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# AN AGRO-FOOD INDUSTRIAL STRATEGY FOR THE BALTIC STATES

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# AN AGRO-FOOD INDUSTRIAL STRATEGY FOR THE BALTIC STATES
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## 1. Introduction

### *Background and Summary*

*The purpose of the SELL-program is to improve cooperation between Finland and the Baltic States in the agro-food sector and, above all, to facilitate Finnish investments in the Baltic food industry. The greatest impediment for such investments is the lack of a coherent institutional framework, and uncertainty about the future. The objective of the present position paper is to present an outline for a common Baltic agro-food strategy. If implemented, this strategy should go a long way to eliminate the obstacles for foreign investment and provide a decisive boost for the important agro-food sector.*

*The central proposition of this position paper is that the striving for membership in the European Union should be the cornerstone of strategic thinking and planning. Sound intrabaltic, external and domestic policies flow almost self-evidently from this central assumption. Due consideration should be given to the fact that the EU will not absorb all the export surplus of Baltic food production. Access to the Russian market, especially, will thus be very important in the longer term.*

### *Current Situation*

While the Baltic economies as a whole ran a growing trade deficit, these countries, particularly Estonia, experienced a significant trade surplus in 1993 in agro-food products[1]. This outcome is surprising considering the extent of official as well as unofficial barriers to exports and the low or inexistent official barriers to imports. This success in agro-food trade can be explained by the under-valuation of Baltic currencies, especially that of the Estonian Kroon, and by the limited purchasing power of the Baltic domestic economies. Furthermore, foreign investment has already had an impact and several surveys have indicated that domestic entrepreneurs are beginning to overcome the many difficulties involved in agro-food trading.

Baltic agro-food exports are concentrated in the low end of the market. Moreover, their packaging and presentation is still generally not up to Western standards. Hence, exports are still destinated mainly to the Former Soviet Union (FSU) countries, or to similar, less demanding markets. There is significant business in adding value to imports for re-export, (for example chocolate and tobacco), as well as in transit trade in both directions between the FSU and other markets.

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[1]Statistical Office of Estonia, "Foreign Trade 1993", Tallinn.
State Committee for Statistics of the Republic of Latvia, "Latvia in Figures 1993", Riga.
Lithuanian Department of Statistics, "Lithuania in Figures 1993", Vilnius.
Unfortunately, The data concerning agro-food production in the Baltic States are not directly comparable due to differing statistical methods (e.g. classification, etc.).

Overall, Baltic agro-food trade with Scandinavia, the EU and former Socialist countries remains at a low level. Furthermore, export is in most cases initiated by foreign parties, not by Baltic enterprises. Baltic agro-food production is constantly suffering from imbalances, as production levels do not correspond to domestic and international demand.

***The Significance of the Baltic Agro-Food Business***

*Today, the agro-food sector comprises about 25% of GNP in the Baltic States. This figure is bound to fall in the future but, even in the long term, agro-food will constitute one of the mainstays of the Baltic economies. With a suitable influx of foreign investment and knowhow, the sector could become very competitive internationally. The prerequisite is a certain concentration, which goes hand in hand with specialization and an undergrowth of small business. Such an efficient structure can be achieved only through private enterprise in the context of a sound market economy.*

The geographic position of the three Baltic countries and their intimate knowledge of Eastern Europe seem to be permanent and defensible advantages in East-West trade, especially if they are supported by an adequate influx of foreign investment. Even so, Baltic agro-food industries are likely to face rapid change in the terms of trade. Domestic production costs will rise and the exchange rates will settle at a higher level. When price-competitiveness is eroding, other more sustainable advantages must be developed. This entails upgrading product quality, increasing efficiency and productivity as well as expanding the product range. The key issue here is that both policy makers and individual businessmen must understand the competitive position of Baltic agro-food products in their ultimate markets. (See Box 1)

**Box 1. The Potential and Competitiveness of Agro-Food in Estonia**[2]

A recent study undertaken within the PHARE program indicated that the dairy sector is of central importance for Estonia's farmers and the national economy. Extensive grasslands, skilled manpower and a low wage level determine the high competitiveness of dairy farming in Estonia. Dairy products and beef are traditional export commodities. Even so, inefficiencies seem to exist in processing and marketing. Possible areas of project activity could comprise: improving raw milk quality supplied by farmers, increasing efficiency of milk collection; modernizing dairy processing and coordinating domestic and export marketing by cooperative organizations.

[2]Commission of the European Communities, PHARE Program, Technical Assistance Program for Estonia-Support for Agriculture and Food Strategy Development; "Assesment of Agricultural Marketing Systems in Estonia", published by DG Agroprogress International, Bonn 1993.

## 2. Baltic Objectives / Goals

***Joining the European Union***

*Joining the EU seems to be a common goal for the three Baltic States, but to become acceptable to the EU they have to fulfill a set of stringent conditions. The creation of these conditions must be the principal objective in the agro-food sector, too. This is a tall order but will not, in itself, guarantee the viability of the agro-food business. The EU cannot and will not accept any appreciable surplus from the Baltic states on its overcrowded markets. Export to third countries with a minimum of subsidies is a must.*

If the Baltic states were to join the EU within, say, 10 years, the EU market has probably moved closer to the world market as a result of further internal policy changes and international trade/tariff negotiations within the World Trade Organization (WTO). The recent Uruguay Round should reduce present surpluses and result in higher world market prices. Thus, a policy trajectory that targets EU membership within a decade would involve lower protection levels than at present. Harmonizing with the CAP reform adopted by the EC in 1992 (see Box 2) would provide a good basis for future positioning in the European agro-food scene.

**Box 2. The Proposed CAP Reform**[3]

The initial objective of the CAP Reform was to reorganize the grainmarket and, particularly, to decrease the price of grain. These actions were to considerably increase the competitiveness of EU agricultural production in worldwide markets. The undertaken reduction in price is compensated by subsidising producers directly, which should reallocate the support to small-holders and decrease over-production. In order to restrain production, the compensation is assessed on the basis of average regional production per area. Additionally, production is restrained by binding the compensation subsidies to compulsory fallow. The 1992 reform forms the first phase of the CAP Reform, and it is still going on.

From the economic point of view, there are no objections to protecting domestic (Baltic) producers against dumping and erratic price fluctuations on international markets. Levies or anti-dumping tariffs are justified if imports arrive at prices that do not reflect the comparative advantage of a foreign producer country but which are due to a direct or indirect subsidy paid for political reasons. Furthermore, the absence of adequate protection discourages foreign investment. Erratically fluctuating prices constitute a major market risk for producers. If these irregularities are levelled out by means of a price stabilization program, producers can base their decisions on more reliable price expectations, which should reduce misdirected investment.

[3]Savia, L. (1994) "Euroopan yhteisön maatalouspolitiikan markkinajärjestelyt EY-tuomioistuimen oikeuskäytännön valossa"; University of Helsinki, Institute for international Economic Law, Helsinki.

***Improving the Institutional Framework***

*Insecurity is the strongest disincentive for any investment, particularly for foreign companies. Thus, strengthening the rule of law should be given the highest priority. Rules that can be circumvented, or apply only to the unconnected, or change capriciously, drive out honest enterprise. Hence, arbitrary action of local or national government is anathema for foreign investors and the same goes for widespread corruption not to mention the affronts of organized crime.*

*The EU provides an obvious model for the extensive set of rules and regulations pertaining to animal and human health, international trade, environmental factors, and the like. But without impartial enforcement they just become so much red tape, which provides increasing opportunities for undue influence.*

Most of the problems touched upon in this section are not specific to the agro-food business, although it provides a singular potential for market distortions. The specific agro-food regime could perhaps be copied in toto from the EU, which at least would make for a smooth transition period when the EU- membership is approaching.

The case for market transparency is particularly strong in the agro-food industries and will require special efforts. It may be advisable to create a distinct agro-food/agricultural market intelligence unit that collects market data in the separate Baltic countries (see footnote on page 2). This database should be analysed and made public in order to improve market transparency for farmers, processors, traders, and policy-makers. These actions would assist market participants and the public authorities in taking adequate decisions.

***Attracting Foreign Investment***

*Foreign investment is the most potent catalyst for the indispensable transformation process in the agro-food business. Besides a credible institutional framework, attracting significant funds from abroad may require additional incentives, such as tax holidays. The best incentive would be a common intrabaltic food market and, most important, good export opportunities to Russia. The persistent fragmentation of the markets and a regulatory muddle are certainly the strongest disincentives.*

After decades of high but misdirected capital accumulation, there is now underinvestment. The restructuring of existing capacities, the development of public sector infrastructure, and the resumption of economic growth all require higher investment. Domestic savings are not being channelled effectively into investment. Without further cuts in living standards, higher investment requires a greater inflow of capital from abroad, including debt restructuring and relief. Public international funds can partly fill the gap, but in order to attract additional investors, the Baltic States must do their utmost to create the proper legal framework and an attractive economic environment. These policies need to be effectively implemented and their coherence as well as credibility must be ensured.

Foreign direct investments can act as a powerful catalyst for economic change (see Box 3). They offer not only financial resources for the Baltic states, but also bring technology, management, a "business culture" and access to foreign markets - each of which can help overcome obstacles to the development of the private sector. The presence of foreign competitors stimulates local producers by increasing competition, and accelerating cross-border transfer of technology (including organizational know-how). Most important, human capital is enhanced by vocational training and/or through transfer of resources from foreign-owned affiliates. At best, foreign companies work as active agents in the process of restructuring, as they are increasingly involved in problems related to the overall development of the host economy.

**Box 3. Experiences of Foreign Companies in Estonia[4]**
The study indicates that considerable development has taken place in Estonia in both the political and economic sphere, particularly in comparison with neighbouring countries. Several companies use Estonia as a bridgehead to Russian markets due to Russia's fluid situation. Other markets are also targeted, such as Poland, Latvia and Lithuania. The Estonian national currency and its low starting point created a strong competitive position, which was enhanced by the availability of a well-educated and relatively cheap labour force. These factors have attracted several foreign companies that are in labour-intensive sectors as well as some companies operating in technology-intensive areas. Finnish companies, particularly, have been attracted by the geographical proximity as well as by the cultural and linguistic similarities. Some obstacles remain, though, due to bureaucratic hurdles, loopholes in the legislation, a handicapped banking sector and increasing criminality.

***Free intra-Baltic Trade***
*The Baltic States have already achieved a considerable degree of free trade for manufactured goods. Free trade should be extended to the food sector as soon as possible as a first step in adopting the EU-framework. This of course, requires the harmonization of external fiscal barriers and the legislation on agro-foods. The driving force is "better sooner than later".*

Reintegrating the Baltic states into the world economy is consistent with re-establishing and developing regional links. Moving towards free trade with the EU impels the Baltic states to seek free trade in agro-foods with each other, because otherwise their exporters will be unnecessarily disadvantaged. Harmonizing on the same EU-standards implies harmonizing with each other. (Compare Box 4)

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[4]Based on a study conducted by Julianna Borsos; "Foreign Companies in Estonia - Industrial Environment and Experiences", Discussion Paper No.488, ETLA-The Research Institute of the Finnish Economy, 1994.

There is a wide range of opportunities for regional cooperation in the agro-food industries, but the main effort should be directed towards developing specialization among the countries of the region, as well as corresponding cross-border investment. The simple introduction of automatic multilateral clearing, i.e. the transferability of bilateral trade balances among trade partners, could help preserve or restore the trade flows that correspond to comparative advantages.

As markets are not yet functioning, the most urgent measure is to create the simplest institutional framework for monetary exchange. Grand schemes for payments unions are a distraction; they are not feasible (and perhaps not desirable).

**Box 4. Cooperation Between the Visegrád Countries**[5]
The Visegrád Agreement signed in February 1991 by Hungary, Poland and Former Czechoslovakia, promised greater regional cooperation in East Central Europe. The most significant result was to demonstrate the partner countries' willingness and ability to engage in future cooperation in the European Community (nowadays European Union, EU). The Visegrad Group may set an example from which the Baltic States can learn in contemplating their own chances for EU membership. Even though the Visegrad Group has had some problems with the so-called sensitive products, it seems that so far they have been more successful than the Baltic States in their way to a common Eastern economic space. The Visegrad agreement provided for more intensive cooperation between the partners. Good regional cooperation was expected to prove their capacity to become integrated and to, eventually, accede the EU. As a result of such developments, The EU signed the Europe Agreements with Poland, Hungary and Czechoslovakia in autumn 1991[6]. These countries are seen as a whole by the EU, e.g., products originally imported from another country within the Group are considered as domestic products. Hence, these countries concluded an agreement on the establishment of a free trade zone in December 1992, in the form of a package of bilateral agreements providing for a ten-year transitional period.

## 3. The Road to the European Union

### *The Finnish Experience*

*Due to external political considerations, Finland had to approach the pan-European market very cautiously, one step at a time. This gave Finland ample time to adjust but preserved inefficient production structures in agro-foods far too long. Thus, Finland can provide concrete examples on both good and bad policies in preparing for the large, open EU-market. The recent, deep recession provides a vivid lesson of how not to behave. Besides the agro-food markets, the labour market has been heavily over-regulated and over-protected, which is the root cause of the present difficulties. Some other aspects of the Finnish experience will be presented during the symposium.*

[5]Based on an article written in the Baltic Review, "Visegrad Group and EC" Based on information given by the Polish Foreign Affairs Ministry; No.3, 1993.

[6]See appendix 1, where the terms of the Europe Agreement are set.

*In comparison, the Baltic States enjoy the clarity of an almost self-evident goal in joining the EU, but the reconstruction of the economic, political and social fabric makes for a heavy, additional burden.*

***Trade Relations with Russia and the Former Soviet Republics***

*As mentioned before, trade with the countries of the former Soviet Union is vital for the long-term success of Baltic agriculture and food industry. A certain cooling-off period has probably been inevitable, but sooner rather than later the work of reconciliation must begin in earnest. Despite the outrages of the past, the Baltic States cannot afford a jingoistic attitude towards Russia. Apart from purely economic considerations, it would become a severe obstacle to the entry into the European Union.*

Export in general is a must for a successful agro-food sector in the Baltic States. Russia and the other FSU-countries provide the natural export markets for Baltic agro-food companies. Of course, the political and economic situation in the former FSU-countries is critical when it comes to restoring the old export levels, but this should not become an excuse for passivity. Understanding the role of the Baltics as a "gateway" is crucial. The springboard position of the Baltic states into Russian markets offers opportunities both to indigenous and foreign companies. Baltic companies possess superior knowledge of the Russian market, language, and culture. Foreigners will rely on Baltic companies for this type of know-how, which brings additional opportunities for the Baltic states. Furthermore, as long as Russia is politically and economically unstable, the Baltic countries should be attractive as stepping stones to future opportunities in the East.

All in all, consistent attempt to upgrade standards is preferable to applying traditional instruments of protection. A sustained effort to improve export performance is the best way to hold on to domestic markets.

***Domestic Policies***

*Most of the relevant decisions in preparing for the EU must be made inside each separate Baltic State. Agricultural policies are a constant headache in most countries and the Baltic States will hardly be an exception. The ownership structure of agricultural land is perhaps the most refractory problem. Cooperatives have been thoroughly discredited in this field, but they certainly offer interesting possibilities in food processing, the coordination of exports and marketing in general. Here, the Finnish experience can provide some guidance. The privatization of the food industry has begun in all the Baltic States, but the process could be enhanced by a critical analysis and the exchange of experiences. Finally, the environmental problems related to agriculture and the food industry should be addressed, but sweeping solutions must probably be postponed.*

Policy-makers have to learn how to use new instruments designed to interact with firms which are increasingly guided by markets (see Box 5). This involves a shift towards the cautious use of indirect policy instruments such as improving the infrastructure, tax incentives and credit support. Moreover, the negative feedback of the market in the form of bankruptcy and unemployment must be allowed to take its course.

Delays in privatization must be overcome; the political problems of privatization become more, not less difficult as time passes. This speaks for avoiding complex schemes and using the full range of alternative privatization techniques now available. Every remaining opportunity to break up large firms should be taken. With the commercialization of state companies, their taxation regime should be the same as that of the private sector.

Non-viable state companies, or parts of them, should be closed as soon as possible but during the radical transformation period, short-run profitability may be a misleading indicator of the viability of a firm. Post-privatization failures will be frequent, and unemployment will continue to rise until the growth of successful firms can take up the slack.

**Box 5. OECD Study on Privatization and Agricultural Policies**[7]

"Privatization has been and continues to be the single most important element of agricultural policy for a large number of CEECs and NIS. It involves not only the transfer of land to private hands but also the de-monopolisation of the sectors supplying inputs and processing and distributing agricultural products, as well as the dismantling of the institutions of the former command economies. In countries such as Poland and Hungary where this process is well advanced, policy-makers have turned to reflections about the longer-term shape and role of the agricultural sectors. Without exception, these discussions have resulted in the formulation of a general objective to foster the development of an efficient, dynamic and self-reliant agro-food sector."

The Baltic economies operate at the expense of the environment, though overall production has declined and pollution levels have fallen accordingly. These problems will become even more acute with the anticipated economic take-off. In order to bring pollution levels to the norms of the European Union, the Baltic states must make considerable investments. For this sector, outside financing will be available in many cases (see box 6).

[7] OECD Observer No. 182 June/July 1993; Based on "Agricultural Policies, Markets and Trade in the Central and Eastern European Countries (CEECs), the New Independent States (NIS) and China: Monitoring and Outlook 1993", OECD Publications, Paris, 1993.

**Box 6. International Sources of Funds for Environmental Protection in Eastern Europe**[8]

- The World Bank Group
- The European bank for Reconstruction and Development (EBRD)
- The European Union (PHARE) and the European Investment Bank (EIB)
- The Nordic Investment Bank (NIB)
- The Nordic Environment Finance Corporation (NEFCO)

In Finland:

- Ministry of the Environment
- Ministry of Foreign Affairs
- Finnfund
- Finnish Export Credit Ltd.
- Fund for Industrial Cooperation Ltd.

## 4. Strategic Pointers

*Industrial policies in general are intended to strengthen the framework conditions for industry, and agro-industrial policies should aim at the stimulation of productivity, efficiency and growth. This can only be done by creating disciplines and incentives for fair and effective competition. Foreign investment is the best tool for achieving these aims in the agro -food sector.*

While EU-membership is the long-term goal, regional cooperation is the indispensable first step along that road. There are strong historic and economic links between all the countries around the Baltic Sea and they are natural partners in matters of trade[9].

The immediate problem of Baltic agro-food industries is twofold: Part of the existing capacities have to be maintained even though they are operating at a loss, while simultaneously major investments are needed in order to upgrade the industry for sustainable growth. The most difficult task is to identify and select those sectors which have a clear comparative advantage based on existing capacities. This can only in part be left to the emerging domestic entrepreneurs and to foreign investors who probably are overcautious.

In the long-run, the entrepreneurship and skills of Baltic farmers, traders and industrialists will determine the future of the Baltic agro-food business. The primary objective should be to achieve international competitiveness. Regional networking, technology transfer, quality upgrading and fair domestic competition should become linchpins in an efficient agro-food sector (see Box 7).

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[8]See Appendix 2 on Finnish cooperation with Central and Eastern European countries in environmental protection; report written by Timo Laukkanen, East Europe -project; Helsinki, July 5th 1994.

[9]A strong case for economic cooperation around the Baltics is made in "Perspectives for the Economic Development of the Baltic Region"; Report by EuroFutures A/B, Stockholm, May 1994.

**Box 7. Strategic Considerations for the Baltic Agro-Food Sector**[10]

- Generate a feasible agro-food strategy
- Create a viable institutional framework
- Attract foreign investment
- Seek preferential trade agreements
- Focus on nearby markets
- Assure adequate border protection
- Revitalise selected industries
- Invest in infrastructure, especially in communication and management of information
- Develop the role of industrial associations
- Support targeted training programs; high priority should be given to marketing and management skills as well as to the training of the cadre of civil servants

Even if some measure of "industrial policy" is justified, the Baltic countries should beware of old fashioned state planning. Selecting the "winners" is a very difficult game where failures abound, both East and West. State intervention goes against the grain of a competitive market, where the winners are selecting themselves.

[10]propositions found in the following studies and surveys:

- SELL Program Pre-Study, Final Report, Part I; Siar Bossard, Tallinn 1992.
- PHARE Program (see page 4) "Assessment of Institutions/Instruments for Agricultural and Food Policy Analysis in Estonia"; DG Agroprogress International, Bonn 1993.
- UNIDO (United Nations) Industrial Development Review Series; "Lithuania: Industrial Re-orientation"; May 1993.
- Ministries of Agriculture in Estonia and Latvia; "Policy Advice on Trade Development in the Agro-Food Sectors"; and working paper of The Estonian Ministry of Agriculture, "Problems in case of the Possible Joining of Estonia with the European Union - Objectives of Agricultural Policy", 1994 (b).

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- Within the Technical Assistance Program for Estonia, Latvia and Lithuania: Support for Agriculture and Food Strategy Development:

1. Assessment of Agricultural Marketing Systems in Estonia; DG Agroprogress International, Bonn 1993.

2. Assessment of Institutions / Instruments for Agricultural and Food Policy Analysis in Estonia; DG Agroprogress International, Bonn August 1993.

3. The Opportunities for Exports of Dairy Products from the Baltic States; DG Agroprogress International, Bonn June 1993.

4. The Opportunities for Exports of Meat Products From the Baltic States; Smits Engineering SA/NV, Brussels July 1993.

5. The Opportunities for Exports of Grain From the Baltic States; ALC Consultants Ltd., Amsterdam July 1993.

6. Review and Assessment of Credit Needs Capabilities, Sources and Institutions in Estonia; DG Agroprogress International, Bonn July 1993.

7. Review and Assessment of Processing Facilities and Capacities in the Dairy Sector of Estonia; DG Agroprogress International, Bonn June 1993.

8. Review and Assessment of Processing Facilities and Capacities in the Cereals and Feed Milling Sector of Estonia; DG Agroprogress International, Bonn June 1993.

9. Integrated Analysis of the dairy, Meat and Cereal Sub-sectors in Estonia; DG Agroprogress International, Bonn August 1993.

- Others:

1. A New Community Standards Policy - The New Approach in Harmonization, Agriculture and Foodstuffs (among other things); Internal Market, Current Status 1 January, Vol. 4, Brussels.

2. Complication of Consolidated EC Food Law; Directorate General, Internal Market and Industrial Affairs; Memorandum, January 1993, Brussels.

3. The CAP-Reform (In Finnish only) Euroopan yhteisön maatalouspolitiikan markkinajärjestelyt EY-tuomioistuimen oikeuskäytännön valossa; by Savia, L.; University of Helsinki, Institute of International Economic Law, Helsinki 1994.

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The uruguay Round Agreement on Agriculture: Some Impacts on Central and East European Countries; Group on East/West Economic Relations in Agriculture, Paris 1994.

Impacts of the uruguay Round Agreement on Agricultural Commodity Markets: Implications for NIS and CEECs; Group on East/West Economic Relations in Agriculture, Paris 1994.

Inter-NIS Relationships in Agriculture: Statistical Tables; Group on East/West Economic Relations in Agriculture, Paris 1994.

Manufacturing Performance: A Scoreboard of Indicators for OECD Countries, Paris, 1994.

Structural Change and Industrial Performance, Paris, 1992.

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APPENDIX 1

**"Problems in Case of the Possible Joining of Estonia with the European Union - Objectives of Agricultural Policy"**

Working paper prepared by the Estonian Ministry of Agriculture, Tallinn, 1994.

# Problems in case of the possible joining of Estonia with the European Union

Objectives of agricultural policy

| | Agricultural policy of EU | Present agricultural policy of Estonian Republic | What should be changed in Estonian agricultural policy in case of joining with EU | Changes in the Estonian agricultural policies in the near future |
|---|---|---|---|---|
| 1 | Providing people with self produced food products with favourable prices. (preference to EU production) | Guaranteeing of provision of main food products | Stabilisation of market | Proceed from the objectives and principles of trade and agricultural supportive policies of EU CAP |
| 2 | Application for stable incomes for farmers | Completing of land and property reform, restructuring of production into farms and unions based on private ownership | In the near future minimal up to moderate projection in the range of budget possibilities | |
| 3 | Stabilisation of the market of agricultural products and food products | Free trade. Lack of protective measures against unfair competition. Import of agricultural products with lower prices than are production costs plus profit | Creation of preconditions for cooperation based of farms and private ownership | |

# Problems in case of the possible joining of Estonia with the European Union (cont'd)

Objectives of agricultural policy

| | Agricultural policy of | Present agricultural policy of Estonian Republic | What should be changed in Estonian agricultural policy in case of joining with EU | Changes in the Estonian agricultural policies in the near future |
|---|---|---|---|---|
| 4 | Enlargement of competitiveness with modernising production and optimising expenses | | Creation of development preconditions conditions for rural regions | |
| 5 | Liberisation of trade conditions through stages | | | |
| 6 | Improvement of environmental conditions | | | |

# Problems in case of the possible joining of Estonia with the European Union

Measures of agricultural policies and production policy

| | Agricultural policy of EU | Present agricultural policy of Estonian Republic | What should be changed in Estonian agricultural policy in case of joining with EU | Changes in the Estonian agricultural policies in the near future |
|---|---|---|---|---|
| 1 | Leaving unused of 15% of countries (exception small producers) | Self-regulation of production | No researches and database enabling to analyse the complex usage of land, labour force and production facilities from the aspect of economy | Joining EU policy |
| | Production quotas to some products | None | 1. Carry out research clarifying the perspectives of land usage from the aspect of the possibilities of usage of labour force and production facilities<br>Deadline: 01.01.1995 | |
| | Bonus for leaving land unused | None | | |
| | Bonus for growing natural resources | None | 2. Preconditions for self-surviving agricultural entrepreneurship based on the private ownership:<br>• increase of mould fertility, productivity;<br>• decrease of production costs and losses<br>• improvement of quality | |
| | Bonus for extensiveness | None | | |
| 2 | Forestring the arable land | No united policy for usage of arable and forestry land | Overview of the possible uniting of Land Board and Forestry Board<br>01.06.1994 | |

# Problems in case of the possible joining of Estonia with the European Union

Trade policy

| | Agricultural policy of EU | Present agricultural policy of Estonian Republic | What should be changed in Estonian agricultural policy in case of joining with EU | Changes in the Estonian agricultural policies in the near future |
|---|---|---|---|---|
| 1 | United market regulation policy and system in member countries: protection of internal market, price and support policy<br>• No trade barriers between member countries<br>• price of imported goods from outside of EU will be increased higher than price level of world market<br>• Export support form the united EU budget | Free trade. self-regulation - no trade barriers | 1. Preparation of draft laws:<br>- law on agricultural market regulation<br>- law on customs value<br>- law against dumping<br>2. Determination of customs tariffs according to GATT regulations and in accordance with the principles of EU trade exchange | 1. Take over the principles of market regulation and protection of internal market in the transition period in possible joining with EU<br>2. Take over EU standards for quality demands, calculation and organisation work, etc. |

# Problems in case of the possible joining of Estonia with the European Union (cont'd)

Trade policy

| | Agricultural policy of EU | Present agricultural policy of Estonian Republic | What should be changed in Estonian agricultural policy in case of joining with EU | Changes in the Estonian agricultural policies in the near future |
|---|---|---|---|---|
| 2 | preferring food products produced in EU member countries. Limiting food products import in the near future with changing import taxes and in the longer perspective firm customs tariffs. Lessening of import limitation tariffs up to 36% | No limitations | Analysis in the range of main agricultural products and food products groups; proceeding from the economic aspect: price level, labour force, payment balance, which goods or raw material import to limitate of what to prefer | Determine stable customs tariffs on the level of EU |
| 3 | Payment of export subsidies: with the tendency to lessen the subsidies for 36% up to the year 2000 and capacities of 21% | No subsidies | Temporary determination of chosen product groups | Joining the system of EU export subsidies |
| 4 | EU customs regulations, quality demands, statistics | Demands valid are more flexible than these of EU | | EU regulations will be valid. EU ready to assist in implementation of the system |

# Problems in case of the possible joining of Estonia with the European Union

Price and profit policy

| | Agricultural policy of EU | Present agricultural policy of Estonian Republic | What should be changed in Estonian agricultural policy in case of joining with EU | Changes in the Estonian agricultural policies in the near future |
|---|---|---|---|---|
| 1 | Application of the stable incomes of farmers, for what intervention prices are for (minimum prices and application prices). In case of lowering of prices under the agreed level the rest will be bought into EU warehouses. | The prices form freely, although the profit law exists regulating the price negotiations between the Government and the producers | In the first stage the recommendation of EU will be implemented:<br>• stabilise seasonal price variations with the price guarantee | Implement profit analysis of agricultural producers and CAP price system in accordance with EU principles. |
| 2 | Payment of direct subsidies in accordance with the area and number of animals | | | |

# Problems in case of the possible joining of Estonia with the European Union

Regional and structure policies

| | Agricultural policy of EU | Present agricultural policy of Estonian Republic | What should be changed in Estonian agricultural policy in case of joining with EU | Changes in the Estonian agricultural policies in the near future |
|---|---|---|---|---|
| 1 | Supporting entrepreneurship in rural regions, not connected with enlargement of agricultural production | Support to the less developed areas through populating activities | | Take over principles of supportive policies of EU on rural areas |
| 2 | Support to scarcely populated areas (less than people for km2) | | | Creation of preconditions for underdeveloped areas |
| 3 | Support for Nordic areas. (north from 62 parallel) | Does not belong to the above-mentioned area | | |
| 4 | Support to areas with environmental damages | None | | Implement EU principles |

| Fishing policy of European Union | Present fishing policy of Estonian Republic | Development problems in Estonian fishing industry | Steps to be taken to join with the European Union |
|---|---|---|---|
| 1. Protection of fish resources, control of fishing and its methods, supervision | 1. Protection of fish resources and organisation of supervision<br><br>2. Development of environmental fishing industry, assisting in preserving of natural diversiy and protection of water resources<br><br>3. Responsibility in developing, propagating and implementing of consientious utililisation of fish resources in Estonian fishing industry | Protection of fish resources and regulation of supervision is insufficient for consientious utilisation of Estonian fish resources<br><br>Lack of fishing experts on the level of counties<br><br>Insufficient opportunities for consulting and complementary teaching from the govrnment's side | A. Export of fish anf fish products on the basis of trade lisences. Export quotas for fish and its products must be based on scientifically rational allowed catches by the fish species<br><br>B. Enforcement of Estonian Sea Inspection (Eesti Mereinspektsioon)<br><br>C. Creation of posts of fishing experts on the level of county governments. His responsibilities would be consulting and organisation of complementary education |
| 2. Guaranteeing of employment in fishing sector<br><br>3. Giving of special status to the ares highly depending on fishing<br><br>4. Development of fish industry | 4. Integration of fish industry into Estonian economical and social development<br><br>5. Restructuring of fishing industry based on demands of market economy | Estonian fishing industry is in the process of restructuring. This causes the movement of labour forces and the need of complementary education in fishing sector.<br>Accomplishment of privatisation process and concentrating on catch of own fish resources. | A. Start-up of the integrated project for developng of coast areas what would allow to use fish waters and coast areas in complex for development of fishing, agriculture, ports and sea transport, tourism etc.<br><br>B. Foundation of quality guaranteeing system for fish products based on the standards of European Union |

| Fishing policy of European Union | Present fishing policy of Estonian Republic | Development problems in Estonian fishing industry | Steps to be taken to join with the European Union |
|---|---|---|---|
| 5. Guaranteeing of a fair competition | 6. Development of Estonian fish market | Due to the fact that fish market and commercial intermediating of fish is not sufficiently organised, some part of fish is not included in a state statistics | A. Foundation of contol system for organising the movement of fish and its products and guaranteeing of reliable statistics<br><br>B. Elaboration of the system of fish auxions supported by the state because it should remarkably improve commercial intermediating of fish |
| 6. Development of international co-operation | 7. Development of international co-operation | At present there is an active international co-operation in the field of administration of fish resources and protection.<br><br>Economical co-operation between countries of the Baltic Sea and creating of preconditions for integrating to European Union is insufficient<br><br>Insufficient exchange of info between the countries of the Baltic Sea | A. Active assisting in a work of a new international co-operation forum in the field of fishing industry - BAFICO (Baltic Fisheries Cooperation)<br><br>B. Assisting in creation of preconditions for Estonian fishing industry to integrate to the European Union<br><br>C. Assisting in development of information exchange system between the countries of the Baltic Sea |

APPENDIX 2

**"International Trade Constraints"**

Seminar on constraints
to agricultural and rural policy reforms
in the new democracies of
Central and Eastern Europe in Tallinn and Viljandi;
1-2 September 1994

Organization for Economic Cooperation and Development (OECD)
Division for Economies in Transition
Directorate for Food, Agriculture and Fisheries

COUNCIL OF EUROPE    CONSEIL DE L'EUROPE

Parliamentary Assembly
Assemblée parlementaire

Strasbourg, 29 August 1994
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COMMITTEE ON AGRICULTURE AND RURAL DEVELOPMENT

Sub-Committee on East-West
Agricultural and Rural Development

Seminar on constraints
to agricultural and rural policy reforms
in the new democracies of
Central and Eastern Europe
in Tallinn and Viljandi
(Estonia)

1 - 2 September 1994

**THEME II:**

**International trade constraints**

by

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This paper is divided into two parts: the first part discusses the major impediments that hinder trade flows between the Central and Eastern European Countries and OECD countries; and, the second part briefly outlines some elements of competition and their impact, on trade in agricultural and food products.

## A. BARRIERS TO TRADE IN AGRICULTURAL COMMODITIES BETWEEN EAST AND WEST

### Introduction

Central and Eastern European Countries have shown little integration into the world economy over the last quarter of a century. Up until 1990, the "Soviet bloc" countries which were members of the Comecon system (CMEA) conducted most of their foreign trade with one another. The opening of markets in OECD countries provide an important opportunity to integrate the Central and Eastern European Countries (CEECs) into the world economy.

In the past, industrial countries responded to Eastern Europe's central planning of trade by imposing both tariffs and quantitative restrictions on their exports; these were on average higher than those applied to developing countries. In addition, non-tariff barriers on exports from CEECs were concentrated in sectors which were considered to be sensitive by western countries, in particular, agriculture, textiles, clothing, iron and steel. However, following the political and economic changes that have occurred in Eastern Europe, OECD countries have been relaxing their trade barriers towards the area. For example, a number of Association Agreements have been signed between the EU and Poland, Czech Republic, Slovakia, Hungary, Romania and Bulgaria. These Agreements are aimed at creating a free trade area for non-agricultural products and at lowering tariffs on agricultural products over a ten year transition period.

The introduction of world market prices and the switch to payment in convertible currencies have brought about a fundamental change in the pattern of production and trade in Eastern Europe. In general, raw material prices (especially for agricultural commodities) have increased while those of manufactured goods have declined. Thus, in many CEECs a considerable proportion of manufacturing tends to be value-subtracting (the end product is worth less than the total cost of the inputs). In the transition from a centrally planned to a market economy, there has been a major re-adjustment of the agricultural sector, resulting in a significant fall in output and exports. Many of the problems in the sector are perceived to be of a more fundamental structural or institutional nature. These problems are often further exasperated by distortions in trade policies, which postpones the necessary restructuring of the industry that is crucial for the longer term viability of the sector.

In many countries, one of the key roles of agricultural trade policy has been to achieve domestic agricultural policy objectives, usually to protect farmers from lower cost competitors abroad. In the CEECs however, taxes on imports and exports of agricultural goods are often more important as a source of revenue for the governments. If revenues are generated by export taxes then domestic prices will be suppressed, on the other hand, if revenues are raised by import taxes then domestic producers of the product concerned are protected.

The main objectives of trade policy in Eastern Europe are to gain access to Western European markets and to develop other markets such as those in the Middle East. However, in order to realise these objective,s the appropriate marketing institutions must be established in CEECs. In addition to the immediate aim of trade expansion, Eastern European countries have a number of other objectives with respect to their foreign trade policies including, modernisation of their industries. In effect, the expansion of trade would result in an increase in output, employment and incomes. At the microeconomic level, foreign trade would also encourage improvements in efficiency of domestic industries. In summary, liberal trading practices are the most effective way to enhance economic growth and to alleviate the problem of large balance of payment deficits in these countries.

## I. Changing Patterns of Trade

The emerging pattern of trade in CEECs arising from the transformation process has little in common with previous trends in export performance and earlier attempts at trade liberalisation in the region. Western Europe has become the most important area of trade growth for Central and Eastern European countries. Trade in agricultural products between Eastern Europe and the Newly Independent States (NIS) has declined since 1990; revealing past structural distortions that will take time for readjustment of OECD market requirements. The domestic economic dislocation resulting from the loss of trade in the East makes enlarged export opportunities to more stable OECD markets crucial for economic growth and political stability in the region. Since 1990, exports to Western Europe, especially in sensitive products represents the only source of consistent export growth for the CEECs. At the same time, many OECD exporters are finding markets in the Eastern Europe for their products. However, in the immediate future, OECD countries are likely to continue to record a trade surplus with the countries in Central and Eastern Europe.

Since 1989, the trade policies of industrialised countries with respect to Eastern Europe have been gradually reduced. Tariff and non-tariff barriers to imports were reduced after countries in Eastern Europe progressively abandoned their centrally planned systems and liberalised prices and foreign trade. Import licences and multiple currency exchange regimes were eliminated and limited currency convertibility was introduced in most countries. These changes have allowed countries in Eastern Europe to abolish state control over foreign trade transactions. Moreover, the EU cancelled specific quantitative restrictions on imports from centrally planned economies and suspended other quantitative restrictions during 1991. However, quantitative restrictions are maintained in sensitive EU sectors such as agriculture, textiles, clothing and iron and steel.

Historically, trade measures of OECD countries towards Eastern Europe were more restrictive than those on imports from other areas. For example, in spite of Poland (1967), Czechoslovakia (1984), Hungary and Romania (1981) being GATT members for many years, because of their centrally planned regimes, it was only at the end of the 1980s that the United States and the EU granted them most favoured nation (MFN) tariff treatment. Consequently, tariffs on their exports were higher on average than those on other developing countries exports. The incidence of non-tariff measures (NTM) increased during the 1970s and 1980s on exports of other countries but NTMs on exports from Eastern European were kept high but stable. This occurred because the Comecon countries with planned foreign trade and currency inconvertibility prevented economic agents from reacting to price signals and profit incentives, thus limiting the affects of import tariff protection. The most commonly used measures to hinder trade flows were quantitative barriers; minimum prices (below which there is a presumption of unfair competition), anti-dumping and countervailing investigations.

Although, the share of foreign trade in CEECs gross national product was significantly lower than comparable western industrial nations, substantial progress has been made in liberalising trade between East and West. More specifically, several measures have been adopted which aim to liberalise trade such as abolishing export subsidy schemes, ending government trade monopolies, teeing exchange rate policies more closely to market forces, eliminating quantitative restrictions and establishing tariff schedules. In Poland, Hungary and the Czech Republic lower protection has been accompanied since the mid-eighties by appreciating real exchange rates, which has resulted in an increase in imports and a deterioration in their trade balances.

In the period 1989-1992, there was a dramatic decline in foreign trade for CEECs, with exports falling by 50 to 60 percent. This collapse in exports had a major impact in terms of the fall in output and incomes and the rise in unemployment. The IMF (1991) has attributed more than 50 percent of the loss in output during the period to the breakdown in trading relations between the CEECs and between the CEECs and the NIS. The economic dislocation from the decline in trade among ex-CMEA partners places greater emphasis on getting improved access to the more stable OECD markets for economic growth and political stability. Moreover, trade among the CEECs and the NIS continues to decline, with an increasing number of trade frictions occurring amongst the former trading partners.

Exports of sensitive products, especially agricultural and food products are relatively more important for countries in Eastern Europe, in particular for Poland, Hungary and the Czech Republic. For example, for some CEECs, exports of sensitive products to OECD markets represent over 50 percent of their total foreign sales of these products. On the other hand, in the case of OECD countries, less than 5 percent of sensitive products in Eastern European countries is no base don an export boom for these products but stems more from the collapse in demand for capital goods both on the domestic market and abroad (capital goods were previously the most important exports for these countries). As the OECD Ministerial Council stated in its 1992 Communiqué, "transition economies will need access to OECD markets for products for which they have significant export capabilities (sensitive products), these products often face a disproportionate number of non-tariff barriers in OECD countries". At the same time, OECD countries have become major exporters of agricultural products, iron and steel, chemicals and textiles to Eastern Europe.

Impediments to trade flows can be divided into three broad groups,, monetary, structural and trade policy impediments, these are discussed in some detail in the remainder of this paper.

## II. Monetary Impediments to Trade

Policies with respect to exchange rates have played a major role in determining the volume and direction of trade flows for many countries in Eastern Europe. During the pre-reform period (pre-1989), the official exchange rates for most CEECs were generally over-valued and together with limited convertibility inhibited trade with OECD countries. Between 1989 and 1991, many of the CEECs introduced their own currencies in an attempt to control inflation and to facilitate convertibility. With the introduction of domestic currencies almost all of the CEECs have devalued their currencies significantly against Western hard currencies. In general, this was perceived to be a necessary step before the CEECs could make the transition to partial convertibility for trading purposes. In many cases, the extent of the devaluations has resulted in the new currencies becoming undervalued relative to their purchasing power parity exchange rates and has thus provided a stimulus to exports by enhancing the price competitiveness of export based industries.

As the fear of potential inflation has increased, many of the CEECs have adopted macroeconomic policies that involve managed exchange rates. As imports increase (in particular, capital goods), and exports decline, the trade deficits have increased. This process has been accompanied by large capital inflows into many of the countries in Eastern Europe, culminating in balance of payments surpluses. This in turn has led to a strengthening of the currencies in some CEECs, and a further increase in imports of traded goods. In general, production cost in countries in Eastern Europe are low when compared to OECD countries and acts as a magnet to foreign investment.

There has been little confidence in the national currencies in Eastern Europe because of high and diverging rates of inflation, and because of their limited convertibility. Real exchange rates have become overvalued in some countries due to large capital inflows, and this makes domestic prices look unreasonably high and exports uncompetitive in international markets. Moreover, converting international prices at an overvalued exchange rate often results in the internal price appearing above the international price indicating that the agricultural sector is protected when in fact the opposite may be true. Other factors such as the relatively underdeveloped foreign exchange markets, financial institutions, export credits and insurance have also played a role in restricting trade withe OECD countries.

## III. Structural/Infrastructural Impediments

Many of the CEECs have inherited an infrastructure that is poorly suited to serve the market institutions that are emerging from the economic reforms. In particular, both transport and communication infrastructures are often in poor condition and severely impede attempts to re-direct the regional pattern of trade flows. A number of surveys of exporters in Eastern Europe suggest that the poor quality of the telecommunication services is the most serious infrastructural barrier to trade in these countries.

The legacy of strict information controls and a poor equipment base (information technology) continue to hamper the export efforts in many Eastern European countries. More specifically, delays in receiving information on domestic regulatory measures and changes in these measures, in addition to, a lack of information on longer term government policies cause extra frustration and higher costs to exporters. Also, the lack of access to commercial information in Western countries relating to product standards, supply requirements and market specifications have acted as a significant barrier to export expansion. A suitable information system which would allow suppliers in CEECs and customers in OECD countries to learn more of each others potential needs could greatly facilitate exports from these countries.

Other structural impediments to trade include an inefficient banking system and general regulatory instability such as constantly changing fees and licence requirements. Some surveys of exporters in CEECs indicate that domestic barriers impede the expansion in exports more than foreign barriers. Lastly, in the case of many Eastern European countries, inefficient border crossings have added an extra impediment to the infrastructural problems outlined above.

## IV. Trade Policy Impediments

Trade policy impediments include both tariff and non-tariff barriers to exports and imports. This section describes some of the tariff and non-tariff barriers to trade between the CEECs and OECD countries.

### Tariffs

In the pre-reform period (pre-1989), many of the OECD countries denied the centrally-planned countries of Eastern Europe the benefits of normalised trade relations, such as most-favoured nation status (MFN) or generalised system of preferences (GSP). However, since 1990 most OECD countries have extended the benefits of normalised tariff treatment on the countries in Central and Eastern Europe. The impact of the more favourable tariffs on the export performance of the CEECs depends to a large extent on the nature of the exports and their sensitivity to tariff changes. For example, in sensitive product sectors such as agriculture and textiles, the likely impact of the tariff changes will be negligible. This is supported by estimates of average MFN and combined MFN-GSP tariffs applied by several OECD member countries to major Eastern European export sectors which show that tariffs on food products continue to be much higher than for other sectors.

A number of preferential trade arrangements have been implemented for the CEECs (Table 1). For example, Association Agreements have been signed between the EU and six of the CEECs; Hungary, Poland, Czech Republic, Slovakia, Romania and Bulgaria. These Agreements attempt to establish free trade zones and cover a range of important industrial exports from Eastern Europe, including some sensitive products. Implementation of the Agreements will take place over a transition period of up to ten years in harmony with GATT developments. Three separate protocols of the Agreements regulate textiles, steel and coal and processed agricultural products. In relation to qualitative restrictions on imports of raw and processed agricultural products, some of these were eliminated on the date of entry into force of the Agreements, while custom duties are to be gradually reduced over a five year period.

Quantitative restrictions and custom duties on manufactured products are to be progressively reduced and abolished over a period of five to nine years. However, special safeguard measures are included in the Agreements to prevent unfair competition. Under certain conditions, participating countries can start anti-dumping investigations and can adopt restrictive measures in order to safeguard their domestic markets. Moreover, during the first five years of the Agreements, countries in Eastern European have the right to impose temporary import tariffs in order to protect infant industries or sectors undergoing restructuring.

Non-Tariff Barriers

Most of the non-tariff barriers that specifically targeted exporters in the centrally planned economies have been eliminated over the last five years. Some of the existing non-tariff barriers between OECD countries and CEECs are part of special arrangements in which bilateral quotas are administered and allow considerable national discretion in determining market access. The remaining non-tariff barriers in OECD countries are largely concentrated in a few sensitive sectors such as agriculture, iron and steel, chemicals and textiles. These products largely account for the positive trade balance that OECD countries have with countries in Central and Eastern Europe.

There are a variety of programmes in OECD countries that provide subsidies either directly or indirectly to their domestic industries, and in turn reduces market access to foreign competitors in both domestic and third country markets. Several CEECs have complained that subsidised OECD products undercut sales on their domestic market and on markets in the Newly Independent States. For some products, in particular iron and steel, some OECD countries maintain "voluntary export restraints" or price regulations. In the case of textiles, participants in the Multi-fibre Arrangement (MFA) have generally limited Eastern European exporters to relatively small market shares in OECD countries, although, in recent times some quotas have been readjusted to permit higher levels of imports.

Exporters from Eastern Europe face other non-restrictive trade regulations such as health and safety measures, quality certification procedures and marking and packing requirements. For example, in 1993 the EC imposed a one-month ban on imports of live animals, meat, milk and dairy products from Eastern Europe for sanitary reasons. This action was cited to be a protectionist measure by several CEECs while the EU however, viewed the action as an urgent health measure.

Exporters including those from the CEECs face a wide variety of rules and regulations that govern specific products or product groups in OECD markets. These rules are usually non-discriminatory and apply to all countries who sell on OECD markets. The continually expanding set of regulations that arise from quality specifications, product norms, environmental regulations and new packaging requirements are more subtle impediments to trade than tariffs and subsidies and often involve substantial costs to exporters.

The findings of trade dispute panels on dumping and countervailing duty cases taken in response to claims of unfair competition in Western countries, have also limited market access for some Eastern European products. Most industrialised countries have established special rules for pursuing unfair competition actions against state-trading countries. However, given the different pace of transition to a market economy in each of the CEECs, the application of these special rules becomes rather ambiguous.

Concluding remarks

Foreign trade will continue to play a crucial role for Central and Eastern European Countries during the transition to market economies. The countries in Eastern Europe will continue to need imports from OECD countries in order to modernise their economies. On the other hand, CEECs need export opportunities in order to safeguard output levels and incomes, and to finance imports. The most effective safeguards for the reform process in the CEECs involves establishing the right policy mix of internal and external policies so as to encourage greater integration into the world economy.

The success in integrating Eastern European economies into the world economy will largely depend on the ability of CEECs to pursue outward and market oriented policies. Many Eastern European countries fear that when Western countries stress regional co-operation they are only trying to distract attention from their own protectionism. With the deepening recession in many Western countries in the early 1990s, developments in Eastern Europe have been seen primarily as a threat as a potential competitor to established markets for Western products.

Global opening of markets is in the long-term interest of all countries. Impediments to trade flows and protectionism cannot halt the relocation of production based on comparative advantage. Nevertheless, the CEECs have considerable structural adjustment still ahead in order to establish the mechanisms of the market system and are only just beginning to build an economy which can hold its own in the market-place.

The 1992 OECD Ministerial Council Communiqué stated that "Ministers recognise the crucial importance of expanding exports for the Central and Eastern European Countries (CEECs) engaged in a process of commercial and economic opening". Member countries should therefore;

support trade liberalisation in these countries by policies of import liberalisation in OECD countries, in general, as well as in sensitive sectors and areas where the CEECs have significant export capabilities, and

provide technical assistance in the identification and reduction of trade barriers.

Possible actions to reduce trade impediments

The examination of impediments to trade suggests that OECD countries might consider some of the following ways to reduce impediments that restrict trade with CEECs. These actions could include to:

- continue to improve market access for the CEECs, making special efforts in areas where these countries have significant export capabilities (e.g. agriculture), and at the same time aid necessary industrial restructuring by technical assistance,

- provide consultations that help CEEC exporters comply with non-restrictive trade measures such as quality certification, health and safety regulations, etc.,

- review the application of procedures for dealing with import surges and unfair competition in light of the progress made by each CEEC toward a market economy,

- provide assistance in restructuring enterprise accounts to improve price and cost transparency,

- continue technical assistance efforts, focusing in particular on problems areas such as infrastructure (improving telecommunications, transport and the customs agencies) and improving information flows through dissemination of regulatory information to exporters, and helping exporters with the standard conventions with respect to markings, packing requirements, etc.

**Table 1: Free Trade Arrangements with Central and Eastern European Countries**

Sweden Trade Agreements with Estonia, Latvia and Lithuania (1992)
Norway Trade Agreements with Estonia, Latvia and Lithuania (1992)
Finland Trade Agreement with Estonia (1992)
Finland Trade Agreement with Latvia (1992)
Finland Trade Agreement with Lithuania (1992)
Switzerland Trade Agreement with Estonia (1992)
Switzerland Trade Agreement with Latvia (1992)
Switzerland Trade AGreement with Lithuania (1992)
EC Association Agreement with Czech Republic, Slovak Republic, Hungary and Poland (1991)
EC Association Agreement with Bulgaria (1993)
EC Association Agreement with Romania (1993)
EFTA Agreement with Hungary (1993)
EFTA Agreement with Bulgaria (1993)
EFTA Agreement with Romania (1992)
EFTA Agreement with Poland (1992)
EFTA Agreement with Czech and Slovak Republics (1991)
Agreement between Czech Republic, Slovak Republic, Hungary and Poland (1992)

*Source: GATT Secretariat*

## B. COMPETITION AS A PROMOTER OF SUCCESSFUL DEVELOPMENT IN AGRICULTURAL TRADE

Introduction

Competition is a fundamental requirement in the development of a market economy. Competitive or free markets are the most efficient way to exploit comparative advantage which in turn largely determines production and investment patterns and the direction of trade flows for any country or region. Therefore, the best policy option would involve a strict noninterventionist (laisser-faire) approach. This approach is based on the predication that competition between private producers promotes the most efficient use of available resources (land, labour and capital). In other words, private markets are the best means of promoting efficiency, and any form of intervention can only reduce efficiency.

The standard approach to evaluating the domestic marketing system has been to measure the extent to which the market functions or fails to function within the framework of certain performance criteria such as efficiency, growth and full employment. In general, marketing efficiency is relevant whether applied to the domestic market or to the international economy. Markets should be organised in such a way as to operate on a least cost basis in performing functions such as storage, processing, distribution and financing. Also the information and price system should result in the allocation of resources to production such that the greatest output is achieved at least cost with the available technology. As with the domestic market system, improvements in international market efficiency can conflict with other performance goals such as economic security. In addition, differences among countries in customs and practices, available technologies, language, political systems and levels of education and economic development lead to rigidities and barriers that further impede movement toward greater productive and allocative efficiency.

Countries in Central and Eastern Europe could be considered as moving from a state of disequilibrium with quantity rationing to a more market oriented position where price equates supply and demand in the market. By encouraging the adjustment process to a market economy, the cost of entry into agricultural production is lower and products will be produced at competitive prices for both the domestic and export markets. however, impediments to trade inhibit market signals and lead to distortions in the allocation of scarce resources.

In the CEECs, the starting point was a pattern of production and consumption that did not reflect a competitive equilibrium. This is clear from the distortionary system of administered prices and quantitative controls which prevented any tendency to allocate resources based on a competitive equilibrium. The liberalisation of prices and the elimination of subsidies will allow markets to adjust to find a more market based equilibrium. However, it should be recognised that risk and uncertainty is a necessary part of this transition process to a market economy.

Privatisation is an essential element in the process of establishing a competitive market. However, it is important to distinguish between public enterprises operating in competitive markets and public monopolies which are often granted an exclusive right to production. Where such enterprises do no enjoy monopoly status, such firms should be subject to competition in the same way as private enterprises. For example, in OECD countries where public monopolies still exist, there has been a move to restructuring these enterprises leading to a separation of potentially competitive activities, which are then subject to market forces.

There tends to be much confusion regarding trade policy and competition policy as both have a common objective, i.e., economic efficiency. Trade policy however, can be viewed as dealing more with the efficient allocation of resources between markets whereas competition policy is more concerned with the efficiency of resource allocation within markets. Competition policy essentially defines the rules and regulations that govern business practices and government policies which affect competition such as aids and subsidies to enterprises, regulation of prices and output of monopolies. The basic underlying objective of competition policy is to protect and preserve competition as the most appropriate means of ensuring the efficient allocation of resources and thus efficient market outcomes. In order to improve the efficiency of international resource allocation, it is important that trade and competition policy complement rather than contradict each other. While countries differ somewhat in defining efficient market outcomes, the application of these concepts result in lower consumer prices, higher quality products and greater product choice.

The elimination of impediments to exports and imports enhances competition and leads to an expansion of trade. In addition, the more competitive a country or industry relative to others, the greater the potential for increasing exports, other things being equal. The concept of competitiveness is a complex issue, particularly with respect to trade in agriculture and food products. There is a large body of knowledge on this concept and on the factors that influence competitiveness in agriculture.

Factors that determine competitiveness in agriculture and food products

Competitiveness has been a pre-occupation of many OECD countries in recent years. Concerns over competitiveness have been fulled by slow or negative economic growth in most OECD countries in addition to fears about the consequences of trade liberalisation. There are many different perceptions of competitiveness and of the factors that determine competitiveness in the agricultural sector; these factors are briefly outlined in this section.

Competitiveness in international food markets, is determined by different factors depending on the type of product produced. One of the most important determinants is the availability of factor endowments and natural resources, which is not only an important factor determining competitiveness but is also a key to the comparative advantage of a country. In the case of agricultural production, natural resource advantages are particularly important, for example, soil type and climatic conditions largely determine what crops can be successfully grown.

Technology can give a country some specific advantages or disadvantages in terms of competitiveness. Technical change may be both cost-reducing and/or quality enhancing. Furthermore, some aspects of technology may be highly mobile across borders especially for resource based enterprises. Other technologies pose constraints that are more important for some countries than other (e.g. waste disposal from animal production). For a country to have a competitive advantage, it must have access to appropriate technology, which usually requires investment in research and development.

The availability of human capital (resources) is critical to competitiveness of specific products or sectors. For most enterprises, unskilled labour input represents a decreasing proportion of the value of the final product while expertise or highly skilled labour represents an increasing proportion, especially where products are tailored to customer's specific needs. Expertise is critical to an enterprise, especially in terms of developing products for niche markets.

Another important factor is management expertise. The quality of management is likely to be a crucial aspect if an enterprise is to pursue the optimal long-run profit maximising strategy associated with competitive markets.

Product characteristics become increasingly important as we move from a commodity and natural resource based export to higher value added exports. Consumers tastes and preferences vary within and across countries, and successful strategies can be designed to serve market niches, in addition to broad market demands. Other non-price factors can also be an important component of product characteristics to processors and consumers, e.g. supply reliability.

Market institutional characteristics such as market structure and firm strategy can also have a major affect on competitiveness. These characteristics can vary substantially across products and countries. For example, cost leadership. The nature of competition or lack of competition in an industry will influence the outcome of strategies or policies aimed at developing domestic and international markets.

The input supply sector is another important component of competitiveness. The relationships between producers and their input suppliers can be critical to the success or failure of an enterprise. Although the availability of local suppliers can offer some advantages to an enterprise, enterprises often source inputs from suppliers who are located in other countries.

The marketing and distribution system can be critical to the success of an enterprise, especially in relation to export markets. For example, the internal transport network in the U.S. gives an important advantage in export competitiveness for grains, while European links to North Africa and the Middle East may give an advantage in their value added exports to that region.

The regulatory environment in which enterprises operate plays a crucial role in determining competitiveness in international markets. In some countries, the rules and regulations may be very specific and thus may constrain the opportunities for an enterprise. While regulations are clearly necessary, for example, to protect the health and safety of the population, different views on what constitutes appropriate regulations or different values on environmental quality can cause these rules to vary across countries.

The relative importance of the factors outlined above varies depending on whether one is dealing with primary commodity production, semiprocessed products or highly processed food products. In addition, the relative importance of the elements of competitiveness also depends on the type of product, and the country or region of production.

<u>Instability and uncertainty arising from the transformation process</u>

Countries in Central and Eastern Europe have adopted either a gradual or radical approach to the development of a market economy. For example, Hungary has adopted a gradual approach to liberalisation and has allowed inertia to slow the pace of transformation. On the other hand, Poland has adopted a more radical approach to liberalisation and to establishing market institutions. This has prompted calls for stabilisation in order to reduce the instability or uncertainty caused by the transition to a market economy. For agriculture, this type of instability can be reduced by a number of market based approaches.

The first strategy that a farm or food processing firm can take to reduce uncertainty is through diversification of products and markets. however, there is often a tradeoff between increased diversification on one hand and economies of scale on the other. Other more sophisticated techniques for reducing risk include, forwards, futures and option markets.

Futures markets can serve a number of purposes in the case of Eastern Europe. The first function is to reduce risk/uncertainty or hedging. A farmer or commodity producer can sell a proportion of the harvest forward using future contracts in order to gain more certainty about future incomes. Although futures may not stabilise incomes they may reduce uncertainty. Second, future markets facilitate price discovery, by allowing producers, consumers or traders to make transactions based on their expectations. Hence, futures prices reflect the markets view as to the likely course of future events and often become a standard reference for making plans and engaging in transactions.

Lastly, futures markets can also serve to reduce barriers to entry into an industry, increase competition and hence aid in the development of market economies. For example, in some countries such as Hungary and Poland, state grain companies are being privatised on a regional basis. This gives each regional grain company a high degree of monopsony over especially as the limited storage capacity and processing facilities tend to be concentrated in their hands. Futures markets can facilitate entry into these activities by reducing the risk involved in grain trading, and in this sense are pro-competitive. By reducing uncertainty they can further enhance the growth of competition in an economy.

* * *

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APPENDIX 3

**"European Union Relations with the Countries of Central and Eastern Europe"**

Background Brief (BB 19) prepared by the European Commission,
January 1994

EUROPEAN COMISSION
DIRECTORATE-GENERAL
Information, Communication, Culture, Audiovisual

External Information

BACKGROUND BRIEF
BB 19 (UPDATED JANUARY 1994)

# EUROPEAN UNION RELATIONS WITH THE COUNTRIES OF CENTRAL AND EASTERN EUROPE

## CONTENTS

## I Overview

Agreements

Relations between the European Union and the countries of Central and Eastern Europe received a new impetus after the changes that took place in those countries in the late 1980s making it possible for them to undertake profound political and economic reforms. The EC established diplomatic relations with each of the states existing at the time. In 1991 the Community recognised the newly independent Baltic States, in January 1992 it recognised the independence of Slovenia and Croatia, and in April 1992 that of Bosnia. As of 1 January 1993 the EC recognised the Czech Republic and Slovakia as successor states of the Czech and Slovak Federative Republic.

*Sectoral trade arrangements* on textiles, steel and meat products had been made with some of the Central and Eastern European countries prior to establishing diplomatic relations. Romania was the only COMECON[1] country with which the EC had a general trade agreement, concluded in 1980, though the first such agreement with the former Yugoslavia[2] was signed in 1970.

Since October 1988 the Community has concluded *Trade and Cooperation Agreement* (see Annex 1) with most of the Central and Eastern European countries[3]. With some of them (Poland, the Czech Republic, Slovakia, Hungary, Romania and Bulgaria) these are to be replaced by comprehensive *Europe Agreements* (signed under art. 238 of the EEC Treaty, see Annex 2) which establish associations between these countries and the European Union and provide the basis for an entirely new type of bilateral relations. Awaiting ratification by all parties concerned, the trade and trade-related provisions of the Europe Agreements have entered into force by way of ***Interim Agreements*** in the case of Poland, the Czech Republic, Slovakia, Hungary and Romania. The entry into force of the Europe Agreement with Poland as well as Hungary will take place on 1 February 1994 (the first day of the second month following the completion of the ratification procedure).

[1] Council for Mutual Economic Assistance, ceased to exist in early 1991.

[2] The former Yugoslavia was not a member of COMECON. It had only an observer status.

[3] A Trade and Cooperation Agreement was signed with the former Czechoslovakia, but not separately with the successor Czech and Slovak Republics. The Agreement with former Yugoslavia is no longer in operation, but a new Trade and Cooperation Agreement with Slovenia was signed in 1993; there are no new agreements with the other states of former Yugoslavia.

Assistance

The European Union supports the process of political and economic reforms in Central and Eastern Europe in several ways. The *Europe Agreements* constitute the new general framework for Union assistance to 6 of the Central and Eastern European countries.

The main instrument of financial and technical cooperation is the Commission's *PHARE* programme which became operational in 1990 for Poland and Hungary and was subsequently extended to cover all the countries of the Central and Eastern European region, including Slovenia, but not the other states of former Yugoslavia. The purpose of PHARE is to support the process of economic restructuring and democratic reforms in these countries. It provides technical, economic and infrastructural assistance to the beneficiary states. The aim is to help these countries achieve market economies based on free enterprise, private initiative and democratic decision-making.

The PHARE programme is demand-driven and concentrates on a limited number of programmes responding to requests from the recipient countries. By the end of 1992 PHARE had committed 2.3 billion ECU for economic reform in these countries and in 1993 a further 1.04 billion ECU is available. This is grant money, used so far mainly for technical assistance and skills transfer, although support in other areas is not excluded, and from 1993 much more will be used for investment. PHARE will start using a multiannual programming mechanism in order to achieve greater coherence both between its various programmes and with the medium- to long-term reform strategies of the beneficiaries. This multiannual approach can be seen in operation for the first time in the 1993 indicative programmes, which set the framework for PHARE operations in 1993 and 1994. It has been proposed that PHARE assistance be focused on the following four domains in 1993: a, economic restructuring; b, human resources development; c, support to public sector consolidation; d, development of infrastructure networks. In order to contribute better to investment programmes, PHARE is developing its cooperation with the *EIB*, the *EBRD* and other financial institutions.

Humanitarian, food and emergency aid for some of the countries of Central and Eastern Europe has been funded from different sources, including PHARE.

The *European Investment Bank*, which is a Europoean Union institution, has also made available its resources, know-how and experience to assist Central and Eastern European countries in their transition to market economies. In decisions taken at the end of 1989 and in April 1991, the EIB Board of Governors authorised lending of up to 1.7 billion ECU (MECU) for investments projects in Bulgaria, the Czech Republic, Hungary, Poland, Romania and Slovakia. Since July 1993 the EIB may also lend up to a total of 200 MECU in Estonia, Latvia and Lithuania; and up to 150 MECU in Slovenia. Until the end of September 1993 the EIB provided a total of 1306 MECU of loans (Bulgaria: 196 MECU, the Czech Republic: 222 MECU, Hungary: 305 MECU, Poland: 303 MECU, Romania: 144 MECU, Slovakia: 138 MECU). According to the forecast of loans a total of 3 billion ECU is planned until 1996 (1994: 75 MECU, 1995: 965 MECU, 1996: 1270 MECU). Priority is given to projects in transport, telecommunication, energy, industry, in particular joint-ventures with European Union partners and direct investment by European Union firms.

The *European Coal and Steel Community* can also make loans in Central and Eastern Europe for restructuring of the steel and coal industries. A total of 200 MECU is earmarked for this purpose.

The *European Union* also grants loans in support of macro-economic policies, mainly *balance of payments loans*. These are complementary to IMF and World Bank loans and are subject to IMF conditions. So far 10 such loans were approved for a total amount of 2.5 billion ECU. Albania received this form of assistance by way of a grant (70 MECU).

The Commission coordinates the assistance offered to the countries of Central and Eastern Europe by all industrialised countries, the so-called *Group of 24 (G-24)*[4]. Action plans have been defined and coordination is developed in priority areas like balance of payments support, food aid and technical assistance in specific sectors.

Trade

As soon as the countries of Central and Eastern Europe committed themselves to radical political and economic reform, the European Union made unilateral trade concessions, abolishing the specific quantitative restrictions which are applied to state-trading countries, and suspended for these countries the quantitative restrictions applicable towards all third countries. The Union's advantageous *Generalised System of Trade Preferences* (GSP) also started to be applied towards the Central and Eastern European countries. As a result the trade flow between the Union and these countries increased considerably.

Trade has grown even more as a result of the entry into force of the *Interim Agreements*. But despite the asymmetrical trade regime, which is in favour of the Central and Eastern European states, the trade surplus in 1992 between the EU and the six countries signatories of Europe Agreements was 2.5 billion ECU in favour of the Community. The meeting of the European Council in Copenhagen on 21-22 June 1993 revised the trade concessions set forth in the

[4]The Group of 24 consists of the members of the European Union, the members of the EFTA, the United States, Japan, Canada, Australia, New Zealand and Turkey.

Europe Agreements and approved new trade concessions in the form of additional protocols.

Expectations for the future

The European Council meeting in Edinburgh in December 1992 decided that the Copenhagen meeting in June 1993 would examine the future development of relations with Central and Eastern Europe. In May 1993 the Commission submitted a proposal to the Council on closer association with these countries. The *European Council in Copenhagen on 21-22 June 1993* approved new measures in four domains in order to foster closer association with the Central and Eastern European countries. They are as follows: a, a structured relationship with the institutions of the European Union; b, improving market access; c, making assistance more effective; d, furthering economic integration. It was declared officially for the first time "that the associated countries in Central and Eastern Europe that so desire shall become members of the European Union" as soon as they satisfy the necessary political and economic requirements.

The EC Troika[5] met the Foreign Ministers of the six associated countries in Brussels on 21 September 1993. It was the first time that Bulgaria and Romania were represented at this meeting.

## II Situation by country

### 1. POLAND

Agreements

A five-year *Trade and Economic Cooperation Agreement* between the EC and Poland was signed on 19 September 1989. It entered into force on 1 December 1989. This non-preferential agreement which contains the clause of reciprocal Most Favoured Nation (MFN) treatment, foresees the gradual abolition by 1994 of quantitative restrictions applied by the European Union on imports originating in Poland. However, in the framework of PHARE, the Union decided to speed up the process and agreed to suspend non-specific and liberalize all specific quantitative restrictions as of 1 January 1990 in all Member States except Spain and Portugal.

[5]The Foreign Ministers of the past, present and future EU presidency, plus the Member of the Commission responsible for external political relations.

Moreover, the agreement provides for cooperation aimed at the development and diversification of EC-Polish two-way trade. The ECSC protocol relating to trade and cooperation in coal and steel products was signed in October 1991.

The *Europe Agreement* between the Union and Poland was signed on 16 December 1991 and was ratified by the Parliament of Poland on 6 July 1992. It received the assent of the European Parliament on 15 September 1992. The parliaments of the twelve Member States have ratified it, and the ratification procedure was completed in December 1993, so the Agreement will enter into force on 1 February 1994 (the first day of the second month following the completion of the procedure). In the meantime, its trade provisions already entered into force on 1 March 1992 by way of an *Interim Agreement*. The trade provisions provide for the consolidation of earlier trade concessions and the gradual establishment of a free trade area over a period of 10 years. Customs duties on both imports and exports on goods originating in the EU and Poland are to be abolished during this period in accordance with the timetables provided in the agreement; other barriers to trade like quantitative restrictions and measures having equivalent effect are also to be abolished; both parties undertake the obligation not to introduce new barriers to trade. The meeting of the *European Council in Copenhagen on 21-22 June 1993* approved new measures in four domains in order to foster the closer association with the Central and Eastern European countries. They are as follows: a, a structured relationship with the institutions of the European Union; b, improving market access; c, making assistance more effective; d, furthering economic integration. It was declared for the first time that these countries can become members of the European Union if they fulfil the necessary economic and political requirements.

A Commission Delegation was opened in Warsaw in September 1990. The Head of the Delegation is Mr. Alexander Dijckmeester.

An agreement making it possible to link Poland to the EU-wide BC-net (Business Cooperation Network) has been signed. Poland is also connected to Euro-Info-Centre and Bureau de rapprochement des enterprises (BRE), and European Documentation Centres are operational in 9 Polish universities and other academic institutions.

Assistance

In the years 1990, 1991 and 1992, 38 projects, for the total amount of 580 MECU from the EC PHARE programme, were approved for Poland. These projects provide funding practically for all major sectors: agriculture, environment, infrastructure, financial sector, education, social sector, public administration as well as privatisation, industrial restructuring, SMEs and structural development in regions. In order to support these priorities, PHARE committed 225 MECU in

1993 on sectorial programmes bringing the total grant aid since 1990 to 805 MECU. Poland also benefits from PHARE regional projects, designed for several Central and Eastern European countries. In 1989/1990 a special food aid programme of 160 MECU was designed for Poland. Poland has not received any balance of payments loans, but the official creditors (Paris club) forgave half of the debt Poland had. The EC played a role in bringing about the Zloty stabilisation fund.

Until 6 September 1993 Poland received 7 *EIB* loans for a total amount of 303 MECU for telecommunication, industry, tourism, environmental protection, energy saving, gas production and distribution, railway and airport modernisation and forest replanting.

Until 30 September 1993 a total amount of 7.346 MECU for 32 projects was committed by the EBRD for technical cooperation with Poland. In 1991, Poland benefited from EBRD loans for a total amount of 113 MECU. In June 1992, the EBRD launched an equity subscription of 40 MECU in the Polish Private Equity Fund, a company to be established to invest in SMEs. Between June and October 1992 Poland received 7 EBRD loans for a total amount of 259 MECU. The beneficiary sectors include telecommunications (188,4 MECU), steel and textile industry (44,8 MECU) and SMEs (70 MECU). The EBRD granted another loan of 30 MECU in April 1993 for the restructuring and modernization of steel industry.

Poland is entitled to ECSC loans in support of restructuring its coal and steel industries.

<u>Trade</u>

Trade between the EU and Poland is conducted under the terms of the *Interim Agreement*. It has increased substantially over the last years. In 1991 the Community became Poland's most important trading partner. In 1992 EC exports towards Poland reached 8.148 billion ECU which amounts to an increase of 3% compared to 1991. During the same period EC imports from Poland increased by 14% and reached 7.077 billion ECU. The trade balance of 1.071 billion ECU was in favour of the Community. The meeting of the European Council in Copenhagen on 21-22 June 1993 approved *new trade concessions* in the form of additional protocols to the Interim Agreements in order to improve the access of the associated countries to the market of the Community.

In 1992 the Community imported from Poland mainly base metals and articles thereof: 19% (18% in 1991); textiles and textile articles: 16% (14% in 1991); agricultural products, including processed agricultural products: 13% (16% in 1991); mineral products: 10% (12% in 1991); and chemical products: 7% (10% in 1991).

For the same period the EC exported to Poland mainly machinery and electrical equipment: 25% (24% in 1991); textiles and textile articles: 11.5% (10% in 1991); agricultural products including processed agricultural products: 11.3% (13% in 1991); chemical products: 10.9% (10% in 1991); transport equipment: 8.8% (15% in 1991).

During the first three months of 1993 the EC exports to Poland reached 2.235 MECU, while the imports amounted to 1.718 MECU. The trade balance of 517 MECU is in favour of the EC. Poland has been the only country among the associated ones that realised a modest growth in its exports towards the EC.

Political dialogue

At the joint request of Poland, Hungary, the Czech Republic and Slovakia the political dialogue, provided for in the Europe Agreements, has already started. The meeting between the EC Troika and the Foreign Ministers of the six associated countries took place for the first time in Brussels on 21 September 1993.

The meeting of the European Council in Copenhagen on 21-22 June called for a multilateral dialogue on matters of common interest.

## 2. HUNGARY

Agreements

A ten-year *Trade and Economic Cooperation Agreement* between the EC and Hungary was signed on 26 September 1988. It entered into force on 1 December 1988. This non-preferential agreement, which contains the clause of reciprocal MFN (Most Favoured Nation) treatment, foresees the gradual abolition by 1994 of quantitative restrictions applied by the Community on imports originating in Hungary. The agreement normalised trade relations and provides for cooperation aimed at the development and diversification of EC-Hungarian two-way trade. The Agreement includes an ECSC protocol relating to trade and cooperation in coal and steel products which was signed in October 1991.

The *Europe Agreement* between the European Union and Hungary, which, when it enters into force, will replace the trade and cooperation agreement of 1988, was signed on 16 December 1991. It received the assent of the European Parliament on 16 September 1992 and was ratified by the Hungarian Parliament in November 1992. The parliaments of the twelve Member States have also ratified it and the whole ratification procedure was completed in December 1993, so the Agreement will enter into force on 1 February 1994 (the first day of the second month following the completion of the procedure). In the meantime, its trade provisions already entered into force on 1 March 1992 by way of an *Interim Agreement*. The trade provisions provide for the consolidation of earlier trade concessions and the gradual establishment of a free trade area over a period of 10 years. Customs duties on both imports and exports on goods originating in the EC and Hungary are to be abolished during this period in accordance with the timetables provided in the agreement; other barriers to trade like quantitative restrictions and measures having equivalent effect are also to be abolished; both parties undertake the obligation not to introduce new barriers to trade. The meeting of the *European Council in Copenhagen on 21-22 June 1993* approved new measures in four domains in order to foster closer association with the Central and Eastern European countries. They are as follows: a, a structured relationship with the institutions of the European Union; b, improving market access; c, making assistance more effective; d, furthering economic integration. It was declared for the first time that these countries can become members in the European Union if they fulfil the necessary economic and political requirements. The Hungarian-EC Joint Committee on the Interim Agreement holds its meetings regularly, the last one was on 4-5 February 1993.

The Commission opened a Delegation in Budapest in November 1990. The Head of the Delegation is Mr. Hans Beck.

An agreement making it possible to link Hungary to the EU-wide BC-net (Business Cooperation Network) was signed in November 1992. Hungary is also connected to Euro-Info-Centre and Bureau de rapprochement des enterprises (BRE), and European Documentation Centres are operational in 5 Hungarian universities and other academic institutions.

<u>Assistance</u>

Hungary has benefited from the Union's PHARE programme which was launched in 1989. Until the end of 1992 33 PHARE projects for over 305 MECU were approved in support of actions in the areas of agriculture, environment, energy and infrastructure, financial sector, public administration, social sector as well as human resources development, privatisation, enterprise restructuring and SME development. PHARE has allocated to Hungary in 1993 approximately the same amount as in 1992 - around 100 MECU. Hungary also benefits from PHARE regional projects, designed for several Central and Eastern European countries.

In order to help Hungary overcome its balance of payments difficulties, the Community has granted it in 1990 and 1991 two loans with a total value of 1050 MECU.

Since 1990 Hungary has also had access to loans from the EIB which are guaranteed by the European Community. The total value of the 6 loans that were provided until 6 September 1993 is 305 MECU for projects in telecommunications, electricity, manufacturing and tourism as well as environment and energy saving, infrastructure and air traffic control.

Until 30 September 1993 a total amount of 5.093 MECU for 26 projects was committed by the EBRD for technical cooperation with Hungary. From 1991 to 15 October 1992 Hungary benefited from EBRD interventions (loans or equities) for a total amount of 825 MECU.

Hungary has access to ECSC loans in support of restructuring its coal and steel industries.

Trade

Trade between the EU and Hungary is conducted under the terms of the *Interim Agreement*. The meeting of the European Council in Copenhagen on 21-22 June 1993 approved *new trade concessions* in the form of additional protocols to the Interim Agreements in order to improve the access of the Central and Eastern European countries to the market of the Union. In 1991 the EC became Hungary's most important trade partner, buying almost half of Hungary's exports and supplying over one third of its imports. In 1992 EC exports to Hungary reached 4.060 billion ECU which represents an increase of 16% compared to 1991. During the same period EC imports from Hungary increased by 10% and reached 3.986 billion ECU. There was a trade surplus of 74 MECU in favour of the Community.

The Community's main imports from Hungary in 1992 consisted of agricultural products, including processed goods: 21% (16% in 1991); textiles and textile articles: 16.48% (15% in 1991); machinery and electrical equipment: 16.43% (15% in 1991); base metals: 10.3% (10% in 1991); chemical products: 5.5% (6% in 1991).

At the same time the Community exported to Hungary mainly: machinery and electrical equipment: 26.8% (28% in 1991); textiles and textile articles: 13.6% (13% in 1991%); transport equipment: 12.06% (10% in 1991); chemical products: 11.2% (12% in 1991); base metals: 5.8% (7% in 1991).

During the first three months of 1993 the EC exports to Hungary reached 1.065 MECU, while the imports reached 885 MECU. The trade balance of 180 MECU is in favour of the EC. The Hungarian export towards the EC decreased during the examined period.

Political dialogue

At the joint request of Poland, Hungary the Czech Republic and Slovakia the political dialogue, provided for in the Europe Agreements, has already started. Meetings of the EC Troika with the Foreign ministers of the six associated countries took place for the first time in Brussels on 21 September 1993.

The meeting of the European Council in Copenhagen on 21-22 June called for a multilateral dialogue on matters of common interest.

## 3-4. The CZECH and SLOVAK REPUBLICS

(until 31 December 1992 The Czech and Slovak Federative Republic)

At the time of the dissolution of the Czech and Slovak Federative Republic (end of 1992) the two successor states declared that they would respect all the obligations stemming from agreements concluded by the CSFR.

Agreements

An agreement between the Czech and Slovak Federal Republic and the Community on trade in industrial products was signed on 19 December 1988.

A ten-year *Trade and Economic Cooperation agreement* was signed on 7 May 1990. It came into effect on 1 November 1990. This non-preferential agreement included the clause of reciprocal MFN (Most Favoured Nation) treatment. It foresees the gradual liberalization by 1994 of quantitative restrictions applied by the Union on imports originating in the CSFR. The agreement provides for cooperation aimed at the development and diversification of EC-CSFR two-way trade. It covers industrial and agricultural goods. Trade in coal and steel products is conducted according to the terms of a ECSC protocol signed in February 1992.

The CSFR and the Community signed on 16 of December 1991 a *Europe Agreement*. But the ratification procedure, which was going on at the same pace as in the case of Poland and Hungary, was stopped because of the dissolution of the CSFR. Negotiations on two *new and seperate Europe Agreements*, respectively with the Czech Republic and Slovakia, were signed on 4 October 1993 and were ratified by the European Parliament on 27 October. Currently they are awaiting the ratification by the parliaments of the twelve Member States. These new agreements (which will replace upon entering into force the trade and cooperation agreement of 1990 between the Community and CSFR) are based on the text of the already signed Europe Agreement between the EC and CSFR. The new element is that they contain an identical human rights clause, as do the Agreements with Bulgaria and Romania, according to the Council Declaration of May 1992. The preamble of the Europe Agreements with the Czech and Slovak Republics emphasizes the democratic achievements of these countries. In the meantime, the trade provisions of the 1991 Europe Agreement already entered into force on 1 March 1992 by way of an *Interim Agreement* and are regulating the trade relations of the two new states with the EC. These provisions consolidate earlier trade concessions (the EC made unilateral trade concessions in January 1991: the CSFR benefited from the Community's Generalised System of trade Preferences (GSP) and the lifting or suspending of quantitative restrictions) and gradually establish a free trade area over a period of 10 years. Customs duties on both imports and exports on goods originating in the EC and the Czech and Slovak Republics are to be abolished during this period in accordance with the timetables provided in the agreement; other barriers to trade like quantitative restrictions and measures having equivalent effect are also to be abolished; both parties undertake the obligation not to introduce new barriers to trade. The meeting of the *European Council in Copenhagen on 21-22 June 1993* approved new measures in four domains in order to foster closer association with the Central and Eastern European countries. They are as follows: a, a structured relationship with the institutions of the European Union; b, improving market access; c, making assistance more effective; d, furthering economic integration. It was declared for the first time that these countries can become members of the European Union if they fulfil the necessary political and economic requirements.

The Commission opened a Delegation in Prague in 1992. The Head of the Delegation is Mr. Leopoldo Giunti.

An agreement making it possible to link the CSFR to the EU-wide BC-net (Business Cooperation Network) was signed in November 1992. The Czech and Slovak Republics are also connected to Euro-Info-Centre and Bureau de rapprochement des enterprises (BRE), and European Documentation Centres are operational in 4 universities and other academic institutions throughout the countries.

Assistance

Since September 1990, when the decision to include the CSFR in PHARE was taken, some 17 projects for a total amount of 233 MECU have been approved. These projects benefit areas like environment, energy, telecommunications, enterprise restructuring and privatisation, SME development and human resources development. In 1993 the financial assistance necessary for the accomplishment of the programmes and operations decided by PHARE is 60 MECU. To support the priorities defined the European Union makes available 40 MECU for commitment to Slovakian programmes in 1993. In addition to that Slovakia and the Czech Republic will continue to benefit (as CSFR did up to now) from PHARE regional projects, designed for several Central and Eastern European countries.

In order to help CSFR overcome its *balance of payments* difficulties, the Community has granted it in May 1991 one medium term loan of 375 MECU.

After the European Community took the decision to extend its guarantee of EIB loans to CSFR, the EIB decided to grant 1 Apex global loan for 85 MECU. The total value of 3 loans that were provided until 6 September 1993 was 222 MECU for projects in manufacturing, tourism, energy saving, environment, telecommunications and motor-car industry. Slovakia received 138 MECU for 4 projects in manufacturing, tourism, energy-saving and environment, road-network, telecommunication and gas storage.

Until 30 September a total amount of 2.186 MECU was committed by the *EBRD* for 15 technical assistance projects in the Czech Republic and 2.42 MECU for 13 technical assistance projects in the Slovakia.

CSFR was eligible for ECSC loans in support of restructuring its coal and steel industries. The successor states are eligible as well.

Trade

Trade between the EU and the Czech Republic and Slovakia is conducted under the terms of the *Interim Agreement*. In 1991 the EC became CSFR's most important trade partner, buying 40% of its exports and supplying about one third of its imports. The meeting of the European Council in Copenhagen on 21-22 June 1993 approved *new trade concessions* in the form of additional protocols in order to improve the access of the Central and Eastern European countries to the market of the Union.

In 1992 EC exports to CSFR reached 6.263 billion ECU which represents an increase of 64% compared to 1991. During the same period EC imports from CSFR increased by 36% and reached 5.535 billion ECU. There was a trade surplus of 728 MECU in favour of the Community.

The Community's main imports from CSFR in 1992 consisted of base metals: 18.28% (16% in 1991); textiles and textile articles: 12% (13% in 1991); machinery and electrical equipment: 11.65% (11% in 1991); transport equipment: 9.35% (10% in 1991); mineral products: 6.3% (8%

in 1991).

At the same time the Community exported to CSFR mainly: machinery and electrical equipment:38% (35% in 1991); transport equipment: 12.11% (10% in 1991); chemical products: 8.2% (9% in 1991); textiles and textile articles: 6.72% (7% in 1991%); agricultural products, including processed goods: 6.65% (7% in 1991).

During the first three months of 1993 the EC exports to the successor republics of the former CSFR reached 1,310 MECU, while the exports amounted to 1,058 MECU. The trade balance of 252 MECU is in favour of the EC. The split of the CSFR affected negatively the trend of slight growth in exports to the EC realised by the CSFR in 1992.

Political dialogue

At the joint request of Poland, Hungary, the Czech Republic and Slovakia the political dialogue, provided for in the Europe Agreements, has already started. The meeting of the EC Troika with the Foreign Ministers of the six associated countries took place for the first time in Brussels on 21 September 1993.

The meeting of the European Council in Copenhagen called for a multilateral dialogue on matters of common interest.

## 6. BULGARIA

Agreements

A ten-year *Trade and Economic Cooperation Agreement* between the EC and Bulgaria was signed on 24 September 1990 and came into force on 1 November 1990. This non-preferential agreement, which contains the clause of reciprocal MFN treatment, foresees the gradual abolition of quantitative restrictions applied by the Community on imports originating in Bulgaria. The agreement normalised trade relations and provides for cooperation aimed at the development and diversification of EU-Bulgarian two-way trade. The agreement includes an ECSC protocol relating to trade and cooperation in coal and steel products.

The *Europe Agreement* between the European Union and Bulgaria, which, when it enters into force, will replace the Trade and Cooperation agreement of 1990, was signed on 8 March 1993.

It was ratified by the Bulgarian Parliament in April 1993 and received the assent of the European Parliament on 27 October 1993. It is currently awaiting the ratification by the parliaments of the twelve Member States. The Europe Agreement with Bulgaria resembles those signed with Poland and Hungary, but contains a human rights clause, as do the Agreements with the Czech Republic, Slovakia and Romania, according to the Council Declaration of May 1992. The trade provisions of the Europe Agreement entered into force on 31 December 1993 by way of an Interim Agreement. Thus Bulgaria benefits from the trade concessions decided at the Copenhagen Summit. These trade provisions foresee the consolidation of earlier trade concessions (the EC made unilateral trade concessions in January 1991: abolition and suspension of quantitative restrictions; started applying towards Bulgaria the EC Generalised System of Trade Preferences), and the gradual establishment of a free trade area over a period of 10 years. Customs duties on both imports and exports on goods originating in the EC and Bulgaria are to be abolished during this period in accordance with the timetables provided in the agreement; other barriers to trade like quantitative restrictions and measures having equivalent effect are also to be abolished; both parties undertake the obligation not to introduce new barriers to trade.

The meeting of the *European Council in Copenhagen on 21-22 June 1993* new measures in four domains in order to foster closer cooperation with the Central and Eastern European countries. They are as follows: a, a structured relationship with the institutions of the European Union; b, improving market access; c, making assistance more effective; d, furthering economic integration. It was declared for the first time that these countries can become members of the European Union if they fulfil the necessary economic and political requirements.

The Commission opened a Delegation in Sofia in June 1992. The Head of Delegation is Mr. Thomas O'Sullivan.

Bulgaria is connected to Bureau de rapprochement des enterprises (BRE). There is one operational European Documentation Centre in Bulgaria.

<u>Assistance</u>

Bulgaria has benefited from the Union's PHARE programme, which was launched in 1989 and was extended to Bulgaria in September 1990. By the end of 1992 18 PHARE projects for over 187 MECU were approved in support of action in the areas of agriculture, environment, energy, telecommunications, financial and health sectors as well as enterprise restructuring, privatisation, SME development and human resources. In 1993 PHARE has allocated for Bulgaria approximately the same amount as in 1992 - around 90 MECU. Bulgaria also benefits from PHARE regional projects designed for several Central and Eastern European countries, including an important project on nuclear safety. In 1991 and 1992 Bulgaria received humanitarian aid in the form of food, medical and energy supplies for about 50 MECU, of which 20 MECU came from PHARE.

In 1991 and 1992 the Community granted Bulgaria two loans to help the country overcome its balance of payments difficulties. The loans for the total amount of 400 MECU are part of a coordinated effort within the G-24.

Bulgaria also has access to loans from the EIB which are guaranteed by the European Community. The total value of the 5 loans which were provided until 30 September 1993 was 196 MECU for projects in energy, telecommunications, air traffic, transport and other small- and medium-sized projects.

Until 30 September 1993 the *EBRD* committed 4,572 MECU for 10 technical cooperation projects in Bulgaria.

Bulgaria is also eligible for loans from the European Coal and Steel Community in support of restructuring its coal and steel industries.

Trade

In 1992 EU-Bulgarian trade continued to rise: EC exports to Bulgaria reached 1.112 billion ECU which is an increase of 6% in comparison with 1991; and during the same period of time EC imports from Bulgaria rose by 19% reaching 897 MECU. The trade surplus of 215 MECU is in favour of the EC.

The Community's main imports from Bulgaria in 1992 were: textiles: 22% (15% in 1991); agricultural products, including processed goods: 20.4% (26% in 1991); base metals: 13.8% (14% in 1991); machinery and electrical equipment: 9.9% (11% in 1991); chemical products: 7.7% (10% in 1991).

At the same time the EC exported to Bulgaria mainly: machinery and electrical equipment: 19.78% (25% in 1991); transport equipment: 19.51% (18% in 1991); textiles: 12.23% (9% in 1991); agricultural products, including processed goods: 11.15% (15% in 1991); chemical products: 10.16% (15% in 1991).

During the first three months of 1993 the EC exports to Bulgaria reached 257 MECU, while the imports amounted to 217 MECU. The trade balance of 40 MECU is in favour of the EC. In the framework of the Trade and Cooperation Agreement Bulgaria has been able to increase its exports towards the EC by 5.1%.

Political dialogue

The meeting of the EC Troika with the Foreign Ministers of the six associated countries took place for the first time in Brussels on 21 September 1993.

The meeting of the European Council in Copenhagen on 21-22 July 1993 called for a multilateral dialogue on matters of common interest.

## 6. ROMANIA

Agreements

Romania was the first COMECON country to have contractual relations with the European Community even before the changes in the late 1980s. In 1980 an *Agreement on trade in industrial products* between the EC and Romania was signed. Both sides had the intention of signing a wider agreement but negotiations were suspended in April 1989 for political reasons. A *Trade and Economic Cooperation Agreement* between the EC and Romania was signed on 5 March 1991. It entered into force on 1 May 1991. This non-preferential agreement contains the clause of reciprocal MFN treatment and foresees the gradual abolition of quantitative restrictions applied by the Community on imports originating in Romania. The agreement normalised trade relations and provides for cooperation aimed at the development and diversification of EU-Romanian two-way trade.

The *Europe Agreement* between the Union and Romania, which will replace the Trade and Cooperation agreement of 1991, when it enters into force, was signed on 1 February 1993. The European Parliament gave its assent to it on 27 October 1993. It is currently awaiting ratification by the national parliaments of eleven Member States. The Europe Agreement with Romania resembles those signed with Poland and Hungary, but it contains a human rights clause, as do the Agreements with the Czech Republic, Slovakia and the Bulgaria, according to the Council Declaration of May 1992. In the meantime its trade provisions entered into force on 1 May 1993 by way of an *Interim Agreement*. The trade provisions provide for the consolidation of earlier trade concessions and the gradual establishment of a free trade area over a period of 10 years. Customs duties on both imports and exports on goods originating in the EU and Romania are to be abolished during this period in accordance with the timetables provided in the agreement;

other barriers to trade like quantitative restrictions and measures having equivalent effect are also to be abolished; both parties undertake the obligation not to introduce new barriers to trade. The meeting of the ***European Council in Copenhagen on 21-22 June 1993*** approved new measures in four domains in order to foster closer association with the Central and Eastern European countries. They are as follows: a, a structured relationship with the institutions of the European Union; b, improving market access; c, making assistance more effective; d, furthering economic integration. It was declared for the first time that these countries can become members of the European Union if they fulfil the necessary requirements.

The Commission opened a Delegation in Bucharest in 1993, the Head of Delegation is Ms. Karen Fogg.

Romania is connected to Bureau de rapprochement des enterprises (BRE) and European Documentation Centres are operational in 2 Romanian academic institutions.

Assistance

The Union's *PHARE* programme was extended to Romania in September 1990 but was then suspended until January 1991 for political reasons. By the end of 1992, 14 projects for 230 MECU were approved. Among the benefiting areas of the economy are agriculture and agro-industry, transport, health and financial sectors, as well as enterprise restructuring, privatisation and human resources development. In 1993 PHARE has allocated to Romania approximately the same amount as in 1992 - 130 MECU. The PHARE Indicative Programme for Romania for the period 1993-1995 was signed on 11 May 1993. Romania also benefits from PHARE regional projects, designed for several Central and Eastern European countries.

Up to now Romania has received 170 MECU of *humanitarian and emergency aid*. 72 MECU of that was provided by PHARE. This aid was destined for orphanages and for children's programmes, as well as general medical and food supplies and emergency aid.

In order to help Romania overcome its *balance of payments* difficulties the Community has approved in 1991 and 1992 two *loans* for the amount of 455 MECU.

The Community has extended its guarantee of EIB loans in Central and Eastern Europe to Romania. The total value of the 4 loans that were provided until 6 September 1993 is 144 MECU for projects in energy, transport, SME development and air traffic.

Until 30 September 1993 the *EBRD* committed 7.585 MECU for 34 technical assistance projects in Romania.

Romania has also access to *ECSC* loans in support of its coal and steel industries.

Trade

Trade between the EC and Romania is conducted under the terms of the *Interim Agreement*. The meeting of the European Council in Copenhagen on 21-22 June 1993 approved *new trade concessions* in the form of additional protocols to the interim Agreements in order to improve the access of the Central and Eastern European countries to the market of the Community.

In 1992 EC exports to Romania continued to rise reaching 1.854 billion ECU which represents an increase of 38%. During the same period the downfall of EC imports from Romania continued. They reached 1.402 billion ECU which is a 5% decrease. The trade surplus of 452 MECU at the end of 1992 was in favour of the Community.

During the first three months of 1993 the EC exports to Romania reached 504 MECU, while the imports amounted to 355 MECU. The trade balance of 149 MECU was in favour of the EC. In the framework of the former Trade and Cooperation Agreement Romania has been able to increase its exports towards the EC by 14.1%.

The Community's main imports from Romania in 1992 consisted of textiles: 35.23% (28% in 1991); base metals: 10.69% (9% in 1991); machinery and electrical equipment: 5.99% ( 7% in 1991); agricultural products: 5.49% (7% in 1991); footwear: 5%.

At the same time the Community exported to Romania mainly machinery and electrical equipment: 21.68% (21% in 1991); agricultural products: 17.52% (19% in 1991); textiles: 17.47% (17% in 1991); transport equipment: 12.83%; chemical products: 6.69% (10% in 1991).

Political dialogue

The meeting of the EC Troika with the Foreign Ministers of the six associated countries took place for the first time in Brussels on 21 September 1993.

The meeting of the European Council in Copenhagen on 21-22 June called for a multilateral dialogue on the matters of common interest.

## 7. ALBANIA

### Agreements

After the establishment of official relations between the EC and Albania in 1991, a *Trade and Cooperation Agreement* between the Community and Albania was signed on 11 May 1992 and it entered into force on 1 December 1992. This ten-year non-preferential agreement is conditional upon respect of human rights and is renewable annually. It provides for MFN status and confirms the removal of specific quantitative restrictions (Albania has benefited from the Community's GSP since January 1992). Steel and textiles are not included in the agreement and are subject to separate negotiations. In the preamble of the Trade and Cooperation Agreement it is mentioned that it could become the basis of a *future* Europe Agreement provided the necessary economic and political conditions are met.

### Assistance

The EC extended the PHARE programme to Albania in January 1992. The amount of PHARE assistance to Albania in 1992 was 25 MECU benefiting the agricultural sector, education, training, research and development, energy, telecommunications and transport. The financial assistance in 1993 amounts to 30 MECU promoting projects in agriculture, health sector, private sector and SME development, banking, tourism, foreign investment promotion, infrastructure and higher education reform.

In 1991, 1992 and 1993 Albania received 300 MECU in humanitarian, emergency and food aid (85 MECU coming from the PHARE programme). It included food and medical aid, and programmes to promote Albanian industry and exports.

Albania has been a recipient of Community aid for its *balance of payments* difficulties. In 1992 it received grant aid of 70 MECU (35 MECU came from the 1992 PHARE budget).

Albania is eligible for assistance from the EBRD as well. Until 30 September 5.199 MECU was committed for 37 projects in technical cooperation with Albania.

The Commission has proposed to the Council to take a decision in favour of an EC budget guarantee to the EIB, intended to cover possible losses occurring after granting loans to Albania.

In September 1992, taking into account the grave economic situation in Albania, the EC decided to include the country in the list of countries eligible for participation in the *European*

*Community International Investment Partners (EC-IIP)* programme[6].

A meeting between senior officials of the G-24, international organisations and the Albanian Prime Minister as well as ministers and senior officials took place in Brussels on 16-17 November 1993. The meeting discussed the following four main topics: a, overview of the general political and economic situation (general macro-financial assistance was provided in the form of balance of payments aid by international financial institutions and the G-24 to cover a substantial part of Albania's external financing gap of US $ 165 million for 1992-93); b, macro-economic reform and balance of payments assistance; c, the 1994-96 Public Investment Programme and future G-24 assistance; d, sector-specific issues.

Trade

Despite the liberalisation of the trade regime between Albania and the EC, imports from Albania to the Community are falling. At the same time EC exports to Albania have risen considerably.The figures for 1992 are following the tendencies: EC imports from Albania have fallen further by 11% (in comparison with the same period of 1991) to only 58 MECU, and EC exports to Albania have grown by 83% reaching 305 MECU. The trade surplus of 247 MECU is in favour of the Community.

The Community imports from Albania in 1992 were mainly agricultural products: 24%; mineral products: 18%; footwear: 16%; textiles: 15%; base metals: 14%.

At the same time the EC exported to Albania agricultural products: 61%; machinery and electrical equipment: 8%; transport equipment: 6%; textiles: 6%; chemical products: 5%.

Political dialogue

Together with the Trade and Cooperation agreement, a joint declaration on political dialogue was signed. The purpose of this declaration is to reinforce and intensify political, economic and cultural relations. A Joint Committee meeting with Albania is foreseen in February 1994.

[6] EC-IIP's objective is to promote investment by private economic operators from the European Union in the form of joint ventures with local economic operators in eligible developing countries to the mutual benefit of both parties (Slovenia, Croatia and Bosnia are also eligible, but no other European countries).

## 8-9-10. ESTONIA, LATVIA, LITHUANIA
(The Baltic States)

Agreements

*Trade and Economic Cooperation Agreements* between the Community and the three Baltic republics were signed on 11 May 1992. The European Parliament approved them on 18 December 1992. The agreements with Latvia and Lithuania entered into force on 1 February 1993, while the one with Estonia - one month later - 1 March 1993 (following the decision of the European Parliament to delay its entry into force in order to give a signal to the Estonian government to improve its human rights' record towards the Russian minority). The Trade and Cooperation agreements establish MFN status for the three countries and confirm the removal of specific quantitative restrictions on imports into the EC. The Agreement with Lithuania (the only state with nuclear facilities) also covers relations with Euratom.The meeting of the European Council in Copenhagen on 21-22 June confirmed the future aim of concluding Europe Agreements with the Baltic States.

The first Joint Committees in the framework of the agreements were held in the respective Baltic capitals on 28-30 April 1993.

On the 5 May 1993 a *Fisheries Agreement* between the EC and Latvia was signed. The agreement covers an initial 10-year period and foresees: i) the exchange of quotas and reciprocal access to fishing zones in the Baltic Sea; ii) access to markets of fisheries products; iii) promotion of joint ventures; iv) financial contributions for training actions in Latvia. The agreement will come into force only after the conclusion of the implementing protocol. The signing of similar agreements with Lithuania and Estonia is expected soon.

The *GSP* (Generalised System of Preferences) was extended by the Community as of 1 January 1992 on the same terms as had been given to Poland, the Czech and Slovak Republics and Hungary.

The Head of the Commission Delegation in Stockholm, Mr. Hans Jorn Hansen, is also accredited to each of the three Baltic States.

Assistance

In 1991 the three Baltic States received 15 MECU from the programme of assistance to the former USSR[7]. This was aid for projects in the areas of agriculture, energy and transport.Since January 1992 the three countries have become beneficiaries of *PHARE* assistance. The amounts allocated to each country are as follows:

-Estonia: 10 MECU for general technical assistance and for TEMPUS;[8]

-Latvia: 15 MECU for general technical assistance and for TEMPUS;

-Lithuania: 20 MECU for TEMPUS, general technical assistance and a programme in support of privatisation of SMEs.

According to the 1993 PHARE indicative programmes signed with Estonia, Latvia and Lithuania, the Community has allocated 12 MECU for Estonia, 18 MECU for Latvia and 25 MECU for Lithuania for projects in four core areas: a.sectoral restructuring; b. infrastructure development; c. human resources development; d. regional programmes. In addition the three Baltic countries benefit from PHARE projects designed for several Central and Eastern European countries.

The Baltic States have so far received 90 MECU in *humanitarian, food and emergency aid* from the EC.

The EC granted 220 MECU of *balance of payments support* to the Baltics (Lithuania: 100, Latvia 80, Estonia 40 MECU). In 1992 the EC approved three loans in support of macro-economic policies in the Baltic States: Estonia: 40 MECU; Latvia: 80 MECU; Lithuania: 100 MECU.

In September 1991 the *G-24* assistance was extended to the Baltic states. The total amount of the assistance provided to the three republics until the end of 1992 was 904.7 MECU (regional assistance excluded). The breakdown of the assistance was: Estonia 255.4, Latvia: 327.4, Lithuania: 321.9 MECU.

Until 30 September 1993 the *EBRD* committed the following amounts for technical cooperation projects: Estonia: 2.577 MECU for 13 projects; Latvia: 3.898 MECU for 14 projects; Lithuania: 3.346 MECU for 14 projects.

<u>Trade</u>

Since the Baltic States only recently regained their independence, statistics on trade with these countries are available only for 1992. Community imports from the three countries together in 1992 were 1.002 billion ECU. The EC exported to the Baltic States goods for 521 MECU.

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[7] Later to become the TACIS programme (Technical Assistance to the Commonwealth of Independent States) under which the Baltic States ceased to be eligible once they became independent.

[8] European Mobility Scheme - a programme launched and financed by the European Community providing scholarship for students in Central and Eastern Europe enabling them to study in the countries of the European Community.

The Community imported mainly mineral products: 60%; base metals: 20%; chemical products: 6%, and exported agricultural products: 46%; machinery and electrical equipment: 18%; transport equipment: 11%.

The European Council in Copenhagen on 21-22 June 1993 invited the Commission to submit proposals for developing the existing trade agreements with the Baltic states into a free trade agreement.

Political dialogue

The joint declaration, adopted on the same day when the Trade and Cooperation Agreements were signed, provides for political dialogue between the three Baltic States and the European Union on matters of particular or mutual interest.

## 11. FORMER YUGOSLAVIA

EC relations with the former Yugoslavia and its successor states

Official EC relations with the former Yugoslavia began with the signature of a non-preferential agreement in 1970, followed by an updated agreement in 1973, later completed by an additional clause covering progressive cooperation in the development field. Following this strengthening of ties, a *Trade and Cooperation Agreement* was concluded in 1980 for an indefinite period. This agreement, which granted preferential treatment for trade, included detailed clauses on economic, technical, financial and social cooperation. Given the political and security crisis, the EC decided in November 1991 to suspend the agreement.

However, preferential treatment granted to former Yugoslavia was maintained by an autonomous decision of the EC to the benefit of the four Republics: Bosnia-Herzegovina, Croatia, Former Yugoslav Republic of Macedonia and Slovenia.

A Commission Delegation was opened in Belgrade at the end of 1980. The Head of the Delegation was recalled in 1992 in the context of the sanctions decided against Serbia and Montenegro.

A separate agreement has now been signed with *Slovenia*, and a Commission Delegation established in Ljubljana (see below).

Assistance

EC loans were made available under a protocol to the 1980 cooperation agreement, and Yugoslavia became eligible for PHARE assistance in the autumn of 1991, receiving grants totalling 35 MECU that year to support the restructuring of enterprises and the financial sector. In 1991 political developments made it impossible to continue cooperation under the PHARE programme, and no grants have therefore been made since (except to Slovenia which was reintegrated in August 1992).

Since the beginning of the conflict in the former Yugoslavia in 1991 EC has granted *humanitarian aid* of 507 MECU. (1991: 13 MECU, 1992: 277 MECU, 1993: 220 MECU up to 25 October 1993). That represents 41%, and together with the assistance of the member-states 65% of the total international humanitarian aid for the victims of the conflict.

Trade

EC trade with Slovenia, Croatia, Bosnia-Herzegovina and Macedonia continues under very difficult circumstances caused by the war in Bosnia-Herzegovina and the implementation of the sanctions towards Serbia and Montenegro. The canceled EC-former Yugoslavia Trade and Cooperation Agreement of 1980 for the present is replaced with a similar agreement only with Slovenia.

## 11 A. SLOVENIA

Agreements

Slovenia was recognized on 15 January 1992. Negotiations on an agreement, similar to the EC-Yugoslavia cooperation agreement of 1980 started in 1992 and on the 5 April 1993, the EC-Slovenia *Trade and Economic Cooperation Agreement*, as well as a financial cooperation protocol and an agreement in the field of transport, were signed. These new agreements have relaunched and extended the cooperation between the EC and Slovenia. The Trade and Economic Cooperation Agreement explicitly indicates the possibility of concluding a Europe Agreement similar to those already signed by the EC with other countries of Central and Eastern Europe. The financial protocol covers the cooperation in the transport field through EIB loans of up to 150 MECU by the end of 1997. In addition to this, 20 MECU of loans were granted to Slovenia by the EC. A joint Memorandum on the first programme of the bilateral cooperation was signed in Ljubljana on 7 June 1993. An agreement concerning the trade of textiles was initialled on 23 July 1993. Exploratory talks with a view to negotiating a Europe Agreement began in December 1993.

Assistance

Slovenia was integrated into the EC's PHARE programme in August 1992, and since then an amount of 5.1 MECU has been contracted from the total grant of 6.7 MECU (the indicative programme comprised assistance to the following areas: privatization, enterprise restructuring and SME development; development of the financial sector; science and technology; public infrastructure-tourism and telecommunications). The remaining 1.6 MECU is expected to be contracted by March 94. In 1993 7.5 MECU has been granted to Slovenia by PHARE.

In February 1993, the *EBRD* released its strategy for Slovenia focusing on five sectors:enterprise restructuring and privatization; small and medium-sized enterprises (SMEs); financial reform; transport and communications; and energy efficiency.

Until 30 September 1993 3.284 MECU was committed by the EBRD for 23 technical assistance projects in Slovenia.

In April 1993 a Commission delegation was opened in Ljubljana, headed by Mr. Marc Janssens.

Political dialogue

On the occasion of signing the Trade and Cooperation Agreement, on 5 April, the Twelve and Slovenia adopted a Joint Declaration on Political Dialogue. Its aim is to accompany and consolidate their rapprochement, support the political and economic changes in Slovenia and contribute to the establishment of lasting links of solidarity and new forms of cooperation. Slovenia has been involved in the preparatory work on the Security Pact.

## 11 B. C R O A T I A

Croatia was recognized as an independent republic on January 15, 1992. After a meeting between European Commission President Delors and Croatian President Tudjman on 6 May 1992 the Commission planned to send an exploratory mission to Zagreb, but postponed it because of the Croatian military involvement in Bosnia. The process of negotiating a Trade and

Cooperation Agreement and of extending the PHARE Assistance, which started in June 1992, has been stopped by the EC because of the military developments. Croatia received 21% of the total EC humanitarian aid provided to the former Yugoslavia. Until 30 September 0.541 MECU was committed by the EBRD for 6 technical assistance projects.

## 11 C. BOSNIA - HERZEGOVINA

Bosnia-Herzegovina was recognized on 7 April 1992. President Delors wrote to Bosnian President Izetbegovic about the Commission's willingness to strengthen relations, and invited a government representative to discuss the establishment of contractual relations.The war has made it impossible to proceed.

On 15 March 1993, the EC established diplomatic relations with Bosnia-Herzegovina. Bosnia-Herzegovina received 50% of the total EC humanitarian aid provided to the former Yugoslavia.

## 11 D. Former Yugoslav Republic of M A C E D O N I A

The EC has accepted the principle of recognizing the Republic, but first wants the problem, raised by Greece, concerning the name of the Republic to be solved. After the Republic was admitted to the UN, on 8 April 1993, negotiations began with Greece over the mutual problematic issues under the auspices of the co-chairmen of the International Conference on the Former Yugoslavia[9].

In October 1992, the EC General Affairs Council in Luxembourg decided on 10 MECU emergency aid for Macedonia. The European Council in Birmingham in December 1992, recognizing the deteriorating economic situation in Macedonia, stressed the need for appropriate measures to prevent this republic from bearing the unintended consequences of UN sanctions against Serbia and Montenegro. The Edinburgh Council decided to provide

[9] To date 11 Member States have recognised the Republic.

Macedonia with substantial economic aid: 100 MECU, of which 50 MECU would be found by the Commission and 50 MECU by the member-states. The Community budget has contributed so far for 60 MECU to the former Republic of Macedonia (25 out of ECHO budget, 35 out of PHARE budget). Both concentrate on the supply of essential goods. Until 30 September 1993 651 MECU was committed by the EBRD for 7 technical assistance projects with Macedonia.

Observance of the embargo on Serbia, which was Macedonia's chief trading partner within the SFRY, accounting for 50% of the trade, has meant the loss of a great many of its outlets and sources of supply, as well as major cost increments affecting transport (160 MECU). Estimated losses due to the embargo are 1.1 billion ECU. The additional sanctions threaten a total shut down of borders and will cause additional losses of approximately 1.4 billion ECU.

In April 1993 Macedonia became a member of the *EBRD*.

## 11 E-F. SERBIA and MONTENEGRO
## (Federal Republic of Yugoslavia)

Serbia and Montenegro adopted a constitution for a new Federal Republic of Yugoslavia (FRY) on 27 April 1992. The Community and its Member States declared that FRY cannot be accepted as sole successor of SFRY and that the succession issue must be addressed by all former Republics. The Community has subsequently opposed participation by FRY in international organisations, including the United Nations.

## TRADE AND COOPERATION AGREEMENTS

The acceptance in 1988 by the USSR and the Central and East European countries that they all could deal bilaterally with the EC opened the way for the Community to negotiate general agreements with these countries. Before then, only sectoral trade arrangements existed with some of them. An exception was Romania, which concluded a trade agreement with the EEC in 1980. Mutual recognition between the European Community and the Council for Mutual Economic Assistance - CMEA (COMECON) was formalised in June 1988 with the signing of the EC-CMEA Joint Declaration.

Within the two years following this Joint Declaration, the EC concluded bilateral agreements for trade, commercial and economic cooperation with Hungary, Poland, the Czech and Slovak Republic, the USSR, Bulgaria and Romania. Similar agreements were concluded with Albania and the three Baltic countries in 1992 and Slovenia in 1993.

*Trade and commercial and economic cooperation agreements* aim at a substantial and harmonious development and diversification of trade and at the promotion of commercial and economic cooperation in areas of mutual interest. They are based on principles of equality, non-discrimination and reciprocity. They are specific for each country and include:
- *trade provisions* aiming at promoting mutual trade, including most-favoured nation treatment, mutual trade concessions, the lifting of the Community's specific quantitative restrictions on imports from the partner countries and provisions for possible further trade liberalisation;
- *commercial cooperation* provisions concerning exchanges of commercial and economic information, contacts between business and professional associations, cooperation between customs departments and the promotion of investment;
- *economic cooperation* in areas of industry, mining, agriculture, energy, research, environment, financial services, training, standards, statistics, and other matters of common interest;
- the establishment of a *joint committee* as a forum for regular consultation.

These agreements thus allow for normal development of commercial and economic relations between the European Union and the Central and Eastern European countries.

EUROPE AGREEMENTS

The Europe Agreements are mixed agreements which have an *indefinite period* of validity and cover Community and national spheres of competence. They mark the beginning of an entirely new era in bilateral relations between the Community and 6 countries of Central and Eastern Europe (Poland, the Czech Republic, Slovakia, Hungary, Bulgaria, Romania) and are based on shared values and understanding of society. They are signed on the condition of continued political and economic reform in the Central and Eastern European countries. For the first time EC agreements contain, in addition to the aspects concerning commercial and economic cooperation, a *political dialogue* dimension and a *cultural cooperation* component. *Europe Agreements* provide for the gradual establishment of *free trade areas* over a period of 10 years. They are geared to the possibility of these countries' *future membership of the Union*. In the preamble to the agreements, the parties recognize that the ultimate objective of the associated countries is to become members of the Union, and association should help them attain this objective.

The agreements have an identical structure and the main aspects are listed below.

*Political dialogue*. It introduces and institutionalizes regular meetings at the highest political level on all topics of common interest and is aimed at achieving convergence in the parties' positions on foreign policy matters.

*General principles*. The transitional period is ten years broken down into two stages of five years each. The breakdown into two stages does not apply, however, to the trade component of the agreement (free movement of goods). Reference is also made to the process of establishing a market economy in the associated countries.

*Free movement of goods*. The agreements are preferential and aimed at establishing free trade arrangements between the Union and the associated countries. The concessions granted for liberalizing trade in industrial products are reciprocal but weighted in favour of the countries from Central Europe, which generally have a longer period than the Union for liberalizing their markets.

Certain *textile and ECSC products* form the subject of special protocols. Textile products will be liberalized by the Union in accordance with a special timetable which is nevertheless in line with the general dismantling of industrial tariffs. Reciprocal concessions are made for agriculture and fisheries. The rules on origin and customs cooperation are also dealt with in a separate protocol. There are special safeguard clauses for the associated countries (balance of payments and infant industries).

*Movement of workers, establishment and services*. With regard to workers, the Agreements are aimed primarily at improving the situation of workers legally established in the Union. With regard to the right of establishment, the agreements provide for full application of national treatment for the establishment and operations of all firms and all professions throughout the Union and the Czech Republic, Slovakia, Hungary and Poland. National treatment will be granted by the Union as soon as the agreements enter into force and there will be transitional periods for the application of this principle by the three counties. National treatment will also apply fully to public procurement.

*Payments and capital transfers, competition, approximation of legislation*. Freedom of financial transfers arising from commercial transactions, the provision of services, investment operations, repatriation of capital invested and the gains from this capital, and also from the movement of persons, are guaranteed.

*Rules on competition* based on the Union's rules are to be applied. The associated countries will endeavour to adapt their legislation to Union legislation.

*Progressive approximation of legislation* is one of the prerequisites for the successful economic integration of the associated countries into the Union.

*Economic cooperation* covers all the sectors in which the Union and the associated countries have a mutual interest (industrial cooperation, investment promotion and protection, standards, scientific and technological cooperation, training and education, cooperation on social affairs, regional development, small and medium-sized enterprises, statistical cooperation, money laundering, drugs, environment, transport, information and media, telecommunications, etc.). One of the objectives of economic cooperation is to enable the three associated countries to meet the challenge of restructuring their economies and making them competitive by the end of the transitional period.

*Cultural cooperation* includes notably the possibility of extending community or Member states' cultural cooperation programmes to the associated countries and may cover areas such as: translation of literary works, conservation and restoration of monuments, training of persons working in the field of culture and cultural events with a European character.

*Financial cooperation*. The associated countries will be able to receive grants under the PHARE programme and loans from the European Investment Bank. In certain circumstances, the Union may be able to examine the possibility of granting macroeconomic financial assistance.

The *final provisions* provide for an association council, which will meet at ministerial level at least once a year. It will ensure that the agreement is implemented and may in certain spheres take decisions binding the parties. An association parliamentary committee, which has an advisory role, has also been set up.

Since the *Europe Agreements* cover both trade and economic cooperation - which are matters of EC responsibility, and political and cultural cooperation - areas where the EU's Member States are responsible, they are known as "mixed agreements" and as such require, after signature, not just the assent of the European Parliament and that of the partner country, but also (under article 238 of the EEC Treaty) ratification by all twelve EU Member States. *Interim agreements* relating only to those parts of the agreements which come solely under the Union's competence and can enter into force following a shorter procedure have come (or will shortly come) into effect until the ratification of the Europe Agreements is completed.

The Europe Agreements with the Czech Republic and Slovakia which were renegotiated following the split of the country as well as the Europe Agreements signed with Bulgaria and Romania contain an identical *human rights* clause according to the Council Declaration of May 1992.

*The European Council in Copenhagen on 21-22 June* agreed that the associated countries of Central and Eastern Europe can become members of the European Union if they fulfil the necessary requirements. In this context an extended multilateral dialogue shall be reinforced on matters of common interest, the Union will accelerate its efforts to open up its markets, it will offer the possibility to the associated countries to participate in Union programmes and underlined the importance of approximation of laws.

State of Negotiation and Ratification of Europe Agreements

(situation January 1994)

| associated state | date of signature of the Europe Agreement | EP assent to Europe Agreements (art. 238) | Ratified by Parliament of assoc. state | Ratified by EC Member States | Interim Agreement in force |
|---|---|---|---|---|---|
| Poland | 16.12.1991 | 15.09.1992 | 08.07.1992 | Member States have ratified it; entry into force on 01.02.1994. | 01.03.1992 |
| Czech Republic | 04.10.1993 | 27 .10.1993 | not yet | not yet | 01.03.1992 |
| Slovakia | 04.10.1993 | 27.10.1993 | not yet | not yet | 01.03.1992 |
| Hungary | 16.12.1991 | 16.09.1992 | November 1992 | Member States have ratified it; entry into force on 01.02.1994. | 01.03.1992 |
| Romania | 01.02.1993 | 27.10.1993 | not yet | not yet | 01.05.1993 |
| Bulgaria | 08.03.1993 | 27.10 1993 | April 1993 | not yet | 31.12.1993 |

The "Visegrad Countries"

On 15 February 1991 a Hungarian-Polish-Czechoslovak summit attended by the three countries' Head of State and Governments was held in Visegrad (a small town at the Danube bend in Northern Hungary). Hungarian Prime Minister Jozsef Antal, Polish President Lech Walesa and Czechoslovak President Vaclav Havel signed a comprehensive cooperation statement in which they set down the basic principles of cooperation of the three countries. The main goal of this cooperation was that the "Visegrad Three" coordinate their efforts at European Integration. After the dissolution of CSFR and the creation of the Czech and Slovak Republics the group consists of four countries. This group, composed of the most economically advanced Central European countries, constitutes the most consolidated cooperation system in the region. The Visegrad countries are establishing a free trade zone and are concerting their action on the international political arena.

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