe's as a whole), or to become such a hub, have turned out to be unrealistic. What is more likely, rather, is that, in future, the Central and Eastern European countries' relations with united Germany will act as the catalyst to which reference has been made.

The potential significance of trade with the East for the viability of many East German firms, and for the likely economic upswing in the new Länder, must be reassessed, however². An analysis of trade relations in quantitative terms bears out this view.

East German firms' relations with the European COMECON countries in terms of imports and exports stagnated, at a very high level, from 1985 to 1989; by November 1991, they had dwindled to about one third of the 1989 level. Imports were particularly affected, declining by three quarters, while export figures were still about 41% of the 1989 level.

² Until 1989, trade with the European member countries of COMECON was a significant factor in the development of the GDR's economy. According to statistics, that group of countries accounted for 70.3% of the total exports of the GDR (excluding German-German trade) (USSR: 40.3%) and 65.1% of its total imports (USSR:37.4%). It should be borne in mind that, because the transferable rouble was overvalued vis-à-vis Western currencies, these proportions are statistically too high. It seems more realistic to the authors that trade with the East accounted for some 50% of the GDR's external trade.

Table 1:

External trading by the GDR / new Länder with the states of Central and Eastern Europe³ since 1985: volume and movement

	Average 1985 to 1988 DM bn	1989		1990		January-November 1991	
		DM bn	%change over prev. year	DM bn	%change over prev. year	DM bn	%change over prev. year
Exports	28.80	28.89	99.1	29.72	102.9	10.69	40.1
Imports	28.15	26.79	96.6	14.81	55.3	6.24	44.5

Source: Federal Statistical Office, IAW calculations

This implosion-like collapse in trade with the East both stems from and has caused the thoroughgoing shock of economic adjustment in the new Länder and can be properly evaluated only in that context. Within two years, gross domestic product fell to about 60% and manufacturing sector output to as low as about 42% (of the 1989 level). This process has not been uniform: while some production areas have been completely wound up, other branches of industry have been less affected by downturns in production.

Table 2:

Major indicators of trends in the East German economy for 1989, 1990 and the first half of 1991

	1989	1990		1st half of 1991	
	DM bn	DM bn	Percentage change over previous yr	DM bn	Percentage change over previous yr
Gross domestic product	284.4	230.0	80.9	85.7	64.4
Gross value added					
- Agriculture and forestry	9.3	8.0	85.1	2.7	69.2
- Manufacturing	130.1	97.6	75.0	27.1	44.6
- Trade and transport	46.2	39.9	86.4	16.7	74.2
- Services and public sector	98.8	85.4	86.5	39.4	86.4
Capital investment	62.0	50.8	81.9	26.0	96.3
Total external trade	82.2	61.6	74.3	14.3	40.2

Source: Federal Statistical Office

However, an analysis of trade relations between the old Länder and the states of Central and Eastern Europe in recent years confirms that there was by no means a general collapse in German trade with the East. On the contrary, in

³ The countries included here, and in the following tables, are the USSR, Poland, Hungary, the CSFR, Romania and Bulgaria; cf. also Tables 2 and 3 in Appendix.

some instances Eastern European states achieved significant growth rates in exports to West Germany, principally because market economy criteria had long been the basis for those exports, but also because government policy in Eastern Europe gave them particular encouragement and, to some extent, trade relations with successful West German firms were stepped up at the expense of East German enterprises.

Table 3:
Trading by the old Länder with the states of Central and Eastern Europe since 1985: volume and movement

	Average 1986 to 1988 DM bn	1989		1990		January-November 1991	
		DM bn	%change over prev. year	DM bn	%change over prev. year	DM bn	%change over prev. year
Exports	18.96	24.44	124.4	23.39	95.7	23.25	108.8
Imports	16.66	19.01	119.1	21.76	114.4	24.01	121.9

Source: Federal Statistical Office, IAW calculations

Much the same can be said of the trade relations of the EC Member States as a whole with Eastern Europe until mid-1991 (cf. Table 5 in Appendix).

Because the positions of the old and new Länder in trade relations with the East have reversed, the significance of the East German economy for trade with Eastern Europe, which used to be considerable, has, in an all-German context, now become much smaller (cf. Table 2 in Appendix). While, in 1989, East Germany still accounted for about 55% of German trade with the East - Germany taken as a whole - that figure had fallen to about one quarter by the end of 1991.

In terms of volume, trade with the East by the new Länder has dwindled to become an insignificant factor for the economy of Germany as a whole. From January to November 1991, it accounted for 1.7% and 1.1% of united Germany's exports and imports respectively. In qualitative terms, however, it must be regarded as much more significant for the economic situation and necessary upturn in the new Länder.

The swift decline in trade with the East did not affect imports and exports simultaneously; decline occurred after fundamental changes had taken place in the relevant regulatory environment.

2.2. Movement in imports

Statistics show that the break in relations between the new Länder and Eastern Europe with regard to imports came with the introduction of monetary union in mid-1990, which created an entirely new business situation for East German enterprises.

Imports from Bulgaria, Romania and Hungary came to a virtual standstill, but imports from the Soviet Union in the second half of 1990 reached only 33.1% of the previous year's level too.

Table 4:
Imports into the new Länder from Eastern Europe
(DM m)

Country	1989	1990			1991 Jan.-Nov.
		Total	1st half	2nd half	
Soviet Union / CIS	15392	9107	6526	2581	4504
Poland	3061	1800	1367	433	717
CSFR	3246	1720	1350	370	667
Hungary	2435	1233	954	279	239
Romania	1335	407	351	56	77
Bulgaria	1324	545	500	45	35

Source: Federal Statistical Office, IAW calculations

The key factors in this development have been as follows:

- (a) East German firms made use of their new opportunities to gain access to better Western products, preferably from the old Länder and other EC Member States. In the main, Eastern European goods and services proved to be insufficiently competitive with regard to technical standard, production quality, allegiance to customers and performance.
- (b) Particularly in the second half of 1990, imports became considerably more expensive, in relative terms, because of the conversion rate between the transferable rouble and the Deutsche Mark (1 to 2.34) which had been laid down for supply contracts that had already been concluded, though that was no longer relevant from 1991 onwards.
- (c) The fact that East German industry, which was the principal customer for primary products and capital goods from Eastern Europe, cut production considerably, and its own fixed asset investment declined at the same time, had a major impact on requirements of imports from Eastern Europe.
- (d) For a long time, there was uncertainty in most cases as to whether East German firms could be salvaged and what scope there was for their privatization. The rapid break-up of the integrated production units (the Kombinate) created a new economic system with uncertain prospects. A number of Eastern European partners therefore geared their economic links to powerful West German firms.

During the last few months of 1991, imports from the CSFR, Hungary and Poland picked up again a little. To what extent that conceals a stable trend remains to be seen.

2.3. Movement in exports

The rate of change with regard to exports has been different. Initially, in the second half of 1990, East German firms succeeded in increasing their exports to Eastern Europe (except for the CSFR and Bulgaria). That was the result, however, of what was a unique transitional situation and, as such, could in no way be a model for the future. The following were significant factors in that short-lived upturn:

- Invoices in connection with supply contracts were still being made out in transferable roubles.
- The exchange rate for the transferable rouble, which was overvalued, provided a powerful export incentive.
- The supply crisis in many Central and Eastern European states, and the lack of decisions on arrangements for subsequent settlement of balance, made

Eastern European countries more interested in additional imports. Because of unused capacity in the East German economy, a prompt response was possible.

- To safeguard confidence in existing contracts and secure East German exporters' cash position, the Federal Republic temporarily granted sizeable subsidies.

At the start of 1991, exports began to decline with much the same ferocity as imports had six months previously. This hit exports to all Eastern European countries, the least decline, in relative terms, being in exports to the Soviet Union and Poland.

Table 5:
Exports from the new Länder to Eastern Europe
(DM m)

Country	1989	1990			1991	
		Total	1st half	2nd half	January - November	% change over previous year
Soviet Union/CIS	16576	17761	8052	9709	8440	53.3
Poland	3116	2944	1069	1875	952	37.7
CSFR	3814	3405	2056	1349	607	19.2
Hungary	2597	2696	1263	1433	353	14.5
Romania	1429	1505	749	756	212	15.5
Bulgaria	1361	1412	819	593	123	9.4

Source: Federal Statistical Office, IAW calculations

The crucial factors in this, which are interrelated, are as follows:

- (a) When the switch to trade based on convertible currencies took place, world market conditions won through in the Eastern European economic area too. It has become plain for all to see that many East German firms are not up to international competition; there is a lack of competitive products and viable marketing strategies; in addition, distribution systems are inadequate.
- (b) The structural adjustment crisis in all Central and Eastern European countries - involving a swift decline in the productive capacity of the economy as a whole, high budget deficits, increasing financial difficulties for firms, an end to industrial cooperation arrangements which in the main emerged within a planned economy environment, and an across-the-board drop in real incomes - has appreciably worsened. This is continuing to have an adverse effect on the degree of intensity and structure of external trade, in particular with the East German market.

2.4. High trade surpluses

Trade between East Germany and Eastern Europe over the last few years has been characterized by the severe imbalance between imports and exports, which has given the GDR / new Länder high trade surpluses.

Table 6:
Trade surpluses achieved by the new Länder vis-à-vis Eastern Europe
(DM m)

Country	1989	1990	Jan.-Nov. 1991	Total since 1989
Soviet Union / CIS	1184	8654	3936	13774
Poland	55	1144	235	1434
CSFR	568	1685	-59	2194
Hungary	162	1463	114	1739
Romania	94	1098	135	1327
Bulgaria	37	867	88	992
Total	2100	14911	4449	21460

Source: Federal Statistical Office, IAW calculations

It should be borne in mind that export surpluses were denominated in transferable roubles until the end of 1990. Their DM value was calculated on the basis of the official conversion factor. No agreements have as yet been reached as to settlement in this regard by the Central and Eastern European countries concerned. Effectively, they constitute interest-free loans to those states.

Surpluses since January 1991 show that, even at the current very low level of trade, very few sales outlets have been opened up in the new Länder by Eastern European firms. Through successful marketing in the old Länder, however, the CSFR, Hungary and Romania have recorded export surpluses (with reference to Germany as a whole).

2.5. Changes in trade structure by group of countries

Two significant conclusions can be drawn from an examination of the regional structure of the external trading activity of the new Länder from 1989 to 1991:

- (a) Relations with the countries of Central and Eastern Europe continue to dominate external trading as a whole by the new Länder. The significance of the EC countries, while it has increased, remains relatively modest, however.

In 1989, the former COMECON countries in Europe accounted for some 70% of GDR trade (not including German-German trade), whereas the EC countries (not including the FRG) accounted for less than 10% of the total. That stemmed from East German producers' inadequate, and worsening, competitiveness. The situation changed following monetary union inasmuch as, initially, Central and Eastern European countries' share of exports rose as high as 78% plus, falling in 1991 (following the introduction of convertible currencies in trade with Eastern Europe too) to a good 60%. The EC countries' share of imports rose somewhat more quickly, though either stagnated or fell in absolute terms, admittedly more slowly than imports overall.

Table 7:
Percentage breakdown of the external trade of the new Länder, mid-1991

	EC countries	EFTA countries	Developing countries	Central and East. Europe
Imports	18.2	8.1	6.1	62.9
Exports	16.8	6.1	7.9	65.1

Source: Federal Statistical Office, IAW calculations

- (b) In connection with trade with the East by the new Länder, the significance, in terms of both exports and imports, of the USSR/CIS, which was already dominant while the GDR still existed, has grown substantially. The crucial factor in this is the fact that, in its raw materials and fuel, the Soviet Union possesses export products which are saleable on the world market and that its imports of East German manufactures benefited from the special terms for Hermes credit guarantees until the end of 1991 at least.

Table 8:
Percentage breakdown of trade with the East by the new Länder

Country	Exports			Imports		
	1989	1990	Nov. 1991	1989	1990	Nov. 1991
USSR	57.4	59.8	79.0	57.4	61.5	72.2
Poland	10.8	9.9	8.9	11.4	12.2	11.5
CSFR	13.2	11.5	5.7	12.1	11.6	10.7
Hungary	9.0	9.1	3.3	9.1	8.3	3.8
Romania	4.9	5.1	2.0	5.0	2.7	1.2
Bulgaria	4.7	4.8	1.2	4.9	3.7	0.6

Source: Federal Statistical Office, IAW calculations

The other Central and Eastern European countries, in some instances, have become much less significant, however. Only relations with Poland and the CSFR remain of significance. Further shifts are likely in the near future, however. The dominant role of the CIS will diminish, while the significance of trade with the smaller Central and Eastern European countries could gradually rise.

The fact that the present situation is very different from the breakdown, by country, of trade with the East by the old Länder is striking. The significance of the USSR in terms of exports and imports has decreased (to 33.6% and 37.6% respectively), while, in certain respects, that of the so-called reforming countries - Poland, Hungary and the CSFR - has risen considerably. The specific reasons for these differences remain to be investigated.

2.6. Changes in trade structure by category of goods⁴

There have been radical changes in the breakdown of imports and exports not only by country, but also by category of goods. They reflect the growing influence of world economic factors over Eastern Europe's economies, together with changes in supply and demand within those economies.

What is striking, with regard to exports, is that a much greater proportion of foodstuffs (including meat and dairy products) has been sold and that there has been a substantial decline in chemicals and machinery. Nevertheless, machinery and vehicles account for by far the largest share of exports from the new Länder to all Central and Eastern European countries (in the first half of 1991: over 40% in respect of Poland, the CSFR and Hungary; 57% in respect of the USSR; and as much as 73% in respect of Bulgaria).

⁴ cf. Appendix, Table 7

Table 9:
Percentage breakdown of exports, by category of goods, from the new Länder to Central and Eastern Europe

Category of goods, SITC Rev. 3	1989	1st half of 1991
0 Food and live animals	1.4	13.9
1 Beverages and tobacco	0.1	0.8
2 Crude materials (not including 0 and 3)	0.9	1.4
3 Mineral fuels	2.4	2.9
4 Animal and vegetable oils	0	0.1
5 Chemicals and related products	9.4	6.1
6 Manufactured goods	10.4	7.5
7 Machinery and transport equipment	60.4	53.4
8 Miscellaneous manufactured articles	13.9	12.2
9 Other commodities and transactions	1.1	1.7

Source: Federal Statistical Office, IAW calculations

The problem for the East German economy is that the decline in exports has particularly hit those branches of industry which used to underpin the export business in the past. In the chemicals category, only medical products and pharmaceuticals in the first half of 1991, together with organic chemical products, achieved impressive export volumes. With regard to machinery and transport equipment, only exports of rolling stock and vessels, worth a little more than DM 1 bn, 96% of which was sold to the USSR, were significant.

A detailed country-by-country breakdown reveals that, for most categories of goods, the USSR/CIS is the dominant importer. In addition to rolling stock and vessels, which have already been referred to, that holds true for machinery and equipment for agriculture, the construction industry, the textiles, leather goods and stationery industries, the food and animal feed industry, and the printing and bookbinding industry. In addition, office equipment and computers also have a part to play, albeit one of diminishing importance. The share accounted for by food and consumer manufactures has increased, but there has been a prompt fall in supplies of products from the electrical and electronics industry, from the precision engineering and optical industry and from the machine tools industry.

The most important exports to Poland in the first half of 1991 were machinery and transport equipment, in particular road vehicles. In addition, supplies of oil and oil products and foodstuffs, in particular meat and meat products, increased substantially.

The dominant exports to the CSFR were electrical machinery, appliances and equipment, special-purpose machinery⁵, metalworking machinery and road vehicles. Chemical products accounted for a comparatively modest proportion of exports - 20% - anorganic and organic chemical products and fertilizers being more significant than in the past. Exports of non-ferrous metals remained virtually constant. The CSFR was far and away the largest Eastern European market for inorganic chemical products and fertilizers and non-ferrous metals. Exports of office equipment and computers, on the other hand, fell off substantially.

Supplies to Hungary of road vehicles and special-purpose machinery, but also of mineral fuels (coal, coke and briquettes) and organic chemical products, were more significant than in the past.

⁵ Special-purpose machinery comprises the following: agricultural machinery, tractors, construction machinery and equipment, machinery for the textiles and leather goods industry and the paper manufacturing and stationery industry, printing presses and bookbinding equipment.

The principal feature of the structural changes in imports from Central and Eastern Europe into the new Länder is that mineral fuels and primary processing commodities suffered the least decline in volume terms, their share increasing considerably as a result.

Table 10:
Percentage breakdown of exports, by category of goods, from the new Länder to Central and Eastern Europe

Category of goods, SITC Rev. 3	1989	1st half of 1991
0 Food and live animals	1.4	0.9
1 Beverages and tobacco	1.5	0.2
2 Crude materials (not including 0 and 3)	4.0	2.3
3 Mineral fuels	29.6	59.3
4 Animal and vegetable oils	0	0
5 Chemicals and related products	4.4	3.9
6 Manufactured goods	14.5	9.7
7 Machinery and transport equipment	35.8	20.8
8 Miscellaneous manufactured articles	4.2	1.7
9 Other commodities and transactions	4.6	1.2

Source: Federal Statistical Office, IAW calculations

Oil and oil products alone accounted for 45.4% of total imports from Eastern Europe in the first half of 1991. Iron and steel and non-ferrous metals accounted for a further 7.4%, the USSR being the main supplier of all these products. Imports of machinery and transport equipment in the first half of 1991 were worth only DM 765 m. Apart from imports from the Soviet Union, only imports from the CSFR (a little over DM 500 m) were of any significance. The decline in the share accounted for by the machinery and transport equipment category stems from the collapse of a good number of collaborative arrangements in this area. In 1989, for instance, machinery and transport equipment accounted for 44.7% of imports from Poland into the new Länder, while the share for the first half of 1991 was 23.2%.

Further features unique to certain countries are to be found in few areas. There was such a substantial increase in the first half of 1991 in purchases of non-ferrous metals from Poland that Poland became the main supplier of non-ferrous metals, after the Soviet Union, and that category of goods accounted for 13% of imports from Poland.

Road vehicles, organic chemical products and rolling stock accounted for the largest proportion of imports from the CSFR (22%). Purchases of special-purpose machinery fell off substantially, however. Mineral fuels (in particular coal, coke and briquettes) have also become negligible in terms of imports.

Special-purpose machinery and vehicles, but also foodstuffs on a large scale, were the main imports from Hungary. Of foodstuffs, cereals and cereal products plus vegetables and fruit were the most important; in this area, Hungary was by far the largest Eastern European supplier to the new Länder. Imports of road vehicles (buses) and wine slumped.

3. Economic policy as a factor in trade with the East by the new German Länder

In view of the frictional effects - in both quantitative and structural terms - on trade with the East by the new Länder which were expected following German reunification, measures were laid down for a transitional period which were designed to ease the necessary adjustment process for the East German economy. This concerned both European Community derogations and German Federal Government decisions.

3.1. Application of the European Community's common commercial policy

In principle, the new Länder were incorporated into the common commercial policy on the day of unification, a form of advance customs union having been in existence since German economic and monetary union came into effect. Adjustment measures concentrated on import arrangements, since exports were not regarded as particularly problematic for the European Community. In this connection, the greatest importance attaches to the tariff measures benefiting the former member countries of COMECON. This relates to the special arrangements to suspend - from 3 October 1990 to 31 December 1992 - the common customs tariff, including anti-dumping duties, applied to certain imports of goods originating in Bulgaria, the CSFR, Hungary, Poland, Romania, the USSR and Yugoslavia on the basis of yearly maximum quantities or values derived from the former GDR's trading agreements with those countries for 1990 and with Poland for 1989. To date, however, the practical impact of suspending tariffs can only be termed modest. By 30 November 1991, under these arrangements, goods to the value of DM 674.3 m had been imported duty-free into the new Länder: DM 245.5 m in the fourth quarter of 1990, DM 128.5 m in the first half of 1991, and DM 300.3 m from July to November 1991. As a proportion of the potential volume of duty-free imports, this amounts on average to 3.8% for the last quarter of 1990 and to 1.8% from January to November 1991.

Take-up by Yugoslavia, Poland and the USSR of duty-free imports has been below average, whereas it has been above average in trade with Bulgaria and Romania. Duty-free admissions from the CSFR and Hungary, too, were above average in 1991.

When evaluating the volume of duty-free imports, it should be borne in mind that some of the goods eligible for duty-free admission and some covered by the 'overall imports' heading are zero-rated anyway in the Common Customs Tariff (CCT). This is particularly true of raw materials⁶. It is not possible to separate precisely the goods which are zero-rated in the CCT from the rest. The same applies to imports under the Generalized System of Preferences (GSP) and the Cooperation Agreement with Yugoslavia.

A comparison of duty-free imports between the fourth quarter of 1990 and the period January-November 1991 demonstrates that all Central and Eastern European countries' shares have declined.

⁶ In Table 11, accordingly, the share of duty-free imports accounted for by the USSR/CIS and Poland, which are the two main suppliers of raw materials, must be ranked much higher.

Table 11:
Take-up of potential duty-free exports in 1990 and 1991 by country

Country	Percentage of imports accounted for by duty-free imports		Percentage of potential volume of goods, under goods protocols, accounted for by duty-free imports	
	3.10.1990 - 31.12.1990	1.1.1991 - 30.11.1991	3.10.1990 - 31.12.1990	1.1.1991 - 30.11.1991
USSR	7.0	6.3	2.3	2.2
CSFR	38.6	9.1	10.2	2.2
Hungary	25.1	11.9	6.7	1.4
Poland	9.9	4.4	3.2	1.1
Bulgaria	49.0	27.3	3.2	0.8
Romania	40.3	17.4	2.7	0.9
Yugoslavia	11.2	2.9	2.2	0.5
Total	13.1	6.9	3.8	1.8

Source: Federal Ministry for Economic Affairs and authors' own calculations

The underlying reasons for this movement are explained in detail in Chapter 2 of the study.

In addition, the above figures on the take-up of the preferential import facility show that the transitional measures have had a very limited impact. Distortions of competition have not occurred. The Community's accompanying trade policy measures have not been able to counteract the adverse impact on traditional trade relations which has been caused by comprehensive structural change in East Germany and in the countries qualifying for this facility.

The low take-up does not allow us to conclude that exemption from customs duties is of no economic importance to many East German firms. Many firms in the new Länder are overhauling their business operations. Market openings, competitiveness and purchasing opportunities have to be analysed afresh. Rethinking a sales strategy takes time, and the Community measures are helping to maintain some traditional business relations. In the fourth quarter of 1990 and from January to November 1991, for example, some 1200 firms in the new Länder made use of the customs duty exemption arrangements.

The continuation of the transitional tariff measures until 31 December 1992 will provide useful transitional aid for the economic stabilization of a number of firms in the new Länder which are undergoing a difficult restructuring process⁷.

The renegotiation of continuing obligations has been affected by further transitional arrangements. The vast majority of the agreements concluded by the former GDR with other states have become irrelevant as a result of German unification and the incorporation of the territory of the GDR into the European Community and indeed, in many instances, as a result of the political and economic upheavals in Eastern, South-Eastern and Central Europe. In a number of cases, it has proven expedient to keep earlier agreements in force. That holds true for joint investment projects. In order to bring terms and conditions into line with the changed circumstances, the authorities of the FRG are holding consultations with the parties with which the former GDR concluded agreements; representatives of the Commission of the European Communities, too, have been involved in those consultations since July 1991.

⁷ cf. the Commission report to the European Parliament and the Council on the application of transitional tariff measures as a result of German unification (SEC(91) 2159 final), p. 7

The decision to allow a two-year derogation from European Community standards and quality requirements - in connection with production in, and imports into, the new Länder - was also designed to make it easier to adjust. There are no research findings on the actual effect of this, but it may be assumed that the decision is likely to have had a negligible impact in practice.

3.2. Federation and Länder assistance for trade with the East

To safeguard confidence in existing contractual obligations towards members of COMECON, as laid down in the Treaty on Unification (Article 29), exports by enterprises in the former GDR were subsidized in the second half of 1990, upon request, to the value of DM 2 bn in total. At the same time, the Government-fixed exchange rate for the transferable rouble and the Deutsche Mark (1 to 2.34) created a powerful export incentive. In spite of what was an incipient structural adjustment crisis, exports to the COMECON countries in the second half of 1990 rose 8% over the same period the previous year.

No assistance was given for imports from those countries, by contrast, which fell 73% during the same period.

The special terms of the Hermes credit guarantees for exports to the Soviet Union and its successor states (advance payments waived; three-year period of grace for repayment of principal) constituted the Federal Government's key instrument in 1991 to encourage trade with the East. This considerably slowed down the decline in exports from the new Länder to the Soviet Union by comparison with exports to the other former COMECON countries. Take-up of the Hermes credit guarantee arrangements for exports to those countries (no special terms; Bulgaria temporarily excluded) has been no more than modest.

Trade with the East is fostered by the various forms of cooperation between these countries and Federal Government ministries and the Länder. At Federal Economic Affairs Ministry level, this takes place first and foremost within the Joint Commissions and their specialist working parties. Following the disintegration of the Soviet Union, moves involving individual ex-Soviet republics got under way to set up standing advisory bodies (Cooperation Councils) to provide support for the reform processes and to promote bilateral economic relations. The German-Russian Cooperation Council was set up on 18 February 1992.

At the same time, German industry has set up consulting agencies (cofinanced by the Federal Ministry for Economic Affairs) in a number of Eastern European countries which subsequently could be turned into bilateral chambers of foreign trade. The Federation has given assistance for, in particular, business management and industry-specific consultancy services in the countries of Central and Eastern Europe (DM 10 m in 1991; DM 16.6 m in 1992).

In addition, the Federation is supporting a variety of management and vocational training measures. DM 14 m was available for this in 1991; some DM 18 m has been earmarked for 1992. Not only have measures been continued in the CIS in 1992, but additional operations have been put in hand in the CSFR, Bulgaria, Romania and the Baltic states too.

In 1991, the Federal Ministry for Economic Cooperation made use of its well established methods to carry out activities in Bulgaria, the CSFR, Poland, Romania and Hungary. This year, they have been extended to the Baltic region and the republics of the former USSR with a view to promoting the development of a market economy. The aim is to provide a flexible response to needs in terms of advisory services by providing funding for studies and specialists.

The new Länder have also taken a number of measures to assist the firms which operate there to trade with the East. The following should be highlighted: the programme for cooperation between the border regions of Brandenburg and Poland, the setting up of Russian-Brandenburgish and Ukrainian-Brandenburgish working parties, the arrangement for industrial cooperation with Hungary and Ukraine (assisted by the Government of the Land of Saxony-Anhalt), and

measures taken by all the new Länder in connection with the initial and in-service training of skilled workers and managerial staff in the countries of Central and Eastern Europe.

3.3. Privatization in the new Länder and implications for trade with Central and Eastern Europe

Taking economic activity out of the public sector, with priority going to the privatization of the means of production, has been the starting point for the most important structural adjustment processes, which have a corresponding impact on external trade.

Privatization has focused on selling 100% stakes in firms to business investors, since this is the best way of providing the requisite capital and know-how. An important motive for buying is the scope that exists for placing a firm on a healthy footing, which is evaluated on the basis of business criteria, including selling conditions. Maintenance and expansion of links with the Eastern European market is a major factor in this connection.

It has proved to be the case, nevertheless, that progress in privatization is not synonymous with growth in trade with Eastern Europe. On the contrary: there are often setbacks initially, as a result of altered business strategies, even if long-term prospects for trade with the East improve. This is fundamentally true for the involvement of foreign buyers in the privatization process, the scale of which can only be termed too low.

Of the total of 5210 firms which the Trust Agency had sold outright or in part by the end of 1991, 248 sales (4.8%) involved foreign investors.

Of the EC countries, there were 44 partners from France, 26 from the United Kingdom, 24 from the Netherlands, 11 from Denmark, 10 from Italy and nine from Belgium. Sales to buyers from Switzerland (42), the US (19), Sweden (18) and Austria (17) were also significant. Foreign involvement has safeguarded some 92,000 jobs (9.2% of the total number of jobs safeguarded through privatization), and some DM 10.5 bn in investment has been pledged (9.2% of the total investment pledged as a result of privatization). The impact of these privatization measures in terms of employment and investment is therefore greater than their share of privatization overall. There is no information as to the scale of foreign investment that has already been made. Realistically, the impact of this to date on trade with the East should be rated as modest. However, a survey of firms in 1991 found that, out of a list of 13 motives for acquiring an East German firm, foreign buyers put 'to tap the Central and Eastern European market' in third place (after 'to acquire the land belonging to the East German firm' and 'to tap the East German market').

As far as a breakdown, by industry, of acquisitions of firms by buyers from EC states is concerned, the focus has been on the primary and producer goods industry; on food, beverages and tobacco; on construction; and on commerce - together they account for two thirds of acquisitions. While development of the East German market is likely to have been the clinching factor behind decisions to acquire firms in the primary and producer goods industry and in the construction industry, with an eye to the likely building boom, the possibility of tapping Central and Eastern European markets, alongside the above motives, could have been more important in connection with the food, beverages and tobacco industries and with commerce.

Table 12:
Breakdown by industry of outright or partial sales of enterprises to buyers from EC states

Industry	Percentage of total number of sales of firms to buyers in EC states
Primary, producer goods	25
Food, beverages and tobacco	17
Construction	13
Commerce	12
Capital goods	11
Services	10
Other	12

Source: IAW calculations based on Trust Agency data

4. Trade with the East by the new German Länder: prospects and scope for growth

An analysis of the present situation allows us to conclude that, for the most part, trade relations between East Germany and Eastern Europe, which were established on the basis of planned economies, already belong to the past.

Those aspects of export and import relations which have remained viable have done so:

- because it has been possible, as a result of relatively high standards, to adapt to market economy requirements;
- because various forms of government support have kept them going for the time being, leaving firms more time to get themselves on their feet again;
- because certain firms are geared to specific needs of Eastern European clients, e.g. spare parts for goods previously supplied, and have been able to continue to satisfy a demand.

The prospects for, and future growth in, trade with the East by the new Länder depend on the following four factors in particular:

- progress in rehabilitating the East German economy as a whole;
- the outcome of the process of structural change towards a market economy and economic stabilization in the states of Central and Eastern Europe, and the related process of revitalizing Eastern Europe's markets;
- the scale and effectiveness of Federation and Länder support for trade with the East.

4.1. Economic upswing in East Germany and the competitive advantages of the new Länder

Swift economic recovery in the new Länder and the prompt privatization and rehabilitation of East German firms are the key prerequisites for a further increase in trade with Eastern Europe. The fact is at present, however, that the economic situation remains complicated⁸.

Contradictory trends are predominant. While some areas of the economy have not yet bottomed out, there are encouraging signs in the construction industry and in certain areas of manufacturing. According to the Institut für Angewandte Wirtschaftsforschung (Applied Economic Research Institute), real gross domestic product, which declined by just under 24% in 1991, is likely to grow by close to 5% in 1992.

Within manufacturing above all, which is of particular importance for trade, stagnation and gradual stabilization will extend well into the first half of 1992, while recovery in appreciable terms will not commence until the second half of 1992. The data available show that production began to consolidate - at a very low level and with an uneven trend - at the earliest from September 1991 onwards.

⁸ cf. in this connection: Institut für Angewandte Wirtschaftsforschung (Applied Economic Research Institute): Ostdeutschland: Der mühsame Aufstieg, Gutachten zur Lage und zu den Aussichten der Wirtschaft in den neuen Bundesländern (East Germany: arduous progress, report on the economic situation and prospects in the new Länder), 10 October 1991

Table 13:
Movement in net output in manufacturing (%)

	August 1991 - August 1990	Change over previous month		
		September 1991	October 1991	November 1991
Manufacturing overall	- 38.6	8.9	4.4	1.5
Of which:				
Primary products and producer goods	- 21.8	8.2	11.1	- 1.3
Capital goods	- 51.2	11.3	- 2.0	6.6
Consumer goods	- 35.0	13.1	9.9	- 2.4
Food, beverages and tobacco	- 11.8	2.6	8.1	- 3.8

Source: Federal Statistical Office, Deutsche Bank, IAW calculations

Industry provides clear evidence of the diminished role of trade with the East - though the scale varies - in overall economic activity. As a result, enterprises' efforts to overcome business bias towards the East German domestic market and the markets in the East have stepped up appreciably, principally on the part of enterprises which are now part of West German firms or have been otherwise privatized.

Nonetheless, there is continuing demand from Central and Eastern European countries, principally (in 1991) from the Soviet Union/CIS. Analyses in the engineering, shipbuilding and rolling stock industries, in the pharmaceuticals industry and in parts of the chemical industry confirm that the CIS remains East German industry's most significant export market. In the short and medium terms, further traditional supply business is likely to collapse. The present modest scope for exports to the other countries of Central and Eastern Europe will persist for some time, though there are signs of increased cooperation to some extent among individual firms for 1992.

The use that is made of forms of cooperation which involve more than trade links alone will also be a factor influencing the future of trade with the East, e.g. the stepping up of scientific and technical collaboration - an area in which there is a particularly great risk that established contacts will be lost.

Consolidation among the key East German exporters is a prime condition for renewed success on the Eastern European markets. Productivity benefits, economic growth, marketing-oriented structural change and staff motivation are likely to come about, and hence exporters will improve their market positions, only if the matter of privatization is settled promptly and they are reorganized on that basis from top to bottom. This is only achievable in the medium term, however. In the short term, it is not unusual for adjustment by firms to involve contraction or stagnation in market share. To date, surveys of firms have failed to reveal significant differences between privatized and Trust Agency firms with regard to expected sales on markets in the East, though a much larger proportion of privatized firms detect a positive trend in demand for their staple products. The importance of the markets in the East to firms in the new Länder is diminishing because improvement in their sales potential on the domestic market and on the Western industrialized nations' markets is the key factor in economic recovery.

East German firms do continue to enjoy certain competitive advantages on Central and Eastern Europe's markets, though, in particular sound knowledge of countries and markets, an array of personal contacts with those countries' economists and greater appreciation of the transformation along free market lines that is now taking place. These advantages can be exploited, however, only if East German firms keep on their marketing staff and provided that links with clients there are not severed altogether as a result of hasty decisions. On the other hand, the general drawbacks of East German firms - characterized by a lower level of management, lower-productivity technologies, inadequate financial resources and a poor reputation by comparison with Western firms - also operate on markets in the East. Since the competitive advantages are rapidly being whittled away, the focus is already on those drawbacks which are closely bound up with the overall economic situation in the new Länder.

4.2. Economic development and the process of reform in Eastern Europe

How the economic situation in the countries of Eastern Europe develops over the next few years, and how successful the essential process of structural adjustment along market economy lines is, will be very significant for future trade with the East by the new Länder.

The process of transforming the economic systems is proving to be a long-term and complex undertaking which is still in its infancy in all Central and Eastern European countries (regardless of specific differences). Many economic reforms must be carried out simultaneously to a large extent. Above all, commodity markets must emerge on which there is competition. The appropriate monetary framework and requisite currency stability must be established; at the same time, a taxation system and a new framework for public finances are also essential. It is very important that Eastern Europe's economies should open up to the world market. Not only must the appropriate institutional and regulatory environment be created; a large number of economists must also be trained, too, with a view to successfully exploiting that environment.

Transformation is being complicated by the fact that, in the process of creating market economies, the countries of Central and Eastern Europe are presently going through painful adjustment crises in the form of production slumps, balance of payments deficits and runaway inflation.

The disbanding of COMECON has had a major impact on the trading activity of all its former members. In general, there has been a swift contraction in trade within what used to be COMECON. At the same time, the smaller Eastern European countries are endeavouring to reduce their ties with the economy of the CIS, which used to be one-sided and excessive. The impact on industrial production and employment has been particularly marked in those countries for which trade within COMECON was particularly significant.

The high level of external indebtedness, of all the countries concerned, in convertible currencies and growing debt-servicing difficulties are narrowing the economic policy-making latitude available to the governments concerned and constitute a major burden on what is an economic new deal.

Central and Eastern Europe's economies are not likely to pick up quickly. Clearly, the situation is not everywhere the same. Hungary and the CSFR are the most likely candidates to be past the worst shortly. Romania and Bulgaria probably have the least internal momentum. The position in the republics of the CIS remains very confused. A dramatic worsening in that position cannot be ruled out. Everything depends on whether free-market reforms can be single-mindedly put in hand, whether the further collapse of the economy into chaos can be lessened and whether better use can be made of the scope for economic cooperation within the CIS.

The main difficulty in reviving trade with the East is that, in all Central and Eastern European countries, goods and services which are good enough for the world market, which could be traded successfully on Western European markets, account for far too low a proportion of total production. Structural

change, towards a market economy, and foreign assistance must therefore be primarily geared to bringing about gradual change in this regard. However, this requires time and a high level of concentration of economic forces. The current marketing potential for a number of categories of goods is not high enough for efficient incorporation into the international division of labour. We cannot yet tell how, and how quickly, the structural changes which are necessary will prove successful.

Formulation of economic policy should therefore be based on the assumption that revitalization of Eastern Europe's markets will not be an automatic process. The countries concerned must evolve before they can become trading partners. It would be correct to provide active assistance with regard to the privatization of industry and to administration. Investment in this will pay off in the long term if prospective trading partners can be acquired in the process.

4.3. Trade with the East by the new German Länder: forecast for 1992

To forecast how, in quantitative terms, trade with the East by the new Länder will develop in 1992 - on the basis of a summary analysis of the circumstances set out above - is a problematic undertaking surrounded by a whole host of uncertainties.

We may nevertheless assume with some degree of certainty that East German firms' exports to Eastern Europe will decline in 1992 by a further one sixth over the previous year (to approx. DM 10.5 bn), while imports are likely to grow slightly by between 5% and 8% to about DM 9 bn.

However, this assessment presupposes 'normal' developments, so to speak, i.e. no major political or nationwide upheavals or disasters in Eastern Europe.

Detailed examination of marketing and supply conditions in the countries of Eastern Europe bears out the overall assessment.

Because of increasing efforts in the Commonwealth of Independent States (CIS) to achieve political and economic sovereignty, and because of the break-up of traditional administrative structures, foreign trade relations, too, have become highly unpredictable. The general economic crisis is worsening and is bound up with a drastic contraction in exports. A growing foreign currency shortage for firms and a further increase in the republics' total indebtedness are likely in 1992, too. To a large extent, therefore, exports to the CIS are tied to special financing solutions. While Russia and other CIS members continue to be the most important partners for the new Länder in their trade with the East, the situation is not likely to bottom out until the second half of the year, however.

The economic situation in Poland is not likely to improve significantly in 1992. In spite of considerable progress in reshaping the regulatory environment along market economy lines, the most important structural adjustments have yet to be made. Structural change has been slight; nevertheless, trade with East Germany has contracted by two thirds within a year. The fact that Polish firms geared themselves to the old Länder early on is harming East German firms' positions, which were adverse as it was; consequently, a swift trade revival is not on the cards.

The Czechoslovak economy, too, is experiencing a severe adjustment crisis. Given the potential that exists, and provided that the country moves closer to the EC, a reversal of what have been negative trends to date seems more likely than in other Eastern European countries. If there is strong growth in trade between the CSFR and West German firms, sales opportunities for the new Länder will remain modest in the short term. Such opportunities are most likely to be found in areas which are receiving assistance under government structural programmes (environmental protection, energy and infrastructure).

Compared with the other Central and Eastern European countries, Hungary has made the most progress in reorganizing the economic system along market

economy lines. The main feature of its trade with Germany is that, as trade with the old Länder expands, its prospects for trade with East German firms are tending to worsen. The scope for cooperation in the area of agricultural machinery is an exception to this.

The general economic crisis in Bulgaria, by comparison with the other Eastern European countries, can only be described as especially severe. The collapse of trade within COMECON dealt the country an extremely hard blow. Germany accounts for a relatively modest proportion of Bulgaria's trade; now that links with East German enterprises have fallen apart, Bulgaria's role in Germany's trade with the East is no more than marginal. At present there are no signs of a marked improvement.

5. Conclusions

5.1. Are there lessons to be learnt with regard to the development of the other former COMECON countries' external trade?

Because the process of transforming the system in the former GDR is inextricably bound up with German reunification, we may infer that the East German process exhibits unusual, indeed unique, features. The changeover from one system to another took place suddenly; and the structural adjustment crisis - of which the collapse, to a large extent, of traditional trade links was a feature or, as the case may be, a consequence - is particularly acute. Nevertheless, because of the assistance being provided by the old Länder the resulting problems can be dealt with far more easily than would otherwise have been the case.

The other Central and Eastern European countries are unable to realize the shared objective of establishing a market economy in this form. The same is true of external trade too. We would highlight two lessons to be learnt.

Firstly, it has become clear that trade relations which have been established in a different political and economic environment will inevitably founder, logically enough, if there is an immediate switch to trading under world market conditions, at world market prices and with convertible currencies. That is true of former intra-COMECON trade in its entirety, though no-one disputes its benefits in a host of areas. In order to limit the damage that has already been inflicted, therefore, special solutions should be sought to maintain or, as the case may be, revive trade between the countries of Central and Eastern Europe, including making use of clearing or barter arrangements.

Secondly, there are lessons to be learnt as to where the main emphasis should lie in the process of liberalizing external trade arrangements, in the countries of Central and Eastern Europe, and how quickly that process should proceed. It was imperative to put an end to the State monopoly on foreign trade in those countries. Private business has been granted greater rights and latitude to organize its external trading relations; its development is closely bound up with this. Government regulatory action is called for during a transitional period, in particular:

- to safeguard higher national economic interests (e.g. by granting export licences),
- to encourage exports (e.g. through an appropriate exchange rate policy, through targeted support for exporters and, in special cases, through subsidies),
- to create the basis for essential imports, in particular food, pharmaceuticals, etc. (e.g. through setting up centralized foreign exchange funds),
- to ensure that previously contracted foreign loans or loans guaranteed by State institutions are serviced (e.g. by placing restrictions on a proportion of foreign exchange earnings).

The above actions that are necessary during a transitional period lead us to conclude that convertibility of national currencies in Central and Eastern Europe can only be phased-in, important requirements for this being that foreign trade must be consolidated (as regards the balance of payments in particular) and that domestic monetary stability must be largely secured.

5.2. Key aspects of a common European Community economic policy towards the former COMECON countries

From the way in which trade by the new Länder with their Central and Eastern European partners has developed, it can now be seen that the EC Commission's original assumptions regarding economic realities in the former COMECON area and the necessary measures to support the process of transforming the system were not sufficiently realistic, meaning that the Community must take renewed action to support both the new Länder and the economies of Central and Eastern Europe. This derives from an appreciation of the fact that the new Länder form the Community's most easterly region and that, as a result of Eastern European countries becoming associated states, their importance is increasing in terms of forging political links and economic integration. They ought to be made stable, out of common interest, to enable them to absorb at least some of the potential pressures emanating from Central and Eastern Europe towards Western Europe. This relates in particular to worker migration and to changes in the division of labour within Europe. It is also obvious that the Community bears increasing responsibility for making a success of the reform process in the former COMECON countries and - by giving them effective help to help themselves - for supporting the restructuring and rebuilding of those countries' economies.

In addition, the process of shaping a Europe-wide economic area calls for expansion, in both quantitative and qualitative terms, of the continental infrastructure. East German border crossings are already turning out to be bottlenecks which are hampering efforts to step up trade.

On the basis of studies to date, key aspects of Community policy towards the new Länder and the former COMECON countries can be summarized as follows:

- (a) The Community's strategy to assist the Länder (use of the Structural Funds) - where its key objectives lie, how effectively funding has been employed - should be subjected to critical examination; substantial sums have already been spent on the basis of that strategy. In view of what are extremely serious problems, checks should be carried out as to whether the scale on which EC assistance is being implemented in the new Länder, the timescales involved and the way in which that assistance is broken down are commensurate with the task of integrating this region promptly.
- (b) In connection with support for Central and Eastern Europe, the key problem the countries concerned have in creating effective ways and means - largely by their own efforts - of integrating themselves into the international division of labour is the fact that their export products have been granted generous and virtually unrestricted access to the Western European market. Given the productivity gap in Eastern Europe, the risks this poses for Western Europe's economy are significantly less serious than was originally assumed. That also holds true for the so-called sensitive areas, including agriculture. The inclusion of the smaller Central and Eastern European countries in the food aid programmes for the CIS is to be welcomed. This must proceed in such a way as to prevent agricultural production structures which are not up to the requirements of the Western European market from being preserved.
- (c) Further prompt elimination of all trade barriers under COCOM rules - with a view to enabling Central and Eastern Europe's economies to gain unrestricted access to all advanced technologies - would also be conducive to economic stabilization and trade with the East.
- (d) The European Community's technical assistance programme for the CIS, under which ECU 500 m is available for 1992, may provide significant impetus for the future of trade relations. The inclusion of East German firms on preferential terms is

precisely what would enable them to become involved in existing collaborative arrangements in science and technology. That also holds true for training-related assistance and for know-how transfers.

- (e) Consideration should be given to extending the transitional arrangements for imports into the new Länder from the former COMECON area. As regards imports from those countries, they will become less significant because of the entry into force of the interim agreements concerning the European Community's association agreements with Poland, Hungary and the CSFR. There would be benefits to some extent, however, if the opportunities that remained were exploited.
- (f) It is also important that a regional policy strategy be formulated for the border regions of the new associated countries and their hinterland, which could be implemented to support trade with East Germany in particular.
- (g) An investigation should be carried out into the extent to which trade with Eastern Europe, in particular by the European Community's structurally vulnerable regions, might be promoted by a system of export credit guarantees along similar lines to the Hermes guarantees in the FRG.

In general, Western Europe must provide much more direct investment much more quickly than in the past and support the growth process with loans, though lending should be tied to progress in carrying through macroeconomic reforms (currency, taxation system, budgetary policy, etc.).

Project-specific funding in communications, transport and other infrastructure areas creates a sound basis for prompter trade in goods and services. At the same time it also makes investment locations more attractive to foreign private capital. In addition, even more attention should be devoted to transfrontier environmental protection responsibilities and joint energy supply measures.

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Table 1
Trade by the new Länder by group of countries

	DM billion		Structure (%)		Change over previous year (%)		Proportion of total trade (%)	
	1990	1st half 1991	1990	1st half 1991	1990	1st half 1991	1990	1st half 1991
Imports								
Total	22 851.6	5 838.1	100	100	-44.5	-65.3	4.0	1.8
EC countries	2 678.4	1 060.4	11.7	18.2	-37.3	-36.4	0.9	0.6
EFTA countries	2 128.6	471.0	9.3	8.1	-41.6	-69.9	2.8	1.2
Developing nations	1 273.3	354.4	5.6	6.1	-36.9	-60.7	1.9	1.0
OPEC	84.5	94.8	0.4	1.6	-70.3	33.2	0.6	1.3
Central and Eastern Europe	14 812.4	3 672.1	64.8	62.9	-44.7	-66.8	40.5	22.9
Exports								
Total	38 072.4	8 467.7	100	100	-7.4	-55.0	5.6	2.6
EC countries	2 930.7	1 421.8	7.7	16.8	-16.5	-7.5	0.8	0.8
EFTA countries	1 529.5	520.2	4.0	6.1	-32.1	-42.0	1.4	1.0
Developing nations	2 115.0	670.7	5.6	7.9	-8.0	-45.4	3.1	2.0
OPEC	369.5	132.0	1.0	1.6	-0.5	-37.9	2.0	1.4
Central and Eastern Europe	19 722.5	5 509.9	78.1	65.1	2.9	-60.7	56.0	31.0

Source: Federal Statistical Office, Wiesbaden, Series 7, Volume 1, December 1990 and June 1991, and IAW calculations

Table 2
Germany's trade with the countries of Central and Eastern Europe - Imports

	New German Länder				Old German Länder			
	1989	1990	1st half 1991	1991 (Nov.)	1989	1990	1st half 1991	1991 (Nov.)
Imports	DM bn				DM bn			
Soviet Union / CIS	15 392	9 107	2 731	4 504	8 392	9 122	5 035	9 028
Poland	3 061	1 800	389	717	3 584	5 164	2 952	5 921
Czechoslovakia	3 246	1 720	348	667	2 493	2 704	1 788	3 912
Hungary	2 435	1 233	135	239	2 677	3 254	1 852	3 653
Romania	1 335	407	49	77	1 539	1 116	531	1 038
Bulgaria	1 324	545	20	35	327	396	209	456
Central and Eastern Europe	26 793	14 612	3 672	6 239	19 012	21 756	12 367	24 008
Imports	Shares				Shares			
Soviet Union / CIS	57.4%	61.5%	74.4%	72.2%	44.1%	41.9%	40.7%	37.6%
Poland	11.4%	12.2%	10.6%	11.5%	18.9%	23.7%	23.9%	24.7%
Czechoslovakia	12.1%	11.6%	9.5%	10.7%	13.1%	12.4%	14.5%	16.3%
Hungary	9.1%	8.3%	3.7%	3.8%	14.1%	15.0%	15.0%	15.2%
Romania	5.0%	2.7%	1.3%	1.2%	8.1%	5.1%	4.3%	4.3%
Bulgaria	4.9%	3.7%	0.5%	0.6%	1.7%	1.8%	1.7%	1.9%
Central and Eastern Europe	100	100	100	100	100	100	100	100
Imports	Change over previous year				Change over previous year			
Soviet Union / CIS		-40.8%	-58.2%	-47.3%		8.7%	15.6%	9.0%
Poland		-41.2%	-71.6%	-58.2%		44.1%	32.6%	27.6%
Czechoslovakia		-47.0%	-74.2%	-59.7%		8.5%	39.1%	59.7%
Hungary		-49.4%	-65.8%	-79.5%		21.6%	26.2%	24.1%
Romania		-69.5%	-65.9%	-60.7%		-27.5%	-7.7%	1.1%
Bulgaria		-58.8%	-96.1%	-93.5%		21.1%	15.3%	27.4%
Central and Eastern Europe		-44.7%	-66.8%	-55.5%		14.4%	22.5%	21.9%

Source: Federal Statistical Office, Wiesbaden, Series 7, Volume 1, December 1990, June 1991 and November 1991

Table 3
Germany's trade with the countries of Central and Eastern Europe - Exports

	New German Länder				Old German Länder			
	1989	1990	1st half 1991	1991 (Nov)	1989	1990	1st half 1991	1991 (Nov)
Exports	DM bn				DM bn			
Soviet Union / CIS	16 576	17 761	4 018	8,440	11 528	10 357	4 284	7 822
Poland	3 116	2 944	667	951	4 470	4 690	3 521	6 657
Czechoslovakia	3 814	3 405	365	607	2 734	3 080	1 824	3,784
Hungary	2 597	2 696	207	353	3 651	3 365	1 881	3 500
Romania	1 429	1 505	160	212	584	1 114	476	892
Bulgaria	1 361	1 412	92	123	1 471	788	293	593
Central and Eastern Europe	28 893	29 723	5 509	10 686	24 438	23 394	12 279	23 248
Exports	Shares				Shares			
Soviet Union / CIS	57.4%	59.8%	72.9%	79.0%	47.2%	44.3%	34.9%	33.6%
Poland	10.8%	9.9%	12.1%	8.9%	18.3%	20.0%	28.7%	28.6%
Czechoslovakia	13.2%	11.5%	6.6%	5.7%	11.2%	13.2%	14.9%	16.3%
Hungary	9.0%	9.1%	3.8%	3.3%	14.9%	14.4%	15.3%	15.1%
Romania	4.9%	5.1%	2.9%	2.0%	2.4%	4.8%	3.9%	3.8%
Bulgaria	4.7%	4.8%	1.7%	1.2%	6.0%	3.4%	2.4%	2.6%
Central and Eastern Europe	100	100	100	100	100	100	100	100
Exports	Change over previous year				Change over previous year			
Soviet Union / CIS		7.1%	-50.1%	-46.7%		-10.2%	-24.6%	-19.7%
Poland		-5.5%	-37.6%	-42.4%		4.9%	72.2%	62.4%
Czechoslovakia		-10.7%	-82.2%	-80.8%		12.7%	38.6%	40.5%
Hungary		3.8%	-83.6%	-85.5%		-7.8%	14.2%	14.0%
Romania		5.3%	-78.7%	-84.5%		90.8%	-21.8%	-12.6%
Bulgaria		3.7%	-88.8%	-90.7%		-46.4%	-37.4%	-19.0%
Central and Eastern Europe		2.9%	-60.7%	-59.9%		-4.3%	4.4%	8.8%

Source: Federal Statistical Office, Wiesbaden, Series 7, Volume 1, December 1990, June 1991 and November 1991

Table 4
Volume and share of trade with the East by Germany and the European Community

	1989	1990	1st half 1991	1991 (Nov.)
	I M P O R T S			
New Länder, DM bn	26.8	14.8	3.7	6.2
Old Länder, DM bn	19.0	21.8	12.4	24.0
EC, ECU bn	27.2	30.0	17.0	
	Percentage of total imports			
New Länder	65.2	64.8	62.9	58.5
Old Länder	3.8	3.9	3.9	4.1
EC	2.5	2.7	2.8	
	E X P O R T S			
New Länder, DM bn	28.9	29.7	5.5	10.7
Old Länder, DM bn	24.4	23.4	12.3	23.2
EG, ECU bn	24.1	27.1	15.0	
	Percentage of total exports			
New Länder	70.3	78.1	65.1	65.6
Old Länder	3.8	3.6	3.8	3.9
EC	2.3	2.5	2.7	

Source: Federal Statistical Office, Wiesbaden; Eurostat; IAW calculations

Table 5
European Community trade with the countries of Central and Eastern Europe, 1989 to 1991

	1989	1990	1st half 1991 ECU m	1989	1990	1st half 1991 Share	1990	1st half 1991 Change over previous year
Imports								
Soviet Union	15 166	16 749	9 496	55.7%	55.8%	56.0%	10.4%	26.8%
Polen	3 858	5 278	2 960	14.2%	17.6%	17.4%	36.8%	23.4%
Czechoslovakia	2 558	2 786	1 741	9.4%	9.3%	10.3%	8.9%	29.7%
Hungary	2 587	3 004	1 697	9.5%	10.0%	10.0%	16.1%	23.5%
Romania	2 548	1 617	734	9.4%	5.4%	4.3%	-36.5%	-13.0%
Bulgaria	531	593	341	1.9%	2.0%	2.0%	11.7%	17.2%
Total	27 248	30 027	16 969	100	100	100	10.2%	23.5%
Exports								
Soviet Union	12 603	13 614	6 462	52.3%	50.2%	43.1%	8.0%	0.9%
Poland	3 945	4 934	3 850	16.4%	18.2%	25.7%	25.1%	107.9%
Czechoslovakia	2 385	2 909	1 785	9.9%	10.7%	11.9%	22.0%	53.4%
Hungary	2 988	3 220	1 734	12.4%	11.9%	11.6%	7.8%	22.2%
Romania	689	1 415	657	2.9%	5.2%	4.4%	105.4%	-2.1%
Bulgaria	1 477	1 034	513	6.1%	3.8%	3.4%	-30.0%	-1.3%
Total	24 087	27 126	15 001	100	100	100	12.6%	24.7%
Balance								
Soviet Union	-2 563	-3 135	-3 034					
Poland	87	-344	890					
Czechoslovakia	-173	123	44					
Hungary	401	216	37					
Romania	-1 659	-202	-77					
Bulgaria	946	441	172					
Total	-3 161	-2 901	-1 968					

Source: Eurostat Volume 6B (External trade), 12/1991, and IAW calculations

Table 6
Trade by the European Community and its Member States with Central and Eastern Europe

	Imports			Exports		
	1989	1990	1st half 1991	1989	1990	1st half 1991
	, ECU m			ECU m		
Belgium-Luxembourg	1 516	1 706	918	1 003	812	589
Denmark	538	602	344	522	640	398
Germany (1)	9 086	11 351	7 714	11 836	15 388	8 676
Greece	583	612	323	301	256	168
Spain	1 396	1 312	463	514	459	262
France	3 625	3 853	1 916	2 627	2 341	1 543
Ireland	151	152	82	102	183	59
Italy	5 483	5 177	2 841	2 661	3 786	1 710
Netherlands	2 402	2 717	1 251	1 541	1 506	897
Portugal	90	71	44	127	75	12
United Kingdom	2 378	2 473	1 072	1 852	1 680	688
EC total	27 248	30 026	16 968	24 087	27 126	15 002
	Percentage share			Percentage share		
Belgium-Luxembourg	5.6%	5.7%	5.4%	4.2%	3.0%	3.9%
Denmark	2.0%	2.0%	2.0%	2.2%	2.4%	2.7%
Germany (1)	33.3%	37.8%	45.5%	49.1%	56.7%	57.8%
Greece	2.1%	2.0%	1.9%	1.2%	0.9%	1.1%
Spain	5.1%	4.4%	2.7%	2.1%	1.7%	1.7%
France	13.3%	12.8%	11.3%	10.9%	8.6%	10.3%
Ireland	0.6%	0.5%	0.5%	0.4%	0.7%	0.4%
Italy	20.1%	17.2%	16.7%	15.2%	14.0%	11.4%
Netherlands	8.8%	9.0%	7.4%	6.4%	5.6%	6.0%
Portugal	0.3%	0.2%	0.3%	0.5%	0.3%	0.1%
United Kingdom	8.7%	8.2%	6.3%	7.7%	6.2%	4.6%
EC total	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%

(1) Including the new Länder from 1991 onwards

Source: Eurostat, Volume 6B (External trade), 8-9/1990, 5/1991 and 12/1991

Table 7
Structure of trade with Central and Eastern Europe by category of goods (in percentage terms)

SITC	New Länder		Old Länder		EC	
	1989	1st half 1991	1989	1st half 1991	1989	1st half 1991
Imports		(1)		(1)		
0 Food and live animals	1.4	0.9	7.8	6.3	6.9	5.9
1 Beverages and tobacco	1.5	0.2	0.5	0.5	0.3	0.4
2 Crude materials	4.0	2.3	7.2	5.2	10.1	6.6
3 Mineral fuels	35.9	59.3	31.4	30.5	33.8	29.0
4 Animal and vegetable oils	0.0	0.1	0.2	0.2	0.2	0.1
5 Chemicals and related products	4.4	3.9	6.0	5.2	5.9	6.9
6 Manufactured goods	14.5	9.7	22.3	21.4	17.9	18.1
7 Machinery and transport equipment	35.9	20.8	6.0	11.1	6.8	9.5
8 Miscellaneous manufactured articles	4.2	1.7	14.3	17.5	8.8	9.8
9 Other commodities	4.6	1.2	4.3	2.3	9.3	13.5
Total	100	100	100	100	100	100
Exports						
0 Food and live animals	1.4	13.9	7.5	8.8	9.7	12.1
1 Beverages and tobacco	0.1	0.8	0.4	0.9	0.6	1.4
2 Crude materials	0.9	1.4	1.5	1.8	2.4	2.1
3 Mineral fuels	2.4	2.9	0.2	1.6	0.4	1.6
4 Animal and vegetable oils	0.0	0.1	0.3	0.2	0.5	0.3
5 Chemicals and related products	9.4	6.1	15.8	13.1	16.2	11.6
6 Manufactured goods	10.4	7.5	22.1	17.7	20.7	13.9
7 Machinery and transport equipment	60.5	53.4	42.2	43.1	35.7	42.7
8 Miscellaneous manufactured articles	13.9	12.2	8.8	10.0	8.6	10.3
9 Other commodities	1.1	1.7	1.3	2.8	5.2	4.1
Total	100	100	100	100	100	100

(1) The half-year figures were calculated by the IAW on the basis of SITC-2 data.

Source: Federal Statistical Office in Wiesbaden, and Eurostat

Table 8

Breakdown, by SITC goods categories, of trade with Central and Eastern Europe and its share of aggregate trade by the new Länder, 1989 and first half of 1991

SITC goods category	Trade with Central and Eastern Europe, DM m		Percentage share of aggregate trade	
	1989	1st half of 1991	1989	1st half of 1991
Imports				
0 Food and live animals	353.1	32.6	12.2	18.5
1 Beverages and tobacco	377.9	7.4	46.0	27.2
2 Crude materials	1 006.6	83.7	42.2	35.3
3 Mineral fuels	7 538.9	2 178.8	91.8	91.9
4 Animal and vegetable oils		2.0		62.5
5 Chemicals and related products	1 127.4	142.7	45.0	51.2
6 Manufactured goods	3 685.7	354.6	55.2	49.1
7 Machinery and transport equipment	9 128.8	763.6	65.4	47.1
8 Miscellaneous manufactured articles	1 070.1	62.6	46.5	18.4
9 Other commodities	1 169.3	44.9	87.9	74.0
Total	26 792.9	3 672.1	65.1	62.9
Exports				
0 Food and live animals	378.1	766.2	33.0	72.3
1 Beverages and tobacco	30.7	42.3	6.0	93.8
2 Crude materials	260.2	78.0	42.9	36.4
3 Mineral fuels	648.6	161.8	31.2	83.7
4 Animal and vegetable oils	1.8	3.2	12.0	59.4
5 Chemicals and related products	2 571.6	336.6	55.2	36.0
6 Manufactured goods	2 850.4	411.8	42.1	39.4
7 Machinery and transport equipment	16 605.0	2 943.8	83.5	75.4
8 Miscellaneous manufactured articles	3 819.4	672.8	75.6	69.5
9 Other commodities	295.8	91.6	79.1	91.1
Total	28 892.4	5 509.9	70.3	65.1

Source: Federal Statistical Office in Wiesbaden, and IAW calculations