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THE EURO-ATLANTIC INTEGRATION, ATTITUDES AND ORIENTATIONS

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iscussion Paper

László Csaba

Hitting a Moving Target: Economic challenges for Hungary in the EU enlargement in comparative perspective[1]

1. An EU torn between Gothenburg and Dublin

One of the most challenging features of accession to the European Union has been triggered by the continuous deepening of integration, reflected in the ever-growing body of *acquis communautaire*. Following the entry into force of the Amsterdam Treaty on 1 May, 1999 this has been compounded by the fact that many such accomplishments of Community policies, that still remained contested among several incumbent member states, have become *non-negotiable parts for the acceding countries*. In short, candidate countries are expected to *deliver more*, not only more than southern European members, but also more *than several of the current incumbents*.

For instance Britain has obtained a negotiated formal opt-out from the "sharp edges of Europe" (Grabbe, 2000) that constitute a serious problem for many of the applicant countries, short of a big bang enlargement (that seems practically unlikely as unaffordable from the point of view of approved EU financial guidelines). Likewise the Danish referendum of September 2000 has "secured" that the Danish opt-out from the single currency is going to be a lasting phenomenon, definitely longer lasting than policy-makers have ever conceived. And last but not at all least, the Irish referendum of June 2001 has indicated the severity of the democratic deficit within the EU, when concerns about the compatibility of traditional and deep-rooted neutrality of the green island with the Common Foreign and Security Policy (CFSP) of the EU as formalised by the Nice Treaty have lead to the rejection of the latter.

It is hard to overlook that candidate countries are not in a comparable position, whatever no matter what the merits or demerits of CFSP, the third pillar co-operation or the single currency. These are all non-negotiable under the Amsterdam Treaty, not least owing to the incorporation of the Schengen acquis into the first pillar by the Treaty. Thus candidates are confronted with a *take it or leave it* approach, even if such fundamentals of the EU are concerned as one of the *four freedoms* (where the Göteborg Summit has institutionalised a de-facto derogation of the EU side) or equal treat-

1 This article is based on the presentation given to the international conference organised by the XXI Century Institute, the Political Science Department of BUESPA and the Swedish Embassy entitled "EU Enlargement and the Swedish Presidency", Budapest, 26-27, June, 2001. Revised and updated as of February 2002.

... period until 2006 does not earmark a penny of direct income support for farmers of those countries that may actually accede as planned, i.e. between 2002 and 2006 (which, in formal terms, is also a derogation on the EU side[2]).

Whereas political statements made after the Gothenburg Summit attempted to reassure applicants of the insignificance of the Irish derailment, and even Commission President Romano Prodi made public statements towards this end, he was soon forced to revoke these in public, joining those urging the Irish to rethink the issue and change their minds in a new referendum. This is likely to take place in November 2002. Now whatever we may think of the democratic qualities of such pressurising (especially *vis-a-vis* a small member-state) the legal fact remains that *no single EU ruling can enter in force without prior ratification* by *all* the 15 incumbent member-states. Therefore applicant countries can by no means be certain *whether* and *when* the stipulations of the Nice Treaty and the related modalities of accession *will be in force*.

True, progress in the latter proved feasible (see below), however the Treaty of Nice addresses issues of constitutional character. Whatever we think of the bits and pieces of this compromise (cf. in detail in Csaba, 2001) the fact of the matter remains that it does re-tailor several procedures, institutions and modalities that are of immediate significance for various aspects of decision-making, especially those related to the practicalities of enlargement, and to the ways a Community of 20 or 27 may function. In concrete legal terms, enlargement is though *possible* also without Nice Treaty until 20 members. However the current *policy debate* (ever since the Helsinki Council of December 1999) focuses precisely on the *number* of candidate to be taken upon board, and *ways* and means of accommodating their diverse claims and concerns.

Thus until the repercussions of the Irish vote are not addressed, it is anything but clear *how many* applicants can in theory be accepted, further that *under what terms* this is likely to happen. Likewise the outcome of the referendum reflects also *a deeper problem* of selling EU enlargement to a growingly sceptical and inward-looking electorate (The need..., 2000). This problem is only exacerbated if - like in the case of the Nice Treaty - there is no exhilarating subject or substance to be sold under a good PR campaign.

Therefore despite the enormous and partly successful efforts of the Swedish Presidency to promote enlargement much more than the preceding French and the following Belgian counterparts[3], *progress* towards *actual* enlargement can be assessed as *partial* at best. As the editorial of the

2 This is reflected in the Commission paper of January, 2002 calling it a 'fair and equitable deal' (in its internet edition). More on this in (Csaba, 2002).
3 Both are traditionally more preoccupied with the internal structure of the EU, though fighting on opposite sides of the conceptual front over the long term EU vision.

... underscored (Enlarging..., 2001) "Ireland may be the only country to subject the Nice Treaty to formal public approval in a referendum. Nonetheless, EU budgetary and policy reforms and the admission of new members will require ratification by all national parliaments". In other words, reforms that pave the way for the affordability of eastward enlargement *are yet to come*.

The growing pre-occupation with domestic concerns, already visible in the context of the election campaigns in Germany and France make improbable, that the atmospheric improvement, so welcomed by some (cf. the editorial in: *Handelsblatt*, 3 July, 2001) can overshadow, let alone overwhelm those *structural hindrances* to meaningful and thorough EU reforms, that are needed for enlargement as well. Traditional British preoccupation with an European super state (managing barely over 1 percent of EU resources), or Spanish insistence on their "right" to get a fair *share* of *other* taxpayers' money, or traditionally inflated Austrian fears of mass migration may be cases in point.

If the EU has always been primarily an élite project, the Irish and Danish referenda have clearly uncovered the *objective limits to this approach* in a modern mass democracy. Therefore élite support for enlargement is clearly a necessary but hardly a sufficient condition for this to happen. Therefore the deadline of 2004 for first accession, implied in Nice and formally promulgated in Göteborg is though a welcome development in terms of political symbolism. It may help orient decision-makers and bureaucracies alike. However it would be misleading to treat these and other unbinding promises at face value.

All in all, following the Swedish presidency the political lure of the big bang approach, favouring the accession of all candidates except Bulgaria, Romania and Turkey, has been increased. The debate in the Bundestag following immediately Göteborg and calling for the *unconditional* inclusion of Poland among the first round candidates (as reported in *Handelsblatt* 23/24 June, 2001) and the optimistic statements on adhering to the roadmap, all reflect a *one-dimensional* purely diplomatic *approach*, looking through these glasses economic matters and domestic policy concerns are minor side conditions to be adjusted to the grand project. *In reality, things work the other way around* - and this is what the Irish and Danish referenda, as well as the substance of Nice on its lacking major efficiency improving reforms is all about.

As long as the successful conclusion of the reform conference on the common agricultural policy, to be concerned 2003 is not secured, furthermore the reform of structural funds, also to be addressed in 2003 is overshadowed by the Spanish blackmailing of Germans in open policy debates, *funding of larger scale enlargement is not secured*. Not only for the period of 2004-2006, but even less for the new financial guidelines to be effective for 2007-2013 but to be approved at the time of first potential enlargements, i.e. 2005-2006. The sheer coincidence is unlikely to enhance the chances of major breakthroughs. Thus the competition in and for EU membership following, notwithstanding our fundamental concerns voiced above, we set out from the premise of "ready or not, here they come" (Best, 2001) and see only the other side of the coin, i.e. *how Hungary has progressed* on the road to EU accession from the economic point of view. By the Gothenburg Council Hungary managed to conclude 22 chapters of negotiations, including such vital ones as on labour, free movement of capital, services, financial sector, customs union and tax policy. This accomplishment, though may be contested on grounds of domestic party politics (Inotai, 2001), has put undoubtedly Hungary, together with Cyprus, *in the forefront*. Not only and not primarily for the large number of chapters concluded, but because of the fundamental importance and complexity of those areas that have been agreed in a mutually acceptable fashion. It seems that *no other remaining chapter*, not even the one on environment *is likely to be more demanding* in terms of compromise and in terms of financial and organisational effort. Thus it may be legitimate for us to adopt a forward-looking stance.

Setting out from the premise that if any enlargement will materialise under the current financial guideline (until 2007) Hungary will be among those admitted, it may well make sense to have a look at the country *as a prospective full member of the EU*, rather than one of the 27 transition economies. Under this perspective requirements and policies of the EU are taken as given or as they are most probable to evolve, and the question is *how far is Hungary* likely to be *from those standards* by the time of accession (including the 18 plus months that are needed for ratification of the accession agreement).

Nominal and real convergence

In terms of real convergence it is worth mentioning that Hungary has been among the fastest growing economies in the globe, showing remarkable resistance to the East Asian, Russian and Brazilian financial crises and the external shocks created by these. GDP started to grow in 1993, accelerating to 4.6 percent in 1997, 4.9 percent in 1998, 4.2 percent in 1999, 5.2 percent in 2000 and 3.8 percent in 2001 with an estimated 3.2-3.5 percent in 2002. This growth has been all the more remarkable, since it has not been accompanied by the deterioration of the current account, a problem encountered in the same period by Poland, Estonia, Malta and the Czech Republic, as well as by the country itself in its earlier growth periods, including the phase of 1993-94. By contrast the current account position was a deficit or 1.7 bn USD in 1996, 982 mn USD in 1997, 2.3 bn USD in 1998, 2.1 bn USD in 1999, 1.4 bn USD in 2000) despite the skyrocketing of oil process) with a deficit of 1.2 mn low in 2001[4]. Debt service ratio, i.e. the

4 Revised figures based on NBH data as reported in: Magyar Hírlap, 19 Feb, 2002.

... per cent in 1996 and it dropped to 18.4 percent by 2000 and 14 percent by 2001.

Thus the previous trade-off between growth and financial stability and the ensuing stop-go cycle could be overcome. In EU parlance *growth has been financially sustainable*.

It would be hard to overlook, however, that if we measure economic performance in the longer run, Hungary has regained its pre-crisis (1989) level of GDP only by 1999 (as reported in: UN Economic Commission for Europe: *Economic Survey of Europe*, 2001/1. statistical annex). In other words, real convergence to the EU average has been going on *only for the last three years*, which is less than impressive if we take the per capita gap between Hungary and the EU-15, with Hungary being at some 52 percent of the EU average in 2001. In other words, there is still a long way to go, there is no reason to lean back in satisfaction.

There is even less room for cheering if one looks at nominal convergence, i.e. the approximation of Hungarian macro financial indicators to those of the EU average and EU reference levels. Inflation has remained sustainably high, with annual rates of 18.3 percent in 1997, 14.3 percent in 1998, 10.0 percent in 1999, 9.9 percent in 2000 and 9.3 percent in 2001 (against the planned rate of 6 percent). General government deficit has rarely been under 4 percent according to Eurostat standards and even growing to 5.2 percent according to the regular monthly published GKI Economic Research[5] official data contain an element of creative accounting, also acknowledged by some advisors of the PM.

This is bad news, since the Stability and Growth Pact of 1997 is part and parcel of the *acquis*, though not legally incorporated in the text of the Amsterdam and Nice Treaties. However, as the public reprimand of Ireland and the warnings to Germany, Italy and Britain, issued by Ecofin and the European Central Bank in 2001 indicate, this *is anything but a declaration of pious intent*. This is not the place to reiterate the economics behind the Pact. However it is evident, that it does call for balanced budgets or even budgets in surplus[6] in "normal" times of high growth, so as to make way for non inflationary borrowing for possible rainier days. Seen from this angle, it is hard to overlook that Hungarian fiscal policy has been extremely lax ever since 1997 in a row. Inflation has stuck in at a 10 percent level since May, 1999 to September 2001. Reflecting this, interest rates are high. Nominal convergence does not follow from high growth rates, and this is bad news for a country aspiring for early membership in EU. True, EMU membership is not precondition for accession, still at the time of membership the commitment for financial improvement should be already *credible*, and not only for diplomats, but also for tens of thousands of market players.

5 cf. Külgazdaság, vol.45.no.6. [2001] p.48.
6 By 2001 already 5 EU countries had a surplus in their fiscal balance (including Ireland), despite the economic slowdown.

to adopt a *multi-year fiscal adjustment programme* in preparation for membership. These pre-accession economic programmes (PEPs) should include not only general information and declaration of goodwill, but also *quantitative* targets reflecting the changed priorities of expenditures and publicised so that electorates could scrutinise progress, i.e. attainment or missing of these objectives (Normann, 2001a).[7]

International experience with such "straightjackets" prove the usefulness of these, especially with countries lacking a history of fiscal responsibility and credibility, such as Israel and Portugal (cf. Gottlieb, 2000 and Braga de Macedo, 2000). While a pre-election year is unlikely to be the ideal timing of adopting such an operation, the urgency of the situation makes such an option highly advisable immediately upon the swearing in of the new government in 2002.

Great leap forward in monetary policy

It has become customary to portray Hungarian monetary and exchange rate policies as exemplary and successful in its implementing the crawling peg régime and warding off international crises (Szapáry and Darvas, 2000). By the year 2001, and quite related to the change in the top leadership of the National Bank, there emerged a view that the previous arrangements have outlived themselves. Regular pre-announced devaluations were increasingly seen as stabilising inflationary expectations. Moreover with headline inflation stuck at 10 percent and the room for manoeuvre constrained by the exchange rate régime, interest rate policy could not be effectively used to counter inflation. The May 2001 figure of 10.8 percent on a year by year base was perhaps the last shock to prompt the government and the NBH to switch to a wide band of floating. Instead of the previous + or - 2.25 percent the exchange rate of the Forint can fluctuate between plus minus 15 percent from the central parity without triggering official intervention on the currency market. Thereby Hungary stepped in the shoes of Poland having adopted a similar régime in April 2000. Accompanying this measure was the liberalisation of short term financial operations so that dealers could hedge themselves against the ensuing exchange rate risks. In less than a month the Forint appreciated by 9 percent, thus contributing to a disinflation in the second half of the year, as in the next six months appreciation continued to 13.2 percent over central parity. By January 2002 annualised inflation declined to 6.6 percent and prime rates to 8.5 percent by February, 2002.

7 It is hardly by chance that the Czech Republic, heading for a 9 percent deficit in 2001 was severely criticised and that the Zeman government reacted also by restraining the autonomy of the Czech National Bank, while rejecting the legitimacy of criticism (Prag...2001). The actual number proved to be 11 percent of GDP.

international financial literature (Lámfalussy, 2000; Kolodko, 2000) advises utmost caution on liberalising short term operations. The monographs quoted above offer detailed empirical evidence supporting the claim that such a step may trigger volatility, invite speculative inflows and may test the banking system severely. It is hardly by chance that at the Ecofin meeting in Malmö in April, 2001 the Commission submitted a longer analytical paper (as reported in: EU..., 2001) calling for the inherent *dangers* of opening up capital markets fully *when savings rates are low* and thus *inadequate* for supporting a sustaining process of catch-up. This arrangement may lead to overvaluation of currency, repeated current account deficits and thus major corrective actions of markets on the currency exchange rate, or creating volatility.

This is a problem, at least for credibility and thus an *ability to comply with ERM-2*. It needs to be addressed even if, formally speaking, an appreciation of say, by 10 percent followed by a depreciation of 25 percent were still within the officially declared band of allowable fluctuation. Thus while the idea of bringing inflation down to 4-5 percent by late 2002 and to 2-3 percent by 2004 is commendable (as declared in Járai, 2001) it is less than trivial to see how it is attainable. If it were to rest only with the appreciating exchange rate, this would draw resemblance to what has been observed with countries ending up with currency crises (Horvath, 1998).

Generally speaking the combination of *lax fiscal policies with tight monetary policies is seen as deplorable* by the *majority* of the financial literature. Meanwhile, statements from the fiscal authorities do not reflect a similar determination of instituting a fiscal correction. Not only regular public statements of the minister of finance (e.g. in: *Népszava*, 10 April, 2001) reflect a continued conviction seeing fiscal corrections as unnecessary. The *three year financial guideline* of the fiscal authority, submitted for consultations with the Commission in the course of the structured dialogue, continues to lack any such items, aiming at a "respectable and Maastricht-conform" 2.5 percent deficit by 2004.[8]

Without wanting to overestimate the relevance of official projections or prejudge post-election economic policies, it needs to be highlighted that a substantial degree of *coherence* between fiscal and monetary policies is one of the few consensus points of various economics and policy textbooks. Moreover the *problem of savings gap*, i.e. a continuously low level of net domestic savings of households may become a considerable constraint on the *attainable growth rates on the longer run* in any catching up economy. Therefore the commandment to focus on *savings rather than redistribution* is a rather technical one, even if the political repercussions are hard to deny. External savings in the form of direct investment can only

8 Gusztáv Báger (2001), director general in the fiscal authority at the time, reporting on preliminary estimates for the period until 2008 replicated these, and not indicated any major fiscal adjustment even for the 2005-8 period, which supports our concern reflected in the main body of the text.

account deficits. ... triggering current

Empirical analyses (Losoncz, 2001) highlight the robustness of Hungarian export growth based on improved competitiveness, thus a sustainable current account position is likely. This, together with the wide band of fluctuation, make speculation against the Forint unlikely, at least as one way bets. Thus convergence to EMU is technically possible if fiscal adjustment is implemented.

4. Adjustment to capping the CAP

One of the traditional lures of the EU for candidates has been its lavish support for agriculture and rural development. It would be hard to deny the historic role played by the EU/EC common agricultural policy (CAP) in overcoming one of the traditional bottlenecks in Europe, that of massive rural poverty and the ensuing urbanisation crises, coupled with, and partly triggered by, the extreme volatility of prices for agricultural produce. However ever since the Mansholt Plan of 1968, the skyrocketing costs and the socially and economically contestable distributional consequences have turned the area as one of the favourite subjects of large scale reform projects. These have aimed at, and following the MacSharry and Fischler reforms in the 1990s, also accomplished the capping of agricultural subsidies, the extinction of incentives to overproduction and the related need to dump the surpluses on world markets (a major cause for ongoing world trade conflict).

It seems that the prospect of eastern enlargement has contributed to the acceleration of reform endeavours and helped their overwhelming of sectoral interests across the 1990s. On the other hand, farming lobbies of central and eastern Europe continued to conceive the CAP as a basic funding for delayed modernisation of their respective production bases. The change of emphasis favouring environmental concerns and de-emphasising quantitative targets, de-coupling of income support from produced quantities and many other innovations of CAP practices went unnoticed. Negotiators from the east continue to bargain for higher production quotas (O. Horváth, 2002), despite the ongoing de-coupling of domestic from world prices. They tend to disregard environmental and animal welfare concerns as falling outside of their competencies.[9]

Deciding over the current financial guideline the Berlin Council of March, 1999 ended with a compromise solution, where sizeable funds were earmarked for assisting candidate countries' *preparation* for membership, while *excluding* potential new members from one of the major forms of rural

9. For a detailed overview of the Hungarian position and its complexities cf. (Halmai, ed, 2000).

... regime, direct income supports (DIS) cf. (Schrader, 2000)..

On the first part two major experiences could be observed in 2000-2001. On the side of the candidate countries, two thirds of the support applications were related to *increasing production* and only one third on health, safety, consumer protection and overall non-farming rural development. Meanwhile the EU envisaged just inverse proportions, with two thirds of funds made available in the broader non-production-related areas and only one third for productive purposes.[10]

A related problem has been the delays in setting up the SAPARD institutions in all countries but also in Hungary. The crux of the matter was the institutional reform requiring both transparency and accountability for spending. In order to secure this aim the independence of the decision-making organs from the agricultural department was made by the EU as a precondition for freeing the funds. Meanwhile the Hungarian ministry understood this as a breach of its competencies (even of national sovereignty), and repeatedly subjected organisational arrangements not meeting the above conditions and continuing sectoral control over the funds. As a consequence in the year 2000 the SAPARD bureau could not be set up, in 2001 it could not be accredited, i.e. it could actually not distribute any funds as yet.

The lesson from this story is that the weak point of candidate countries in general and of frontrunner Hungary in particular, is not the size of farming, but the weak *administrative capacity* of authorities, that may turn into a bottleneck in managing community funds.

One of the fundamental features of the emerging reform projects of the EU for the longer run (Mann, 2001a) is the emphasis on quality of life items, environment, food safety, animal rights and further strengthening the element of de-coupling of income support from meeting production targets. The role of national co-financing is going to grow in significance, whereas production supports are likely to be further decreased by at least 20 percent in 2007-2013, despite the growing number of applicants. The foot and mouth disease has had a beneficial effect in upsetting the quantitative targets agreed in Berlin. It triggered contingency measures and further calls for *ecological farming,* instead of fostering quantitative growth at any cost.

While especially the French but also some other net beneficiaries caution against too radical changes, these are not to be stopped any longer. The EU has already launched a *pilot project* from this year, effective from 2002 that small holders will *qualify for a lump sum* up until 1075 euro/year, making the current bulky paperwork superfluous (Mann, 2001b). This support is *entirely independent* of what these people produce or not produce, further it alleviates the current problem in which 20 percent of farmers receive 80 percent of all supports, and these are not the poorest units.

10 On the diminishing role of production-related subsidies in EU cf. (Elekes, 2001).

ly correct but politically irrealistic, since direct income supports need to be covered, basically from net contributors. The limits to the latter has clearly been signalled by the May 2001 decision of Ecofin to reimburse the 7.5bn euros overpaid by member states in 2000, due to higher growth and higher inflation. This happened at a time when money for the reconstruction of the Balkans under the Stability Pact were missing just as much as funding for the rapid reaction force, or the development of Eurofighter.[11] Thus the much reiterated idea of Franz Fischler of phasing newcomers in might become the only realistic option, while DIS for incumbents start to be phased out in 2004-6. This does mean unequal treatment for the transitory period for farmers of newcomers, which will be overcome by setting the appropriate guidelines for 2007-2013 (co-decided by the first new entrants).

Re-tailoring structural funds

Structural funds aim at accelerating regional development in the EU. There are two basic ways of looking at their role. The traditional approach sees them as governmental means to counteract tendencies of growing disparities. The market-oriented approach sees the single market as the major achievement and gain for EU regional development and considers these funds as additional lubricants for self-sustaining development.

The spending under this heading has been the fastest growing item in the 70s and 80s, growing from 5 percent of total community funds of 1975 to 40 percent by the current guideline. The novelty of the latter has been that it stopped the previous *quasi-automatic growth* of the share of these funds and tying these to GDP growth.

It is important to bear in mind that despite the ongoing emotional debate on the role of these funds, quantitative evidence shows their contribution to overall welfare quite limited, adding up to 0.1 - 0.5 percent of *additional* growth of income at the regional (not the national) level (Tóth, 2001). Likewise it is important to know that all regional spending equals to 0.46 percent of total GDP of the EU, thus overall growth can by no means be generated by these. If growth is not conditional upon them, growth-promoting policies should concentrate upon creating *overall favourable business climate* rather than maximising the net inflow of EU structural funds.

Analytical studies of the prospective regional policies of the EU (Iván, 2001) highlight *major changes in the ways these funds will be administered* by the time Hungary will have become a member. The state looses its role of a gatekeeper in administering the funds, which can be mobilised only if co-funding, both from public and private sources is being secured. As mismanagement of these funds did play a role in bringing down the Santer Commission, meticulous controls are likely to *intensify*. The simplifying elements discussed in terms of agriculture are unlikely to be adopted in this area. Modulation, i.e. targeting expenditures to multi-yearyear programmes, normally exceeding one electoral term, and further strengthening the co-funding elements are likely to prevail.[12] In other words, unlike in Greece or Spain, the probability of seeing highways and ports under the sign of "built from EU assistance" is unlikely to play a prominent role in the future of Hungary.

This feature is compounded by some developments that do not derive directly from regional policies in Hungary, but set the limits to what can and cannot be attained. Besides the above mentioned limited administrative capacities, municipalities are blended out as an outcome of their long-standing political battle with the central government. Only five percent of personal income tax remains for local level spending against 50 percent a decade ago.

The peculiarities of Hungarian history do not allow for heeding the standard advice and enhance the role of local taxes, as tax awareness is low and its correlations to local services are not frequently understood by the electorate. Public-private partnerships are not developed, and the decision to build the new highways from domestic resources (to support local SME) further diminished the chances for these to emerge.

In a further wound point, following *the failure* of the centre-left coalition, the centre-right also fell short of *introducing the system of regions to replace traditional small counties*. The ministry of interior decided to revert the project and revive the traditional units of administration (*Népszava*, 25 June, 2001) that are known to be unfit for administering EU money. It is all the more surprising as both Poland and Slovakia have recently managed to restructure their respective administrations in order to make these compatible to EU requirements.

Looking from the angle of prospective changes in both the CAP and in the structural funds, it looks particularly unfortunate to concentrate both cat and mice, i.e. agriculture and regional development in a single department. To a large extent the story is about creating non-agricultural, non-farm-related sources of income for a population that is to be kept where it is. All the more so as moving out of the cities has become a mass phenomenon (Budapest alone having lost over 700 thousand inhabitants in the last decade). Since farming departments are the traditional rallying points for agricultural producers, other interests, such as regional, services, educational, environmental can only be poorly represented by such a department. Experience over the 1990-2001 period in Hungary regretfully supports empirical evidence to this insight. Thus the recent idea to restructure governmental departments is more than welcome.

11 This project may collapse due to Germany's' unwillingness to fund its agreed share (Shishkin, 2002).

12 This may make the January 2002 Commission proposition look hypocritic in its 'compensating' low farming subsidies for higher outlays earmarked in the structural funds, since the latter may not become realistically available for candidates.

Environment is rightly seen as one of the most substantial challenge for enlargement. On the one hand, environmental legislation is the fastest growing body of EU law. Only in 1989-91 more items were added to the *acquis* than in the preceding decades. The fact that *qualified majority voting*, an anathema for most EU policies, has turned into reality, allows for environmental fore-fighters to push their agenda through EU fora (cf. Sbragia, 2000).

Analyses of environmental policies in the EU testify to two major trends relevant for our subject. First, frontrunners are able and willing to enforce regulations that are costly, and normal domestic decision-making processes would often not be ready to internalise such concerns, unless the point of EU compatibility required that. Second, frontrunners like Sweden fear, with a degree of justification, that following the enlargement a new majority of laggards, combining the southern and eastern members, may emerge that may lame or even revert progressive and forward looking initiatives.

For this reason EU incumbents often see as a *test of seriousness* for applicants' deliberations if and how these treat environmental concerns. The more frequent is the reference to poverty, the deeper is the fear that candidates do not really mean to comply, or have not truly internalised how global a concern the environment is. For several countries with a relatively low trade exposure, environmental consciousness is what may unite candidates and incumbents. And for the time being green parties are in the governments of France and Germany, their priorities often echoed by conservative parties, as in Austria. Thus the political weight of this dimension is truly big.

Given the delicate position of environmental law in EU, the joint position often has a *fundamentalist* flavour, not appreciating the economic limitations of less developed countries. On the other hand, candidates have not proved to be terribly convincing in presenting credible calculations of how they envisage cleaning up the environment. It is all the more so, if not only major improvements are missing, but even the share of environmental outlays is diminishing, as in the biannual budget of Hungary.

It is beyond doubt that making way for private investors is the only conceivable alternative for funding the costs of half a century of negligence in Hungary and other postcommunist economies. Therefore further privatisation and even more reliance on foreign strategic investors may be the offensive part of such a strategy that supposes the necessary concession in terms of the inflated original transitory requests, *a process already accelerated under the Swedish presidency*. In fact, Hungary sustained only 4 of over 30 requests for derogation, and the remaining difference is that of sequencing (and funding) the measures, not their necessity.

In a way negotiations have proven to be *much less rigid as could have been feared*. There is a growing understanding that environmental catch-up is a gradual process, a large part of which is likely to be realised *only*

need for further efforts. The truth is that the traditionally weak position of the environmental department within the government and the relative de-emphasis of environmental issues in the items of the domestic policy agenda, render this task a gargantuan one.

Medium-term outlook for EU enlargement

In a sense the Swedes proved to be *effective in promoting their three e-s*. Enlargement did gather momentum by the deliberations of Gothenburg, by making the target date explicit and enforcing the road map, although its ritual description as a breakthrough was obviously an over-interpretation of achievements. *Employment* situation did improve - the unemployment rate of 8 percent by early 2002 - but this would be hard to ascribe directly to any policies, rather than to strongly positive growth rates in the eurozone (1.3 percent for 2001) and to the creeping deregulation of labour markets across the union. This circumstance is underscored by the fact that the Stockholm Council of March 2001 ended with a compromise, with all parties refraining their more ambitious aims of liberalisation (as of the energy markets or transferability of social security claims, even in terms of freeing the capital markets, as suggested by the Lámfalussy commission) - reflecting the preoccupation with national agendas (Urkuti, 2001). Last but not least the progress made in terms of the *environmental* chapter was more attributable to the softening of negotiating stances of both sides in Brussels rather than anything else.

What has been attributable, at least in part, to Swedish and Belgian efforts is the pushing of reform and enlargement agenda. Observers of Gothenburg have not failed to call attention to the fact that target dates were approved against the wishes of the Germans and the French, a fairly unconventional event. Similarly political pressure and the ramifications of foot and mouth disease, coupled with domestic forces pushing environmental farming have *converted Germany from the conservative camp over to the reformist camp in terms of agricultural policies* (Norman, 2001b). This implied a go-ahead for reform projects of the Commission prior to the review of the Berlin compromises, originally scheduled for the end of 2002. This move may have a favourable impact on the ability of the EU to cope with at least some new entrants in a less discriminatory fashion.

It would be hard to overlook the fundamental facts, i.e. that applicant countries' combined GDP amount only to 6 percent of that of the EU, their combined share in EU trade is a mere 6.5 percent. Therefore most estimates expect a maximum of 0.1 percent of additional growth for EU incumbents and an additional 0.3 - 0.8 percent annual growth for acceding countries (Hungary being in the upper part). Thus pure economic considerations may hardly dominate the enlargement, and sufficient political will, if it ever emerges and is being formulated by the policymaking on both sides, is in a position to bring about the first enlargements on schedule.

on overcoming present bottlenecks inside the country. The latter approach is justified by the insight, that external policy conditions actually may turn *unexpectedly favourable*, as the low point of the Nice Summit was followed by the Swedish and Belgian presidencies and by the calling into being of the Convention for 2002-2003, where candidate countries may also participate in the debates.

In concrete terms EU maturity requires successful mastering of some traditional "transition leftovers": *stabilisation, liberalisation and privatisation.* This textbook-like agenda for Hungary requires concerted efforts on the fiscal and monetary sides to bring about organic and sustaining disinflation to levels, making EMU qualification conceivable in 2-3 years following accession, as currently planned by the NBH. Liberalisation would call for abolishing remaining constraints on pricing and market entry ensuring the equal treatment for foreigners and domestic players in all walks of life, including public procurement (Dávid, 2001). Last but not least broad-based public sector development and new privatisation by listing large new corporations on the capital market could reinvigorate the Budapest stock exchange, bringing about a lastingly favourable investment climate.

There is good ground for us to conclude this overview on an *optimistic note*. On the EU side, constant "crisis-management" is nothing new, but it is its *traditional modus operandi*. Thus slow but steady progress, even on contested issues, is plausible also in the future. On the Hungarian side, the programme outlined above enjoys the broad consensus of experts across the party lines (except for extremists).

To put it differently, *foot-dragging* on specifics has been and is likely to remain *tactical, while the ability to learn seems to be strategic*. If this is not a benevolent misreading of facts, step by step improvements are possible. These are both necessary and sufficient for Hungary to qualify in the first round of eastward enlargement in the EU in the middle of the current decade. The remaining tasks are though considerable, *but by no means insurmountable*. The very fact, that the Commission of the EU started to talk about numbers in January 2002 is a good sign: they, too, mean business.

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