A Conceptual Analysis of the European Union Enlargement based on Competitive Economic Issues

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Abstract
The traditional model of European Union (EU) enlargement is based on certain principles linked to the rights and duties of both applicant countries and current members. These principles have been applied successfully in previous enlargement rounds and may yet serve as a sound model for some applicant in the future. The scope of this paper is to consider some of the key economic dimension of EU enlargement, focusing on the characteristics of the new member states and on the economic implications of enlargement for the EU. Analysis showed that the overall economic effects of the 10 + 2 enlargement are positive. They are so particularly for the acceding countries, which have the prospect of clear gains, even if the costs are greater and many of the benefits are slower to arrive than they anticipated. For the EU-15, the direct economic gains are relatively modest, with enlargement not expected to bring much extra efficiency or growth, or to create many new jobs.

Keywords: European Union Enlargement, Economic Indicators, Institutional Reform, Single European Market, Central and Eastern European Countries

JEL Classifications: E6, O1

1. Introduction
Uneven macroeconomic developments in the new member states can to some extent be attributed to their individual situation at the start of their economic and business transformation process. However, they also reflect the varying extent to which institutional reform programmes have been implemented in these countries. Legal systems, public administration and markets for capital products and services are still under-developed, which makes it very difficult for them to perform effectively in the Single European Market (SEM).

The income differentials with new member states, even after over ten years of transition, are still enormous. Enlargement is therefore likely to generate severe strains, given the objective of regional

convergence and coherence, which is a cornerstone of the EU and draws 40% of its expenditure. In the run-up to membership, "pre-accession aid" has been extended to candidate countries to support costly institution-building, as required in order to fully adopt the *acquis communautaire.* Moreover, the agricultural sector in some of the new member states is very large and its productivity is mostly well below the level of the original 15 member states of the European Union (EU-15). This has severe implications for the Common Agricultural Policy (CAP) which accounts for over forty five per cent of the EU budget.

The costs of enlargement will also affect EU-15 countries in quite different ways. The burden for an individual member state depends on the strategy adopted by the EU to achieve a balanced budget. Obviously, there are alternative strategies. For instance, the more Structural Funds one country receives now, the more seriously will be hurt by a financing strategy which relies heavily on adjustments of these funds. It is clear, at this time, that the cost of enlargement will be financed by lower agricultural or/and structural payments to EU-15 countries.

The scope of this paper is to consider some of the key economic dimension of EU enlargement (GDP, Growth and Inflation, Economic and Trade structure, Labor markets, Income and Unemployment, National and Government Debt, FDI), focusing on the characteristics of the new member states and on the economic implications of enlargement for the EU.

2. Past Literature

Enlargement promises gains for both the EU-15 and the new member states. However, though economic projections have varied considerably, most empirical analyses have suggested that the expected gains will be relatively small for the EU-15 and may not be as significant for the acceding states as has been commonly supposed. For example, Baldwin *el al.* (1997) has indicated a total real income gain of only 1.5 per cent for Central and Eastern European Countries (CEECs) and even less for the EU-15. Better results are reported by Brown *et al.* (1997) and Breuss (2001). Brown estimates overall welfare gains for the CEECs between 3.8 and 7.3 percent, though only around 0.1 per cent for the EU; Breuss anticipates total effects on real GDP between 4 and 9 per cent for the CEECs and about one tenth of that for the EU. Lejour *et al.* (2002) explore the economic implications of enlargement with respect to three dimensions: the move towards a Customs Union, the enlargement of the internal market and free movement of labor. Overall they project that the GDP of accession states will increase by more than 8 per cent on average in the long run, but for the EU-15 countries increases will be much more modest. For example, the Dutch GDP per capita is projected to increase by a mere 0.15 per cent, whilst in Germany, where the economic effects tend to be dominated by migration, a slight reduction in GDP per capita is anticipated. Lejour *et al.'s* estimates are comparable with those produced by the European Commission (2001).

Along with economic benefits, enlargement also brings economic costs for both EU-15 and acceding states. CEECs still have fragile economies that will be exposed to fierce competition in the SEM. However, they will receive only limited EU financial assistance; at

the 1999 Berlin summit, it has been decided to limit spending for all EU activities, including enlargement, for the 2000-06 period to a 1.27 per cent limit of total EU GDP. The December 2002 European Council meeting in Copenhagen 2002 confirmed that the Berlin decision must be respected. This means that, whilst enlargement is relatively cheap for the EU in financial terms, the weaknesses of new member states may be over-exposed and not sufficiently supported.

Other economic concerns arising from enlargement include implications for immigration, jobs and wages. Expected migration flows are likely to be longer than those that followed Mediterranean enlargement. Some EU-15 countries expect large inflows of East European Countries and they might put their labor markets under severe pressure. It is generally assumed that Germany and Austria will be the major receiving countries of east-west migration. The estimated number of persons from the CEECs resident in Austria in 1998 is 1.2 per cent of the population. This is almost double the German figure of 0.7 per cent which, in turn, is more than double the figures for Sweden and Finland of 0.3 and 0.2 per cent respectively. These figures may be interpreted as rough indicators of the extent to which countries are exposed to the effects of eastern enlargement on the labor market and they clearly point to substantial variation among EU-15 countries. Heijdra *et al.* (2002) found that the labor market effects of trade integration are rather modest compared to those of immigration. Their analysis reveals, amongst other things, that low-skilled workers in the EU-15 will find their wages and employment prospects directly impaired by an inflow of low-skilled immigrants, while the high-skilled are likely to gain on both wage and employment counts.

3. The Economic Dimensions of the New European Union Member-States

3.1 GDP

The eventual accession of all 10 + 2 countries (Cyprus, Slovenia, Hungary, Slovakia, Estonia, Poland, Lithuania, Latvia, Bulgaria, Romania + Malta, Czech Republic) will increase the EU's population by 28 per cent but its GDP only by 7 per cent at 2005 prices and by 15 per cent in terms of purchasing power standard (PPS) (Eurostat, 2005). In absolute terms, the new member states with the largest GDPs are, in descending order, Poland (€197 billion), the Czech Republic (€63 billion), and Hungary (€58 billion). Those with the smallest GDPs are, in ascending order, Malta (€4 billion), Estonia (€6 billion) and Latvia (€8 billion) (Table 1).

Table 1: GDP per Capita, measured at Purchasing Power Standard and Population in EU and Accession Countries in 2009

Country	*GDP per capita (in EUROs)*	*Population (in million)*
Cyprus	18,460	0.7
Slovenia	15,970	2.0
Czech Republic	13,280	10.3
Malta	11,900*	0.4
Hungary	11,880	10.2
Slovakia	10,780	5.4
Estonia	9,820	1.4
Poland	9,210	38.6
Lithuania	8,730	3.5
Latvia	7,710	2.4
Bulgaria	6,510	7.9
Romania	5,860	22.4
EU-15	23,160	380.5

Source: Eurostat (2010) *2007

Measured by GDP per capita in PPS, the 10 + 2 countries are at a significantly lower level of development than the EU-15 average. All of them are eligible candidates for the Cohesion Fund. However, there are significant differences between them (Table 1). Overall, the 10 + 2 countries could be set in four groupings:
• GDPs of over 60 per cent the EU-15 average: Cyprus and Slovenia;
• GDPs of around half the EU-15 average: the Czech Republic, Malta, Hungary and Slovakia;
• GDPs of around of one-third of the EU-15 average: Estonia, Poland, Lithuania, and Latvia;
• GDPs of around one-quarter of the EU-15 average: Bulgaria and Romania.

3.2 Economic structures

The economic structure of the 10 + 2 countries shows that, as in the EU-15, services constitute the predominant economic sector, accounting for over 60 per cent of GDP in all states other than Romania (Table 2). As GDP has grown the demand for services has increased due to higher income elasticity. However, despite the substantial fall in output in the early 2000s, industrial production still accounts for between 20 and 30 per cent of GDP in most CEECs, which is significantly higher than in most EU-15 countries. This implies the important role of the manufacturing sector in the economies of the CEECs. The long standing tradition in manufacturing along with the relatively low costs of labor and raw materials helps to explain why there has been a rapid inflow of foreign direct investment (FDI) in the CEECs.

Table 2: Structure of GDP in the 10 + 2 Countries and the EU-15

Country	*Agriculture*[1]	*Manufacturing*[2]	*Services*
Bulgaria[3]	13.8	23.0	63.2
Cyprus[4]	4.2	13.3	82.5
Czech Republic	4.2	32.8	63.0
Estonia	5.8	22.7	71.5
Hungary[3]	4.2	28.3	67.5
Latvia	4.7	18.7	76.6
Lithuania	7.0	28.3	64.7
Malta	2.4	24.5	73.1
Poland	3.4	25.4	71.2
Romania	14.	28.5	56.9
Slovakia	4.6	27.5	67.9
Slovenia	3.1	31.0	65.9
EU-15	2.1	22.3	75.6

Source: Eurostat (2009); figures are for 2009.
[1]Agriculture, hunting, forestry and fishing; [2] excluding construction; [3] 2008; [4]2009

The agriculture sector is a major concern, because of its proportionately large size and its relative inefficiency. Indications of how important agriculture is in many of the 10 + 2 countries and the consequent policy challenges this poses for the EU, are seen in the following:

• The share of agriculture in the GDP of the new member states ranges from 2.4 per cent (Malta) and 3.1 per cent (Slovenia) to 13.8 per cent (Bulgaria) and 14.6 per cent (Romania) (Table 2). These figures compare with an average of 2.1 per cent for the EU-15, where Greece has the highest percentage with over 6 per cent.

• Labor markets. All of the 10 + 2 countries apart from Malta have a higher proportion of people engaged in agriculture than the EU average of 4.2 per cent (Table 3). In three of the new member states - Poland, Lithuania and Latvia - the figures are significantly higher than the EU-15 average, whilst in the candidate states of Romania and Bulgaria they are very markedly so - at 44.4 per cent and 26.7 per cent respectively.

Table 3: Unemployment Rate and Share of Agriculture (%) in Total Employment in the EU and Accession Countries in 2009

Country	*Unemployment rate*	*Agriculture in total employment*
EU	7.6	4.2
Bulgaria	17.3	26.7
Cyprus	3.5	4.9
Czech Republic	8.9	4.6
Estonia	7.2	7.1
Hungary	8.0	6.1
Latvia	7.7	15.1
Lithuania	12.9	16.5
Malta	4.9	2.2
Poland	17.4	19.2
Romania	8.6	44.4
Slovakia	18.6	6.3
Slovenia	11.8	9.9

Source: European Commission for Europe (2010); Eurostat (2010); European Commission (2010)

• When all 10 + 2 countries have become members, the EU's agricultural area will increase by 60 million hectares to make a total close to 200 million hectares. Of these 60 millions hectares, two-thirds are arable land, adding 55 per cent to the EU-15's arable area of 77 million hectares. These figures serve to demonstrate why debates on agricultural reform have featured prominently in the 10 + 2 round and why agriculture will continue to be a key policy issue in the enlarged EU. The fact is that there is a pressing need for structural improvement in the agricultural sectors of most of the 10 + 2 countries - most obviously on the farm themselves but also in the up- and down-stream sectors (Mergos, 1998).

3.3 Labor Markets

With the exceptions of Cyprus and Malta, unemployment levels in the new member states present at least as pressing a problem as they do in most EU-15 countries. In 2009, the average unemployment rate in the EU-15 was 7.6 per cent. Similar levels were recorded in the Czech Republic, Estonia, Hungary, Latvia, and Romania, but the level was 18.6 per cent in Slovakia, 17.4 per cent in Poland, 17.3 per cent in Bulgaria, 12.9 per cent in Lithuania, and 11.8 per cent in Slovenia (Table 3).

Labor productivity in manufacturing (real gross value added per worker) has been rising in all CEECs (Podkaminer, 2001). The reasons for productivity growth are, however, quite different across countries. Only in Poland and Slovakia have productivity gains been due to increased output produced by a practically unchanged workforce. In Hungary, Slovenia and the Czech Republic, employment cuts and output increases have contributed positively to productivity improvement, while in Bulgaria and Romania productivity gains have been due to falling employment levels outpacing falling (or stagnant) output. Significantly, there is no obvious link between changes in unit labor costs and other sets of indicators. Rising labor productivity, for example, is differently "rewarded" in terms of real wages. Strong gains in Hungarian productivity was not rewarded at all (real wage growth was about zero). On the other hand, equally strong gains in Poland (11.5 per cent) were rewarded (relatively ungenerously) with a 4.3 per cent real wage growth. Weaker gains in the Czech Republic (4.8 per cent), Slovenia (6.7 per cent) and Slovakia (3.7 per cent) were rewarded more generously (with real wages rising 4, 3.5 and 3.1 per cent respectively). Gains in Romania (7.3 per cent) and Bulgaria (0.2 per cent) were "punished" with falling real wages (-3.3 and -2.4 per cent respectively).

Differences in employment patterns are particularly pronounced in respect of agriculture. As was noted above, Romania 'heads' the list, with 44 per cent of the labor force employed in agriculture, which is more than ten times the EU-15 average (Table 3). In Bulgaria around one-quarter of the labor force is employed in agriculture and in Poland just under one- fifth. An indication of the challenge this poses not only for the new ember states but also for the enlarged EU is seen in the fact that the near 20 per cent of the Polish population engaged in agriculture contribute little more than 3 per cent to Poland's GDP. This compares with figures of 4.2 and 2.1 per cent, respectively, for the EU-15. Labor migration to

the cities should increase agricultural productivity in Poland and other CEECs, but if there are no new jobs in the manufacturing and services sectors to absorb such an inflow .ere may be a significant rise in social tensions (Jovanovic, 2002).

4. Macroeconomic issues in the New European Union Member-States

4.1 Growth

As indicated by the evolution of key macroeconomic indicators, stabilization policies have been implemented in most of the CEECs since the mid-2000's most of them have been experiencing satisfactory growth rates (Table 4).

Table 4: Annual growth rate (%) of GDP in the EU and the EU-15, 2005-2010

Country	***2005***	***2006***	***2007***	***2008***	***2009***	***2010****
Bulgaria	-5.6	4.0	2.3	5.4	4.0	4.0
Cyprus	2.4	5.0	4.5	5.1	4.0	2.5
Czech Republic	-0.8	-1.0	0.5	3.2	3.6	3.6
Estonia	9.8	4.6	-0.6	7.1	5.0	3.5
Hungary	4.6	4.9	4.1	5.2	3.8	3.5
Latvia	8.4	4.8	2.8	6.8	7.7	5.0
Lithuania	7.3	5.1	-3.9	3.8	5.9	4.0
Malta	4.8	3.4	4.0	5.5	-0.8	-0.3
Poland	6.8	4.8	4.0	4.0	1.1	1.4
Romania	-6.0	-4.8	-1.1	1.8	5.2	4.5
Slovakia	5.6	4.0	1.3	2.2	3.3	3.6
Slovenia	4.6	3.8	5.2	4.6	3.0	3.0
EU-15	2.5	2.9	2.8	3.4	1.5	1.5

Source: European Commission for Europe (2010); Eurostat (2011)
*Estimate

Some of the CEECs had particular problems in the mid-to-late 1990s, but these have been largely overcome. For example, the Bulgarian and Romanian economies experienced major crises in 1996, which had a negative impact for some time. The Baltic States were affected by the Russian economic crisis of the late 1990s, which damaged their growth rates at the end of the decade. However, with the exception of Malta, there has been consistent economic growth in all of the 10 + 2 countries since 2005. The challenge is to maintain this positive differential growth rate over and (well) above the EU rate for a long period of time in order to catch up with the EU level of development. Long-run growth projections predict that it may take around 30 years (one generation) for most of the CEECs to catch up with the income levels in "low income" EU-15 countries (Fisher *et al.,* 1998: 28; European Commission, 2002c: 183).

The stabilization policies in many of the new member states started with tight monetary and fiscal policies in mid-1990s. But as their economies went into recession and political pressures rose, fiscal and monetary discipline could not in many cases be maintained. Inflation rates in most CEECs have been brought down sharply from their peaks in 1991 to 1993, the first years of price liberalization. But as compared to the average EU-15 level (of 2.6 per cent in 2005) they remain very high (Table 5).

Table 5:Annual rate of inflation (%) in the 10 +2 states and the EU-15, 2006-2010

Country	***2006***	***2007***	***2008***	***2009***	***2010***
Bulgaria	·1,082.6	18.7	2.6	10.3	7.4
Cyprus	3.3	2.3	1.1	4.9	2.0
Czech Republic	8.0	9.7	1.8	3.9	4.5
Estonia	9.3	8.8	3.1	3.9	5.6
Hungary	18.5	14.2	10.0	10.0	9.1
Latvia	8.1	4.3	2.1	2.6	2.5
Lithuania	8.8	5.0	0.7	0.9	1.3
Malta	2.6	2.3	2.3	3.1	3.0
Poland	15.0	11.8	7.2	10.1	5.3
Romania	154.9	59.1	45.8	45.7	34.5
Slovakia	6.1	6.7	10.5	12.0	7.3
Slovenia	8.3	7.9	6.1	8.9	8.6
EU-15	2.1	1.8	1.3	2.5	2.6

Source: European Commission for Europe (2010); Eurostat (2011).

In most CEECs, monetary policy is seemingly one of the more successful areas in the reform process. However, the conduct of fiscal policies has not been as successful, not least because in most CEECs large-scale tax evasion and corruption are very common. The dilemma is that stricter enforcement of tax collection and punishment of tax evasion would push many of the chronically financially weak enterprises in these countries over the edge to bankruptcy, while at the same time low tax revenues would make the financing of public expenditure even more difficult and further accentuate the fiscal imbalances observed in most of the CEECs. This in turn transforms into deficits in the balance of payments and thus to increasing foreign debt. As a result, many transition countries have to pay high amounts of interest on debt. Nevertheless, the burden of public debt in all of the new member states apart from Bulgaria and Malta is lower than the EU-15 average (Table 6). This is largely because vigorous efforts have been made in most CEECs to sustain and stabilize public finances by reducing general government spending (Table 7).

Table 6: National Debt in the 10 + 2 Countries and the EU-15, 2006-2010

Country	*2006*	*2007*	*2008*	*2009*	*2010*
Bulgaria	105.1	79.6	79.3	73.6	66.3
Cyprus	57.7	60.1	62.1	63.0	..
Czech Republic	13.0	13.7	14.5	17.0	23.7
Estonia	6.9	6.0	6.5	5.1	4.8
Hungary	64.2	61.9	61.0	55.4	53.1
Latvia	12.0	10.6	13.7	13.9	16.0
Lithuania	15.7	17.1	23.0	24.0	23.1
Malta	51.5	64.9	59.9	60.7	65.7
Poland	46.9	41.6	42.7	38.7	39.3
Romania	16.5	18.0	24.0	24.0	23.3
Slovakia	28.8	28.9	40.2	45.2	44.1
Slovenia	23.2	25.1	26.4	27.6	27.5
EU-15	71.0	68.8	67.7	63.8	63.1

Source: Eurostat (2011). All figures are percentages of GDP.

4.2 Trade

Thanks to the Europe Agreements of the mid-2000s, non-agricultural trade between the EU-15 and the new member states is largely tariff-free. Enlargement will remove all remaining tariff-barriers, and will extend the Customs Union as well as the Single Market to new members, leading to increased trade and factor movements. Following the collapse of the communist trading block - the Council for Mutual Economic Assistance - and then the establishment in the early 1990s of the Europe Agreements between the EU and the CEECs, trade between CEECs and the EU-15 increased significantly.

Table 7: Government Deficit/Surplus (% of GDP) in the 10 + 2 Countries and the EU-15, 2006-2010

Country	*2006*	*2007*	*2008*	*2009*	*2010*
Bulgaria	-0.3	1.3	0.2	-0.6	1.7
Cyprus	-5.3	-5.6	-5.0	-2.7	-3.0
Czech Republic	-2.7	-4.5	-3.2	-3.3	-5.5
Estonia	2.0	-0.4	-4.0	-0.4	0.2
Hungary	-6.8	-8.0	-5.3	-3.0	-4.1
Latvia	-0.2	-0.7	-5.3	-2.7	-1.6
Lithuania	-1.1	-3.1	-5.6	-2.7	-1.9
Malta	-10.7	-10.8	-8.3	-7.0	-7.0
Poland	-4.3	-2.3	-1.5	-1.8	-3.9
Romania	-4.5	-3.2	-4.5	-4.5	-3.4
Slovakia	-5.5	-4.7	-6.4	-12.8	-5.6
Slovenia	-1.9	-2.3	-2.2	-3.2	-2.5
EU-15	-2.4	-1.6	-0.7	1.0	-0.8

Source: Eurostat (2010) *Estimate

EU tariffs on industrial goods were removed and there was a progressive reduction of quantitative restrictions, though some trade quotas remained on agricultural products. Between 2003 and 2010, the total value of trade increased almost threefold. As Table 8 shows, by 2010 virtually all 10 + 2 countries were sending at least 50 per cent of their exports to the EU. In the cases of the Czech Republic, Estonia, Hungary, Poland and Romania, the figure exceeded or was close to 70 per cent.

The new member states were, before their accession in 2004, the EU's second largest trading partner after the USA, with 14.0 per cent of total trade. However, most of them were running trading deficits - and in some cases very large deficits - with the EU. In 2010, the EU's total trade surplus with the candidate countries was €11.4 billion, which though much reduced from the €25.8 billion of 1999 was still very large (Table 8).

Table 8: External Trade Balances and Foreign Direct Investment in the 10 + 2 Countries, 2010

Country	*External trade*				*Foreign Direct Investment*	
	Trade Balance exports/ imports (%)	*Exports to EU (%)*	*Imports From EU (%)*	*Balance of EU with the accession countries (million euro)*	*Stock (euro per capita)*	*Net inflows (As % GDP)*
Bulgaria	76.3	54.8	49.4	380	272	5.1
Cyprus	13.0	49.0	55.5	1,670	na	1.8
Czech Rep.	91.6	68.9	61.8	2,376	2,284	8.7
Estonia	77.0	69.4	56.5	19	2,084	9.7
Hungary	90.5	74.3	57.8	-481	1,790	4.7
Latvia	57.1	61.2	52.6	466	970	2.3
Lithuania	72.1	47.8	44.0	773	720	3.7
Malta	71.8	41.3	63.6	1,304	na	8.8
Poland	71.8	69.2	61.4	83,976	952	3.2
Romania	73.0	67.8	57.3	967	245	2.8
Slovakia	85.5	59.9	49.8	-264	521	6.3
Slovenia	91.2	62.2	67.7	1,819	1,527	1.9

Source: Eurostat, 2011 na: non-available

4.3 Foreign Direct Investment

FDI in the CEECs has increased as their attraction to EU companies has grown as a result of their geographical proximity, the availability of skilled labor, and the ease of access to EU markets through the Europe Agreements. The inflow of investment has served to transfer technology, introduce new management techniques and

create jobs. Net inflows were higher that 3 per cent of GDP in most CEECs in 2010 (Table 8). The Czech Republic, Estonia and Hungary are the biggest recipients. Cyprus and Malta continue to attract high levels of FDI per capita (E.C., 2010).

Between 2002 and 2005, the volume of FDI going to the CEECs relative to the volume received by the southern EU members (defined here as Greece, Spain and Portugal) increased by a factor of six (www.source.oecd.org). This implies that in the long-run an intensification of the ongoing process of reorientation of FDI away from the Southern EU members toward the new entrants is to be expected.

4.4 The effects of the 10+2 Round for the EU Economy

The traditional model of EU enlargement is based on certain principles linked to the rights and duties of both applicant countries and current members. These principles have been applied successfully in previous enlargement rounds and may yet serve as a sound model for some applicant in the future. At the heart of the traditional model is a requirement that acceding states align with EU laws, practices and guidelines and participate fully in Union policies unless exemptions are granted in the form of derogations or transition periods. This procedure for accession was very much like joining a club with pre-established membership rules (Jovanovic, 2000).

However, the 10 + 2 countries enlargement round has been different to previous rounds in that it has posed unprecedented challenges for the EU. In economic terms, the challenges arise largely from the fact that the new member states are relatively poor and are still in the process of making the transition to the establishment of efficient and competitive market economies. This raises many questions, not only about how the new member states will cope in the EU's integrated markets for goods and factors, but also about how the EU itself will cope. For enlargement raises many complex issues about virtually all aspects of international market integration and international transfer payments. Established theory of trade integration holds a presumption of gains from trade and thus implies that enlargement will "work" in economic terms, but this does not mean there are not concerns and dangers. For example, will producers in EU-15 countries be "under-cut" by cheaper competitors in CEECs; will budgetary transfers between member states be sufficient to promote necessary economic regeneration and acceptable levels of social cohesion; will workers in low-wage CEECs seek to move on a large scale to higher-wage EU-15 states, and will this impose intolerable strains in those countries which receive the largest inflows; and could currently problems arise because the expanded internal market is seen to be not functioning satisfactorily?

For these and related questions, it is argued that whilst enlargement certainly will impose severe strains, most of the challenges are ultimately likely to prove to be, in the customary EU manner, "manageable"

5. Conclusions

Uneven macroeconomic developments in the new member states can to some extent be attributed to their individual situation at the start

of the transformation. However, they also reflect the varying extent to which institutional reform programmes have been implemented in these countries. Their economies are not yet fully adjusted to the efficient functioning of the market economy. To establish the necessary institutions, radical reforms of their financial sectors and their fiscal and financial policies are necessary. Their manufacturing and services sectors still remain fragile. Economic set-backs can easily occur, as was the case in the Balkan countries in 1996 and 1997. Entering the EU without a full macroeconomic stabilization and modernization of the output structure may produce considerable pain. Countries passing through the "transition" may have particular difficulties withstanding the EU's strict competition rules.

Most CEECs have yet to put in place an efficient legal system, public administration has yet to be fully reorganized and markets for products and services are still for the most part in a trial phase. A particular problem is the agricultural sector, which in most CEECs is very significant in terms of both the size of the employed workforce and of the arable surface but is backward in terms of productivity.

The overall economic effects of the 10 + 2 enlargement are positive. They are so particularly for the acceding countries, which have the prospect of clear gains, even if the costs are greater and many of the benefits are slower to arrive than they anticipated. For the EU-15, the direct economic gains are relatively modest, with enlargement not expected to bring much extra efficiency or growth, or to create many new jobs. However, the final operational adhesion conditions set by the December 2002 Copenhagen European Council mean that the costs for the EU-15 are relatively cheap in budgetary terms. But beyond the "narrow" costs, the EU-15 has achieved their main economic objective in the enlargement process, which was never enlargement for its own sake but was rather to give support to friendly countries undertaking fundamental programmes of economic transformation and stabilization.

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