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STRATEGIC ISSUES FOR THE EU10 COUNTRIES

MAIN POSITIONS AND IMPLICATIONS FOR EU POLICY-MAKING

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Edited by **Krisztina Vida**

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INTRODUCTORY REMARKS

Krisztina Vida

The present report is displaying and analysing the behaviour of the ten Central and Eastern European member states (EU10) in the formulation of some of the most topical issues under discussion in the European Union. The countries in focus are Bulgaria, the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, Slovakia and Slovenia.

The country studies start with a general overview of the political and economic situation of each country, their EU-strategies including tackling the current crisis of the euro area, as well as their commitments in the framework of the Europe 2020 strategy. The chapters then continue with these countries' positions on the following policy areas: the upcoming multiannual financial framework (MFF) for 2014-2020, the reform of the common agricultural policy (CAP) and of cohesion policy, energy policy cooperation, enlargement and European neighbourhood policy, as well as any country-specific issue if relevant.

The report attempts to identify the key EU-related priorities of the EU10, their abilities to influence European Union policies alone or jointly and to look at the impact they make on the processes of European integration. The main question is, what the interests of these states are within the above mentioned policy areas and how they are able to represent them at the EU level. It is also important to look at the alliance building patterns of these states along given policy issues. In a broader perspective, the results of this report show the image of the EU in these countries, and their ideals concerning European integration in general and their place and goals as part of it in particular.

This study was put together by an international team the members of which were the following experts. *Yasen Georgiev* (executive director of the Economic Policy Institute, Sofia) and *Mariana Trifonova* (research fellow at the Economic Policy Institute, Sofia), *Ahto Lobjakas* (research fellow at the Estonian Foreign Policy Institute, Tallinn), *Elżbieta Kawecka-Wyrzykowska* (professor at the Warsaw School of Economics, Head of the Jean Monnet Chair of European Integration, Warsaw), *Darina Malová* (professor of Political Sciences at the Comenius University, Bratislava) and *Martin Pašiak* (assistant professor at the Comenius University, Bratislava). The project coordinator (Krisztina Vida) as well as the Hungarian participants are all working at the Institute of World Economics which is part of the Research Centre for Economic and Regional Studies of the Hungarian Academy of Sciences. The Hungarian authors are: *Miklós Somai* and *Krisztina Vida,* senior research fellows, *Sándor Meisel* and *Gábor Túry,* research fellows and *Ágnes Orosz,* research assistant. The statistical database used in this book dates back to the summer of 2012. The volume was closed on 15 October 2012.

We hope that our research team could make a useful contribution to the international discussion on the examined region's position in the European Union and its impact on EU policy-making.

BULGARIA

Yasen Georgiev – Mariana Trifonova

1. Domestic political framework, EU strategy of the government

1.1. Overview of internal politics

Bulgaria's current government took office after the parliamentary elections in July 2009. It was formed by the Citizens for the European Development of Bulgaria party (known by its Bulgarian abbreviation – GERB) and headed by its leader, Boyko Borisov. Since GERB did not receive a majority in the National Assembly (the Bulgarian legislature which elects and dismisses the Prime Minister as well as, upon his motion, the members of the Council of Ministers), the party formed a multi-party government coalition relying on the parliamentary support of several smaller parties which declared themselves against the three-party-coalition that previously governed the country.

The relatively stable public support which GERB enjoys – particularly due to the strong individual popularity of its

leader and Prime Minister – contributed to the success the party achieved at the local and presidential elections jointly conducted in October 2011. Subsequently, the run-off election for Bulgaria's presidency was won by the GERB candidate Rosen Plevneliev, Regional Development Minister in Borisov's cabinet.

The main task for the current Bulgarian government, after taking office, was to regain the European Commission's confidence and restore credibility. It was in 2008 when considerable amounts of EU assistance were suspended as a result of shortcomings in the management and use of European funds. Furthermore, Commission reports within the cooperation and verification mechanism (CVM) used to criticise the ineffective measures against organised crime and corruption as well as the inefficiently performing judicial reform. Having all these issues on the political agenda, GERB's government concentrated on improving the communication with Brussels and undoubtedly registered overall progress in this regard. At the same time, there is still room for improvement in the field of the judiciary.

1.2. EU strategy of the government

Bulgaria had a National EU Accession Strategy that was drafted in 1998. But after joining the EU in 2007, Bulgaria has not adopted any official and comprehensive EU strategy. Nevertheless, the country's particular priorities in this field can be more or less derived from the mission statement of the Ministry of Foreign Affairs of the Republic of Bulgaria (see later, under the "External relations, enlargement, European neighbourhood policy" heading).

When taking into consideration the latest developments in the eurozone and the crisis management efforts in EU as a whole, Sofia tends to support the common EU approaches.

Thus, regardless of being outside the euro area, Bulgaria decided to ratify the amended Article 136 of the Treaty on the Functioning of the European Union with a view to making the European Stability Mechanism operational. Furthermore, despite the initial opposition to the Pact for competitiveness (later called Euro Plus Pact) on behalf of the Bulgarian Ministry of Finance and the Bulgarian National Bank – due to the country's position against tax systems' harmonisation in the EU – Bulgaria eventually joined the Euro Plus Pact. The justification behind this was summarised by the Bulgarian Prime Minister as follows: "If we don't join, we will learn from the media what is happening in Europe and then there is no one to blame that it is at one or two speeds."[1]

In this regard, the Bulgarian position relating to the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union (TSCG) known as the Fiscal Compact is also worth mentioning.[2] The government received the parliament's mandate for participation in the negotiations provided that the Treaty would neither lead to financial obligations for Bulgaria, nor result in commitments for harmonisation of the country's tax policy with those of the other contracting parties. What is more, this parliamentary decision supported only the implementation of the third Title of the Treaty (introducing stricter budgetary discipline) while the whole TSCG would enter into force once Sofia has joined the eurozone. Last but not least, Bulgaria insisted on dropping out Title IV of the Treaty which stipulates a common economic policy as well as close coordination in the field.

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1 *Quoted Boyko Borisov, Prime Minister: http://www.euinside.eu/en/comments/bulgaria-comments-euro-pact-and-esm*
2 *Bulgarian National Assembly (2012)*

2. General economic analysis

2.1. Overview of main macroeconomic developments

The Bulgarian economy registered accelerated growth rates before the outbreak of the crisis driven primarily by the high lending activity of the banks and significant capital inflows. However, the easy access to financing boosted mainly sectors such as real estate, construction, financial services and trade; that altogether channelled the financial crisis into the small and open economy of Bulgaria. The worst year was 2009 when the economy contracted by 5.5%. From then on the economy started slowly bouncing back, though, not because of the previous drivers but due to increasing export volumes which contributed to the GDP growth and affected positively the current account balance in 2010 and 2011.

On the one hand, the hike in exports did not prove to be enough for mitigating the effects of the crisis on the labour market. On the other hand, the rise of the unemployment rate increased the overall workers' productivity. From 2010 on the country's macroeconomic framework continued the pre-crisis trend and remained stable with a low budget deficit (particularly when the EU average is considered) and with favourable public debt levels which rank Bulgaria among the best performing EU countries. Despite these positive indicators along with the exchange rate of the national currency – the Bulgarian lev that is pegged to the euro within the currency board system – Bulgaria's application to join the European Exchange Rate Mechanism was undermined by the high inflation rates in the years before 2009. Therefore, one of the main goals the current government declared when taking office in mid-2009 was to lower the inflation rates and join the eurozone in 2013 – an ambition that vanished upon the uncertainties of the single currency.

Table 1, Main macroeconomic indicators of Bulgaria

	2009	2010	2011	2012 (f)	2013 (f)
Real GDP growth rate (annual change, %)	-5.5	0.4	1.7	0.5	1.9
GDP/capita, EU27=100	44	44	45	n.a.	n.a.
Gross fixed capital formation/GDP (%)	28.9	22.8	20.9	n.a.	n.a.
FDI inflow (BEUR)*	2.4	1.2	1.3	1.2	n.a.
Private consumption/GDP (%)	63.2	62.8	60.7	n.a.	n.a.
Public consumption/GDP (%)	16.3	16.2	15.5	n.a.	n.a.
Exports of goods and services (BEUR)	16.6	20.7	25.6	n.a.	n.a.
Imports of goods and services (BEUR)	19.7	21.4	25.3	n.a.	n.a.
Current account balance/GDP (%)	-9.0	-0.4	0.8	0.6	-0.3
Unemployment rate (%)	6.8	10.2	11.2	12.0	11.9
Inflation (HICP)	2.5	3	3.4	2.6	2.7
Interest rates (10y)	7.22	6.01	5.36	n.a.	n.a.

*Eurostat, European Commission, * WIIW (f = forecast)*

2.2. Fiscal stability, economic and social competitiveness

The Bulgarian Convergence Programme for 2012-2015 submitted to the European Commission in April 2012, describes the strategic fiscal policy objectives with regard to both budget balance and government debt.[3] It sets a medium-term budgetary objective of a structural deficit of 0.5% of GDP in 2015 in line with the revised Stability and Growth Pact (SGP). It includes also the budgetary aspects of major structural reforms, underlying the priorities and targets in the National Reform Programme of the Republic of Bulgaria (2012-2020). The most important structural reforms presented in the Convergence Programme cover fields such as the pension system and social inclusion, labour market

3 *Ministry of Finance of the Republic of Bulgaria (2012a)*

and education. These are included also in the Commission's proposal for Council recommendations to Bulgaria together with the low level of research and innovation, insufficient administrative capacity in managing infrastructural projects and poor use of EU funds (despite the consistent progress in the last two years).[4]

Along with the country-specific recommendations, in May 2012 the Commission recommended that the Council abrogate the excessive deficit procedure (EDP) for Bulgaria. Actually, the country has been under EDP for a short while, starting in July 2010. The deadline for correction was 2011 when the deficit was already below the 3% of GDP reference value. Moreover, the Commission's 2012 spring forecast projected the general government deficit to remain below the reference value and to further decline over the forecast period.[5]

Table 2, Public finances in Bulgaria

	2009	2010	2011	2012 (f)	2013 (f)
Public budget balance (% of GDP)	-4.3	-3.1	-2.1	-1.9	-1.7
Public debts (% of GDP)	14.6	16.3	16.3	17.6	18.5

Eurostat, European Commission (f=forecast)

The National Reform Programme – NRP (2011-2015) was approved by the Council of Ministers in April 2011. Its update (2012-2020) was prepared within the framework of the 2012 European Semester and addresses the recommendations made in the conclusions of the 2012 Annual Growth Survey. The implementation of the measures set in the National Reform Programme aim at increasing the standard of living as an ultimate goal of Bulgarian economic policy and raising the average income level in the country from 44% of the EU average in 2010 to 60% of it in 2020. Last but not least, with the 2012 update of the National Reform Programme of the Republic of Bulgaria the government kept the national targets for implementing the Europe 2020 strategy as defined in its first version (2011-2015).[6]

Table 3, Europe 2020 targets of Bulgaria

Europe 2020 targets	Situation in Bulgaria in 2010	Bulgarian Europe 2020 targets
Employment rate – 75% of 20-64 year-olds	65.4%	76%
R&D – 3% of GDP to be invested in R&D	0.6%	1.5%
Climate change / energy		
Reducing greenhouse gas emissions by at least 20%	-9% (between 2005 and 2010)	-20% compared to the 2005 level
Covering 20% of energy consumption from renewables	12.6%	16%
Energy use in Mtoe (2009) Increasing energy efficiency by 20%	17.57 Mtoe	-3.2 Mtoe
Education		
Reducing school drop-out rates below 10%	13.9%	11%
Reaching tertiary education attainment by at least 40% of 30-34 year-olds	27.7%	36%
Poverty / social exclusion Reducing the number of people in or at risk of poverty or exclusion by 20 million	1,565,000	-260,000

European Commission

4 *Recommendation for a Council Recommendation … (2012)*
5 *Ibid.*
6 *Ministry of Finance of the Republic of Bulgaria (2012b)*

3. Position and potential impact of Bulgaria on current key issues

3.1. EU budget: the multiannual financial framework for 2014-2020

According to the latest official position of Bulgaria, presented in a joint report of the Committee on European Affairs and Oversight of the European Funds and the Budget and Finance Committee, Sofia supports in general the expenditure side of the multiannual financial framework for 2014-2020. On the contrary, the revenue side of EU budget caused significant disagreements. Concerns were expressed regarding the proposal to decrease the GNI-based instalment to the EU budget which would lead to a greater risk of "Europe of two speeds". What is more, each country's contribution to the EU budget is seen to be in correlation with the size of its economy, i.e. with its GNI.

The official position welcomes the simplification of the system of own resources, though, not via introducing new EU taxes which would divert the financial burden away from the member states towards the EU citizens and companies, thus reducing citizens' disposable income and affecting companies' competitive advantages. More precisely, the Commission's suggestion for the adoption of a European financial transaction tax (FTT) as well as a European VAT are considered not in compliance with the EU principle of proportionality since the system of own resources should respect the member states' fiscal sovereignty. Furthermore, as it was mentioned, this is believed to lead to an additional tax burden for EU citizens and business. Eventually, this would provoke negative attitudes towards the EU among the European tax payers. Moreover the FTT might be counterproductive for Europe, unless an agreement on this issue is reached worldwide.[7]

3.2. Common agricultural policy after 2013

Bulgaria advocates a more just distribution of direct payments as one of the chief instruments for support in the field of agriculture. The future distribution scheme should not harm the new member states. Although the provisions in Bulgaria's Accession Treaty envisage 2016 as the year of level-off for the country, Sofia urges for an earlier evening out of direct payments, namely in 2014. Having in mind the structure of agricultural holdings in the country, serious concerns exist over the chance of a handful of monopolists receiving up to 80% of the funding. For this reason, Bulgaria supports the income capping for big farms. Increasing the financial support for stock-breeders is also one of the priorities on the negotiation agenda for the country.

Bulgaria welcomes the introduction of a set percentage for eco farming (so-called greening of the CAP) but is reluctant towards accepting a fixed 30% share and proposes a more diversified approach taking into account local specificities.

Following the in-depth discussions in the Agriculture and Forests Committee and the Committee on European Affairs and Oversight of the European Funds in the end of 2011, the parliament urged for an equitable direct payments distribution among member states to provide for an equal competitive basis. A more ambitious approach is needed in order to promote convergence between the different levels of support. A proper option could be the national top-up to reach its maximum for Bulgaria and Romania in 2014 instead of 2016. The necessity for more measures with an environmental focus is acknowledged but Bulgaria does

7 *Bulgarian National Assembly (2011)*

not support fixed rates and proposes more flexibility on member state level. Approval is given to the possibility of tying direct payments to production outcomes. The National Assembly insists on an increase from 10% to 20% to the national payment package limits for new member states. The statement proposes unabsorbed resources under the direct payment packages (outside the fixed or mandatory part) to remain in the first pillar and to be used for the promotion of intensive sectors and stock-breeding. The National Assembly adheres to the idea of maximising farm support but strongly believes that the level of the capping must be re-examined on the basis of a comparative analysis of the agricultural holdings' structures in all EU member states. Reservations are expressed towards taking 2011 as a basis year as it may be disadvantageous for new farmers.

Although the two parliamentary committees welcome the establishment of a Common Strategic Framework, they articulate reservations towards the binding of the content and structure of the rural development programmes to ex-ante conditionalities. They stress the necessity to synchronise the requirements regarding these conditionalities. Support is given to the establishment of thematic sub-programmes targeting specific issues, namely young farmers, small agricultural holdings, mountainous areas and short supply chains. With reference to the justifiable investments in the second pillar, Bulgaria insists on a re-consideration in order to extend the scope of justifiable investments to the stock-breeding sector.

3.3. Cohesion policy after 2013

Bulgaria has declared cohesion policy as one of the country's priorities in the debate on the next MFF 2014-2020. The government believes this policy's funding should be either sustained or increased within the total EU budget.

Although Sofia supports the alignment of cohesion policy with the Europe 2020 strategy, the country believes that developing basic infrastructure should remain among the priorities in the regions where such support is still needed. "The country welcomes the establishment of the new Connecting Europe Facility but it must not be introduced at the expense of reaching the goals set under the cohesion policy. Earmarking the necessary funds for modern, highly functional infrastructure in the field of transport, information and communication technologies within the multiannual financial framework 2014-2020 will contribute to the adequate functioning of the single market".[8]

The general position[9] of Sofia towards the package acknowledges the role of the Structural Funds for achieving economic, social and territorial cohesion of the regions in the EU. Bulgaria calls for effective management of the funds without additional administrative burden for the beneficiaries and the delivery structures. An emphasis is put on the flexibility for member states to implement cohesion policy while taking into account local needs. A major concern is raised with reference to the proposed ceiling of 2.5% of GDP for the national cohesion allocations as it is not in line with the solidarity principle.

When it comes to the Common Provisions Regulation Proposal support is expressed for the adoption of a Common Strategic Framework and for a more focused approach through 11 thematic objectives. Bulgaria favours the introduction of ex-ante conditionalities as a guarantee for the effective implementation of the future programmes, as well as macroeconomic conditionalities which are believed to have a disciplining effect on member states. Approval is also given to the proposed instruments for territorial

8 *Parliamentary Committee on European Affairs and Oversight of European Funds (2011a)*
9 *European Affairs Council, Framework position 2011/0276 (COD) – 15 November 2011*

development (Community-led Local Development and Integrated Territorial Investments) and the extended scope of financial instruments for the next period. Multifund programmes financed by the Structural and the Cohesion Funds are also supported. Nevertheless, Bulgaria disagrees with a few parameters of the proposal, for example the introduction of the 5% performance reserve; as the proposed mechanism is not viewed as a tool for more effective implementation of programmes. The country does not favour the transfer of resources from the Cohesion Fund to the Connecting Europe Facility either.[10] Although approval is given for the suggested rates of co-financing for the CSF Funds in the less developed regions, objection is raised towards the current proposed rate of 75% for the ERDF for cooperation programmes.[11]

Green light is given to the European Regional Development Fund (ERDF) and the Cohesion Fund[12] (CF) Regulation Proposals in terms of the scope of support and the investment priorities. Bulgaria does not support the concentration requirement for 50% of the ERDF money to be allocated to thematic objectives 1, 3, and 4 because Sofia considers it as a restriction linked to the programming of the funds.[13]

As regards the European Social Fund Regulation Proposal,[14] here too, an approving statement has been issued referring to the scope of support. Bulgaria supports the concentration requirement of 20% for the thematic objectives of promoting social inclusion and combating poverty. Sofia opposes the concentration requirement at Operation Programme level of 60% of funds on up to 4

10 *European Affairs Council, Framework position, 2011/0302 (COD)*
11 *Krasteva, D. (27 January 2012)*
12 *European Affairs Council, Framework position, 2011/0274 (COD) – 15 November 2011*
13 *European Affairs Council, Framework position, 2011/0275 (COD) – 15 November 2011*
14 *Ibid.*

investment priorities and considers it a limiting requirement.

Discussing the European Territorial Cooperation Regulation Proposal,[15] positive feedback is given on the concentration of programmes on up to 4 thematic objectives and the possibility for a sole project beneficiary. The suggestion to merge the functions of the Managing Authority and the Certifying Authority is perceived as a viable option, while Bulgaria calls for the ability of each member state to authorise the Managing Authority to perform verification on its territory.

Finally, regarding the Proposal to amend Regulation 1082/2006 on European Groupings for Territorial Cooperation (EGTC),[16] Sofia welcomes the expansion of the scope of the regulation to allow participation of third countries in EGTC. Bulgaria opposes the proposal of the Commission to introduce a "Silent Consent System" that allows the establishment of an EGTC in the absence of justified objections of the national bodies within reasonable time.

Following the first positioning stages of the deliberations on the upcoming MFF, Sofia clearly emerged as one of the countries constituting the group of "Friends of Cohesion" (as opposed to "Friends of Better Spending"). On 1 June 2012 in Bucharest Bulgaria subscribed to the Joint Statement declaring the strategic importance of this policy area (see the full text in the Appendix). On 25 June 2012, 15 countries, Bulgaria included, submitted to the EU General Affairs Council a document[17] on the use of cohesion policy funds for quality investments. It was aimed at backing the "Friends of Cohesion" argument that cohesion policy contributed greatly to the economic and social cohesion

15 *Ibid.*
16 *Ibid.*
17 *Friends of Cohesion on Quality Investment, Room Document for 26.06 GAC*

of many regions in the EU. One of the good examples in particular was the Sofia Metro, with the building of 11 new stations and 10.5 km of lines.[18]

To sum up, Bulgaria considers the financial resources for cohesion policy in the Commission's proposal as the absolute minimum to which no additional cuts should be made.

3.4. Energy policy

Energy policy is one of Bulgaria's main concerns, especially since the gas crisis in 2009 when the vulnerability of its gas supplies and the heavy dependence on Russia was revealed.

In June 2011 the National Energy Strategy until 2020 was adopted, under the title "For Reliable, More Efficient and Clean Energy". It represents the political vision of the government in compliance with the current European framework of energy policy and the world trends in terms of energy technology. The Energy Strategy aims at tackling the major challenges ahead of Bulgaria's energy sector, namely: 1) high energy intensiveness of GDP – energy intensiveness of the national GDP (at purchasing power parity) is 89% higher than the EU average; 2) high dependency on energy resource imports – Bulgaria meets 70% of its gross demand through import and has a traditional single origin – the Russian Federation; 3) necessity for environmentally sound development.

The main priorities in the Energy Strategy can be summarised in the following five directions: to guarantee the security of energy supply; to attain the targets for renewable energy; to increase energy efficiency; to develop a competitive energy market and policy for the purpose of

18 *MFA website, 26 June 2012*

meeting the energy needs, and to protect the interests of the consumers.

In the context of the Fukushima nuclear disaster in 2011 it became particularly challenging for Sofia to convince its European partners that it is justifiable to continue developing nuclear energy (hopefully also with EU financial support) with a particular focus on the construction of the Belene nuclear power plant. It was meant as a substitute for the loss in electricity supply after gradually decommissioning the Kozloduy nuclear power plant – a responsibility Bulgaria has assumed as part of its Accession Treaty to the European Union. At the end of March 2012, the government announced that it had given up on Belene NPP, clarifying that the Russian reactor that had already been ordered would be delivered and installed as a new unit in Kozloduy. Additionally, further efforts would be focused on prolonging the life of the two operational reactors while the infrastructure available at the Belene platform could be used for a gas power plant.

So far the country has twice become subject to criticism on behalf of the European Commission due to the insufficient harmonisation of EU directives on the single European energy market. In November 2011, Brussels initiated a procedure against Sofia for failure to provide equal access of suppliers to its gas market. On 27 February 2012, the European Commission sent 15 reasoned opinions to 8 member states, including Bulgaria, to urge them to comply with their legal obligations under the Electricity and Gas Directives of the Third Energy Package that needed to be transposed by 3 March 2011. Minister Delian Dobrev explained that the obstacle for the implementation of the gas directive lies in a few confidential clauses in the transit contracts but Russian Gazprom approved their disclosure at the end of 2011 and the documents were handed over to

the Commission in the beginning of 2012.[19]

3.5. External relations, enlargement, neighbourhood policy

The accession to the EU at the beginning of 2007 marked the achievement of the main strategic foreign policy priority of several consecutive Bulgarian governments. Now the focus is on the successful involvement in the multilateral coordination and decision-making in the Union. Sofia is working hard on concluding the European integration process by joining the economic and monetary union and the Schengen space. The country would like to gain a leading role in the formulation of the European policy towards the Western Balkans and the Black Sea region. In fact, Bulgaria wants to be a major factor of peace and stability in the region while also developing relations based on equal partnership with Russia. All foreign policy moves are however formulated through the prism of the country's EU membership and in consonance with the Euro-Atlantic realities, with the aim of contributing to the stability of the region.[20]

Special attention is paid to the active participation in the implementation of the EU's common foreign and security policy (CFSP) as well as the common security and defence policy (CSDP). Currently, Bulgaria contributes or has recently contributed to a dozen of EU-led civilian missions and military operations.

In March 2012 during an ambassadorial conference, aimed at discussing and clarifying the new foreign policy priorities with reference to the current national agenda, Minister Nickolay Mladenov pointed out that diplomacy must facilitate the country on its way out of the crisis by

19 *Dnevnik.bg, 3 April 2012*

20 *Ministry of Foreign Affairs of the Republic of Bulgaria (2012)*

attracting foreign investors and placing Bulgarian business on foreign markets.[21]

Bulgaria has always been a strong supporter of the EU's enlargement and has officially listed this issue among the country's priorities within the MFF 2014-2020 debate (General Affairs Council of 26 March 2012).[22] Sofia views the European integration of all Western Balkan countries as one of the key tools for tackling complicated ethnic issues and history-related sensitivities on the peninsula, thus bringing stability to the region in general. Bulgaria has expressed its willingness to assist those states every step of the way through the exchange of good practices, lessons learned and practical advices on the negotiation procedure. A concrete example of such a commitment is the introduction of the Sofia Forum for the Balkans. It is "an annual meeting of high-level policy and opinion-makers from the Balkans, together with their counterparts from the EU, the United States, the Middle East and North Africa, for in-depth discussions about key issues that, although regional in nature, concern Europe and the transatlantic relationship."[23]

Prior to the Council decision granting Serbia candidate status (1 March 2012) Bulgaria's MFA published an official statement once again confirming the country's commitment to supporting the European integration process of Serbia and Kosovo.[24] Foreign Minister Mladenov welcomed the agreement signed on 24 February 2012 between Belgrade and Pristina on Kosovo's regional representation and on the joint management of border crossing.[25]

Sofia is among those member states that openly

21 *Bulgarian Diplomatic Institute (April-May 2012)*

22 *Kilnes and Sheriff, April 2012, p. 4*

23 *http://www.sofiaforum.org*

24 *MFA website, 23 February 2012: http://www.mfa.bg/en/news/view/32403*

25 *MFA website, 24 January 2012: http://www.mfa.bg/en/news/view/32408*

support on high political level Turkey's accession to the Union, although there are some minor bilateral and border issues that are yet to be properly addressed and resolved. Staying faithful to its principal position of supporting all states striving towards EU membership, Sofia has long ago expressed its support for Iceland's integration when the island state first filed its application in 2009.

Geographic and historical specificities (country's traditionally friendly and reputable bilateral relations with the states of the former Soviet bloc, North Africa and the Middle East) determine Bulgaria's interest in both the southern and eastern dimensions of the European neighbourhood policy. Sofia has declared ENP among its priorities under the MFF 2014-2020 Heading 4 expenditure[26] but so far has failed to demonstrate a sufficiently consistent and focused approach towards the countries involved in it, especially in Eastern Partnership.

For instance, Bulgaria's Foreign Minister, Nickolay Mladenov initiated the so-called Sofia Platform (Bridging Europe and the Middle East)[27] – an international forum to facilitate the exchange of experience in democratic transition with special regard to the recent revolutions under the sign of the Arab spring. On the 20 June 2011 EU Foreign Affairs Council Mr. Mladenov declared: "In order for democratisation in North Africa and the Middle East to succeed, the EU must help bolster their civil societies. That is why Bulgaria supports the formation of the European Fund for Democracy, which eases the access of young non-profit organisations from the region to European financial support."[28]

Bulgaria's commitment to the countries of the eastern

26 *Kilnes & Sheriff, p. 4*
27 *http://www.sofiaplatform.org/*
28 *MFA website, 20 June 2011: http://www.mfa.bg/en/news/view/31455*

dimension is marked by the 2010 appointment of the former Prime Minister Phillip Dimitrov as Head of the EU's Delegation to Georgia – an extremely valuable diplomatic achievement for a new member state. In late 2011, Minister Mladenov supported the initiation of negotiations on a deep and comprehensive free trade agreement (DCFTA) with Tbilisi in a joint letter with his counterparts from the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland and Romania.[29] Similar backing was offered to Moldova's negotiations on a DCFTA in December 2011.[30]

3.6. Special issues for Bulgaria

Upon entering the EU in 2007 Bulgaria has set as one of its prime goals membership in the Schengen zone and has continuously worked towards meeting all technical requirements. Corruption, inefficient judiciary and organised crime are the main concerns that prevent the country from joining the "border-free" area. Prime Minister Boyko Borisov and his Deputy as well as Minister of the Interior Tsvetan Tsvetanov put it as a chief objective on their European agenda for 2011: "I think the entry into Schengen is a national priority for both the government and the Bulgarian citizens."[31] But Bulgaria's membership in Schengen did not materialise due to the Dutch veto in a Council vote on 22 September 2011. As one of the EU's founding members, the Netherlands expressed their doubts in terms of Bulgaria's capacity to ensure border stability and prevent criminal elements from entering the area. The situation was aggravated by fears over waves of mass immigration through Greek territory triggered by the revolutions in the Arab world.

29 *MFA website, 15 November 2011: http://www.mfa.bg/en/News/view/32014*
30 *MFA website, 16 December 2011: http://www.mfa.bg/en/News/view/32161#*
31 *Kovacheva, R. (2011a)*

During the last meeting in 2011 of the Justice and Home Affairs Council (12 December 2011) a compromising arrangement was proposed by the Polish presidency – a two-step entry with air and water borders opening in March 2012 and full-fledged membership (land borders) set for June 2012, provided all countries reach unanimity at the time. However, the Netherlands refused to re-examine their stance prior to the emergence of the next progress report under the cooperation and verification mechanism (CVM) for Bulgaria.

After the disappointing outcome in September 2011 the Minister of Foreign Affairs warned that "The Bulgarian citizens are not second-class citizens in Europe, nor is Bulgaria's EU membership a second-hand one" and in case of an unfavourable vote outcome Bulgaria "shall need to carefully consider our entire policy from now on regarding the support we give to the reform of the European legislation on Schengen".[32]

On 8 February 2012 emerged the long-anticipated CVM report but it once again proved insufficient for the Netherlands to change their stance. Prior to the European Council on 1 March 2012 the Dutch Prime Minister Mark Rutte announced that "We need two [cooperation and verification mechanism] reports that point in the right direction."[33] With this statement he hinted at the importance of the annual progress report scheduled for July 2012. Consecutively, the conclusions from the European Council meeting postponed the decision for September 2012 and summarised the situation in this way: "The European Council, recalling its discussions in 2011, reiterates that all legal conditions have been met for the decision on Bulgaria's and Romania's accession to the Schengen Area to be taken.

32 *Kovacheva, R. (2011b)*
33 *Vogel, T. (2012)*

[...] The European Council requests the Council, during the intervening period, to identify and implement measures which would contribute to the successful enlargement of the Schengen Area to include Romania and Bulgaria."[34]

4. Summary and conclusions

Being part of the most recent enlargement wave, Bulgaria has yet to discover and utilise its potential for policy and decision-making impact. It is often the case for official Bulgarian positions within the current EU agenda to be unavailable to the public. Therefore, conclusions on the positions of Sofia could be sometimes drawn only and entirely on the basis of interviews and public events with the participation of high-level decision-makers. This hampers substantial national debates on future EU policies and reforms and prevents public opinion from receiving a clear picture on what Bulgaria wants to achieve at EU summits and how the country defends it.

Nevertheless, recently a slight change has emerged with reference to the debt crisis and the demand for new financial and fiscal regulation. The Bulgarian government saw it as an opportunity to highlight the country's strong points, namely one of the lowest levels of public indebtedness in Europe, fiscal discipline, prudent and conservative financial policy, stable macroeconomic framework leading to the only improvement in credit rating among EU countries in 2011. Those actions could be viewed as an attempt to re-shape the popular image of Bulgaria as a land of corruption, organised crime and inefficient judiciary and pave its way to the Schengen area and to the common currency – a goal that the country continues to pursue although with some

34 *European Council 1/2 March 2012 Conclusions, items 40-43*

pre-conditions and concerns over the final outcome of the debt crisis in the eurozone. In this regard, stability and fiscal discipline may be utilised as political tools to ensure better negotiation positions for Bulgaria in the debate on the new multiannual financial framework for 2014-2020.

It is worth noticing that Bulgaria's key priorities in this perspective involve the preservation or even increase of funding in areas that Bulgaria considers vital for its further development. To a certain extent those efforts correlate to the current financial framework during which capacities needed for the absorption of EU funds still lag behind the EU average. Now, five years after accession, the government believes that the system's bottlenecks such as bad programming, administrative burden and misappropriation practices have been resolved to a sufficient degree and hopes for a re-run of funding opportunities.

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CZECH REPUBLIC

Gábor Túry

1. Domestic political framework, EU strategy of the government

1.1. Overview of internal politics

The Czech government has a strong majority in the lower house (parliament) since the end of July 2010 when the President gave the mandate to Petr Nečas as Prime Minister. The right-wing coalition was formed by the Civic Democratic Party (Občanská demokratická strana), the Tradition Responsibility Prosperity 09 (TOP 09 – Tradice Odpovědnost Prosperita 09) and the party called Public Affairs (Věci veřejné). The Prime Minister has a strong mandate in the government preventing from instabilities typical for the previous coalition. This political stability is indispensable for an effective post-crisis management. Nevertheless, since the foundation of the government 10 ministers (from 9 portfolios) left the government which means more than two thirds of the ministers were changed. There was some turbulence inside the coalition because of corruption

affairs of some ministers. At the end of 2010, Pavel Drobil the Minister of the Environment was sacked because of corruption charges. A year later, in October 2011, the Prime Minister fired the Minister of Agriculture, Ivan Fuksa because Mr. Nečas was unsatisfied with his work in the ministry. But political analysts pointed out that in reality this reflected the internal conflicts inside ODS, because Fuksa is a member of the internal opposition within the party, led by Petr Tluchor.

The biggest challenge for the Czech Republic has recently been the economic downturn of the international markets. The post-crisis period overwrote all expectations. The government had to solve the post-crisis social and economic problems, launching economic stimulus programmes while maintaining the fiscal balance. The government launched and implemented such forward-looking structural changes of the public household as the multi-pillar pension system and the new system of financing the healthcare services. The restrictive measures and the structural reforms encountered considerable social resistance. In July 2011, the workers of transport companies held a 24-hours strike against the restrictive (reform) measures of the government. The Prime Minister declared that the government is ready for some compromises but the reform will be implemented.

Inside the government the most crucial conflict was recently in the case of the so-called Fiscal Compact which finally had not been ratified by the Czech Republic (similarly to the United Kingdom). The TOP 09 led by the Deputy Prime Minister and Minister of Foreign Affairs, Karel Schwarzenberg threatened to leave the coalition if the Prime Minister was not to sign the document. However, the position of Nečas was steady on this, similarly to Václav Klaus the President of the Czech Republic, who said he would never sign such an agreement. The Prime Minister actually declared his

country had three objections to the initiative.[1] First, the ratification process would be quite complex and President Klaus would not sign it anyway. Secondly, he stated that this agreement would bring nothing for the country. The right to take part in the official euro summits would not increase the Czech Republic’s limited possibilities to real participation in the deliberations. Thirdly, insufficient attention is being paid to the debt criterion whilst, according to the Czech position, the current crisis was mainly due to debts.

Behind these arguments however internal political motivations can be found as well; introducing tighter EU control of national budgetary policies might worsen Nečas’ long-term positions not just inside the ODS but in the parliament as well.

1.2. EU strategy of the government

Concerning the great variety of the parties in the Czech legislature (see tables below) it is no wonder that the two chambers have thus far taken a different approach to dealing with EU issues.[2] While the coalition has notable majority in the lower house, in the upper house the situation is the opposite. Therefore, while the Chamber of Deputies is more eurosceptic, the Senate is more supportive vis-à-vis issues of European cooperation, including the future reforms of the EU.

1 *Král, D. (2012)*
2 *Král, D. – Bartovic, V. (2010)*

Czech Senate *(upper house of October 2012)*

		Ideology	Seats	%
coalition	Civic Democratic Party	Liberal conservatism	25	31
	Coalition STAN (Mayors and Independents)+TOP09	Conservatism	3	4
opposition	Czech Social Democratic Party	Social democracy	41	51
	Christian and Democratic Union – Czechoslovak People's Party	Christian conservatism	5	6
	Communist Party of Bohemia and Moravia	Communism	2	2
	Independent candidates		5	6
	Total		**81**	**100**

Website of the Senate[3]

Czech Chamber of Deputies *(lower house, parliament)*

		Ideology	Seats	%
coalition	Civic Democratic Party	Liberal conservatism	53	27
	TOP 09	Conservatism	41	20
	Public Affairs	Conservative liberalism	24	12
opposition	Czech Social Democratic Party	Social democracy	56	28
	Communist Party of Bohemia and Moravia	Communism	26	13
	Total		**200**	**100**

Website of the Chamber of Deputies[4]

3 http://www.senat.cz/senatori/zasporadek.php?lng=cz&kedni=29.10.2012&O=8

4 http://www.volby.cz/pls/ps2010/ps52?xjazyk=EN

The core concept of the government and the Ministry of Foreign Affairs about European cooperation is that the European Union is not an aim in itself but integration means a set of opportunities and tasks via which the member states can achieve their goals.[5] The strategy and the action plan of the government are based on this approach. At the EU level, the Czech politicians are active in searching for the potential coalition partners to ensure the representation of the interests of the country. Their main priority areas include: strengthening the influence in the decision-making mechanisms, strengthening the competitiveness of Europe as a whole, common economic and financial stability, energy security, reinforced role of the Czech Republic and of the EU in the world. The well-known Czech euroscepticism can be detected in the fact that the country did not join either the Euro Plus Pact or the Fiscal Compact and it is among the last ones to deposit the ratification of the amended Article 136 of the TFEU.

As regards interest representation in practice, the case of the excessive deficit procedure coupled with suspending some cohesion assistance against Hungary was a good example. In early 2012, the Czech Prime Minister called on his EU partners to wait with this decision. Mr. Nečas also asked for the clarification of the concrete conditions under which such a severe sanction can be lifted. (This argument was however not supported by the Slovak Prime Minister of the time, Iveta Radičová.) The Czech standpoint against the EU decision in March did not come as a surprise. The reason behind was the fact that, at the same time, the European Commission wanted to freeze the transfers from the Cohesion Fund to the Czech Republic because of inadequate auditing and monitoring system of the payments.

The following example also illustrates how the country

5 *Government of the Czech Republic (2011a)*

is asserting national interests and promotes a desired model of European integration. In February 2012, the Czech Prime Minister and the British Prime Minister, David Cameron wrote a joint letter to the head of the European Council, Herman Van Rompuy about an initiative seeking economic growth and completion of the single market.[6] The “Plan for Growth in Europe” was signed by 13 EU member states.[7] The signatories of the letter stressed that the future growth of the European Union is impossible without further reduction of the remaining barriers. These restrictions are obstructing the trade of goods and services, for example in the energy and digital market and in the science and research area as well.

2. General economic analysis

2.1. Overview of main macroeconomic developments

The Czech economy – after the reform period of the late 1990s marked by structural changes in the Czech industry as a whole, and since the beginning of the 2000s – has been moving together with the international economy. That is why with the current financial and economic crisis the Czech figures showed an immediate decline too. If we take into account a longer period, the most dynamic development was registered in the mid-2000s when the economic growth was around 7%. Economic downturn could not have come at the worst moment. Shrinking external demand checked the promising trends. From 2007 till 2009 (the deepest point) the GDP fell by 11 percentage points.

In 2010, after the worst year when the drop was close to 5%, GDP growth was better: 2.7%. But since that year, growth has been sluggish. It seems that the Czech economy, just like the European and other developed economies, was not able to reverse the negative growth trends in the short run. In 2011, only the performance of foreign trade could – to some extent – moderate the decline of overall economic development (see Table 1). At the same time, consumption of households as well as government consumption showed worsening figures. Based on the latest (June 2012) forecast economic revival will be postponed to the year of 2013, while 2012 will be marked by stagnation. The reason of this negative trend is the shrinking demand of both households and government. The third pillar of GDP growth, namely net export has been positive since 2010 but its dynamism has been weakening since 2011.

Table 1, Main macroeconomic indicators of the Czech Republic

	2009	2010	2011	2012 (f)	2013 (f)
Real GDP growth rate (annual change, %)	-4.7	2.7	1.7	0.0	1.5
GDP/capita, EU27=100	82	80	80	n.a.	n.a.
Gross fixed capital formation/GDP (%)	24.8	24.4	23.9	23.6	23.7
FDI inflow (BEUR)*	2.1	4.6	3.9	3.5	n.a.
Private consumption/GDP (%)	50.3	50.3	50.5	51.0	50.9
Public consumption/GDP (%)	21.7	21.4	20.9	20.4	20.1
Exports of goods and services (BEUR)	84	101	116	122	n.a.
Imports of goods and services (BEUR)	79	97	110	115	n.a.
Current account balance/GDP (%)	-3.4	-4.4	-3.6	-3.2	-3.2
Unemployment rate (%)	6.7	7.3	6.7	7.2	7.2
Inflation (HICP)	0.6	1.2	2.1	3.3	2.2
Interest rates (10y)	4.84	3.88	3.71	n.a.	n.a.

*Eurostat, European Commission, * WIIW (f = forecast)*

6 *Prague Daily Monitor (20.20.2012)*
7 *Government of the Czech Republic (2012a)*

2.2. Fiscal stability, economic and social competitiveness

The update of the Convergence Programme for 2011-2015 was approved in April 2012 by the Czech government. It includes all recommendations issued by the European Council, and the programme is harmonised with the National Reform Programme too.[8] The document includes a response to the management of the anti-crisis programmes which caused budgetary imbalances. The goals are the following: consolidation of the public budget is the priority for the coming period. The consolidation efforts focus not only on reducing the general government deficit but also on improving structural parameters of the system, such as the quality of public finances, support for the business environment, bureaucracy reduction, fighting corruption, and strengthening the Czech economy's pro-growth attributes.[9]

In 2011, the wages in the state administration were reduced by 10% and the remuneration of judges and institutional officials was also lowered (see Table 2). On the other hand, wages in education were increased. Social transfers were eliminated or their size reduced. General cuts in the state budget were made, thus non-mandatory regular and capital expenditures were also decreased. On the revenue side, the amount of social security contributions was maintained and, motorway toll rates were increased. The volume of the changes equals 2.1% of GDP, and concerns mostly the expenditure side. The measures resulted in a lower budget deficit in 2011 (3.1%). In accordance with the excessive deficit procedure, the government continues the consolidation measures in 2012 too. The official deficit target for 2012 was therefore revised downwards and a

8 *Government of the Czech Republic (2012b)*
9 *Ministry of Finance of the Czech Republic (2012a)*

2.9% rate can be expected which can further improve in 2013 (see Table 3).

Table 2, Structure of active measures carried out *(% of GDP)*

	2010	2011	2012
Direct taxes	0.3	0.5	-0.3
Indirect taxes	0.8	0.0	0.6
Other revenues	0.1	0.3	0.2
Social benefits	0.3	0.2	-0.1
Government sector wages	0.2	0.2	-0.1
Other expenditures	0.5	0.4	0.4
Total impact on balance	2.2	1.6	0.7

Ministry of Finance of the CR

Table 3, Public finances in the Czech Republic

	2009	2010	2011	2012 (f)	2013 (f)
Public budget balance (% of GDP)	-5.8	-4.8	-3.1	-2.9	-2.6
Public debts (% of GDP)	34.4	38.1	41.2	43.9	44.9

Eurostat, European Commission (f=forecast)

To promote the deficit cut, in August 2011 the Czech government approved the reform of the tax system to ensure sustainability of the budget. The basis of the reform is simplicity coupled with eliminating all exceptions. The former system will be replaced by a new and transparent system and in the case of income tax and corporate tax an equal flat rate of 19% will be introduced. All tax exceptions and allowances will be cancelled, and the reform will abolish the tax holiday for meal passes. For the corporate sector, the only way to get tax allowances is if they engage in development. The reform has many opponents in the trade unions, in the left-wing opposition parties and within

the coalition as well. The implemented tax reform will immediately decrease the revenue side of the budget by 8.9 billion crowns in 2013 and by another 22 billion crowns in 2014[10] (1 euro = 25 crowns).

In connection with the National Reform Programme the ECOFIN Council recently highlighted the weakest points of the economy which stand in the way of growth. These are the following:[11]

1. *high structural deficits and the long-term sustainability of public finances;*
2. *the continuing structural weaknesses in the labour market;*
3. *continued barriers to business and a lack of efficient public administration and legal framework;*
4. *lack of economic diversification resulting from a lack of support for innovative capacity and corporate research and development;*
5. *low labour productivity due to inadequate knowledge and skills;*
6. *inadequate backbone transport infrastructure network.*

To give the adequate answer to the above statements and to respond to the Council's specific recommendations addressed to the Czech Republic, in July 2011 the updated National Reform Programme for 2012 was approved. To this document the Council has formulated 6 recommendations which are the following:[12]

1. *sustainable public budget (taking measures against revenue shortfalls or expenditure slippages);*
2. *implement the planned pension reform in order to improve the long-term sustainability of public finances;*
3. *enhance participation in the labour market by reducing the barriers for parents with young children to re-enter the labour market;*
4. *improve the performance of the public employment service;*
5. *improve the performance of the public employment service in order to increase the quality and effectiveness of training, job search assistance and individualised services, linking funding of the programmes to results;*
6. *enhance the effectiveness of the public administration.*

10 *Ministry of Finance of the Czech Republic (2011)*
11 *Government of the Czech Republic (2011b), pp. 7-8*
12 *Government of the Czech Republic (2012b), pp. 10-11.*

In June 2012, the reaction of the Commission to the Czech Convergence Programme was published. The European Commission approved the government measures aimed at improving the fiscal balance. They stressed to continue the current measures for consolidation of public finances accompanied by restructuring the expenditure side. The recommendations adverted to the education system as well, and underlined the importance of equal opportunities on the labour market too. Long-term sustainability of the pension system is a crucial element in public finance consolidation. The Czech government has approved the new multi-pillar pension system to prevent further imbalances of the pay-as-you-go (PAYG) system. The new scheme (based on voluntary participation) will however not solve the financing problem of the current pension system. Therefore the European Commission called for further measures in

this policy area.

As regards the Czech competitiveness performance in the light of the Europe 2020 strategy (see Table 4) the country has a relatively good record. The employment rate is above 70% and the national target is to reach 75% by the end of the decade. Progress is being made towards this target, although beyond the government's pro-employment policy the process is exposed to cyclical developments too. Spending on research and development is among the highest in the EU10 region. As to early school leaving, the country is already one of the best performers with a rate of 5.4% in 2009 and 4.9% in 2010, both well below the EU target. The rate of diploma holders has also improved from 17.5% in 2009 to 20.4% in 2010. Thanks to the high number of students currently enrolled in tertiary education, this indicator is expected to increase further (the national target being 32%). The number of persons at risk of poverty or social exclusion is still below the 2008 level (1.566 million) and stood at 1.495 million in 2010; thus the trend is an improving one. The target is to reduce the number of those in such a situation by 30,000 by 2020. With regard to energy efficiency the Czech authorities have not yet set the national target, the method of assessing national progress on energy efficiency is currently under discussion between the institutions in the context of the proposed Energy Efficiency Directive. Concerning renewable energy sources, their share in gross final consumption was 8.5% in 2009, while in the field of transport it was 3.4%. The national target is to reach 13% of renewables in energy consumption and 10% in all modes of transport by 2020.

Table 4, Europe 2020 targets of the Czech Republic

Europe 2020 targets	Situation in the Czech Republic in 2010	Czech Europe 2020 targets
Employment rate – 75% of 20-64 year-olds	70.4%	75%
R&D – 3% of GDP to be invested in R&D	1.6%	1% of public sector spending
Climate change / energy		
Reducing greenhouse gas emissions by at least 20%	68% of the 1990 level	-9% compared to the 2005 level
Covering 20% of energy consumption from renewables	8.5%	13%
Energy use in Mtoe (2009) Increasing energy efficiency by 20%	42.29 Mtoe	n.a.
Education		
Reducing school drop-out rates below 10%	4.9%	5.5%
Reaching tertiary education attainment by at least 40% of 30-34 year-olds	20.4%	32%
Poverty / social exclusion Reducing the number of people in or at risk of poverty or exclusion by 20 million	14.4% of the population	-30,000

European Commission

3. Position and potential impact of the Czech Republic on current key issues

3.1. EU budget: the multiannual financial framework for 2014-2020

When Prague hosted a Prime Ministers' meeting in October 2011, the key massage about the next financial framework (2014-2020) was the following. "The future EU budget must contribute to strengthening of the EU's competitiveness and

growth while ensuring its internal cohesion."[13] The Czech Republic emphasises that the rules on fair competition should define the future development strategies. The Czech industry, especially the manufacturing industry, was successful in the last decade. After the economic reforms and the real privatisation were finished, Czech companies – owned by foreigners, Czech owners or by the state – showed an outstanding performance. They won several public procurements and benefited from EU development funds not just in the Czech Republic but in the Central European region as well.

As regards the country's concrete stance on the proposed size of the MFF, the Czech Republic belongs to the group of countries that focus on better spending (against spending more). Prague would not like to see an increasing EU budget and is particularly hostile towards any EU-level taxation[14] as proposed by the Commission (namely, the EU VAT and the financial transaction tax).

3.2. Common agricultural policy after 2013

Future plans on the CAP direct payments are one of the major issues concerning the next financial period. The Czech Republic agrees with the principle of evening out direct payments across the EU but the Minister of Agriculture is strongly opposed to capping payments for large farms.[15] The average agricultural farm size of the country is rather big as a result of historical heritage. With the new system as proposed by the Commission, Czech farmers would lose 26-59% of total direct payments. That loss of income will cause

13 *Visegrad Group Presidency Communication on multiannual financial framework http://www.vlada.cz/assets/media-centrum/aktualne/Visegrad-Group-Presidency-Communication-on-Multiannual-Financial-Framework.pdf*
14 *Europolitics (27 January 2012)*
15 *Euractiv (26 April 2011)*

notable competitive disadvantage. Therefore, a number of EU member states, including the Czech Republic, strongly disagree with the European Commission proposal. Apart from the Czech Republic, Germany, Italy, Slovakia, Romania and the United Kingdom have also signed a declaration in that regard.

The Czech Republic agrees with the principle of pursuing environment-friendly agricultural activities but is convinced that more incentives can be introduced via the present system (e.g. cross-compliance). Therefore the proposed measures aimed at making 30% of the payments conditional on the so-called greening are not welcome by Prague in their present form (due to increased red tape and potential sanctions). Maintaining the coupled payments is justified according to the Czech position and its scope could even be extended further (e.g. to include pigs).[16] The idea of gradually evening out direct payments is supported by the Czech Republic, while its status is not going to alter significantly according to the proposed scheme.

3.3. Cohesion policy after 2013

As regards financing cohesion objectives between 2014-2020, there is an obvious intention to reduce the budget of the Structural Funds by the net contributors of the EU budget. Even though the Czech Republic is against a general increase of the EU budget (as mentioned above), the country strongly opposes any cuts made to cohesion spending in the upcoming multiannual budgetary period. In other words, the Czech Republic insists on maintaining the current system of cohesion funding.

16 *The Czech Republic's views on the CAP reform proposal http://eagri.cz/public/web/file/150207/Pozice_SZP_CZ_final_AJ.doc*

Government priorities under the future cohesion policy are articulated in the National Development Programme. The Czech Republic puts emphasis on the partnership principle in the future cohesion policy and wants to ensure the intersection of transnational, national, regional and local (municipal) priorities. According to Prague, this approach must be better reflected in the decision-making processes as well.[17]

On the basis of the document entitled "Position of the Czech Republic on the future of EU cohesion policy after 2013"[18] the Czech Republic wants to maintain the current system of financing. The paper emphasises that it is an important instrument to close the gap between the poor countries or regions and the developed ones. It has three main roles such as solidarity, cohesion and partnership. What is crucial about the goals after 2013 is that cohesion policy should maintain its achievements and, at the same time, strengthen linkages with the objectives of the Europe 2020 strategy where appropriate. Therefore the main expectations vis-à-vis the future cohesion policy are the following:

- *concentrating support on less developed member states and regions;*
- *maintaining its added value by supporting areas where the Community intervention is more effective than the national one;*
- *further deepening the European Territorial Cooperation at the cross border, interregional and transnational level;*
- *as regards sustainable development, successful coping with "new" challenges of a pan-European nature requires sharing of objectives and coordination of procedures together with consistent application of the subsidiary principle.*

Furthermore, the Czech Republic welcomes the attention paid to urban issues and the introduction of an integrated approach to the support of the development of cities. The cities play a key role in regional development. As regards the proposed Connecting Europe Facility the Czech Republic is not against it but as the joint declaration[19] by the Visegrad countries and Slovenia of 22 March 2012 put it, these countries "express their opposition to the proposed transfer of 10 billion euro from the Cohesion Fund budget to the Connecting Europe Facility with distinct objectives and rules". The Czech Republic has also reservations vis-à-vis the capping of assistance at 2.5% of GDP.

3.4. Energy policy

The Czech Republic consumed 42.29 million tonnes oil equivalent energy according to the 2009 statistics of the EU's Energy Portal.[20] After Belgium this was the second highest rate among the five 10 million countries of the EU and was higher than that of Romania. The country has one of the lowest energy dependency levels in the EU with a ratio of just 27% (the EU average being around the double).[21] In the Czech Republic the biggest consumers of energy are industry and transport followed by households and services. Consumption and production patterns differ greatly: within

17 *Government of the Czech Republic (2011b), p.18.*

18 *Position of the Czech Republic on the future of EU cohesion policy after 2013 http://ec.europa.eu/regional_policy/archive/conferences/4thcohesionforum/doc/contributions/cz_nat_cont_en.pdf*

19 *Joint Declaration of the Visegrad Group of Countries and Slovenia on the Commission's Proposals for the Future Cohesion Policy Regulatory Package*

20 *http://www.energy.eu*

21 *Ibid.*

consumption solid fuels, petroleum products, gases and nuclear power play an important role while production is mostly concentrated on solid fuels and nuclear power.[22]

Concerning strategic issues, the government set the national target of maintaining the current pace of decline in energy intensity, which is also in line with the target of 20% higher energy efficiency set by the EU.[23] With a view to decreasing pollution and promoting sustainability the Czech Republic also pledged to cover 13% of its energy consumption by renewable sources by 2020 (the current rate being above 8%). This was laid down in the strategic document entitled "National Renewable Energy Action Plan of the Czech Republic".[24]

The Czech Republic has been emphasising the importance of strengthening the single European market since it entered the European Union. The Czech Republic and the United Kingdom put recently forward a joint initiative to liberalise further the EU's energy market as well. Not surprisingly, since the CEZ (České Energetické Závody i.e. Czech Power Plants) is the biggest public energy company in Central and Eastern Europe and has therefore a basic interest in liberalising the energy market in the European Union.

3.5. External relations, enlargement, neighbourhood policy

Concerning the EU's common foreign and security policy the Czech standpoint emphasises the sovereignty of the member states.[25] The country intends to continue its strong engagement in EU activities in the neighbourhood,

22 *http://www.energy.eu/country_overview/Czech_Republic_2011.pdf*
23 *Government of the Czech Republic (2011b), pp. 67-68.*
24 *Ministry of Industry and Trade (2010)*
25 *Ministry of Foreign Affairs of the Czech Republic (2011)*

especially in the Western Balkans, Eastern Europe, Southern Caucasus and the Middle East. Prague will continue to support the European and Euro-Atlantic course of foreign policy provided it is backed by the society. Actually, the Czech Republic takes part in the funding and implementation of European development cooperation and humanitarian aid as well as in some EU missions carried out in the framework of common security and defence policy. Namely, the Czech Republic took part in the EUFOR RD Congo mission in the Democratic Republic of Congo from July 2006 till November 2006, in the EUFOR Althea mission[26] in Bosnia and Herzegovina from December 2004 till June 2008, and again from June 2010 on, and recently also joined the EU NAVFOR "ATALANTA" mission in Somalia to protect vessels from piracy. [27]

Concerning the question of EU enlargement, the standpoint of the Czech Republic is supportive. Prague would welcome Iceland in the EU and because of some economic reasons it also supports the membership of Turkey.[28] The Czech Republic has not just corporate interests (CEZ), but the Turkish market is important for a great number of other Czech companies too. The Western Balkan region has a high priority in the Czech external relations; the country has been participating in peacekeeping operations of the United Nations there. Prague is interested in the stability and prosperity of the region and once the membership criteria are met all these countries should be able to join the Union.

The Czech Republic would like to see a balanced EU approach towards the southern and eastern neighbours and in the Czech view the European neighbourhood policy must

26 *To provide deterrence and to contribute to a safe and secure environment for the implementation of the 1995 Dayton Agreement.*
27 *Ministry of Defence and Armed Forces of the CR – current deployments*
28 *Bartovic, V. – Král, D. (2010)*

be based on the true will of the individual partner countries to cooperate and implement reforms. Partnership with the Eastern European countries i.e. with the former Soviet Republics has a high priority in the Czech diplomacy. The Eastern Partnership initiative during the Czech presidency in 2009 highlighted that next to the economic relationship the political relations must have an important role as well. Even though the Czech diplomacy can be very pragmatic, the question of democracy and human rights is also a crucial point in the context of the bilateral relations.

4. Summary and conclusions

In the Czech Republic – despite conflicts between the coalition partners – the internal political situation is stable: a three-party centre-right coalition is governing the country. Internal tensions are however present especially as regards structural reforms and EU policies. In the latter field it is important to highlight that the government, and especially the President, are rather eurosceptic. The cautious or even distant attitude of the Czech political leadership is well demonstrated by the fact that the Czech Republic is not a signatory party either to the Euro Plus Pact or to the Fiscal Compact. The crisis hit the highly export-dependent Czech economy very harshly. Growth is still sluggish, consumption has not recovered yet. At the same time, the government has been introducing restrictive measures to consolidate public finances. The Czech Republic has reservations vis-à-vis the Commission's proposal on the upcoming MFF especially as regards the increase of bureaucracy involved with the proposed greening or the capping of direct payments to big farms (typical for the country). The system of cohesion assistance should not change substantially according to Prague which does not support channelling money away from less developed countries and regions to richer ones. The Czech Republic has one of the lowest energy dependency rates in the EU nevertheless it is keen on having a real European energy market with more interconnection projects. Prague is willing to promote enlargement towards all European countries which meet the necessary criteria. It also backs the Eastern Partnership programme of the EU.

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ESTONIA

Ahto Lobjakas

1. Domestic political framework, EU strategy of the government

1.1. Overview of internal politics

The President of Estonia, Toomas Hendrik Ilves was re-elected on 29 August 2011 in a parliamentary vote for a second five-year term. Supported by the two partners in the governing coalition, the Reform Party and the Respublica and Pro Patria Union, as well as the oppositional Social Democrats, Ilves received 73 votes out of a total of 101.

The current government was re-formed in the wake of the 6 March 2011 elections by the Reform Party (RP) and the Respublica and Pro Patria Union (RPUP), which took 33 and 23 mandates, respectively, again out of a total of 101 seats. The RP is a right-wing pro-free-market party; its agenda is mostly dominated by economic desiderata such as deregulation, improvements in the business climate, the continuation of the current flat-tax regime, etc. The RPUP

styles itself as a patriotic-conservative force and supports the current relatively restrictive citizenship policies – while its economic programme does not deviate markedly from that of the RP. Both coalition parties support Estonia's active involvement in the EU. Both have undergone a marked shift in this respect from 2004-2005 towards backing a more active role of the EU's central institutions in most fields, including that of foreign policy. The Reform Party was the main force behind Estonia's accession to the eurozone on 1 January 2011. The two governing partners both have allowed relations with Russia to enter a virtual freeze since 2007-2008.

The Prime Minister, Andrus Ansip, has been in office since 12 April 2005 – which makes him one of the longest-serving prime ministers in the EU. However, his popularity has recently been dented by what the public has increasingly come to view as his arrogance. Most recently, Ansip's dismissive comments targeting opponents of the Anti-Counterfeiting Trade Agreement (ACTA) provoked wide uproar and led to street protests. The Prime Minister responded by issuing what looked like a reluctant apology and a promise not to head the "next government". As the coalition presently enjoys a large and stable majority, this in effect means Ansip has every intention of continuing as Prime Minister until the 2015 elections.

The main opposition force is the leftist Centre Party (CP), a populist grouping led for almost 20 years by a single dominating leader, Edgar Savisaar, who has conducted a number of purges. The CP regularly takes around 25% of the vote, but Savisaar was last able to form a government in 1991. His party did a short stint in 2005-2007 as the junior coalition partner under Andrus Ansip. Significantly, however, with the exception of 13 months in 2004-2005, the CP has had the upper hand in the Tallinn City Council. The Estonian

capital city, Tallinn – accounting for nearly one third of the country's population – is by far the largest local authority in the country. The Centre Party heavily relies on Russian-speaking voters. As long-term non-citizen residents are entitled to vote in local elections, but not in parliamentary elections, this fact gives it a considerable edge in local polls. In 2009, the CP took 31.5% of the total nationwide vote while the RP came a distant second with 16.7%.[1]

1.2. EU strategy of the government

Throughout much of 2011 (and the sovereign debt crisis and its offshoots), the Estonian government has stuck very close to what it takes to be the German orthodox line in fiscal and monetary policy. This most fundamentally stems from the conceptualisation of the euro (and the EU at large) as first and foremost a security-political project. In early 2011, there was a marked shift away from the hitherto predominant British "orientation" in favour of a more continental emphasis.

Symptomatically, Estonia announced in July 2011 its backing to the German-French drive to equip the EU with an autonomous operational headquarters for its military operations – something which Britain has consistently and publicly argued would damage NATO.[2]

Secondly, the German position with its strong emphasis on budgetary discipline accords with the current government's own fundamental economic preferences (which include an abhorrence of the open loan markets, leaving the country with the lowest public debt burden in the EU: around 10% of GDP in 2012). Thirdly, cohesion

1 *Estonian National Electoral Commission: http://www.vvk.ee/varasemad/?v=kov09*
2 *Lobjakas, A. (2012)*

within the European Union and the EU's common cause as such have consistently been among Estonia's top foreign policy priorities since 2004. As long as the German line does not deviate too much from the "Community method", Estonia is in its element: relations with Berlin should remain good and the country can go on cementing its reputation as an economic model student in the EU.

Correspondingly, Estonia has backed the early (i.e. 2012) introduction of the European Stability Mechanism (ESM), the reinforcement of the European Financial Stability Facility (EFSF), both Greek bail-out packages, bank recapitalisation, private involvement in Greek debt restructuring, ECB independence, strengthened financial surveillance, and – most emphatically – any and all measures to strengthen fiscal discipline across the eurozone.

There has been a recent little hiccup with the government's legal ombudsman ruling Estonia's participation in the ESM, although desirable politically, would be unconstitutional as it could result in the country's parliament being outvoted. The ombudsman has referred the matter to Estonia's State Court (i.e. constitutional court), which in the end approved it. Thus, Estonia completed the ratification of the ESM Treaty (as well as of Article 136 of the Treaty on the Functioning of the European Union) by early October 2012.

An integral ideological component of the government's stance is the frequently voiced domestic contention by the Prime Minister (as well as the Finance Minister and others) that the modern Continental European welfare states are unsustainable. There has been an added public emphasis on issues linked to advancing competitivity and the functioning of the internal market, but it is difficult to judge the extent to which the Estonian leadership has seriously raised this at summits.

Estonia has also displayed a marked preference for the Community method and EU27-level solutions (a preference it believes is shared by Germany). The British veto at the 8-9 December 2011 summit was accordingly scathingly received by officials (at least in private). Overall, there has been a distinct shift away in the course of 2011 (and, coincidentally, since accession to the eurozone) from Estonia's traditional tendency to align with Britain in favour of a closer relationship with Germany and France.

What the Estonian government continues to reject emphatically is any suggestion that it is ready to cede sovereignty. Instead of "fiscal union" Estonian ministers prefer to speak of a "stability union". Tax harmonisation in particular is a topic studiously avoided by officials – beyond general positive nods in the direction of moves towards standardisation of the tax base. It remains stated Estonian policy since 2004 that tax issues are a matter for sovereign governments.

2. General economic analysis

2.1. Overview of main macroeconomic developments

According to Eurostat figures, Estonian gross domestic product grew at an impressive rate of 7.6% in 2011 while in 2012 it is predicted to slow to 1.6%, and to rise again to 3.8% in 2013 (this following a 14.3% contraction in 2009 and a 2.3% increase in 2010).

Unemployment fell to 12.5% in 2011 and is project to decrease further to 10.4% in 2012 and 9.8% in 2013. Inflation, at 5.1% in 2011, will slow to 3.9% in 2012 and 3.4% in 2013. Estonia's public sector recorded a 1.0% surplus in 2011 which will turn into a 2.4% deficit in 2012 as a result

of a carbon quota investment programme and increased pensions expenditure. Government borrowing will however shrink in 2013 to 1.3% of GDP.

Facing what is likely to turn into a protracted crisis, the government's Estonia 2020 programme focuses on the need to boost exports (which weathered the 2008-2009 crisis remarkably well). Key here is said to be increases in productivity. Between 2003 and 2010, Estonia recorded an average annual productivity growth of 3.2% which translated into an average annual GDP growth of 3%. Between 2010 and 2020, the aim is to attain an average of 3% in annual productivity increases (as opposed to an EU-wide projected annual average of 1%) which should, in turn, translate into an annual GDP growth of 4.4% throughout the period. To this end, the key sectors to be targeted by the government include R&D, training and education, business infrastructure and investment climate.[3]

All of this will take place against the backdrop of persistent high levels of long-term and structural unemployment, as well as generally negative demographic trends (which are expected to see Estonia's working age population drop from 908,000 in 2010 to 801,000 in 2030).[4]

Analysts warn that Estonia remains highly dependent on the state of the Swedish economy, which in turn is vulnerable to shocks in Germany. Hardo Pajula, a leading analyst with the SEB bank, says Estonia is "today already in a sense a part of the Swedish economy" given the dominance of Swedish banks and the export sector's dependence on Ericsson. Pajula points out that while Swedish growth forecasts remain high, real estate prices in the country continue to increase, suggesting a housing bubble which could burst as soon as the Swedish central bank is forced to raise interest rates.[5]

Table 1, Main macroeconomic indicators of Estonia

	2009	2010	2011	2012 (f)	2013 (f)
Real GDP growth rate (annual change, %)	-14.3	2.3	7.6	1.6	3.8
GDP/capita, EU27=100	64	64	67	n.a.	n.a.
Gross fixed capital formation/GDP (%)	21.5	18.8	21.5	23.1	23.9
FDI inflow (BEUR)*	1,3	1,2	0,1	1,0	n.a.
Private consumption/GDP (%)	53.6	52.1	50.9	51.9	51.6
Public consumption/GDP (%)	22.0	20.9	19.5	19.3	18.9
Exports of goods and services (BEUR)	9.0	11.4	14.8	15.4	16.6
Imports of goods and services (BEUR)	8.2	10.4	14.0	14.8	16.0
Current account balance/GDP (%)	4.6	3.8	0.6	-0.3	-0.3
Unemployment rate (%)	13.8	16.9	12.5	11.6	10.5
Inflation (HICP)	0.2	2.7	5.1	3.9	3.4
Interest rates (10y)	-	-	-	-	-

*Eurostat, European Commission, * WIIW (f = forecast)*

As the above table shows, growth in upcoming years is expected to be export-led, with private consumption picking up just a little of the slack and public expenditure forecast to decrease as percentage of GDP. It is important to bear in mind, however, that exports are likely to remain a fickle area in the foreseeable future. Sweden's status as a non-eurozone country may give Estonia an initial competitive advantage as the euro weakens, but eventually both countries' economic health will be dependent on that of Germany. In other words, the future of the eurozone and the path the current crisis will take remain major unknowns in this equation.

3 *http://valitsus.ee/et/riigikantselei/eesti2020*
4 *Ibid.*

5 *Hardo P. (2010)*

2.2. Fiscal stability, economic and social competitiveness

Estonia submitted its 2011 Stability Programme covering the period 2011-2015 and its 2011 National Reform Programme on 29 April 2011. The 12 July 2011 EU Council recommendation noted that the Estonian economy has "bounced back quickly" from the global financial crisis. The document noted that the crisis, which hit Estonia "particularly hard", had amplified the reversal of the domestic real estate and consumption boom, causing a cumulative loss of GDP of about 19% in 2008-2009 and with a peak unemployment rate of 16.9% in 2010.[6]

Table 2, Public finances in Estonia

	2009	2010	2011	2012 (f)	2013 (f)
Public budget balance (% of GDP)	-2.0	0.2	1.0	-2.4	-1.3
Public debts (% of GDP)	7.2	6.7	6.0	10.4	11.7

Eurostat, European Commission (f=forecast)

With the political situation stable and the next elections likely to take place only in 2015, the government will have a relatively free hand in putting into practice its continued austerity drive, which remains predicated on the goal of keeping budget overshoots well within the limits specified in the Fiscal Compact, as well as avoiding entering public debt markets (all of Estonia's government debt at this point remains institutional).

The recommendation describes the assumptions underlying Estonia's budgetary projections as "plausible". This includes the medium-term budgetary strategy of the Estonian Stability Programme to maintain structural

6 *Official Journal of the European Union (27 July 2011)*

balance. According to the Bank of Estonia, the country's budget achieved a slight structural surplus in 2010 and 2011, projected to remain in place beyond 2013.[7] To this end, the government has committed itself to holding back growth in government consumption expenditure.[8] Estonia has undertaken a commitment under the Euro Plus Pact to write the public sector budget balance requirement into law.

The optimisation of energy consumption (Estonia's "resource intensity" is among the highest in the EU while energy efficiency remains low), further reforms in the education system (particularly higher education), a greater investment in innovation, as well as public service reform are identified as key areas in terms of competitiveness.

Echoing the Estonian government's own diagnosis and programme, the Council also recommends that Estonia "take steps to support labour demand and to reduce the risk of poverty, by reducing the tax and social security burden in a budgetary neutral way, as well as through improving the effectiveness of active labour market policies, including by targeting measures on young people and the long-term unemployed, especially in areas of high unemployment." Greater opportunities for lifelong learning are also something underscored by the Council.

7 *Bank of Estonia (2011)*
8 *Official Journal of the European Union (27 July 2011)*

Table 3, Europe 2020 targets of Estonia

Europe 2020 targets	Situation in Estonia in 2010	Estonian Europe 2020 targets
Employment rate – 75% of 20-64 year-olds	66.7%	76%
R&D – 3% of GDP to be invested in R&D	1.6%	3%
Climate change / energy		
Reducing greenhouse gas emissions by at least 20%	41% of the 1990 level	-11% compared to the 2005 level
Covering 20% of energy consumption from renewables	18.9%	25%
Energy use in Mtoe (2009) Increasing energy efficiency by 20%	5.29 Mtoe	-0.71 Mtoe
Education		
Reducing school drop-out rates below 10%	11.6%	less than 9.5%
Reaching tertiary education attainment by at least 40% of 30-34 year-olds	40%	at least 40%
Poverty / social exclusion Reducing the number of people in or at risk of poverty or exclusion by 20 million	21.7% of the population	-49,500

European Commission

In the current climate of budgetary restraint, the categories of employment, education and poverty/social exclusion are likely to prove the biggest challenges for the government's 2020 strategy. The outcome of the 2015 general elections will prove vital in this respect. The elections themselves will, in turn, obviously fundamentally depend on the evolution of the eurozone crisis. While Estonia is relatively well-positioned to handle even a longish economic slump, the situation might change should the crisis take on a more serious political hue (countries dropping out of the eurozone and elements of the EU itself threatening to unravel). Estonia's membership in both the eurozone and the EU has been predicated first and foremost on security concerns – as long as these continue to be met,

internal political stability should not be an issue.

3. Position and potential impact of Estonia on current key issues

3.1. EU budget: the multiannual financial framework for 2014-2020

Estonia believes that the present framework, in terms of its size, is "optimal" for 2014-2020 – i.e. that significant increases would be unjustified in light of the increasing pressures on member state budgets. Instead, the government holds, the EU must make more efficient use of existing funding levels.[9]

Senior officials suggest in private conversations the government could be sympathetic to attempts to reduce the 2014-2020 EU budget by a tenth. Officials also note that the October and December summits of 2012 are likely to prove politically decisive vis-à-vis the MFF; meaning that the positions outlined below could be subject to change in the coming months.

Currently, Estonia estimates it will remain a net beneficiary in 2014-2020 and accordingly tries to position itself to maximum advantage. Calculating its expected take from the combined cohesion/rural development/fisheries funds to equal 3.71% of GDP, the government opposes the tighter ceilings advocated by the European Commission (above all the 2.5% GDP limit on cohesion expenditure), which would reduce Estonia's total receipts to around 3% of GDP instead of the 3.43% (based on 2007-2009 GDP figures) expected.[10]

9 *Government of Estonia (2011)*
10 *Ibid.*

3.2. Common agricultural policy after 2013

Estonia remains broadly supportive of the common agricultural policy. However, Prime Minister Ansip as well as other ministers have consistently criticised the European Commission draft proposal which suggests direct payment levels between old and new member states would only reach parity in 20 years time. Ansip told a delegation of Estonian farmers in February 2012 that "the government wants direct payments to rise to 90% of the EU average by the end of the next financial perspective for 2014-2020."[11] The Estonian argument in a nutshell is that farmers in all EU member states must be able to operate in equal conditions. "The present system distorts competition and puts the Estonian farmer at a disadvantage in comparison with their Western European counterparts." The Estonian government believes the desired adjustments are possible within the current volume of the financial perspective, i.e. no extra resources are needed.[12]

Estonia opposes the introduction of national self-financing to the first pillar (direct payments), which it fears could further harm competitiveness given member states' unequal resources. Estonia is, however, on balance supportive of shifting funds from the first pillar to the second pillar (i.e. rural development expenditure).[13]

However, informal indications suggest the government may be willing to compromise on direct payments and accept an increase in infrastructure spending (above all involving transport projects) in exchange. This would be broadly in line with the government's recent emphasis on reinforcing Estonia's logistical and communication links with the rest of the EU via projects such as Rail Baltica and Via Baltica.

11 *Government press release: http://valitsus.ee/et/valitsus/54002/peaminister-ansip-kohtus-pollumeeste-esindajatega*
12 *Ibid.*
13 *Government of Estonia (2011)*

3.3. Cohesion policy after 2013

The government backs the Commission proposal of a "partnership agreement" linking together the cohesion, regional development, social, rural development and fisheries funds. It also wants improved conditions for their more efficient use (singling out for particular criticism the fact that it took more than a year to reallocate spending targets within these budgets during the response to the 2008 crisis). Cohesion expenditure must be linked with stricter conditionality to Europe 2020 goals.[14]

Estonia opposes the proposed 2.5% of GDP ceiling on cohesion assistance arguing it makes no allowance for wealth differences among member states, causing low-GDP countries to lose out in absolute and relative terms. In particular, Estonia sees no reason why countries with no significant absorption/administrative capacity problems should lose out (presumed problems in this area form an important part of the Commission's argument). Accordingly, Estonia supports differentiated ceilings taking account of the differences in circumstances in different member states.[15]

Estonia also opposes the EU proposal that today's convergence regions in Germany, Spain, Greece, Malta and (in one instance) Poland retain 2/3 of the funds they are eligible for under the current framework. In areas falling under 90% of EU average (especially those in the UK; Germany, France, Italy, Spain and Belgium), the

14 *Ibid.*
15 *Ibid.*

government sees no need for further funding increases. The government is also in favour of a gradual phasing out of any funding to avoid development reverses. Estonia is not against a certain reduction of co-financing levels, but argues moves here should be “moderate” and inclusive of VAT on own expenditure. With a view to the eurozone problems, Estonia argues that crisis states should benefit from higher EU financing ceilings, opposing any Structural Funds concessions for those whose fiscal situation remains suspect.[16]

3.4. Energy policy

Estonia is the only country in the world generating most of its energy needs from oil shale.[17] The oil shale is of local provenance and puts Estonia in a rare position (in the context of the EU) of relative energy independence. This has significant security-political ramifications well appreciated by Estonia’s successive governments. Above all, the country’s generally complex relationship with Russia is spared a further complication – and Moscow is denied the kind of leverage it wields to considerable effect with regard to most other Eastern European countries.

Over the past decade, the proportion of domestic energy carriers – oil shale, peat and timber – have hovered around 65% in the overall energy mix. Correspondingly, around a third of the energy needs is imported. The two most important articles in this list are Russian natural gas (accounting for around 10-15% of the total Estonian energy consumption) and oil sourced from both Russia and Lithuania.[18]

16 *Ibid.*
17 *Merle M. (2010)*
18 *Government of Estonia, Ministry of the Economy and Communications (2009)*

However, there is a problem inherent in Estonia’s oil-shale-based concept of energy production (and security). Burning oil shale generates vast amounts of pollution releasing carbon dioxide, sulphur dioxide and nitric oxide. The climate and energy package adopted by the EU in 2008 puts limits on emissions, reducing quotas in manner designed to attain a 20% reduction in greenhouse gas release by 2020 on 2005-2007 levels. From an economic vantage point, this would be enough to render oil-shale-based energy unaffordable compared to the relatively cheap electricity available from Russia. However, security considerations ensure that the government will strive to further cut the country’s dependence on Russia. Current plans foresee a drop of oil shale in the energy mix to some 30% in about 15 years, giving way to other energy sources (wind, biomass, etc). Electricity production from oil shale will also be modernised to reduce pollution. The objective is to cover domestic demand at all times.[19]

The government last year signed an agreement with the French energy giant Alstom for the modernisation of the power units at the Baltic Thermal Power Station, worth nearly one billion euro.

The government is considering supporting the construction of an LNG terminal either in Estonia itself or in Latvia.[20] The current coalition agreement contains a loose commitment to study the feasibility of building a nuclear power plant in Estonia.

Estonia’s EU Accession Treaty granted the country a transition period for harmonising its electricity market with single market regulations, committing it to a 35% opening by 31 December 2008, with full liberalisation to follow by 31

19 *Maigre, M. (2010)*
20 *Ibid.*

December 2012.[21]

Estonia has long sought to impose anti-“carbon leakage” measures on third country electricity importers (read: Russia), but remains relatively isolated regionally, with Latvia and Lithuania seemingly far less interested in reducing their dependence on Russia.

On a broader scale, Estonia supports a more forceful EU approach to energy independence, especially from Russia.

3.5. External relations, enlargement, neighbourhood policy

Maintaining EU cohesion at all costs is one of Estonia’s predominant foreign policy interests. Given the growing emasculation of the EU’s common foreign and security policy as a result of the constitutional and economic crises, and the accompanying trend towards renationalisation of foreign policy in the EU, Estonia is putting increasing stock in ensuring the continued relevance and vibrancy of the existing common stock of EU positions.

Partly as a result of this and partly stemming from a calculated drive to multiply its leverage on important issues, Estonia, as a rule, closely adheres to the letter (and often the spirit) of EU common positions on most key issues. Central among the latter is relations with Russia. Thus, Estonia’s positions on EU-Russia relations usually closely mirror the EU’s common stated strategy insofar as one exists. On the EU-Russia visa dialogue, Estonia supports the “long-term” goal of visa-free movement, but also insists that Moscow must first properly meet all EU conditionality. Foreign Minister Urmas Paet told the Riigikogu in February 2011 that the abolition of visas would happen “naturally” for a Russia committed to the rule of law. “Like all other

21 *Government of Estonia, Ministry of the Economy and Communications (2009)*

countries, Russia must first demonstrate it respects the principles of democracy and complies with the technical requirements. This is the position of both Estonia and the European Commission, as stated by the President of the Commission, José Manuel Barroso.”[22]

The Eastern Partnership project is one of the few issues on which Estonia is prepared to lead from the front. After the EU Foreign Ministers’ meeting in November 2011, Mr. Paet said the EU predicates its Russia policy on its relations with the eastern neighbours: “Success in relations with the eastern partners may translate into success in relations with Russia, and special attention should be given to Ukraine’s developments and choices.”[23]

Estonia also tends to take a relatively uncompromising line on broader international themes. Addressing in early December 2011 the Russian veto on UN sanctions against Iran, Mr. Paet said it was “irrational” for Moscow to regard NATO and the EU as threats: “if there is anyone who presents a danger to Russia it is Iran with its nuclear programme.”[24]

Estonia is an unequivocal, if not always very vocal supporter of further EU enlargement. The government backs the expansion of the EU in the Balkans as well as Turkey’s eventual membership – all subject to the countries’ meeting the Copenhagen criteria. It also argues for an open door policy in the eastern neighbourhood.[25] Whilst recognising that progress in Ukraine and Georgia, in particular, has stalled, Estonia continues to argue for an active EU policy of political and economic engagement in the region with the aim of promoting democratisation and closer integration with the EU – including the long-term prospect of EU

22 *Speech by Foreign Minister Urmas Paet to Riigikogu, 8 February 2011*
23 *Paet on 13 November 2011*
24 *Paet on 2 December 2011*
25 *Speech by Foreign Minister Urmas Paet to Riigikogu on 8 February 2011*

membership for all Eastern Partnership countries interested in it.

Estonia is keen for the visa liberalisation dialogue with Russia not to overtake those being pursued with the eastern neighbours. Estonian Foreign Minister Urmas Paet has consistently over the years said Russia must first fulfil all EU political and technical criteria. He has also pointed to a "political logic" which must bind the EU in this area: "Three Eastern Partnership countries have unilaterally abolished visas for EU citizens. Political logic dictates the EU must first take steps to consider their requests for reciprocity before it can proceed to Russia."[26] Estonia also insists on strict reciprocity in any visa concessions made by the EU to third countries.

3.6. Special issues for Estonia

The Baltic Sea Strategy remains a major Estonian priority within the EU, but has not come to much in recent years, in particular due to an absence of dedicated EU funding. The government has said it will try to secure a budget line for the strategy within the framework of the next financial perspective.[27] Estonia's aims for the Baltic Sea Strategy, meanwhile, remain relatively vague – what is sought is "regional added value" and better longer-term integration of the programme into EU-wide initiatives and projects.

Within the Europe 2020 envelope of topics, Estonia attaches great importance to the further development of the internal market, especially the free movement of services – within the latter, in turn, digital services occupy an increasingly important place.

26 *Paet on 11 February 2010*
27 *Chairman of the Estonian Parliament's EU Affairs Committee, Marko Mihkelson in a press release on 2 March 2011: http://www.riigikogu.ee/index.php?id=67927*

Cyber defence remains a quintessential Estonian concern. Estonia insists on the EU's setting minimum standards on combating cyber crime. It wants cyber defence to become an integral part of the CFSP. Free access to the internet is a basic right promoted by Estonia.

4. Summary and conclusions

Domestically, Estonia is likely to continue to be in a strong position until the next elections in 2015. Recent months have, however, indicated that internal political stability remains vulnerable to sudden scandals. These usually involve Russia in some fashion: in December 2010, opposition leader Edgar Savisaar was accused by the government of having solicited campaign funds from Russia, in December 2011 a number of leading figures in the Republica and Pro Patria Union were exposed as having a stake in a company arranging Estonian residence permits for rich Russian clients. While political corruption is becoming an increasingly touchy subject for the population at large, the Russian factor greatly magnifies the sensitivity of the issues.

Economically, Estonia is likely to remain relatively invulnerable given the government's strong budgetary position and the absence of market-traded public debt. As a consequence, the country will easily be able to afford continuing to side with the "hawks" in the EU's fiscal and debt debates.

The government does not really have any red lines in the conventional sense of the term. It will, if need be, absorb the likely reverses as regards the direct payments issue irrespective of whether it wins any concessions in other areas. The only issue with a serious potential for Estonian dissent is tax harmonisation – although even here

the government has long sought to place the issue of further EU reform within the very broad ambit of Estonia's security interests. This first became a pronounced trend in the run-up to the accession to the euro area on 1 January 2011 when the Prime Minister repeatedly stressed Estonia's motivation had above all to do with security-political considerations.

Russia also remains a potentially explosive issue for Estonia, although here as in most other cases, Tallinn is very aware that any suggestion of intra-EU discord is far more damaging to its long-term interests than possible losses on specific policy issues.

In fiscal matters this will force Estonia into something of a balancing act in the short and medium term, however. Its natural interests in debates over CAP and Structural Funds ally it with Poland and the other EU10 states. The ideology underlying Estonia's economic policy, on the other hand, puts the country closer to Germany, the Netherlands and Finland.

Overall, Estonia's impact on concrete EU decisions is likely to remain low. However, its symbolic status as a budgetary poster child could create considerable room for manoeuvre for the government. Whether the government will choose to exploit that space will remain to be seen.

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HUNGARY

Krisztina Vida

1. Domestic political framework, EU strategy of the government

1.1. Overview of internal politics

As a result of parliamentary elections in April 2010, the centre-right party alliance of Fidesz-KDNP (Fidesz Hungarian Civic Alliance – Christian Democratic Peoples' Party) had a landslide victory by gaining more than two thirds of the mandates in the unicameral legislature. A similar victory was achieved by the alliance in the local elections in autumn 2010. The remaining one third of the seats in the Hungarian parliament is occupied by two socialist blocks (MSZP, the Hungarian Socialist Party and the DK, Democratic Coalition – a faction that split from MSZP), by a radical right wing party (Jobbik, Movement for a Better Hungary) and by a green-liberal party (LMP, Politics Can Be Different).

This historically unprecedented result was among others due to a loss of credibility of the previous two socialist-liberal

governments. Actually, between 2004 and 2010 Hungary was the only new member state of the EU which after its accession (and prior to the crisis) did not show any signs of convergence to the Union average and regularly reported the lowest growth rates. At the same time, public finances were mismanaged and public debts rose from 53% to more than 80% of GDP.

The main priority of the government which took office at the end of May 2010, has therefore been to regain the balance of public finances (by gradually decreasing the indebtedness and by keeping the budget deficit close to 3% of GDP), as well as to substantially increase employment, one of the lowest in the EU. To this end, the government introduced several measures including the downsizing of the public administration, the reform of the pension system (first by re-nationalising the private branch of contributions and reviewing early retirement schemes as well as disability pensions), the temporary introduction of special taxes (e.g. on financial, telecommunication, retail and energy services) or the launch of massive public work programmes offered to unemployed people (for a payment that is the double of the unemployment benefits). The new Basic Law – replacing the interim Constitution of 1990 – was also adopted by the parliament in 2011, and entered into force in 2012.

However, as the government and the parliamentary majority wanted to live up to its mandate, there has been an unusually hasty law-making process which in most cases did not allow for thorough preparations and wide ranging consultations with the opposition and all parties concerned. As a result, the government had to face harsh domestic, as well as international criticism. Even the EU expressed reservations regarding for example the new media law, the modification of the Central Bank law or the new rules on retirement of judges. In parallel with

infringement procedures in those areas, the European Parliament adopted a resolution on eight "anti-democratic" measures of the Hungarian government in February 2012. The Hungarian government recurrently expressed its openness and willingness to settle all concrete issues as fast as possible – thus most of the disputed cases were settled relatively quickly. At the same time, the government rebuffed general criticism on the quality of democracy in Hungary and protested against applying double standards with regard to Hungary. (See for example the EP request to review the Constitutional Court's competences even when it is not regulated by the acquis and there is no single model for that in the EU.)

While introducing reforms at an unusual speed and carrying out its "unorthodox" economic policy the government has been losing popularity but it still enjoys the strongest support among the citizens according polls. Internal political stability is actually of utmost importance in the difficult times of consolidating public finances and trying to revive the economy in the context of the protracted euro area crisis.

1.2. EU strategy of the government

As to the Hungarian EU strategy,[1] the core idea is that Budapest is interested in a strong and united Europe and would oppose any developments towards the models of several circles or multi-tier Union. Hungary showed its commitment to a stronger EU when it held the Council presidency in the first half of 2011 (even the motto was: "Strong Europe with a human touch"). To prove this commitment one can mention the highly intensive preparatory and reconciliation work of the presidency to get

1 *Ministry of Foreign Affairs (2012a)*

the six-pack for economic governance adopted, to launch the single European patent system or to pave the way for Romania's and Bulgaria's Schengen membership.

As to the latest developments, Hungary is strongly interested in the stabilisation of the euro area. At the same time, Budapest has a more cautious stance vis-à-vis such intergovernmental agreements as the Euro Plus Pact or the treaty on a fiscal union (TSCG). While Hungary did not join the former it has finally signed up to the latter (but it will fully bind Hungary only upon adoption of the common currency). In broader terms, Hungary is a champion of the Community method and is against the intergovernmental approach. The core principles of the Hungarian EU-policy are among others the realisation of citizens' Europe (the EU must deliver to its citizens), strengthening the European social model based on common values, equal rights and equal treatment of all member states, the preservation of the acquis and the common policies, avoidance of fragmentation of the EU. Hungary's commitment to European values is underpinned by the fact that the new Basic Law incorporated the EU's Charter of Fundamental Rights.

2. General economic analysis

2.1. Overview of main macroeconomic developments

Having a relatively small sized and open economy, Hungary has been hit very hard by the global financial and economic crisis. Gross domestic product shrunk to nearly 7% in 2009 – well below the average recession rate of the EU27 (-4.3%). Since then Hungary recorded very modest growth rates and for the year 2012 a slight recession, while for 2013 just 1% expansion is predicted by Eurostat (see Table 1).

In 2011, in terms of gross output by far the most dynamic sector has been agriculture. At the same time, the industrial sector showed a very modest expansion (thanks to manufacturing, while constructions fell back sharply). Finally, the services sector was practically stagnating (the least successful being the financial sector). Seen from the point of view of end-use of GDP, the figures indicate that growth was driven by exports the value of which has been spectacularly increasing since 2009 while steadily surpassing imports. At the same time both, private and public consumption was stagnating in 2011 while gross fixed capital formation continued to decline (and to reach historically low levels).

As can be seen from the forecasts for this year and for 2013 (see Table 1) none of the internal drivers of growth is likely to revive: public consumption is reduced due to austerity measures, private consumption is sluggish due to uncertainties and high rate of indebtedness of households, while investments continue plummeting. The only sector of the national economy that will be contributing to growth next year (and reduce recession in 2012) is the export sector which shows a very dynamic performance.

Table 1, Main macroeconomic indicators of Hungary

	2009	2010	2011	2012 (f)	2013 (f)
Real GDP growth rate (annual change, %)	-6.8	1.3	1.6	-0.3	1.0
GDP/capita, EU27=100	65	65	66	n.a.	n.a.
Gross fixed capital formation/GDP (%)	20.7	18.0	16.8	16.2	15.8
FDI inflow (BEUR)*	1,5	1,7	3	1,7	n.a.
Private consumption/GDP (%)	54.5	53.3	53.0	52.8	52.4
Public consumption/GDP (%)	22.7	21.8	20.8	20.0	19.3
Exports of goods and services (BEUR)	71	84	93	101	110
Imports of goods and services (BEUR)	66	78	86	92	99
Current account balance/GDP (%)	-0.2	1.0	0.9	2.2	3.7
Unemployment rate (%)	10.0	11.2	10.9	10.6	9.6
Inflation (HICP)	4.0	4.7	3.9	5.5	3.9
Interest rates (10y)	9.11	7.28	7.64	n.a.	n.a.

*Eurostat, European Commission, * WIIW (f = forecast)*

Hungary's most important export items (making up some 60%) are machinery and vehicles produced mostly in plants run by multinational investors. In 2011, Hungary has registered a positive trade balance with its EU partners (both old and new members) while it accumulated a significant deficit vis-à-vis its Asian partners.[2] All in all however, Hungary was able to accumulate a total of 7.4 billion euro trade surplus last year and continued to have a positive current account balance as well. For 2012 and 2013 an even better external trade performance can be expected with net exports of 9 and 11 billion euros respectively.

In Hungary – as in most EU countries – the recession had serious consequences on the labour market. Despite the unusually difficult context however, the government's core priority has been to increase the Hungarian employment rate which used to be the EU's lowest ever since membership. Thanks to some new measures, such as revised pension rights or massive public work projects, unemployment started to go downwards (reaching 10.9%) while the employment rate showed a modest improvement last year (60.7%). According to national statistics, the number of those having a job increased by 76,000 between June 2011 and June 2012.[3] However, the regional discrepancy of unemployment figures remains substantial and the problem of long-term joblessness is also alarming. A further challenge is brain-drain, especially in the health care sector (a phenomenon boosted by the abolishment of all remaining barriers to labour movement as of 1 May 2011).

As regards the monetary developments – contrary to most EU countries – the recession and sluggish growth in Hungary has been accompanied by relatively high inflation rates throughout the past couple of years (around or above 4%) and due to upward modification of VAT and excise duties, the year 2012 may not bring about lower inflation either. In parallel, interest rates have been among the highest in the EU (i.e. well above 7%) in reaction to the mentioned stubbornly high consumer price levels. While this monetary policy did not seem to be successful in fighting inflation, it has also been subject to criticism because of both hampering investment activities and rendering government borrowing more expensive. In this light the decreasing trend of the past months has to be welcome. The third component of monetary issues, namely exchange rates have been extremely volatile during the past few years, hardening the lives of hundreds of thousands of citizens who took up loans in foreign currencies (mainly Swiss francs) due to the unbearable interests at which forint-denominated

2 *External trade statistics of the Hungarian Statistical Office, end of 2011: http://portal.ksh.hu/pls/ksh/docs/hun/xftp/gyor/kul/kul21111.pdf*

3 *The publication of the Hungarian Statistical Office is cited by this web page: http://gazdasag.ma.hu/tart/cikk/c/0/142117/1/gazdasag/KSH_76_ezer_fovel_dolgoznak_tobben_mint_egy_evvel_ezelott*

loans were on offer. The situation of the majority of these households has become so critical that the government had to intervene in their favour. Different schemes have finally been adopted in a joint effort with the banking sector: the financial sector accepted to bear two thirds of the burden of the "exit measures" against the indebted citizens' covering one third of the costs. Nonetheless, even these measures cannot solve completely this painful issue while some of the foreign banks started to shrink their activities in Hungary.

2.2. Fiscal stability, economic and social competitiveness

As to public finances, the Hungarian performance has been among the worst ones in the EU before the crisis. The country has been under excessive deficit procedure since 2004 while since then it also reported a steady increase of public debts. This meant that Hungary could not pursue an anti-cyclical economic policy in the crisis on the contrary; it had to introduce fiscal austerity in the middle of recession. The government has now to square the circle: namely it wants to reduce both fiscal indicators (public deficit and debts) and at the same time launch growth and enable job creation. Actually, the Hungarian public deficit figures show a promising trend recently, the Commission however is not yet convinced that the below 3% level can be maintained in a sustainable manner in the foreseeable future (due to some one-off or temporary revenue items). Therefore the Commission – although it recognises the achievements of fiscal policy efforts of the government so far – did not lift the excessive deficit procedure against Hungary yet. In connection to this, the freezing of cohesion assistance in 2013 was also proposed by the Commission and finally adopted by the ECOFIN Council in March, however this sanction was removed a few months later, after the government's additional package of measures reaching 0.5% of GDP was

adopted. At the same time, Hungary started to decrease its public debts too, but due to the fact that around 40% of the debts are denominated in foreign currencies the debt ratio is highly exposed to exchange rate movements. Furthermore, until there is no economic expansion the country has little chance to grow out of indebtedness.

Table 2, Public finances in Hungary

	2009	2010	2011	2012 (f)	2013 (f)
Public budget balance (% of GDP)	-4.6	-4.2	4.3	-2.5	-2.9
Public debts (% of GDP)	79.8	81.4	80.6	78.5	78.0

Eurostat, European Commission (f=forecast)

In April 2011 – in the framework of the European semester – the Hungarian government submitted its Convergence Programme[4] spanning from 2011 to 2015. The document is based on the structural reform programme, in Hungary called the Széll Kálmán Plan (named after a Hungarian Prime Minister during the Austro-Hungarian Monarchy). The Plan aims at restructuring and reducing state redistribution and rendering public expenditure "growth-friendly". The updated version of the plan was submitted in April 2012 and its major measures can be summarised in a nutshell as follows.

On the revenue side the government introduced the new banking tax as well as extraordinary sectoral levies, while in parallel reduced the personal income tax (to a flat rate of 16%) and corporate tax was also cut back (to 10% for SMEs). At the same time, there has been an increase of VAT from 25 to 27%. While the extraordinary sectoral levies are to be phased out in the coming years, new taxes are being

4 *Convergence Programme of Hungary (2012)*

introduced as of mid-2012 and also during 2013. These include a tax on telecom services, on financial transactions, on insurance services and the new system of electronic road toll will also substantially contribute to the revenue side of the public budget in the coming years. Furthermore, the nationalisation of the savings in the private pension funds had not only a considerable one-off effect on the budget (thanks to which in 2011 the public balance was +4.3% of GDP) but also a very positive long-term effect, namely, that the state does not have to complement the public pension fund any more. The latter was necessary because approximately 20% of pension contributions have been transferred onto private accounts instead of the public pension fund, thus the state had to make up the missing amounts when paying the actual pensions. On the expenditure side, among other measures, the government launched the streamlining of public administration, reduced unemployment benefit and sick pay, reviewed the pension entitlement system, cut back drug subsidies, restructured the financing of public transport, and revised support for state-owned enterprises.

As a result of all those consolidation measures the programme calculates – rather optimistically – with a relatively fast stabilisation of public finances and foresees a 1.5% budget deficit and a 64.1% public debt ratio to GDP by 2015.

The crisis and the fiscal consolidation efforts of the government have also had an unfavourable impact on social policy in general. Due to less resources and the commitment to keep budget deficit under tight control, the government had to revise several items of its social policy. To the positive steps belongs the raising of the minimum wage level by around 19% or the launching of new programmes for integrating disadvantaged groups (with special regard

to the Roma). However, measures such as the radical reduction of unemployment assistance or the drastic cut back of state funded places in higher education belong to those unpopular decisions which might have longer-term repercussions for the society.

As to Hungary's programme to strengthen its competitiveness, the updated National Reform Programme[5] was also submitted to the European Commission in April 2012. This document is partly based on the above mentioned structural reform programme and – in line with the Europe 2020 strategy – sets out major targets to be achieved by the end of the decade. According to the plan the Hungarian headline goals are the following: increasing employment rate to 75%, increasing expenditure on research and development to 1.8% of GDP, reducing the share of people living in poverty by 5%, and within the population aged 30-34 increasing the share of diploma holders to 30.3% by 2020. In the field of energy and climate protection the Hungarian government pledged to increase the share of renewable energy sources in the final consumption to 14.6%, to achieve energy savings of 10% and to cap the rise of green house gas emissions outside the emission trading system at 10% relative to the 2005 level.

5 *National Reform Programme of Hungary (2012)*

Table 3, Europe 2020 targets of Hungary

Europe 2020 targets	Situation in Hungary in 2010	Hungarian Europe 2020 targets
Employment rate – 75% of 20-64 year-olds	60.4%	75%
R&D – 3% of GDP to be invested in R&D	1.2%	1.8%
Climate change / energy		
Reducing greenhouse gas emissions by at least 20%	69% of the 1990 level	-10% compared to the 2005 level
Covering 20% of energy consumption from renewables	7.3%	14.65%
Energy use in Mtoe (2009) Increasing energy efficiency by 20%	25.31 Mtoe	-2.96 Mtoe
Education		
Reducing school drop-out rates below 10%	10.5%	less than 10%
Reaching tertiary education attainment by at least 40% of 30-34 year-olds	26%	30.3%
Poverty / social exclusion Reducing the number of people in or at risk of poverty or exclusion by 20 million	30% of the population	- 450,000

European Commission

3. Position and potential impact of Hungary on current key issues

3.1. EU budget: the multiannual financial framework for 2014-2020

As regards the size of the EU budget, Hungary believes[6] that the debate should not have started with capping the total revenue ceiling of the budget but rather with defining the most important challenges and priorities the Union would like to tackle via common financing. In other words, the revenues should be tailored to financing needs and not vice versa (so-called bottom-up approach). Furthermore, the net

6 *Ministry of Foreign Affairs (2012b)*

balance (or "juste retour") approach should be overcome. Even though in the midst of the crisis Hungary understands the reservations of the net contributor countries, the total sum for the seven years period, as proposed by the European Commission in mid-2011, should not be curtailed more in the Hungarian view. The amount of 1,025 billion euros (excluding items outside the MFF) would mean a 5% increase in real terms compared to the current financial framework and this is acceptable for Hungary. The main concern is therefore not so much the final amount but the internal restructuring of the expenditure items leading to a clear diminishing of the share of both key policies, namely agriculture and cohesion.

Hungary is also convinced that the revenue side[7] should be made more transparent. As to the traditional own resources (TOR) and the GNI-based national contributions, Hungary agrees to keep them as they are. Moreover, Hungary is in favour of cutting back the national part of TOR collection costs from 25% to 10% as this would diminish the GNI contributions. Hungary would also welcome the abolishment of the present VAT contribution system (monthly transfers of 0.3% of national VAT revenue with the 50% GNI cap) as it is highly bureaucratic. The Commission – with the full support of the European Parliament – proposes to introduce two new own resources: a European VAT and the financial transaction tax (FTT). The proposed VAT resource would be a simpler and less bureaucratic one compared to the current system, however, as it does not enjoy substantial support from the member states, it is not likely to be introduced. The new FTT revenue is meant to be shared by the member governments (one third) and the EU budget (two thirds). This can be seen as an important leverage on the national (GNI-based) contributions to the EU

7 *Hetényi (2012)*

budget while also creating a brand new source for national governments. Even though both new own resources might be interesting for Hungary, they do not enjoy real support for political reasons. Namely, the Hungarian position is that none of them would be desirable as they would impede the national autonomy of taxation. As the Prime Minister had stressed it in a TV-interview in the end of May 2012, any taxation by the EU would lead to a bureaucratic model of the United States of Europe without legitimisation by the citizens. Finally, as regards the correction mechanisms, Hungary is against them and would prefer their phasing out. Nevertheless, Hungary can accept their justification, but would definitely support a radical simplification of rebates (preferably in the form of lump-sum payments to the states concerned).

As to the expenditure side, Hungary attaches utmost importance to both cohesion policy and the common agricultural policy and agrees with the other expenditure items as proposed by the Commission (which are actually identical with the current budget lines).

3.2. Common agricultural policy after 2013

For Hungary the agricultural sector is highly important. According to the Hungarian Statistical Office it makes up more than 4% of total gross domestic product and in a wider sense agribusiness accounts for around 13% of GDP. Due to the ideal conditions for farming activities, this sector can also be perceived as one of the driving forces to revive the national economy and to create jobs.

According to the Ministry of Foreign Affairs, "Europe must not give up on producing sufficient and safe food for its citizens."[8] Therefore Hungary continues to be interested in a supranational, strong, sustainable, efficient, competitive and fair common agricultural policy. Consequently, Budapest is concerned about the nominal freeze of CAP expenditure. This will lead to the significant decrease of the total amount to be earmarked for the management of natural resources in the coming seven years (from 413 to ca. 383 billion euros at 2011 prices). In the field of direct payments[9] Budapest supports the principle of evening out inequalities across the Union. As Hungary will be at 100% level of direct payments per hectare in 2013 – according to calculations based on the Commission proposal – Hungarian farmers would receive annually nearly the same amount in 2014-2020 as in 2013. At the same time, according to different calculations, assistance for rural development might be cut back slightly.

As regards the Commission's proposal in general,[10] Hungary welcomes the institution's intention to preserve the two pillar structure of the CAP as well as to offer special support to the young farmers, to the small farms and to farms in special (unfavourable territorial) conditions. Furthermore, the possibility of coupled (production-related) support is also in line with Hungary's interests.

However, Hungary has several reservations vis-à-vis the proposal.[11] Budapest is cautious about the so-called greening as there are already enough green components in the CAP, and the new aspects may result in increased administrative costs for the farmers. According to Commission calculations as much as 87% of the Hungarian farmers would face extra costs under the obligation of complying with those new

8 *Quotation and information from an internal position document received from the Ministry of Foreign Affairs.*
9 *Horváth – Stelbaczky (2012)*
10 *Ministry of Foreign Affairs (2012b)*
11 *Horváth – Stelbaczky (2012)*

conditions. In case of non-compliance, the farmers would not only lose the green component of the funds (30%) but would also be subject to sanctions (deduction from the remaining support). Therefore these proposals are not supported by Budapest. Furthermore, the capping of assistance given to big farms is not really welcome either. According to preliminary calculations by experts, some 190 big Hungarian farms would lose some 10 million euros per year which however would remain within the country and would be transferred to the second pillar (for "innovation" purposes).

3.3. Cohesion policy after 2013

Due to its underdeveloped position, Hungary is a net beneficiary of the EU's cohesion policy to which it attaches great importance in the catching up process. Hungary supports[12] a strong cohesion policy to be pursued in the next financial framework too. Hungary agrees that proper linkages between the Europe 2020 strategy, the National Reform Programmes and the National Development Programmes must be ensured, therefore the introduction of the Common Strategic Framework is welcome. However, in close connection to this, Hungary is not keen on using the Country Specific Recommendations, issued by the Commission, as a kind of binding reference point for the elaboration of national development programmes as Budapest wishes to retain a greater freedom in formulating the national/regional priorities.

In the debate about cohesion policy after 2013, Hungary underlines the following points. Cohesion policy represents a Treaty-based commitment which helps evening out internal asymmetries on the internal market, thereby strengthening

12 *Ministry of Foreign Affairs (2012b)*

global competitiveness of the Union. It is actually an investment tool which plays a key role in boosting growth in the member states without inducing debts.

As to financing cohesion objectives between 2014 and 2020, Hungary is disappointed by the Commission proposal as it calculates with some 5% less assistance compared to the current financial framework. Moreover, the share of the money to be earmarked for the classical "convergence" objective within cohesion policy will shrink from 57% to 48%.[13] At the same time, the newly defined transition regions (with GDP per capita between 75% and 90% of EU average) would benefit significantly more (11.6%) than the current category of phasing out/phasing in regions (6.8%). Hungary does not have any regions that would qualify for a transition status while the central region with Budapest is already above 90%. This is a special challenge for Hungary, as Budapest pushes up the average rate of the whole central region which – without the capital – would be a convergence region. Therefore Hungary does not support the proposal for transition regions while it would like to have some remedy for the mentioned special problem.

Regarding the new assistance ceiling, Hungary did not welcome the idea to set the 2.5% of GDP upper limit. This cap would mean an unjustified decrease of the funding (in the case of Hungary it might mean at least a 20% cut back) due to projected sluggish growth and due to the fact that currently the country benefits from a 3.5% cap. This approach does not take into account the absorption performance of the beneficiary countries either. Hungary, together with the Baltic states, insists that the total amount of money earmarked for economic, social and territorial cohesion across the EU should not be less (for eligible regions) in the next financial framework than in the 2007-

13 *Bajusz (2012)*

2013 period.

Furthermore, there is a joint position[14] by the Visegrad countries on three points: to preserve the current financing rules (not to increase the administrative burden for member states and regions), to revise the idea of the Connecting Europe Facility (as it would only shorten the resources available to the cohesion countries' domestic development), and to give a special treatment to the capital cities and their surrounding regions (as they are the most developed regions but struggling with special challenges). Coming back to the Connecting Europe Facility Hungary has fears that it will be exposed to competition among the member states via applications therefore the less developed countries might have less chances than justified by their underdeveloped infrastructure. The idea of regrouping 10 billion from the Cohesion Fund in favour of this instrument is not supported by Hungary and by the same token a reduction of the remaining 40 billion dedicated to the CEF would be welcome.

As regards the proposals for the new rules (the list of key objectives and investment priorities in line with the Europe 2020 strategy, preconditions for assistance and potential sanctions) Hungary is rather cautious about them due to the fact that they imply a more complicated implementation with more bureaucracy.[15] The intention of the European Commission to make sure EU money is spent efficiently is understandable but the new rules might actually work against simplicity and transparency.

14 *Bruxinfo (2011a)*
15 *Juhász (2012)*

3.4. Energy policy

According to 2009 figures of the EU's Energy Portal,[16] in Hungary energy consumption was 25.31 million tonnes oil equivalent – a rate below most of the 10 million inhabitant EU countries such as Greece, the Czech Republic or especially Belgium. The Hungarian energy dependency rate (imports divided by gross consumption) is nearly 60% which puts Hungary in the middle range among the EU27.[17]

In Hungary by far the greatest consumers of energy are households (34%) and transport (29%) while the services and the industrial sector have a smaller share (18 and 16% respectively). As to energy sources, the most important ones are gases (36%) and petroleum products (31%) while electricity accounts for 17% and renewables for just 6%.

As regards production, the picture is quite different. In Hungary, the greatest share of domestic production comes from nuclear energy mainly generated in the Paks nuclear power plant (35%). In the second place can be found gases (20%), followed by renewables (17%), solid fuels and petroleum products (14-13% respectively). Hungary's energy imports are dominated by gases and petroleum products mostly coming from Russia.

The Hungarian government's external energy strategy is based on two pillars: greater integration (interconnections) within the Union as well as greater diversification of import sources coming from outside. Under the Hungarian presidency the EU pledged to create an integrated and interconnected internal market for energy by 2014 which is very much in line with the Hungarian priorities. In this context, Hungary will participate in the establishment of

16 *Energy Portal of the EU containing all energy-related statistics used here: http://energy.eu*
17 *Energy Portal of the EU: http://www.energy.eu/country_overview/Hungary_2011.pdf*

the North-South gas pipeline project (linking among others Poland, Slovakia, Hungary and Croatia). With regard to concrete projects[18] agreed last November in Brussels by energy ministers of the countries involved, Hungary will participate in the following projects: interconnection of the Hungarian-Slovak as well as the Hungarian-Croatian electricity grids, interconnection of the Hungarian-Slovak as well as the Hungarian-Slovenian gas pipelines and also rendering the Hungarian-Romanian gas network technically a two way pipeline. These projects have relatively short deadlines, varying between 2015 and 2016. At the same time, Hungary is also a signatory party to the Nabucco gas pipeline project where gas supplies will come through Turkey and which can be interconnected with the above mentioned sub-regional gas network too.

The energy policy of Hungary focuses on increasing energy efficiency (a series of new measures and rules have been adopted in this regard), on safe use of nuclear energy (Hungary does not intend to give it up) and to increase the use of renewable energy sources for which Hungary has good potentials, e.g. in terms of wind, water or geothermal sources of energy.

As to harmonisation efforts, Hungary has a good performance, the Commission initiated against Hungary infringement procedure[19] only in one case recently, namely regarding the implementation of the second energy liberalisation package in June 2010 but the issue was rectified.

18 *Bruxinfo (2011b)*
19 *European Commission (2011)*

3.5. External relations, enlargement, neighbourhood policy

Hungary fully shares the European Union's foreign, security and defence policy goals and priorities and participates actively in most of the EU's missions worldwide. Hungary's top priority is stability in its immediate neighbourhood; therefore most forces are concentrated in the missions carried out in the Western Balkan region. Hungary has thus been strongly engaged in the EU's EUFOR Althea (military) as well as the EUPM (police) missions in Bosnia and Herzegovina, and the EULEX mission in Kosovo too. Furthermore, Hungary has been contributing to the following missions: EUMM civilian monitoring mission in Georgia, EUPOL COPPS and EUBAM Rafah (police and border assistance missions in the Palestine National Authority), in the EUJUST LEX rule of law mission in Iraq, in the EUPOL mission in Afghanistan, as well as in several missions in Africa (especially in Congo, in Somalia and recently in Libya).[20] Hungary attaches great importance to NATO as well, and supports an optimal division of labour between NATO operations and EU missions.

Hungary has always championed for enlargement of the EU as it is convinced that the widening of the Union can make it stronger. Hungary sees the enlargement waves of the EU a historical success.[21] Regardless of governing coalitions there has always been a consensus in the Hungarian political elite that once any European country fulfils the membership criteria, it should be allowed to join the EU.

Hungary is not only advocating this position but has also done a lot for it during its presidency term in the first half of 2011. It was actually thanks to the highly intensive mediation work of the Hungarian diplomats that by the end of June 2011 the accession negotiations with Zagreb

20 *Ministry of Foreign Affairs of Hungary (2012c)*
21 *The Hungarian government's portal: http://eu.kormany.hu/bovites*

could be concluded, leading to the signing of the Accession Treaty under the Polish presidency. Hungary also promoted the negotiating process with Iceland and wanted to see advancement in the Turkish case too. Unfortunately, talks with Ankara seem to be in a deadlock, nevertheless Hungary used to invite all official candidate countries' representatives to all the informal Council meetings during its presidency to demonstrate that they belong to the "European family".

Hungary strongly hopes that the successful conclusion of the Croatian accession process and the country's joining in July 2013 can send an encouraging signal to all other Western Balkan countries which are in different stages of their rapprochement to the European Union. Hungary would like to see all candidate countries from the region – namely the Former Yugoslav Republic of Macedonia, Montenegro and Serbia – at the negotiating table as soon as the remaining questions and disputes are cleared. Hungary also backs the three potential candidate countries, namely Albania, Bosnia and Herzegovina and Kosovo.

With regard to the EU's neighbourhood policy,[22] Hungary used to underline the importance of a balanced approach by the EU towards both the southern and the eastern partner regions, which should also be reflected in terms of financing. In that regard, Hungary would like to see greater funds to be earmarked for the European Neighbourhood Policy Instrument (ENPI) in the upcoming financial framework. Due to Hungary's geographical position, the Eastern Partnership has a priority over the Union for the Mediterranean. Hungary expects that sooner or later visa liberalisation and association agreements with all countries concerned can be launched/signed (except for Belarus at the moment). Hungary is ready to offer its know-how in terms of its experience in legal harmonisation,

22 *Based on information obtained from the Ministry of Foreign Affairs.*

institution building or project management and absorption capacity to the Eastern Partnership countries, with which energy cooperation can also be an important point on the agenda.

3.6. Special issues for Hungary

Two issues can be mentioned here[23] both of which were also high on the agenda of the Hungarian presidency: the Roma strategy (due to an important Roma population in Hungary and across Europe, facing poverty and social exclusion) and the Danube strategy (due to the suboptimal use of the river offering lots of promising opportunities for cooperation).

First, Budapest was successful in introducing the issue of the Roma strategy to the EU agenda. According to the June 2011 European Council Conclusions, there is now an EU Framework for National Roma Integration Strategies aiming at improving the situation of the Roma population in terms of education, employment, health care and housing by 2020. Member states are to elaborate their own action plans in this regard and the Commission will carry out annual monitoring, and will report to the European Parliament and the Council about the implementation of those national programmes. Member state actions are to be aligned with the Europe 2020 strategy and financial assistance may come from the Structural Funds where appropriate.

The filling up of the EU's Danube Region Strategy – a macro region strategy involving the cooperation of 14 countries along the river – with real content was also among the realised priorities of the presidency. During the first half of 2011 national coordinators have been appointed and agreement was met on several concrete

23 *Vida (2011)*

projects to be launched, in the framework of 11 action areas. Although according to the official position of the EU the Danube strategy is characterised by three “no-s”: no extra money, no new institution, no EU law, the Hungarian presidency introduced three “yes-es” relating to jointly targeting available money on the projects to be launched, to harmonise ideas and proposals across the partners and also to introduce a new and integrated approach to spatial planning along Europe’s second longest and “most international” river.

4. Summary and conclusions

Since May 2010, Hungary is being ruled by a centre-right and Christian democrat party alliance (Fidesz-KDNP) that enjoys a two thirds majority in the parliament. Due to the very severe situation of the country in mid-2010 (unseen indebtedness of individuals, local governments and the state itself, as well as an extremely low share of the population paying taxes via legal jobs, and virtually no signs of catching up ever since membership in the EU) the new government launched radical reforms and introduced unusual, even “unorthodox” measures to tackle the problems. This has led however to a too hasty lawmaking process due to which the government had to face strong criticism both inside the country and also on an international scale. As regards Hungary’s EU strategy, its core idea is to have a strong European Union with strong common policies. Hungary would like to avoid the formation of a multi-tier Europe and supports the Community method of cooperation. In terms of macroeconomic trends, Hungary was very severely hit by the crisis and has still a sluggish growth. While the government is making all efforts to keep budget deficit below 3% of GDP, the Commission will not lift the excessive deficit procedure against Hungary (in force since 2004) until it is convinced that the target can be met via sustainable structural reforms. Many of those reforms were already launched in Hungary, in terms of both tax reforms and expenditure restructuring but more efforts are needed.

The Hungarian government has a realistic approach to the Commission’s proposal on the size of the new multiannual financial framework, at the same time no further cuts would be acceptable. Regarding the proposed reforms on the revenue side, Hungary is against both new own resources (namely the new VAT revenue and the FTT). On the expenditure side, Hungary attaches utmost importance to both the CAP and cohesion policy therefore it formulated its criticism on several points of the Commission proposal, with special regard to further greening of the CAP (entailing extra costs for farmers coupled with severe sanctions), or within cohesion policy the introduction of transition regions and the Connecting Europe Facility both channelling money away from the least developed regions. The capping of cohesion assistance at 2.5% of GDP was not welcome by Budapest either. In the field of energy Hungary – just like the EU as a whole – is interested in a fully integrated internal energy market and a greater diversification of import sources to ease the dominant import dependence from Russia. In this framework Hungary is participating in several concrete projects (North-South projects, Nabucco pipeline). As to energy production, Hungary would like to continue nuclear power generation and has also pledged to increase the production and use of renewable energy. As regards enlargement, Budapest has always been a champion of further widening once the membership criteria are met by any European country. Due to its geographic and geopolitical situation Hungary would like to see the entire Western Balkan region in the EU and as close ties with the Eastern Partnership countries as possible.

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LATVIA

Sándor Meisel

1. Domestic political framework, EU strategy of the government

1.1. Overview of internal politics

Domestic political developments of Latvia were rather stormy and turbulent in 2011. After the parliamentary elections held in October 2010 the five parties of the newly formed saeima and the coalition government led by the head of the former cabinet Valdis Dombrovskis envisaged to continue the management of the crisis started in 2009. The 2011 budget was in line with the economic policy of the previous Dombrovskis government. In May 2011, President Zatlers unexpectedly called for a referendum to dissolve the parliament. By this step he aimed at breaking the deadlock between the legislative power and the judiciary on the elimination of the oligarchs' strong influence on the legislature. The President's decision coincided with the normal expiration of his mandate. A few days later the parliament said no to Zatlers' re-election and voted for

Andris Běrziņš to assume the post of the President of Latvia. The referendum initiated by President Zatlers was held in July 2011. Citizens opted for the dissolution of the saeima and opened the way to an early parliamentary election in September. The winner Harmony Centre, a pro-Russian centre-left party was not able to find partners for a coalition. Thus, a centre-right coalition government was formed in October 2011 under the leadership of Dombrovskis and with the participation of Dombrovskis' Unity group, Zatlers' newly created Reform Party, the National Alliance and independent ministers.

The forces in the present saeima, the remaining stable majority of the right wing parties, the aspirations of the government and those of the Prime Minister do not anticipate major changes in the country's general political orientation and in Latvia's attitude towards the main developments in the European Union. No major shift in economic policy is expected either. The economic policy measures since the beginning of the crisis management have been taken and pursued under the strict surveillance of the EU and the IMF and with the strong commitment of the leading political forces to complete the anti-crisis programme. This latter is reflected in Latvia's Convergence Programme and National Reform Programme. The exit strategy aiming at stabilising the economy, reducing imbalances and creating a sound basis for growth – as outlined in the IMF/EU-supported programme – still holds. Meanwhile, the global environment has deteriorated, worsening also the Latvian economic outlook and thus making the implementation of reforms more difficult. However, taking into account the new composition of the parliament, the preconditions are there for a faster and deeper reform process.[1]

1 *Swedbank Baltic Sea Report No. 28, 19 October 2011*

1.2. EU strategy of the government

The main characteristic features of the Latvian EU strategy in the accession and post-accession period were first of all the rather fast integration into common policies and institutions and acceptance of the EU conditionalities and asymmetric adjustment. Later, the Latvian policy has been focused on the remaining "leftovers"[2] namely: joining the Schengen area and the eurozone, eastern neighbourhood policy and the development of the European energy policy. These elements still remain in the forefront of the country's EU policy.

As a new momentum of this policy we have to mention the Latvian attitude towards the plans and steps of the European Union aiming at resolving the present crisis and difficulties of the euro area.

In the years of the global financial crisis Latvia had to ask for external financial assistance. The efficient and massive credit facilities of the IMF, EU and some Nordic banks helped the country to overcome the most serious short-term economic problems. Thus, the solidarity, including financial solidarity is of high importance in the approaches of the Latvian political leaders aiming at preventing crisis situations and finding appropriate solutions for the euro area. The Latvian government in the early stage of the euro crisis "announced its support for measures promoting stronger coordination and fiscal discipline at the EU level. So as not to foster a Europe of two speeds, the Latvian government urged that such measures be applied to all member states and not only to those members of the euro area. Latvia also backed the idea of the European semester, and the obligation of annually presenting stability and convergence programmes. However, according to

2 *The notion used by Vilpišauskas (2011)*

Latvian political leaders, the right balance should be found between EU surveillance and the preparation process of the national budget." The process should not limit "the rights of the institutions of the member states to determine and implement their chosen policy."[3]

Latvia was among those non-euro area countries that joined the Euro Plus Pact and that agreed on the measures leading to a greater fiscal integration decided on the EU Summit of 9 December 2011. The Latvian position was clearly explained by a high-ranking representative of the Foreign Ministry, saying that in the process of strengthening the economic and monetary union attention should be paid to three aspects. First, "the necessity to ensure compliance with the principles of democracy when deciding on matters vital for the society, such as possible amendments to the Treaty". Second is "providing for the balance between the EU's competences and national competences of the member states." Third, "a concerted action of involving all EU members in preparing decisions for an improved management of the eurozone's economy" is necessary.[4]

In May 2012, the Latvian parliament – with a convincing majority of the votes – has ratified the Fiscal Compact and has started the work to enact its principles into national legislation. "By ratifying the Fiscal Discipline Treaty in the parliament, our country has taken a significant step towards being part of the core of the European Union, that is, being among those keen to foster the economic growth and global competitiveness of the block. Latvia has already successfully proved that with a responsible fiscal policy, it is possible to overcome the crisis and resume growth. In the years to come, we will continue Latvia's economic breakthrough and keep a responsible fiscal policy high on the national policy agenda" noted the saeima's speaker.[5]

2. General economic analysis

2.1. Overview of main economic developments

Data reflecting general macroeconomic situation in Latvia show strong signs of recovering from the deep crisis of 2008-2010. The country experienced slight (0.3%) decline of the GDP in 2010. Next year the growth rate climbed up to 5.5%. According to Eurostat figures, as well as the Swedbank analysis,[6] due to the global slowdown in 2012 GDP growth is expected to be somewhat moderated (2.2%) and may reach 3.6% in 2013, which is slightly higher than forecasted before.[7] The growth is clearly export and investment driven. Investments are particularly strong in the exporting sectors and in the EU financed infrastructure. At the same time, private consumption remains weak and is anticipated to rise slower than GDP. Employment and wages have started to grow but the improvements will be sluggish and uneven. Unemployment rate in 2011-2012 will be still high but somewhat lower (14-16%) as compared to the 2010 level (18.7%).

Latvia's export structure has become more diversified over the years and the recent growth in export has contributed significantly to the overall economic recovery and the rebalancing of the economy towards tradable sectors. Nevertheless, major structural problems remain. Latvia's labour productivity, in terms of real GDP per

3 *Source of the citations: Bungs (2010a)*
4 *Source of the citations: Ministry of Foreign Affairs of the Republic of Latvia, press release of 6 December 2011*
5 *Ministry of Foreign Affairs of the Republic of Latvia, press release of 31 May 2012*
6 *Swedbank Economic Outlook, 24 April 2012*
7 *Swedbank Economic Outlook, 23 August 2011*

employed person is still significantly below the EU average and also below the level of other countries with economic similarities such as Lithuania and Estonia.[8]

The competitiveness of the country has improved due mainly to the lower than in the pre-crisis years labour costs. In the medium term they are expected to rise but only gradually, without damaging competitiveness. Lending activity of the banks is increasing and has resulted in better access to financing. The business environment has improved both from the point of view of funding and legal easing.

Table 1, Main macroeconomic indicators of Latvia

	2009	2010	2011	2012 (f)	2013 (f)
Real GDP growth rate (annual change, %)	-17.7	-0.3	5.5	2.2	3.6
GDP/capita, EU27=100	51	55	58	n.a.	n.a.
Gross fixed capital formation/GDP (%)	21.6	18.3	21.5	22.3	23.8
FDI inflow (BEUR)*	0.1	0.3	1.1	0.5	n.a.
Private consumption/GDP (%)	61.4	63.0	62.1	62.4	62.3
Public consumption/GDP (%)	19.6	18.4	16.2	15.9	15.3
Exports of goods and services (BEUR)	8.1	9.7	11.9	12.8	13.9
Imports of goods and services (BEUR)	8.4	9.9	12.7	13.8	15.1
Current account balance/GDP (%)	8.6	3.0	-1.2	-1.8	-2.6
Unemployment rate (%)	17.1	18.7	16.1	14.8	13.3
Inflation (HICP)	3.3	-1.2	4.2	2.6	2.1
Interest rates (10y)	12.4	10.3	5.9	n.a.	n.a.

*Eurostat, European Commission, * WIIW (f = forecast)*

Thus, in the coming years Latvia will have to face further challenges in order to improve the structural framework of the country's development path. Latvia is witnessing serious negative demographic trends. Diminishing population may negatively influence the tendencies of the internal demand.

8 *European Commission (2012)*

At the same time, it translates into the need for developing more sustainable social and pension systems. Latvia for a long period has been characterised by imbalances and rigidities of its labour market. The employment rate is one of the lowest in the EU. Resolving structural problems of the labour market, eliminating mainly geographical and qualification mismatches, improving the education system are also necessary preconditions to boost economic growth and to continue sustainable stabilisation of public finances.

2.2. Fiscal stability, economic and social competitiveness

Latvia submitted its National Reform Programme (NRP) and the updated Convergence Programme in April 2012. In its assessment of the similar Latvian document of 2011, the European Commission stated that both programmes reflect the objectives and actions required under the economic reform programme committed to by the Latvian government in connection with the EU financial assistance. According to the European Commission the macroeconomic scenario underpinning the budgetary projections in the Convergence Programme appears plausible.[9] In the latest assessment of 2012, the Commission gave a more detailed and more critical opinion. It states that overall, the policy plans submitted by Latvia are adequate, but in some areas they lack the ambition to address the challenges in a comprehensive way. The most pressing challenges facing Latvia are to continue growth-friendly fiscal consolidation and implement wide-ranging structural reforms to achieve sustainable growth and catch up with other EU countries. In particular, strong implementation of further measures will be important, inter alia in the fields of energy markets and energy efficiency, higher education and vocational training,

9 *European Commission (2011)*

management of state-owned enterprises, administration and the judicial system, competition and public procurement policies, restructuring and sales of state-owned banks and management of EU funds.[10]

The implementation of the IMF/EU programme has strengthened public finance discipline. The government deficit shows a declining trend. Although in 2011 it grew to 3.5% of GDP, according to the financial consolidation programme it is expected to remain below the 3% level in 2012 and 2013. After having reached a 45% level in 2010, government debt is likely to stabilise at around 40-45% in the coming years. Fiscal consolidation will continue, as the figures of the adopted 2012 national budget show, but to a much smaller extent than before. The fiscal consolidation part envisaged in the updated Convergence Programme relies on reduction of primary expenditure, mostly through general government consumption and social benefits. Austerity measures will mainly include spending cuts, while no tax hikes are expected.[11] Inflation – after a substantial jump to 4.2% in 2011 – is expected to be lowered to around 2.5% in 2012-2013. Despite the favourable developments of the past two years and the government's efforts, the introduction of the euro in 2014 seems to be problematic, although cannot be excluded.

Table 2, Public finances in Latvia

	2009	2010	2011	2012 (f)	2013 (f)
Public budget balance (% of GDP)	-9.8	-8.2	-3.5	-2.1	-2.1
Public debts (% of GDP)	36.7	44.7	42.6	43.5	44.7

Eurostat, European Commission (f=forecast)

10 *European Commission (2012)*
11 *Saeima press release of 16. 12. 2011*

The Latvian NRP was prepared by a broad inter-ministerial working group, where social partners were closely involved. The Cabinet of Ministers and the parliament also were consulted on several occasions as regards the Europe 2020 targets, the negotiation mandate with the Commission and the final text submitted to the Commission. Latvia defined the following main commitment to the national targets within the National Reform Programme.[12]

Table 3, Europe 2020 targets of Latvia

Europe 2020 targets	Situation in Latvia in 2010	Latvian Europe 2020 targets
Employment rate – 75% of 20-64 year-olds	64.7%	73%
R&D – 3% of GDP to be invested in R&D	0.6%	1.5%
Climate change / energy		
Reducing greenhouse gas emissions by at least 20%	40% of the 1990 level	-17% compared to the 2005 level
Covering 20% of energy consumption from renewables	30%	40%
Energy use in Mtoe (2009) Increasing energy efficiency by 20%	4.33 Mtoe	-0.67 Mtoe
Education		
Reducing school drop-out rates below 10%	15.2%	13.4%
Reaching tertiary education attainment by at least 40% of 30-34 year-olds	35%	34-36%
Poverty / social exclusion Reducing the number of people in or at risk of poverty or exclusion by 20 million	834,000	-121,000

European Commission

While social security expenditure as a share of GDP increased during the crisis, Latvia spends relatively little on social protection and social transfers. They have only little impact on poverty reduction, as a large share of them

12 *European Commission (2011)*

is redistributed back to middle- and high-income earners. Government policies to reduce poverty are concentrating on reducing income inequalities, easing tax burden on working families and improving access to the labour market. The government has decided to continue in 2012 most measures under the Emergency Social Safety Net Strategy adopted during the crisis.

The effects of an aging population and emigration will appear soon, posing serious challenges to the future sustainability and adequacy of the pension system. Several reforms are to be introduced: retirement and early retirement age limits will be gradually increased from 2014 on, the minimum insurance period will be raised from 10 to 15 years and the pension indexation will remain frozen until the end of 2013, consumer price indexation to be introduced afterwards. The contribution rates to the mandatory funded pension scheme are to be restored from 2% to 6% in January 2013.

3. Position and potential impact of Latvia on current key issues

3.1. EU budget: the multiannual financial framework for 2014-2020

Prior to the European Commission's proposal on the multiannual financial framework (MFF) for 2014-2020, in July 2011, both the saeima and the government approved Latvia's initial negotiating position over the multiannual budget. According to the Latvian national position, the country will focus on two key priorities. First, sufficient financing of cohesion, so that Latvia could faster achieve the EU average level and create favourable conditions for growth of the national economy and for the development of infrastructure. Second, providing a level playing field for the Latvian farmers in the common European market.[13] In the later stages of the discussions on the EU budget, after the publication of the Commission proposal, the Latvian government and the President formulated and reiterated several times their criticism on the Commission's text. The main point of the Latvian criticism is that cohesion funding planned for the country and direct payments to its farmers within the upcoming MFF is not satisfactory, and the solution should be sought to avoid a possible reduction in cohesion assistance and to address the unfairly low historically established level of direct payments.[14] The high representatives of the Latvian government stressed their conviction that fiscal consolidation and economic recovery measures implemented in Latvia would be a good argument for further negotiations in order to ensure more favourable conditions for Latvia.[15]

In October 2011, the Latvian government issued a detailed document summarising the main element of its views on the multiannual financial framework for 2014-2020 and on the European Commission's proposal.[16]

According to this document Latvia supports the continued use of a seven-year planning period. It corresponds to a compromise between sufficient financial predictability and the complexity of negotiating a financial framework. The Latvian government thinks that the overall size of the MFF should remain approximately the same as the current budget. However, Latvia prefers a bottom

13 *Ministry of Foreign Affairs of the Republic of Latvia, press release of 14 July 2011 and of 26 July 2011*
14 *Ministry of Foreign Affairs of the Republic of Latvia, press release of 10 November 2011 and of 6 December 2011*
15 *Ministry of Foreign Affairs of the Republic of Latvia, press release of 15 November 2011*
16 *Government of the Republic of Latvia (2011)*

up approach, where the size of the budget is determined by the actual needs of different EU policies, allowing the implementation of the Europe 2020 strategy and keeping up with global competition. Latvia is pleased that the overall structure of the budget has been kept. However, it believes that cohesion policy as one of the most important policies deserves the maintaining of a separate sub-heading in the future budget.

On the income side Latvia supports the idea that an emphasis should be put on the GNI-based own resource, since it requires the smallest administrative burden and is fair. The government agrees that the complex old value added tax based resource should be abolished, but at this stage does not support its replacement with a new one. Before moving forward with the introduction of new resources and especially of the financial transaction tax, Latvia would like to see impact assessments. Without such assessment it cannot support the financial transaction tax. Concerning traditional own resources, Latvia does not support the reduction of TOR collection costs from 25% to 10%.

3.2. Common agricultural policy after 2013

Agriculture and agricultural transfers are high priority issues for Latvia. Riga generally supports ideas aiming at modernising the CAP, at the same time wants to see Latvian interests duly taken into account. CAP is one of the most sensitive issues for Latvia in the debates on the future of the common policies and of the multiannual budgetary framework.

In October 2011, the European Commission officially presented the proposals on the CAP for the period of 2014-2020, including direct payments financing envisaged

for member states. According to the first Latvian reaction, “the proposal on reallocation of direct payments is a micro cosmetic move and window dressing, not real convergence.”[17] It falls short of having any ground from the impact assessment that the Commission produced earlier. Therefore it is not acceptable to Latvia. Latvian farmers receive three to five times less direct payments compared to most of the other farmers in other member states. Ever since the reform of the CAP in 2003, payments are decoupled from production and therefore already for eight years EU direct support is distorting competition inside the Union having vastly differentiated aid levels. In the government’s view, the proposal of the Commission is an outright discrimination of farmers in Latvia; it goes against the principle of fairness and equality. The distribution of direct payments envisaged by the Commission is not based on objective criteria, having a minimum effect on reduction of the huge gap between member states. The proposal discriminates Latvia’s farmers. Even more, the proposal for the reform means that after 2013 the EU support in agriculture will still be based on historical and outdated criteria from the 1990s. Thus, it does not reflect the actual market situation, and a new modern approach is needed for achieving Europe 2020 strategy goals. In the discussions on the Commission proposals, the Latvian government expressed its regret that the obvious lack of equal treatment of the EU farmers – as concerns support schemes – is still being overlooked and the proposed convergence of direct payments is not satisfactory.[18]

The Latvian demand is clear: Latvian farmers must be entitled to at least 80% of the average EU-level of the direct payments. The direct payments granted to any other

17 *Ministry of Foreign Affairs of the Republic of Latvia, press release of 12 October 2011*
18 *Ministry of Foreign Affairs of the Republic of Latvia, press release of 24 April 2012*

member state shall not exceed the level of 120% of the EU average. Latvia currently cannot support the proposal to make 30% of direct support conditional on the so-called greening, as there is still no analysis on the financial impact of this measure. Riga also considers the Commission's proposal regarding rural development as too general. This line is broadly accepted among not only farming organisations but also by the wider society.[19]

3.3. Cohesion policy after 2013

Concerning the proposals on the future cohesion policy of the EU after 2013, the Latvian criticism addressed several points. First, the possible decrease of the available financing. Latvia believes that the competitiveness of the EU cannot be achieved without internal cohesion. Therefore, without disputing the importance of global competition for future EU growth, the Convergence objective of cohesion policy is still one of the most urgent and important goals to be preserved also after 2013.

Second point is the capping of cohesion assistance at 2.5% of GDP. That would not reflect the actual absorption capacities that member states demonstrated in the current and previous planning periods. Besides, it is unfair. There are still significant disparities among the regions and the proposed capping mechanism would cut back cohesion policy resources allocated to the least developed countries, thus, would potentially widen the development gap among regions.

The third point of criticism is about the weak concentration of the funds on the less developed regions. For Latvia it is essentially important to keep the existing

19 *Ministry of Foreign Affairs of the Republic of Latvia, press release of 12 October 2011*

architecture of the cohesion policy and channelling the most substantial part of the resources to the development of the economically weak regions. This view does not mean that Latvia opposes making cohesion policy more efficient by clearly defining a limited number of thematic priorities in order to maximising the added value of this policy.

The fourth criticism is addressed to the unclear link between the new Connecting Europe Facility and the overall goals of catching up, although several envisaged projects in this framework are of great importance for the country.

The Latvian position stresses that the amount of money coming from the Cohesion Fund is of decisive importance in ensuring economic growth in Latvia. Despite the difficulties caused by the economic crisis, Latvia has successfully absorbed the financial instruments that have been available, and they helped to warm up the economy. Latvia is the best example demonstrating how a country can be returned to the path of growth by combining fiscal discipline measures with a targeted application of cohesion policy. According to the government, "this model should be implemented also elsewhere in Europe, to this end, adequate cohesion allocations should be ensured for the needs of each country and region", stressed the Minister of Foreign Affairs at the Bucharest meeting of the Friends of Cohesion Policy group.[20]

It is important for Latvia to make sure that during the next financial period resources from the Structural Funds are available at a sufficient level and can be used to even out differences in the standards of living in different regions of the EU. For that reason, Latvia cannot accept the proposal, especially the limitation of financing to 2.5% of GDP.[21]

20 *Ministry of Foreign Affairs of the Republic of Latvia, press release of 4 June 2012*
21 *Ministry of Foreign Affairs of the Republic of Latvia, press release of 12 October 2011*

3.4. Energy policy

Very strong and actively represented Latvian interests in the area of energy and energy policy are defined first of all by the fact that the country is heavily dependent on external energy resources. In 2009, the gross energy consumption of Latvia was 4.33 million tonnes of oil equivalent of which nearly 59% was originating from abroad. With this energy dependency ratio the country is above the EU27 average.[22]

Most of the energy in Latvia is consumed by households (39% which is higher than the EU27 average), followed by the transport sector (26% – lower than the EU average). The share of industry is 17%, which is below the average. Services consume 15%, agriculture 3% and both data are around the EU27 level. As far as the energy mix of the country is concerned, the share of renewable sources is high (37%), followed by petroleum products (30%) and gas (28%). The shares of electricity and of solid fuels are small (3 and 2% respectively), finally, there is no nuclear power production in the energy mix.

In the field of energy policy on the EU level, Latvia supports all initiatives aiming at improving security of supplies, diversification of supplier countries and regions. High priority of the country is – similarly to its Baltic neighbours – ending the isolation of the Baltic gas and energy market, developing secure interconnections with other EU members, increasing energy efficiency, maintaining and extending the share of renewable resources. Latvia supports the proposal to give the EU energy sector bigger weight in the upcoming MFF. At the same time, the country stresses that transition to the carbon-free economy will require additional funds at the EU level.

22 *Energy Portal of the EU*

3.5. External relations, enlargement, neighbourhood policy

Foreign policy of Latvia concentrates on clearly defined priorities and fields of interest. In the past few years principal attention of foreign policy was devoted to the following:

- *pursuing national interests in the European Union;*
- *expanding the Baltic states cooperation, with special focus on seeking joint solutions, in line with Latvia's interests, in trilateral energy and defence projects;*
- *strengthening Nordic-Baltic cooperation in all areas of interstate cooperation;*
- *building relations with Germany and Poland in a targeted manner;*
- *carrying out objectives defined in the NATO Strategic Concept;*
- *making external economic relations more dynamic through more effective efforts of diplomatic missions, enhancing cooperation with competent institutions in the area of economic cooperation (including future OECD membership), organising visits for companies to traditional and new markets, setting up a required legal framework;*
- *strengthening strategic partnership with the United States in security policy matters and in exploring possibilities for expanding economic cooperation;*
- *support for reinforcing stability and democracy in the Eastern Partnership countries;*
- *furthering relations with the Russian Federation;*

- *seeking solutions to facilitating cooperation with the diaspora abroad;*
- *providing support to Latvian citizens and permanent residents abroad and ensuring travel for foreign nationals with the purpose of activating economic and tourism relations.*[23]

Concerning the European Union, the following Latvian interests have been formulated:

- *the necessity of overcoming economic crisis in Europe;*
- *identifying interests and launching consultations on more beneficial conditions in the EU's multiannual financial framework, in view of the impact by EU-funded policies on Latvia's economy;*
- *preparations for the Latvian presidency of the Council of the European Union;*
- *communication of topical EU matters to the public;*
- *including in the EU programme documents the projects of priority for Latvia;*
- *preserving Schengen as an area for free movement.*[24]

Latvia continues its engagement in the EU's security and defence policy. Riga is convinced that the EU should concentrate more on strategic interests and new types of threats and devote special attention to raising the implementation effectiveness of the security strategy. The improvement of the EU and NATO relations and a deepening of strategic partnership in all levels is a priority for the

23 *Ministry of Foreign Affairs of the Republic of Latvia, Annual Report (2012)*
24 *Ibid.*

country. The broadening agendas of both organisations and growing operational demand determine the need for joint solutions and harmonisation of efforts, especially, in the area of building and developing capabilities, their mutual complementarity and potential deployment in international operations within the same territory.[25]

Latvia has participated with its staff in the following EU missions: the EU Rule of Law Mission in Kosovo (EULEX KOSOVO) with one expert, the EU Monitoring Mission in Georgia with two civilian experts. The Latvian observers have also been placed in Gori, near South Ossetia. Latvia also participates with three experts in the EU Police Mission in Afghanistan (EUPOL Afghanistan). In addition, Latvia supports the implementation of the EU Naval operation (EU NAVFOR ATALANTA) and the expected extension of its mandate. Riga gives financial contribution to the budget of operations without deploying its military contingent. This is also the case with Latvia's participation in the military mission for training the Somali Security Forces (EUTM Somalia) and contributing the joint budget of the EU military operation in Bosnia and Herzegovina (EUFOR ALTHEA).[26]

Enlargement of the EU is seen by the Latvian political leaders as a means to secure stability in Europe. Latvia supports the enlargement process based on individual approach and the fulfilment of the accession criteria. Riga played an active role in the accession process of Croatia by according general political support, by mediating in resolving the Slovene-Croatian conflicts and by sharing its accession experience. Latvia clearly supports the accession of the Western Balkan countries too, considering their

25 *Ministry of Foreign Affairs of the Republic of Latvia: The EU Common Security and Defence Policy*
26 *Ministry of Foreign Affairs of the Republic of Latvia: Participation in international operations*

membership perspective and accession process as an essential tool contributing to the success and continuity of their economic, social and political reforms. The Minister of Foreign Affairs recently stressed that Riga welcomes the launching of EU accession negotiations with Montenegro, as the country has achieved considerable progress with introducing the rule of law and fighting corruption and organised crime. At the same time, he added that there was still a lot to be done for Montenegro to fully comply with the Copenhagen criteria.[27] Latvia fully supported granting candidate status to Serbia at the European Council meeting in March 2012. At the same time, Riga advocated carrying out a feasibility study, which looks at the potential of concluding a stabilisation and association agreement between the EU and Kosovo that should serve as the next step towards regional stability.[28]

For the country it is particularly important to further develop close relations with the eastern neighbours by way of implementing joint projects in the framework of the Eastern Partnership (EaP). Riga supports the advancement of the negotiations on deep and comprehensive free trade agreements with those countries that are ready to meet the necessary conditions. Latvia also makes efforts to resolve the problems of visa free circulation of citizens of interested countries. According to the Latvian position it is vital to take a differentiated approach in this process. The EU should provide more support to those partner countries, which are more successful and faster in their reforms. Latvia highly commends the commitment of Moldova and Georgia to implement reforms and their progress in negotiations with the EU on free trade agreement and on visa liberalisation. Besides the framework developed by the EU, Latvia

27 *Ministry of Foreign Affairs of the Republic of Latvia, press release of 1 June 2012*
28 *Ministry of Foreign Affairs of the Republic of Latvia, press release of 28 February 2012*

established and maintains active bilateral relations with the EaP countries and encourages their European orientation.[29]

Although Riga emphasises its interests in developing first of all Eastern Partnership, according to Latvia, the future financing of the programmes for the European neighbourhood regions (southern and eastern countries) must take into account the commitments taken on the political level and also the geographical balance between those regions.

3.6. Special issues for Latvia

Latvia has strong natural and historical self-interest in the Baltic Sea region strategy in order to enhance the competitiveness and sustainability in the region. Riga is actively participating in formulating such initiatives. For Latvia the priority areas of cooperation in this region are establishment of interconnected energy networks, improving the business environment, enhancing environmental protection and strengthening public security, especially in order to fight crime in the region.

4. Summary and conclusions

In the first years of EU membership Latvia played a relatively passive role in formulating, initiating and shaping common policies and actions. It can be explained by lack of administrative capacity, experience and clear definition of integration goals. During the global crisis main preoccupation of the governments was focused on regaining financial stability and creating conditions for future growth.

29 *Bungs (2010b)*

Successes in this difficult process strengthened the self-confidence of the Latvian political elite that obviously results in increased activity in discussions on current issues of vital importance for the country. Being a non-member of the eurozone but having clear ambition to join it, Latvia represents a constructive approach to strengthening economic governance and creating closer fiscal cooperation. The proposals on the multiannual financial framework and initiatives aiming at reforming the most important channels of financial distribution (especially cohesion policy and the CAP) in many elements do not coincide with the Latvian interest. In the second half of 2011 and in the first half of 2012 Latvian politicians actively tried to use all fora to articulate the country's economic priorities, to defend Latvian interest and to influence the current discussions.

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LITHUANIA

Sándor Meisel

1. Domestic political framework, EU strategy of the government

1.1. Overview of internal politics

In the recent year the domestic political background in Lithuania was rather calm. No major changes and shifts were seen. The President, Dalia Grybauskaité enjoys stable position and high popularity. The Lithuanian legislature, the seimas has been elected in October 2008. The Prime Minister Andrius Kubilius and his three-party coalition government have been supported by a strong majority in the parliament. This support allowed the government to pursue its severe austerity programme. The consolidation measures made it possible to overcome the risk of insolvency. They were able to mitigate the effects of the global crisis and to re-establish a more balanced economic path. At the same time, the head of the government had to pay the price of the crisis management by a sharp decline of his popularity and finally, by losing the elections of October 2012.

Lithuania retains the strategic objective of adopting the euro as soon as 2014 or 2015, even though public opinion and support for this objective are somewhat weaker than previously.[1] Anyway, the prospective euro area membership has been an important driver for the adjustment process during the crisis and may play the same role in the coming years. The latter, together with the directions of the future economic policy depend on the composition of, as well as on the balance of political forces in the upcoming – most likely leftwing – coalition and new government.

1.2. EU strategy of the government

The Lithuanian government in 2007 adopted its detailed document on the country's EU strategy and its priorities.[2] It states that "Lithuania is interested in the strong and unanimous easy-to-approach European Union capable of competing on a global scale in the modern world and securing its common and individual interests in an efficient way. Lithuania supports further deepening of EU integration in the areas such as creation of the EU internal market, energy, and all other areas relevant to Lithuania, and will consistently seek to keep abreast and ahead of these processes. Also, the stronger the EU is, the more successfully Lithuanian national interests can be met."

The main strategic guidelines of this document among others stress the need for strong ties among European people, for opportunities and well-being of all, free and effective internal market. It states that the single currency represents the way towards further integration. The EU budget should address common problems. Attention should be focused on developing information society, integrated

1 *Swedbank Baltic Sea Report No. 28, 19 October 2011*

2 *Strategic guidelines of Lithuania's European Union policy for 2008-2013*

and efficient energy policy, clean environment, sustainable transport and rural development. Creation of an area of freedom, security and justice, as well as upgrading the EU's relations and cooperation with third countries, especially with neighbouring states are also among Lithuanian priorities.

Lithuania has formulated its strong position concerning the management of the global financial and economic crisis and about the recent plans to remedy the present crisis in the eurozone too.

During the financial and economic crisis, Lithuania experienced how fast and deep the world economy turbulences may affect small and outward-oriented economies in a globalised world, and how important solidarity among countries can be. The challenges and risks of the euro area crisis are also well understood by the leading persons of Lithuania. President Grybauskaité clearly stated that "the ongoing process in the eurozone and the protracted debt crisis will also affect Lithuania's economy therefore we would strictly comply with the fiscal discipline obligations and, in view of possible risks, demonstrate responsibility when forming the state budget for 2012."[3] In this spirit she welcomed the agreement reached on the EU Brussels summit held on 9 December 2011. The Lithuanian President stressed the importance of the fact that an absolute majority of the member states understood the complicated situation and had made a very important step forward to enhance the fiscal and economic discipline and responsible financial behaviour. She underlined that the agreement to be applied to the eurozone countries would be open to the remaining EU member states determined to adhere to responsible economic and financial policies. According to the President, this is a proof that Europe is

3 *President of the Republic of Lithuania, press release of 26 October 2011*

uniting and will cooperate more closely in economic policy coordination matters.[4]

Lithuania together with other 24 EU member states, signed the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union (Fiscal Compact). When submitting the Treaty for parliamentary ratification, the President underlined that "it is beneficial to Lithuania because it commits to stringent fiscal discipline and responsible economic policies. Lithuania is already implementing stringent fiscal policy rules. The Fiscal Compact will discourage excessive spending and financial populism. Regardless of which political party is in power, it will be obliged to deal with state finances in a responsible manner. Strict fiscal policies would help EU member states avoid insolvency problems, ensure their financial stability, prevent debt crises from arising in the future, and create a foundation for sustainable growth."[5]

This is a clear and straight supportive position and contribution from a country with aspirations to belong to the core of the EU and to become member of the euro area. "Lithuania and the Nordic-Baltic region as a whole can serve as an example for EU countries of the responsible attitude towards the management of finances and economic policy."[6] Nevertheless, Lithuania has reservations concerning strengthening the economic governance and the European semester. It wants to avoid a situation whereby a step towards the obligatory confirmation procedures of the national budgets would lead to an obligatory confirmation of taxes or budget expenditures, as such a scenario would not be favourable to Lithuania.[7]

4 *President of the Republic of Lithuania, press release of 9 December 2011*
5 *President of the Republic of Lithuania, press release of 30 May 2012*
6 *President of the Republic of Lithuania, press release of 16 November 2011*
7 *Valančiūtė, (2010)*

2. General economic analysis

2.1. Overview of main economic developments

In 2011, as a promising sign of recovery, the Lithuanian economy enjoyed a rather spectacular expansion: GDP growth rate reached 5.9% which was the second highest in the EU (behind the Estonian one). The recovery is expected to continue, although at a somewhat slower pace. It may come to around 2-3% this year and to 3.5% in 2013. Since the Lithuanian economy and its growth depend to a great extent on exports, the projected more moderate trend may be influenced by the global economic environment. Despite the strong dependency on exports, earlier major economic and financial imbalances have been reduced and the resilience against global turmoil is greater. The external balances have been substantially improved compared to the pre-crisis levels but recently the balance of trade and that of the current account are sliding into deficit.

Unemployment is decreasing although the government has to handle the still existing structural unemployment and labour market rigidities, due mainly to the long lasting mismatch between the skills of the unemployed and the needs of companies. Thus, it will be necessary in the future to introduce improvements in the functioning of the labour market. The main steps of further reforms would focus on making the labour market more flexible and easing the overregulation by moving toward more liberalisation. In order to remedy the mismatches between labour market demand and vocational skills further reforms are also needed, although as a result of crisis management, important structural improvements have been introduced in the Lithuanian system of education, especially in the higher education.

As a consequence of the anti-crisis measures, the competitiveness of the Lithuanian economy has improved. Real unit labour costs have declined and are now the lowest in the region. Due to the fact that unemployment still remains above the "natural" level, the upward pressure on wages will remain weak.

The Lithuanian government's main priorities were to improve the business climate, to reduce the scope of the shadow economy and attract more foreign direct investment. Nevertheless, the results are mixed. On the one hand, the rates of taxes, especially those of the personal income tax and corporate income tax are among the lowest in the region. On the other hand, the inflow of FDI is increasing but is still below the pre-crisis level. In combating or at least contracting the shadow economy, the governments have been introducing several measures to strengthen the rules but the success remains only partial and slow progress was made against corruption too.

Table 1, Main macroeconomic indicators of Lithuania

	2009	2010	2011	2012 (f)	2013 (f)
Real GDP growth rate (annual change, %)	-14.8	1.4	5.9	2.4	3.5
GDP/capita, EU27=100	55	57	62	n.a.	n.a.
Gross fixed capital formation/GDP (%)	10.5	16.4	18.8	19.6	20.6
FDI inflow (BEUR)*	0.05	0.6	0.9	1.0	n.a.
Private consumption/GDP (%)	69.1	64.4	63.8	64.8	64.7
Public consumption/GDP (%)	22.0	20.5	18.9	17.8	17.2
Exports of goods and services (BEUR)	14.5	18.8	24.0	26.2	28.5
Imports of goods and services (BEUR)	14.9	19.1	24.4	27.0	29.3
Current account balance/GDP (%)	2.8	1.1	-1.6	-2.0	-2.1
Unemployment rate (%)	13.7	17.8	15.4	13.8	12.7
Inflation (HICP)	4.2	1.2	4.1	3.1	2.9
Interest rates (10y)	14.0	5.6	5.2	n.a.	n.a.

*Eurostat, European Commission, * WIIW (f = forecast)*

2.2. Fiscal stability, economic and social competitiveness

The Lithuanian economy was severely hit by the crisis and underwent a sharp adjustment in 2009. Lithuania's membership in ERM2 was underpinned by sizeable fiscal consolidation and public and private wage adjustment. This policy action combined with an improved global environment helped to secure access to international capital markets and laid ground to the economy to return to growth in 2010, and even more in 2011. The government's measures to step up the pace of structural changes are set out in the updated National Reform Programme (NRP) and the Convergence Programme submitted to the European Commission in April 2012. As the similar Lithuanian document of 2011,[8] the updated version also reflects Lithuania's commitment to improve its competitiveness.[9]

The financial adjustment measures taken during the crisis resulted in a visible improvement of the public finances. The fiscal deficit went down from a high 2010 level (more than 7%) to 5.5% of GDP in 2011 and this year will be around 3%. The government debt – following its doubling by 2010 compared to the 2008 level – seems to stabilise at 38-40% of the GDP. Average annual inflation reached 4.1% in 2011, but is likely to come down to around 3% in 2012-2013.[10] The main task of the government in 2012 has so far been to avoid the worsening of these data. This makes it necessary also for the new government to continue the implementation of budget consolidation measures and not to stop stabilisation prematurely.

8 *European Commission (2011)*
9 *European Commission (2012)*
10 *Swedbank Economic Outlook, 23 August 2011 and 24 January 2012*

Table 2, Public finances in Lithuania

	2009	2010	2011	2012 (f)	2013 (f)
Public budget balance (% of GDP)	-9.4	-7.2	-5.5	-3.2	-3.0
Public debts (% of GDP)	29.4	38.0	38.5	40.4	40.9

Eurostat, European Commission (f=forecast)

In the assessment of the 2012 Lithuanian Convergence and National Reform Programmes, the Commission expressed also some points of criticism.[11] The country faces the most pressing challenges in the fields of public finances, the labour market, the energy sector as well as poverty and social exclusion. The budget deficit has to be further reduced to reach the medium-term objective. This would also help maintain the confidence of financial markets. A low labour force participation rate, shortage of skilled labour and skill mismatches, aggravated by high outmigration, are other major concerns in the medium and long term, given the ageing of the population. The growing poverty and social exclusion threatens to put an even higher strain on public finances in the near future. The country's infrastructure, particularly its energy system, lacks competition and interconnections and thus is a factor that hinders growth. Low energy efficiency, especially of buildings, as well as the low level of research and development spending and poor performance in innovation are pressing issues. Finally, in light of the persistent uncertainties in international financial markets, prudent and pre-emptive policies in financial regulation and supervision remain important.

Lithuania's targets specified in the National Reform Programme (NRP) for 2014-2020 set up the long-term development trajectory for the necessary modernisation of the country's economy and put imminent reform priorities in a broader context.[12] That was stressed in the last year assessment of the European Commission. The recent assessment added some other points. Although the policy plans submitted by Lithuania are relevant and substantiated, in some areas they do not address the challenges in a comprehensive way. The NRP contains further plans to maintain financial stability, foster employment, improve the business environment and regulation, further restructure state-owned enterprises, and improve energy connections and infrastructure. Medium-term plans include implementing social insurance reform, continuing reforms in the energy and health care sectors, as well as improving the business environment and conditions for research and innovation.[13]

Lithuania's social security system is also posing several problems, as the European Commission points out. Firstly, its pension system needs to be reshaped to become sustainable in the long run. Secondly, the global crisis has exposed a sizable number of people to the risk of poverty or social exclusion and resulted in a greater income inequality. Lithuania has addressed the recommendations related to social policies partially. More determined efforts are needed to reform the pension system. The effectiveness of the social protection system is still hampered by inadequate assistance and coverage and could be better targeted. However, the NRP does not present a clear solution. High income inequalities also remain an important issue.[14]

11 *European Commission (2012)*

12 *European Commission (2011)*

13 *European Commission (2012)*

14 *European Commission (2012)*

Table 3, Europe 2020 targets of Lithuania

Europe 2020 targets	Situation in Lithuania in 2010	Lithuanian Europe 2020 targets
Employment rate – 75% of 20-64 year-olds	64.4%	72.8%
R&D – 3% of GDP to be invested in R&D	0.8%	1.9%
Climate change / energy		
Reducing greenhouse gas emissions by at least 20%	44% of the 1990 level	-15% compared to the 2005 level
Covering 20% of energy consumption from renewables	15%	23%
Energy use in Mtoe (2009) Increasing energy efficiency by 20%	8.35 Mtoe	-1.14 Mtoe
Education		
Reducing school drop-out rates below 10%	8.1%	less than 9%
Reaching tertiary education attainment by at least 40% of 30-34 year-olds	43.8%	at least 40%
Poverty / social exclusion Reducing the number of people in or at risk of poverty or exclusion by 20 million	985,000	- 170,000

European Commission

3. Position and potential impact of Lithuania on current key issues

3.1. EU budget: the multiannual financial framework for 2014-2020

Opinions recently formulated by Lithuanian government officials are in line with and confirm the position formulated already in the course of the EU budget review in 2008.[15]

According to the Lithuanian opinion the multiannual financial framework for 2014-2020 should be based on the following basic provisions:

- *the budget should focus on generating the highest EU value added;*
- *budgetary allocations should be least possible distorting in terms of competition;*
- *the principle of coherence among EU policies should be applied;*
- *the budget should focus on supporting economic, social and territorial cohesion and promote solidarity of member states;*
- *the budget should be modern and flexible in response to emerging challenges.*

Concerning the total amount of the budget, Lithuania acknowledges that cuts in the 2014-2020 period may be necessary given the current financial realities, but severe cuts would reduce the European Union's capacity to act as a powerful global player. The size of the EU budget that is being proposed by the European Commission is acceptable for Vilnius, because it already includes the saving measures. Nevertheless, further cuts may reduce the amount of EU support to Lithuania for the period of 2014-2020. This case should be avoided.

Lithuania emphasises the three main priorities concerning the objectives and structure of expenditures:

- *strengthening the competitiveness of the EU (including efficient functioning of the single market, innovation policies, energy policy and integrated energy market, eco-friendly energy technologies),*
- *promotion of solidarity (including the continuity of EU cohesion policy, faster convergence),*

15 *Position Paper of the Republic of Lithuania on EU budget review (2008)*

- *ensuring security (efficient border control, efficient migration policy, reinforcing the EU's role as a global player, promotion of the neighbourhood policy with special attention to eastern neighbours).*

As far as the financing of the common budget is concerned, Lithuania wishes to see an improved system of own resources in order to ensure its transparency, effectiveness and sufficiency. Elimination of the VAT-based own resource and the EU financing system relying mainly on the GNI-based resource would be a real step forward in modifying the own resources system. Lithuania wants to ensure that in financing the EU budget, the fairness of contributions paid by member states is ensured, the less developed members should not make contributions for more developed countries. Therefore Lithuania is of the strong opinion that there should be no correction mechanisms in the own resources system, and no additional EU taxes should be introduced.

In the debates on the future multiannual financial perspective of the EU launched in 2011, the government formulated its starting position and priorities declaring that "Lithuania's key priorities in the new financial programme are the continuation of adequate funding of the EU's cohesion policy, ensuring equal direct payments to farmers in all EU member states, extending EU financing for energy infrastructure projects that are important for Lithuania and the whole Union. Furthermore, the EU's continued financing of the Ignalina nuclear power plant closure as stipulated in Lithuania's Accession Treaty is of utmost importance for the country."[16] Not surprisingly, Lithuania was not satisfied with the proposed principles of the new budget, particularly with the areas of cohesion, agriculture and energy security.[17]

16 *Ministry of Foreign Affairs of the Republic of Lithuania, press release of 29 July 2011*
17 *Ministry of Foreign Affairs of the Republic of Lithuania, press release of 20 October 2011*

3.2. Common agricultural policy after 2013

The Lithuanian starting position concerning future reforms of the CAP is based on the assumption that the CAP should remain a really common policy financed from the EU budget, thus Lithuania opposes any re-nationalisation. The country stands for equal competitive conditions for all member states, producing of competitive raw materials and food products, provision of high-quality food, application of uniform standards, development of rural territories, ensuring the implementation of the specific and multifunctional European agricultural model. Lithuania emphasises the need for fair allocation of CAP payments and for diminishing the existing disparities in financing and assisting agricultural producers. The official Lithuanian position underlined several times that the Commission's proposal was very unfavourable to the Baltic countries. "Big differences remain between "old" and "new" member states. Farmers in the Baltic states cannot compete equally on the single European market. Such situation cannot continue any longer."[18]

Following the European Commission's proposals in 2011, strong disagreement was formulated in Lithuania concerning the future of the common agricultural policy. Fair distribution of direct payments has a direct impact on successful growth of the EU economy and on the countries with relatively important agricultural sector. The Commission proposal, according to the Lithuanian government, "is obviously lacking ambition, the inequality of distribution remains too big, and this will continue to hinder effective functioning of the EU's internal market, and will hurt the competitiveness of the EU."[19]

18 *President of the Republic of Lithuania, press release of 29 June 2012*
19 *Ministry of Foreign Affairs of the Republic of Lithuania, press release of 20 October 2011*

3.3. Cohesion policy after 2013

Very similar reservation was declared about the main issues of the cohesion policy after 2013. Cohesion policy is to ensure that disparities between EU regions are reduced, however, the Commission proposal "could bring opposite results. This is contrary to the interests of the EU and Lithuania and to similar countries, and it is completely unacceptable", said the Lithuanian Minister of Foreign Affairs.[20] The proposed ceiling of 2.5% of GDP will dramatically reduce funding for the least developed EU regions, disproportionately affect the countries that have experienced the greatest decline of GDP and need help, and, moreover, will penalise member states with the best absorption rates of cohesion appropriations. Lithuania would receive less assistance because its GDP has fallen, even though the country was able to independently cope with the crisis. The Foreign Minister also asked the Commission to introduce more clarity with regard to the Connecting Europe Facility, a new instrument aimed at accelerating infrastructure development in transport.[21]

In general, Lithuania acknowledges that the new challenges, such as, demographic changes, increasing the global pressure to modernise, climate change, global energy situation are essential. These issues are in line with Lithuanian priorities, they should be addressed at the EU level. However, these new challenges should not overshadow the main objectives of cohesion policy and should not alter the purpose of this policy. Lithuania also believes that the EU structural assistance delivery mechanism may be simplified. According to the Lithuanian opinion, for the countries that suffered the most during the recession European structural support is a very important

20 *Ibid.*
21 *Ibid.*

factor in looking for ways to resolve the crisis and boost economic growth. This support is especially significant and relevant for the Baltic countries.[22]

3.4. Energy policy

Lithuania (similarly to Latvia) is highly dependent on energy supplies, coming mainly from Russia. The gross energy consumption of the country in 2009 was 8.35 million tonnes oil equivalent, out of which over 51% represented imports. In 2009 (the year before the complete closure of the Ignalina nuclear power plant) nuclear energy represented 31% in the consumption, the share of petroleum products and natural gas was 29% and 25% respectively. Renewables covered 10% of total consumption, while the share of other sources was rather low (2-3%).[23]

Energy policy issues have always played an important role in shaping the Lithuanian attitude towards the developments of the EU. Lithuania clearly supports all EU efforts to elaborate a truly common energy policy which guarantees secure access to energy at reasonable and stable prices. Lithuania as one of the initiators welcomed the decisions of the European Council held on 4 February 2012 that were taken regarding the creation of a competitive and well-functioning internal energy market. Energy security and the ending of the energy isolation of the Baltic region is also one of the key priorities of Lithuania. The Baltic states have been integrated in the EU politically and economically for more than eight years already, however the energy systems of especially Lithuania and Latvia are still dependent on Russia. The only way to protect Lithuania from monopolistic energy prices is integration into the

22 *President of the Republic of Lithuania, press release of 29 June 2012*
23 *Energy Portal of the EU*

European energy networks. Power and gas interconnections, the liquefied gas terminal are the most important factors to ensure economic independence in the region.[24] Lithuania wants to see a due incorporation of energy policy issues into the new multiannual financial framework. Moreover, the Lithuanian President at the Summit of 9 December 2011 made a successful proposal to include into the European Council statement the provision that energy isolation of the EU regions should be ended by 2015. After this political support Lithuania will seek financial assistance under the EU financial framework for the projects that are important for its energy security.

Lithuania devotes much attention to the external energy policy of the European Union. Vilnius emphasises that solidarity between EU members in this respect should not mean just empty pledges or an empty concept. If the EU makes practical steps to build energy interconnections and talks with one voice with partners from third countries, Europe soon will witness decreasing energy prices for the citizens.[25]

Lithuania has a specific energy policy issue which is related to the Ignalina nuclear power plant. Upon joining the EU Lithuania committed to close the plant for its own sake and for the sake of the entire Europe. The EU promised to financially contribute to the closure, which was completed by 2010. Since than, the Lithuanian economy and energy sector have to bear a heavy burden, and to face energy security challenges. Lithuania's dependence on supplies of natural gas and electricity from Russia has increased compared to pre-accession years, while integration with the EU has been absent. The dismantling of the plant was an unprecedented process, inadequate of the county's

24 *President of the Republic of Lithuania, press release of 1 December 2011*

25 *Ministry of Foreign Affairs of the Republic of Lithuania, press release of 20 March 2012*

size and economic capacity. Thus, further financing of the costs of the closure is of high importance for the country. Lithuania wants to see a strong commitment from the EU and real channels of financing, either in the EU budget, or elsewhere. "The European Union must fulfil its promise to finance the closure process to the end… Lithuania is carrying out its contractual obligations and hopes that the EU will do the same", stated once again the Foreign Minister at the General Affaires Council's meeting on the financial framework.[26]

3.5. External relations, enlargement, neighbourhood policy

Priorities of the Lithuanian foreign policy have been relatively stable. Consistent protection of national interests in the European Union, the implementation of the NATO's agenda, dynamic efforts to strengthen Lithuania's territorial, energy and technological security by exploiting all options offered by international organisations, the enhancement of the transatlantic dialogue, and constructive relations with neighbouring countries based on mutual respect and benefit constitute Lithuania's foreign policy priorities.

Lithuania has been an active participant of the CSDP missions in different parts of the world. Vilnius has taken part in the EU missions in the territory of the former Yugoslavia. The country was present with its military forces also in the missions in Iraq and Afghanistan. Lithuanian foreign policy objectives in the field of security and defence are among potential policy gains from security integration in the framework of the EU and NATO. According to the position of the government, CSDP could become an efficient means of ensuring its interests if CSDP and CFSP policy instruments are integrated efficiently and a full operational EU system

26 *Ministry of Foreign Affairs of the Republic of Lithuania, press release of 15 November 2011*

of crisis management is created. This would turn CSDP into an appropriate instrument for solving the "frozen" conflicts in the post-Soviet area, which is of high importance for the country.

Lithuania has always supported the enlargement policy of the EU, especially the accession of Croatia and the future membership of Iceland. Iceland was the first country to recognise Lithuania's independence. Regarding other countries, the government expressed several times its readiness to assist and support their accession process if they continue their reforms and become prepared for accession. Lithuania hopes to accelerate the move to further enlargement during its Council presidency in the second half of 2013.

While the Union for the Mediterranean is a low salience issue in Lithuania, the Eastern Partnership is one of the most important, top priority fields in Lithuanian foreign policy. It is an important field of action where it can provide different unilateral and multilateral proposals for the development of the initiative. At the Warsaw summit of the EU and Eastern Partnership countries on the 30 September 2011, President Grybauskaité underlined the need to speed up the process. Lithuania actively upheld Ukraine's goal to sign free trade agreement and the aspirations of Georgia and Moldova to start negotiations for such agreements. She stressed that visa liberalisation should be speeded up, it should not be slower than for Russia, and the same requirements should be applied to all eastern neighbours without double standards.[27] Efforts to bring the eastern neighbours closer to the EU by promoting the reforms, which are necessary for their closer integration, can be explained by both economic interdependency and a value-based approach.[28]

27 *President of the Republic of Lithuania, press release of 30 September 2011*
28 *Vilpišauskas (2011)*

3.6. Special issues for Lithuania

One of the special Lithuanian problematic fields has already been mentioned: the Ignalina nuclear power plant.

Together and in cooperation with Latvia and Estonia, Lithuania is active and strong supporter of the common Baltic Sea Strategy. The government stresses that the EU Strategy for the Baltic Sea Region is the first macro-regional strategy of the EU aimed not only at a more intense integration and development of the Baltic region, tackling common challenges in a more effective way, but also at making this regional approach a model for other EU regions.

Lithuanian concern and interests include among others energy security, environmental and economic issues. The country formulated four priority areas in the framework of the Baltic Sea Strategy: energy independence, enhancement of competitiveness of the region's economy, improvement in transport in the Baltic Sea states, thus, improved accessibility of the region and closer dialogue with third countries. Vilnius is ready to support the most ambitious version of the Baltic Sea Strategy and the objective to develop this region into a really integrated area of the EU. Through these plans and policy Lithuania wishes to increase both the competitiveness of the region and of the entire EU and to create an additional lever for getting out of the financial and economic crisis.

4. Summary and conclusions

The overall attitude and position of Lithuania on key European policy issues can be characterised by deliberate selection of those fields that are of the highest interest to the country and by the efficient concentration of its efforts

on these questions. Such issues are first of all the reform of both cohesion policy and the common agricultural policy and especially the development of a truly common energy policy with strong external dimension. Lithuania is also among the most active players in shaping and promoting the EU's relations with eastern neighbourhood countries. It is among those member states that are eager to build groups and coalitions with countries having more or less similar interests and actively initiates such cooperation, especially with countries of the Baltic region and certain Eastern European partners.

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PL

POLAND

Elżbieta Kawecka-Wyrzykowska

1. Domestic political framework, EU strategy of the government

1.1. Overview of internal politics

Parliamentary elections to both the senate (upper house) and the sejm (lower house) were held in Poland on 9 October 2011. They resulted in an impressive victory of the governing liberal-conservative Civic Platform (Platforma Obywatelska, PO) over its main rival, the conservative-nationalist Law and Justice (Prawo i Sprawiedliwość, PiS). Donald Tusk has become the first Polish Prime Minister to be appointed for a second term since the fall of communism. Both, the Civic Platform and its junior partner, the Polish People's Party (Polskie Stronnictwo Ludowe, PSL) agreed to continue their governing coalition after the elections. Members of the governing parties had, at the beginning of 2012, a simple majority of all votes (53%) in the lower chamber of the Polish parliament.

In his first address to the new parliament on 18

November 2011, Mr. Tusk laid out a programme of major fiscal and other measures, some of which were to make an impact already next year, most from 2013, while others, notably the proposed reform of the pension system, will bring benefits in the long term. The main elements of the reforms are the following:[1]

Immediate measures*:*

- *a 2-percentage point increase in the incapacity benefit contributions paid by employers, which took effect on 1 February 2012 (it will deliver the lion's share of the anticipated savings). The employer contributes 6.5% of the gross salary, while the contribution paid by the worker remains unchanged at 1.5%;*
- *a new tax on minerals (copper, silver), introduced in the second quarter of 2012;*
- *making owners of large farms pay health insurance contributions, as of February 2012;*
- *the closing of loopholes in capital-gains tax laws effective from 2012;*
- *the abolition of the internet-access tax break;*
- *cuts in child tax credits for the wealthy, or less generous income-tax deductions for high-earning creative workers, all to come into force as of 2013.*

The most important long-term measures are:

1 *Tusk announces major reform agenda for new government: http://www.polishmarket.com/113484/Tusk-announces-major-reform-agenda-for-new-government.shtml. Out of those proposals, the followings ones have been implemented by the middle of 2012: changes of the incapacity benefit contributions paid by employers (in February 2012); a new tax on copper and silver (in March 2012); modified health insurance contributions by farmers (in February 2012); increase of the retirement age (in May 2012); new pension rules for the unformed forces (in May 2012).*

- *a gradual increase of the official retirement age for men and women to a uniform level of 67 years, up from 65 and 60 respectively, starting from 2013 and to be completed until 2020 (men) and 2040 (women);*
- *less generous pension rules for the uniformed forces, miners and some other state employees, from July 2012;*
- *a change in the way pensions are adjusted to inflation: this change should be neutral for the budget while entailing some redistribution towards lower-income groups.*

Business groups and analysts welcomed the main elements of the programme, particularly the proposed pension reforms. However, they warned that the rise in employer-paid incapacity benefit contributions would increase non-wage labour costs and might stunt job creation or even increase unemployment. Public administration will also see cuts, with the exception of spending on the armed forces and the police – the military and the police will see a pay rise by 300 Polish zloty in 2012. While the majority of Poles supported the creation of the coalition cabinet after the autumn 2011 parliamentary elections, 100 days later (at the beginning of February 2012) this support has shrunk to 32%. At the same time, 38% of respondents were against the Tusk government. In October 2011, just before the parliamentary elections, the "first" Tusk government was positively assessed by 40% of persons asked and negative opinion was expressed by 28% of the polled citizens.[2]

2 *Sondaż (2011)*

1.2. EU strategy of the government

Poland held its first rotating presidency of the EU Council in the second half of 2011. Its priorities for the six-month term included strengthening the single internal market, strengthening the external energy policy of the European Union and its trade relations with third countries.[3] Another important task was to help the EU in its efforts to manage the sovereign debt crisis threatening Greece and the eurozone, although Poland's role was limited in that respect, as the country has not adopted the euro yet.

A broader reflection on the EU's future and Poland's position on it has found its expression in a speech delivered on 28 November 2011, in Berlin at the German Society for Foreign Affairs by Foreign Minister Radosław Sikorski, entitled "Poland and the Future of the European Union".[4] In his address, Mr. Sikorski underlined the need to deepen the integration of the EU in economic matters, preferably through European federalism. He also requested Germany to take the lead in solving the euro crisis.[5] The opinions on the speech were divided in Poland.

2. General economic analysis

2.1. Overview of main macroeconomic developments

In the past couple of years the Polish economy recorded the best economic performance among the EU member states. First of all, Poland is the only EU country which had positive GDP growth in recent years, including the recession year of 2009 (see Table 1). That is not to say that Poland has remained untouched by the financial crisis, but its relatively large domestic market (which reduces its dependence on exports) coupled with EU-funded public sector investments helped it through the first wave. In 2011, Poland's gross domestic product grew by 4.3% which represents an acceleration compared with the previous year (see Table 1).

The main engine of economic growth was domestic demand, which increased by 3.8% in 2011 (private consumption rose by 3.1%, while gross fixed capital formation went up by 8.7%). Fixed investments have been financed to a great degree by the EU's Structural Funds and the Cohesion Fund.[6] Economic performance of Poland has been in recent years much better than that of the other Visegrad countries, especially compared to the Czech Republic and Hungary where sluggish growth seems to prevail.

3 *In order to achieve these targets, the Polish presidency concentrated officially on three fundamental priorities: "European integration as the source of growth", "Secure Europe", and "Europe benefiting from openness", see more: Programme of the Polish Presidency: http://pl2011.eu/en*

4 *R. Sikorski, "Poland and the future of the European Union": http://polonia.nl/?p=6772*

5 *"The biggest threat to the security and prosperity of Poland would be the collapse of the eurozone. And I demand of Germany that, for your own sake and for ours, you help it survive and prosper. You know full well that nobody else can do it."*

6 *Polish Market (2012)*

Table 1, Main macroeconomic indicators of Poland

	2009	2010	2011	2012 (f)	2013 (f)
Real GDP growth rate (annual change, %)	1.6	3.9	4.3	2.7	2.6
GDP/capita, EU27=100	61	63	65	n.a.	n.a.
Gross fixed capital formation/GDP (%)	21.2	19.9	20.2	20.4	20.1
FDI inflow (BEUR)*	7.9	6.7	9.5	9.0	n.a.
Private consumption/GDP (%)	61.1	61.3	61.3	61.2	61.6
Public consumption/GDP (%)	18.5	18.9	18.1	17.8	17.7
Exports of goods and services (BEUR)	122.5	149.8	165.9	173.0	183.6
Imports of goods and services (BEUR)	122.3	154.1	170.0	175.0	186.2
Current account balance/GDP (%)	-3.1	-3.7	-4.3	-3.9	-4.2
Unemployment rate (%)	8.2	9.6	9.7	9.8	9.6
Inflation (HICP)	4	2.7	3.9	3.7	2.9
Interest rates (10y)	6.12	5.78	5.96	n.a.	n.a.

*Eurostat, European Commission, * WIIW (f=forecast)*

The report called "Poland's Public Finance in the Time of a Crisis", drawn up by the Ministry of Finance, sums up the period of 2008-2011 and presents a strategy for the coming years. According to this report, Poland has achieved – during the period in question – the highest economic growth rate of all EU member states: 15.8%, while the GDP of the European Union fell during the same period by 0.5%. Economic growth, avoidance of financial sector crisis, and – compared to the entire European continent – just a small increase of public debts (in relation to GDP) considerably contributed to the positive assessment of Poland's credibility appreciated by the financial markets and resulted in the IMF granting a so-called flexible credit line to the country. Poland has also managed to maintain its good rating (A+) which was deteriorated in the case of the majority of other EU member states.

According to Eurostat forecasts as of mid-2012, Poland would record a GDP growth of 2.7% in 2012, and a similar rate is expected in 2013 too. Inflation is predicted to reach 3.7% by the end of the year (and might further decline next year). Poland is one of the three EU member states that did not see its growth projection cut back in the European Commission's February 2012 review.[7] Moreover, the mentioned 2.7% is an upward modification (from 2.5%) issued in May 2012 by the Commission. The global economic crisis has caused an increase in unemployment and had an adverse impact on the Polish labour market, though a less severe one than in other EU countries. At the end of 2006, the unemployment rate in Poland was nearly 14%. At the end of 2008, it was reduced to 7.1%, but by 2010 it reached 9.6 with a similar rate to follow in 2011 (9.7%). For 2011 the ratio of jobless people was forecasted to increase slightly to 9.9%.[8]

2.2. Fiscal stability, economic and social competitiveness

One of the main goals of the Tusk government's reforms has been a substantial reduction of public debt and deficit. The latter is to be brought to the EU ceiling of 3% of GDP in 2012 while government debt is to be lowered to below 55% of GDP in 2013.

Table 2, Public finances in Poland

	2009	2010	2011	2012 (f)	2013 (f)
Public budget balance (% of GDP)	-7.4	-7.8	-5.1	-3.0	-2.5
Public debts (% of GDP)	50.9	54.8	56.3	55.0	53.7

Eurostat, European Commission (f=forecast)

7 *European Commission (2012)*
8 *Program konwergencji. Aktualizacja 2012*

Public debt rate relative to GDP has been in recent years around 55%, below the 60% Maastricht criterion. The main factor triggering its increase seems to be the constitutional ceiling at 60% and related executive acts which encourage the government to control effectively the public finances situation. The budget deficit has been for many years above the 3% ceiling, reflecting not only increased spending in the slowdown period but also structural deficiencies. Poland must cut its deficit to 3% by the end of 2012, or will face the risk of EU sanctions (under the Stability and Growth Pact), including a suspension of the Cohesion Fund. As regards Poland's competitiveness in the light of the Europe 2020 strategy, the country would like to increase its relatively low employment rate to 71% and to more than double gross domestic expenditure on R&D by the end of the decade. Some of the targets to fight climate change are a big challenge due to widespread use of coal.

Table 3, Europe 2020 targets of Poland

Europe 2020 targets	Situation in Poland in 2010	Polish Europe 2020 targets
Employment rate – 75% of 20-64 year-olds	64.6%	71%
R&D – 3% of GDP to be invested in R&D	0.7%	1.7%
Climate change / energy		
Reducing greenhouse gas emissions by at least 20%	83% of the 1990 level	-14% compared to the 2005 level
Covering 20% of energy consumption from renewables	7.9%	15.48%
Energy use in Mtoe (2009) Increasing energy efficiency by 20%	95.31 Mtoe	-14 Mtoe
Education		
Reducing school drop-out rates below 10%	5.4%	less than 4.5%
Reaching tertiary education attainment by at least 40% of 30-34 year-olds	35.3%	at least 45%
Poverty / social exclusion Reducing the number of people in or at risk of poverty or exclusion by 20 million	27.8% of the population	- 1 500 000

European Commission

3. Position and potential impact of Poland on current key issues

3.1. EU budget: the multiannual financial framework for 2014-2020

Poland's opinion is that the debate on the review of the EU's budgetary system is crucial for the Union not only for economic reasons (size of compulsory contributions to the budget by the member states, size of transfers and related advantages, etc.), but first of all because a debate about the future of the European budget is inseparably linked to a discussion on the future of the European Union and its

priorities.[9]

One of the crucial issues in this debate is the size of the EU budget. Poland is against further reduction of the budget. The continuation of such a trend will make meeting old and new challenges impossible. Poland stressed that in recent years the budget has increased in nominal terms but its relative size (share of total European Union GNI) has shrunk (to below 1% in terms of payments actually executed), even though the Union has enlarged and taken on new policy responsibilities. Poland is against freezing and/or further cutting back the EU budget. Poland argues that a bigger budget will encourage growth throughout the bloc. The Polish presidency declared in 2011 that the new EU budget should be an investment tool used for the purpose of implementing the Europe 2020 strategy.[10]

The Polish government supports the proposal of a new tax on financial transactions (FTT) as an own resource of the EU budget. The argument is that it is difficult to find an optimal budgetary resource and FTT seems to be a better solution than other proposals presented earlier by the Commission (especially as compared to the idea of a tax on CO2). With regard to the proposal on the European VAT, the general position is that this would be more transparent, easier to calculate than the present VAT-based resource and would result in the elimination of the British rebate (based now on VAT-related contributions). The European VAT proposal seems to have a number of advantages over the previous VAT-based revenue also from expert's point of view.[11]

Following Poland's proposal, 14 other countries have

9 *Prime Minister D. Tusk speech on 23 February, 2011: http://m.onet.pl/biznes/5017083,detal.html*
10 *Presidency Programme: http://pl2011.eu/en/program_and_priorities*
11 *E. Kawecka-Wyrzykowska (2008)*

supported (in May 2012) the declaration stating that the EU budget is "the main instrument of support of investment, growth and new jobs in the whole EU, as well as of structural reforms at the national levels".

3.2. Common agricultural policy after 2013

According to Poland, the positive elements of the Commission proposal in general are the following. Poland shares the goals: the CAP should be more competitive, more environment friendly as well as more pro-innovative. It should also address better food supply needs. Poland welcomes the proposal of a new instrument for risk management in agriculture which would be more responsive and better suited to meet new economic challenges. Also, Poland welcomes the digressive reduction of the biggest disparities (capping and other instruments) and some preferences for small farms.[12] The cutting back of the size of the CAP budget is however not welcome. In the years of 2014-2020 the average annual budget for CAP payments, as suggested by the Commission, is to remain below the level of 2013 (both pillars included), i.e. some 383 billion euros will be committed for the seven years period for natural resources.[13]

As regards the concrete points of the proposal, the assumptions underlying the Polish government's position[14]

12 *Agriculture of Poland on 12.10.2011; European Commission Delegation in Poland.*
13 *European Commission data, cited by J. Plewa, presentation of EU CAP after 2013, Delegation of European Commission in Poland, 10 October 2011, Warsaw.*
14 *Stanowisko Rządu Rzeczypospolitej Polskiej w sprawie przyszłości Wspólnej Polityki Rolnej Unii Europejskiej po 2013 roku, przyjęte przez Radę Ministrów 12.06.2009 (Position of the Government of the Republic of Poland on the future of the Common Agricultural Policy of the European Union, adopted by the Council of Ministers on 12.06.2009): http://www.minrol.gov.pl/pol/Informacje-branzowe/WPR-po-2013-roku/; Polska wizja Wspólnej Polityki Rolnej po 2013 roku – założenia i wstępne propozycje, Warszawa, listopad 2008 (Polish Position on the CAP after 2013, Nov. 2008): http://www.minrol.gov.pl/eng/content/view/full/2440, 10*

can be summarised as follows.

- **A)** *Previous instruments of the CAP (market interventions, direct payments, second pillar support) have positively affected the development of Polish agribusiness and rural areas, and have contributed to a tangible reduction of disparities between the Polish agricultural sector and that of the other EU countries.*
- **B)** *Poland aims at ensuring equal conditions for competition across all EU countries. Equal competition is possible only in the framework of the fully European (EU) mechanisms and instruments of the CAP; therefore Poland is against any renationalisation of the common agricultural policy.*
- **C)** *Any reforms of the CAP should have an evolutionary character. In order to adjust the CAP to new tasks (resulting among others from the Europe 2020 strategy) and challenges (the last ones are more and more of global, and not only of European dimension), the CAP instruments have to be modified so as to comply better with those new needs.*
- **D)** *Further simplification of the CAP is necessary and could also have an evolutionary trend.*
- **E)** *Poland supports the idea of strengthening rural areas and ensuring territorial cohesion across the EU (as in many regions, in particular in Central and Eastern Europe, agriculture remains an important sector of economic activity). Direct and indirect role of agricultural activity in rural areas is of crucial importance not only for economic, but also for social reasons, as well as for reasons of maintaining the landscape.*

- **F)** *After 2013, direct payments should remain the main instrument of the CAP, and should continue to be responsible for the following three aspects: first, support and stabilisation of agricultural income; second, compensating costs related to complying with high environmental standards; and third, maintaining agricultural production in regions with the most difficult conditions. Poland insists that direct payments be fairly distributed among all farmers across the EU. The amount of money provided for direct payments should not be less than in the present financial perspective. As regards the system of calculating the direct payments, the Commission has proposed SPS to be in force in all EU members after 2014, with some alignment of the level of payments. According to Poland, big disparities in the levels of payments among the EU members will remain under this system. Therefore, Poland proposes an area-based flat rate that would be an objective and fair basis for payments calculations. Furthermore, according to the Commission other market instruments should be based on the direct payments envelope. The consequences of such an approach to direct payments basis involve the probability of increased income disparities among EU farmers and also distortion of competition on the single European market. Therefore, the flat rate based on area would be a better solution.*
- **G)** *The second pillar is to be equipped with slightly more money than in the present perspective (now 21% of the CAP budget, later 25%). This pillar should be more important because of its functions (positive impact on environment; improved competitiveness of the agricultural sector etc.).*

- **H)** *Under the Commission's proposal there is a risk that in both pillars there will be more than less bureaucracy (especially with regard to the greening in the first pillar).*[15]
- **I)** *According to Poland, there is a lack of money under the proposed CAP budget for new tasks of this policy area resulting from the health check of 2008 which will affect negatively the competitiveness of EU agriculture in the future. Another issue is that the proposals do not address the objectives of the Europe 2020 strategy and unfortunately the whole policy will be further complicated not simplified.*

3.3. Cohesion policy after 2013

Poland has always argued that the cohesion policy should remain the Union's key policy as a tool which has benefited and shall continue benefiting all EU member states and which has been the best instrument of economic growth.[16] Accepting the view that a lot of new development challenges are ahead of the EU, Poland has stressed that if those challenges are to be effectively met, it is absolutely necessary to strengthen the Union's cohesion. Enhanced cohesion should include both its social, economic and territorial dimensions. In other words, Poland argues that the degree of the EU cohesion will determine the ability of the EU to adapt to a number of challenges facing the Union. Without further cohesion, the disparities in development levels will constitute a barrier to the deepening of integration.

The Polish presidency contributed much to the discussion on the cohesion policy after 2014. Using several valuable contributions of previous years, the Polish presidency prepared a roadmap which "converts key topics of the EU reflection into concrete actions to be taken for the purpose of integrating the territorial approach into the EU strategic planning, coordination of policies and institutional arrangements when delivering the Europe 2020 strategy."[17] In Poland's opinion, this document "could facilitate more coherence and systematic tracking of actions. National Territorial Cohesion Contact Points could act as a coordinator of the implementation of the Roadmap."[18]

Generally, the Polish government has supported the idea of a results-oriented cohesion policy[19] (based on the place-based development approach of public intervention as presented in the famous report of 2009, prepared under the direction of F. Barca).[20] Under this approach, public interventions should be tailored to places and should mobilise all actors at "place level" and use all natural and institutional resources of "places". The main principle underlying cohesion policy should not be "reduction of disparities" and "catching up" but support for growth potential, specific for each region. In other words, convergence seen as a guiding principle of cohesion policy may be a powerful motivating factor for many activities but cannot be the only centre of gravity of the policy. Results-oriented approach has been

15 *Wstępna ocena najważniejszych założeń pakietu legislacyjnego WPR2020 z perspektywy Polski (Preliminary opinion on the most important assumption of the legislative package CAP 2020 from Poland's perspective), 12.10.2011: http://www.minrol.gov.pl/pol/Aktowka/Ogloszenia/Wstepna-ocena-najwazniejszych-zalozen-pakietu-legislacyjnego-WPR2020-z-perspektywy-Polski, 10*

16 *Presidency Programme ... ibid. According to one of recent reports, each euro invested in the Visegrad countries has resulted in 61 cents of additional exports in the EU-15 countries, see: Ocena korzyści uzyskiwanych przez państwa UE-15 w wyniku realizacji polityki spójności w Polsce, 2012 Benefits of the EU-15 resulting from the implementation of cohesion policy in Poland): http://ibs.org.pl/site/upload/publikacje/raport%20strony%20ue-15.pdf*

17 *Roadmap (2011)*

18 *Ibid.*

19 *Stanowisko Rządu... (2012)*

20 *F. Barca (2009)*

reflected in the draft document "Strategia Rozwoju Kraju 2020" (Strategy of National Development 2020) which is to be a crucial basis for the use of EU Structural Funds in the coming years.[21] The assumption of this document is that regional development and reduction of disparities should not be based on equal distribution of financial means among all regions (let us remember that all regions in Poland qualify at present for ERDF as their GDP per capita is not higher than 75% of the EU average). The main targets of regional support should be metropolitan areas which are able to use the natural and institutional resources of their "places" and can strengthen the neighbouring areas due to the close functional and economic ties with them.[22]

The Commission's proposal to cap the maximum amount of total cohesion assistance to 2.5% of GDP of a beneficiary country has not been accepted by Poland, albeit not openly rejected. The government has argued that this ceiling should be different for individual countries. Moreover, the ceiling should be set at such a level as to guarantee – at least – the present value of support (in case the increase of money for cohesion policy is not possible).[23]

Under the Commission's proposal, an important element of results-oriented cohesion policy should be the setting up of clear outcome indicators. Indicators should be clearly interpretable, statistically validated, truly responsive and directly linked to policy intervention, and promptly collected and publicised. Poland stresses, that the idea of results-oriented approach may appear difficult to be implemented. The cohesion policy has by definition a long-term dimension, therefore it may be difficult if not impossible, to measure the results in short run and apply

21 *Projekt Strategii Rozwoju Kraju 2020 (draft proposal of Strategy of Country's Development 2020): http://www.mrr.gov.pl/rozwoj_regionalny/polityka_rozwoju/srk_2020/strony/srk_2020.aspx*
22 *Poland's position was presented by K. Niklewicz (2012)*
23 *Ibid.*

them as a criterion of future payments appropriations.

Another point of criticism is the Commission's proposal to strengthen the principle of conditionality. The most controversial issue is the proposal of macro-economic conditionality. According to this rule, the Commission (based on Council decision) would be empowered to suspend part or the whole amount of payments for countries which do not meet the conditions of the Stability and Growth Pact. The Polish government argues that this is a very dangerous rule.[24] First, it would result in suspension of money for countries which need the money most. Second, regions, entrepreneurs and other beneficiaries might be punished in form of suspension of structural support for lack of financial discipline of ministers of finance. As a result, conditionality may be hindering, instead of supporting, the development of less prosperous EU members and make more difficult the reduction of the socio-economic disparities in the EU. With regard to other aspects of the future cohesion policy, the Polish government has presented a relatively detailed position. It has stressed the necessity to support the following elements of the Commission proposal.[25]

A) *"A more integrated territorial approach to policy-making, taking into account the objectives of the policy enshrined in Articles 174 and 175 of the Treaty.*

B) *Better coordination between the EU funds (ERDF, ESF, CF, EAFRD, EMFF) through a common regulatory framework, and better coordination between cohesion policy and other EU policies or instruments*

24 *Let us notice that the present cohesion policy rules already involve some kind of macroeconomic conditionality but are not so much demanding as the recent Commission proposal.*
25 *Polish Presidency Conclusions on the territorial dimension of EU policies and the future cohesion policy (2011)*

having clear impacts on the EU territory.

C) *Enhanced strategic programming through a Common Strategic Framework (CSF), Partnership Contracts, and Operational Programmes.*

D) *Concentration of resources on meeting current challenges in the economic, social and territorial development to maximise also the contribution of Europe's territories to the delivery of the Europe 2020 strategy.*

E) *Strengthening of the urban dimension.*

F) *A commitment to partnership and multi-level governance.*

G) *Enhancement of administrative capacity of different institutions and actors operating at various levels (European, national, regional, local) to deal with issues related to programming and management of policy intervention."*

Also, a number of issues requiring further clarification and discussion with a view to improving the efficiency and effectiveness of the future cohesion policy have been listed. These include among others the following: a) Ensuring that the new programming framework promotes the integration and complementarity between European, national, regional and local polices. b) Providing adequate flexibility for programme strategies to meet the requirements of individual territories. c) Ensuring the reduction of administrative burden and simplification of the entire framework of programming. c) Maximising the possibility for the funds to be jointly used to finance programmes in order to facilitate an integrated approach. In January 2012, the Polish government adopted a position on all Commission

proposals of legislative acts covering cohesion policy.[26]

3.4. Energy policy

Poland's production of primary energy is based mostly on solid fuels (in that mainly coal and lignite).[27] This is in stark contrast with the majority of other EU members as the sources of energy production in the EU27 on average are much more differentiated. Similarly to the majority of EU member states, Poland is a net importer of energy (only Denmark is a net exporter). The share of imports in gross energy consumption amounted in 2009 to 31.7% which was well below the EU27 average. The ratio of import dependency in Poland is relatively low mainly because of large net exports of coal. At the same time, Poland is almost in 98% dependant on imports of petroleum fuels and in almost 66% on imports of gasses.[28]

The role of respective energy sources in Poland is the following. Poland has a low production of oil (around 1.3 Mt in 2009), and imports 95% of its needs. Approximately half of Poland's oil imports come from the Russian Federation, while the United Kingdom, Iran, and Norway also supply significant amounts of oil.[29] The production of natural gas (4.5 bcm in 2009) covers approximately one third of the gas needs. Supplies come primarily from Russia, to a lesser extent from CIS countries (mainly Turkmenistan) and around 6% from Germany.

Coal plays a dominant role in Poland's energy supply. The production of coal and lignite has however been falling

26 *Rząd RP… (2012)*

27 *Electric capacity by source is (2009): coal 87%; hydropower 7%; oil 3%; gas 1,8%; wind, geothermal 1%; biomass 0.2%, Supply: Energy Sources: http://www.enercee.net/poland/energy-sources.html*

28 *Europe's energy portal: http://www.energy.eu*

29 *Supply: Energy Sources, ibid.*

slowly over the last decade (163 Mt in 2000 compared to 135 Mt in 2009). This results mainly from a systematic decrease in hard coal extraction. The production is distributed between 60% bituminous coal and 40% lignite. Approximately half of coal production is intended for electricity production and another 22% for exports (14 Mt) which makes Poland the world's tenth largest coal exporter. The share of energy produced from renewable sources in the total primary energy production is gradually rising. In 2001 it amounted to only 5.1%, while in 2010 it reached 7.9% of the total energy produced. Renewable sources include mainly biofuels and wind energy. Poland currently does not operate nuclear power plants. However, according to Poland's energy policy the government plans to introduce nuclear energy by 2030. The programme envisages the construction of two nuclear power plants of 3000 MW each, with the first plant to be commissioned in 2020.

Poland's energy sector is facing huge challenges. In order to meet the strict EU environmental requirements the modernisation of existing installations is necessary as the existing system is old. It will also be important that investments are undertaken in the area of improving energy efficiency in the Polish power generation and transmitting sectors (the Polish power transmission and distribution system generates energy losses of 9.4%, which is one of the highest in Europe). Another problem is that around 87% of Poland's energy currently comes from polluting coal which hampers its drive to reduce carbon emissions. For the same reason the country says it needs "more time than others" to meet its CO2 reduction targets outlined in the Europe 2020 strategy. Poland also wants to reduce its reliance on natural gas imports from Russia as it is seen as a threat to the national security of energy supply. On 10 November 2009, the Council of Ministers of Poland adopted the Resolution no. 202/2009 on Energy Policy of Poland until 2030.[30] The document contains a long-term development strategy for the energy sector, the forecasted demand for fuel and energy, and an action programme until 2012. The main target is improved energy efficiency. This should alleviate the impact of growth in demand for fuels and energy, which in turn will contribute to increased energy security, due to reduced dependence on imports. The target is also to limit the impact of energy on the environment by cutting back emissions of greenhouse gases. All these goals should allow meeting the environmental protection commitments set out by the European Union (i.e. the "3x20%" targets to be reached by 2020).

In recent years Poland, like other EU member states, has been adjusting domestic legislation to successive EU laws relating to the energy sector and in particular to the third energy legislative package adopted by the EU in 2009, which entered in to force in March 2011. In autumn 2011, the Polish Ministry of the Economy stated that Poland adopted the laws of the energy package. The Commission expressed, however, its reservations with regard to adjustment of laws on liberalisation of prices of gas and electricity.[31]

Another instrument promoted by the third energy package is the so-called Third Party Access (TPA). This rule requires setting up an operator of energy infrastructure (pipelines, high voltage lines) which is independent from the producer of energy (the so-called unbundling). According to government information, TPA rule has been adopted in the recently renewed agreement with Russia on gas supplies. Other legal instruments enabling greater adjustment of the Polish market to the other EU member states' markets are

30 *Energy Policy of Poland until 2030: http://www.mg.gov.pl/files/upload/8134/Polityka%20energetyczna%20ost_en.pdf*
31 *http://www.wnp.pl/tematy/,2749_0_0.html*

three bills: the new Energy Law, the Law on natural gas and the Law on renewable energy sources.[32] In December 2011, the Ministry of Economy presented those bills for public consultation.

The security of gas supplies is to be enhanced in the future thanks to the new Trans-Caspian Gas Pipeline System. During the Polish presidency (in July 2011), the mandate for negotiations on the EU's agreements with Azerbaijan and Turkmenistan about the legal framework for the Trans-Caspian Gas Pipeline System was worked out. [33]

3.5. External relations, enlargement, neighbourhood policy

Poland's foreign policy priorities for the years 2012-2016 were presented by Foreign Minister Radosław Sikorski in an address before the Polish parliament on 1 April 2012, in which the Minister pointed to Germany and the US as the country's main allies. The EU's common security and defence policy (CSDP) is very important for Poland. Mr. Sikorski has described it as the second pillar of Poland's security policy, the first one being membership in NATO.[34] This policy makes it possible for the EU to conduct missions outside the EU borders in order to ensure peace, prevent conflicts and enhance international security.

Regarding CSDP missions with Polish contribution – according to the Foreign Minister – the country has taken part in a number of operations in areas far from its immediate neighbourhood. For example, Poland supported

32 *Energy policy: http://www.mg.gov.pl/Bezpieczenstwo+gospodarcze/Energetyka/Polityka+energetyczna*

33 *This mandate was adopted by the General Affairs Council in September 2011. The Southern Corridor is a priority corridor of imports of large quantities of gas to the EU, as it is aimed at ensuring diversification of sources of supply for Europe (in addition to the Norwegian, Russian and Algerian sources). See: Major results of the work of the Polish Presidency of the European Union Council (2011)*

34 *Polish Foreign Policy Priorities 2012-2016*

France during the Congo, Balkan and the EUFOR Tchad/RCA missions (the Polish contingent was one of the biggest ones). Poland also contributes to Eurocorps and was invited in 2011 to become its fully-fledged member. During its presidency, Poland persuaded all EU member states to activate the operational headquarters for EU operations in the Horn of Africa. Furthermore, Poland's contribution to CSDP has been reflected recently in the proposal (presented in January 2011) to set up the European Endowment for Democracy (EED). On Poland's initiative, the declaration on the EED was adopted during the Polish presidency. The EED, as a new instrument for supporting democratic transition processes in authoritarian countries and countries in the process of system transformation, fills the gap in the existing set of EU instruments.

Poland favours gradual accession of applicant countries to the EU, including the Balkan countries and Turkey.[35] This process should contribute to the stability in Europe. The EU's enlargement strategy (and concrete decisions with regard to individual applicants) should be based on rules of cohesion, conditionality and social communication. At the same time, the EU too should be ready to include new members.

Two eastern neighbours of Poland (Belarus and Ukraine) are addressees of the EU neighbourhood policy and in particular, of its regional component "Eastern Partnership" (Belarus, on the condition of proper reforms). The Eastern Partnership summit organised by the Polish presidency in September 2011, which gathered leaders from the EU and six former Soviet states, gave – in the opinion of the Polish government – new impetus to strengthen contacts with eastern partners.[36] Poland has supported the idea to

35 *Rozszerzenie Unii Europejskiej (Enlargement of the EU): http://polskawue.gov.pl/Rozszerzenie,Unii,Europejskiej,7652.html.*

36 *Major results of the work of the Polish Presidency of the European Union Council (2011)*

intensify concrete actions under the Eastern Partnership, among others speeding up negotiations with Ukraine on the Partnership Agreement (including a deep and comprehensive free trade arrangement). Negotiations were concluded in 2011 and the document was initialled by both parties on 19 July 2012. Because of the domestic political situation in Ukraine this agreement has not been signed yet.

In February 2012, Poland expressed its concerns relating to a new Commission document "Delivering European renewal" presented in 2011.[37] According to Poland, the Commission proposal reflects an unbalanced approach as regards priorities of cooperation with the EU's neighbours suggesting stronger actions (including aid) for Mediterranean countries than for eastern neighbours. Also, the Polish government has expressed its support for „Fast launching of effective negotiations on a deep and comprehensive free trade agreement with Georgia and Moldova".[38]

4. Summary and conclusions

As a result of autumn 2011 parliamentary elections, Poland has a stable political situation with the majority of all votes taken by two governing parties in sejm, i.e. in the lower chamber of the parliament. Public support for the government has shrunk in the first months of its term, partly because of the negative public assessment of the way some reforms have been introduced. Still, this support is at around 30% of all respondents. Despite the global financial and economic crisis, Poland has been recording for a number of years a relatively high economic growth and – as the only

37 *Stanowisko Rządu...(2012)*
38 *Ibid.*

EU member – avoided recession in 2009. The European Commission forecasts for 2012 for Poland are also relatively good. The public debt ratio to GDP has been in recent years around 55%, i.e. below the 60% Maastricht criterion. Public deficit is to be reduced to the 3% level this year and the consolidation of public finances continues next year too.

The Polish presidency of the Council in the second half of 2011 has increased the awareness of EU issues in the Polish society and the importance of the developments in the EU for domestic affairs. Poland is very much interested in the satisfactory outcome of the negotiations on the multiannual financial framework 2014-2020, mainly because the country is now the biggest beneficiary of the EU funds under cohesion policy. Also, there is the general awareness of the mobilising role of EU funding in many other areas of activities. The government has supported the idea of the financial transaction tax, and a general support for new VAT-based resource (European VAT) has been expressed too.

The most detailed position has so far been worked out with regard to cohesion policy. The general approach underlying the Polish position is that the main targets of regional support should be metropolitan areas which are able to use the natural and institutional resources of their "places" and can strengthen the neighbouring areas due to the functional and economic ties with those areas. This means a substantial shift in the approach to the future EU regional policy. Earlier, a more egalitarian approach was applied: cohesion support first of all for the poorest regions.

The general opinion in Poland on the Commission's proposal on CAP changes is more critical than on other issues. The most controversial elements for Poland are: the basis of calculating direct payments (Poland supports the idea of an area-based flat rate), more bureaucracy instead of simplification of CAP rules, lack of money under the

proposed CAP budget for new tasks of agricultural and rural policy.

Poland is currently implementing its energy policy until 2030 which should allow meeting the environmental protection commitments set out by the European Union. The focus is on improved energy efficiency. Due to high dependence on solid fuels (coal and lignite) meeting the Europe 2020 goals will be difficult and costly, especially regarding the reduction of CO2 emissions.

Poland favours successive EU enlargements, providing that the applicant countries meet political and economic criteria of EU accession. In the framework of the European neighbourhood policy, Poland's priorities are the following: the EU should devote more attention to its eastern neighbours, in particular to Ukraine, Belarus, Moldova and Georgia. Stronger commitment should be reflected in greater financial and organisational support for those countries, as well as more conclusive actions in order to conclude agreements on deeper trade liberalisation with those partners.

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ROMANIA

Ágnes Orosz

1. Domestic political framework, EU strategy of the government

1.1. Overview of internal politics

In Romania after the November 2008 parliamentary elections, the government was formed by the centre-right Democratic Liberal Party (Partidul Democrat Liberal, PD-L) and the centre-left Social Democratic Party (Partidul Social Democrat, PSD)."[1] However, one year later – due to internal tensions in the coalition leading to a governmental crisis – the configuration of the structure of the parliament has changed; the PSD became along with the National Liberal Party (Partidul National Liberal, PNL) a major opposition party. Even though the potential new Prime Minister, Liviu Negoiţă (PD-L) was mandated by the President on 6 November 2009, parliament did not consider

1 *Quote from OSCE (2010)*

the presidential proposal.[2] As a consequence, outgoing Prime Minister Emil Boc remained in office as caretaker Prime Minister.

The Romanian government called a presidential election for 22 November 2009, and for the second round between the two candidates who received the highest number of votes for 6 December 2009. Thus, incumbent centre-right President Traian Băsescu of the Democratic-Liberal Party (PD-L) faced off with former Foreign Minister Mircea Geoană, the leader of the Social Democratic Party (PSD).[3] The run-off ended in a narrow victory by 50.33% in favour of Băsescu.

The PD-L did not have any parliamentary majority and the parliament surpassed the 14-day limit for the hearing of the members of Negoiţă's cabinet, thus extending the political deadlock in Romania and leaving Emil Boc in office as Prime Minister. On 17 December 2009, he was given a mandate by President Traian Băsescu to form a new government, afterwards receiving the vote of confidence from the parliament. At that time, a new governing coalition was formed by PD-L and the Democratic Alliance of Hungarians in Romania (UDMR) with the support of the other national minorities and independent MPs.[4] The government formation by Boc could be considered as an end of a political crisis.[5] In spring of 2010, a new party, the National Union for the Progress of Romania (Uniunea Naţională pentru Progresul României, UNPR) was born; it was formed by a group of independents who left the Social Democratic Party. Since its formation the party supported the government led by Emil Boc.[6]

2 *Ibid.*
3 *OSCE (2009): Romania. Presidential election 22 November 2009. OSCE/ODIHR, Warsaw*
4 *Who later formed UNPR.*
5 *DW (2009)*
6 *Infopolitic: Uniunea Naţională pentru Progresul României*

A new austerity budget for 2010 was approved as a first act of the Boc government. For the year 2010 the cabinet introduced austerity measures including cuts in public wages by 25% as well as pensions by 15% and a raise of VAT rates to 24% (up 5%) with the aim of reaching 1.2 billion euros additional revenue. Furthermore, the interventions were also accompanied by massive layoffs in the public sector to maintain budget balance.[7] The implemented fiscal consolidation was one of the most extensive in the European Union that is why it is not surprising that country-wide demonstrations occurred later on.[8] As a consequence of the demonstration on 6 February 2012, Prime Minister Emil Boc with the entire government resigned. President Băsescu nominated Mihai Răzvan Ungureanu, previously the head of the foreign intelligence service, as Prime Minister in charge of forming a government.[9] At the end of April 2012, the President appointed Victor Ponta, the head of the Social Democrat Party after the previous government being unseated in a non-confidence vote. The new cabinet was formed by Romania's leftist opposition alliance, the Social-Liberal Union[10] (Uniunea Social Liberală, USL) which gained strong public support in the local government elections in June 2012. The USL has made one step further for a potential victory on the forthcoming elections, however even Ponta's resignation has been likely due to a plagiarism scandal. In the meantime, there was a political clash between Mr. Ponta and Mr. Băsescu the former installing another President temporarily. But after an invalid referendum in Romania in the end of July, Mr. Băsescu could finally remain in office. While the plagiarism scandal has calmed, recently the ongoing political crisis and the status of democracy have

7 *Pietras, J. (2012)*
8 *Canaragajan, S. – Brownbridge, M. – Paliu, A. – Dumitru, I. (2012)*
9 *Euractiv (2012a)*
10 *Political alliance between PSD, the National Liberal Party and the Conservative Party.*

been hitting the international media.

1.2. EU strategy of the government

Romania has voiced interest in its association to the consolidation of the European economic and monetary union, bringing back on a track of sustainable growth the eurozone, to which Romania is tightly connected. Romania in general is a pro-European country all major parties in parliament are in favour of deepening and advocate a more integrated union that might lead to a kind of a United States of Europe.[11]

Romania announced its decision to join the Euro Plus Pact during the March 2011 European Council meeting with the aim of strengthening public finances and promoting sustainable growth. Since its adoption Romania has made significant progress, especially in the field of financial stability.[12] The Romanian government even has approved the signing of the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union (the so-called Fiscal Compact) which enforces strict budget rules for member states that ratify it.

Romania is interested in further being a strong and serious partner for the promotion of the Eastern Partnership (with special regard to assisting Moldova in its rapprochement to the EU)[13] and the Strategy for the Danube Region is also a priority for the government. Romania is in favour of the construction of the Nabucco gas pipeline as an accentuated EU-funded project.

Romania received balance-of-payments assistance from the EU in May 2009 (up to 5 billion euros). The EU assistance came in conjunction with loans of the IMF (13 billion euros), the World Bank (1 billion euros) and the EIB and the EBRD (1 billion euros). The package was designed to enable the economy to withstand short-term liquidity pressures while improving competitiveness and supporting an orderly correction of imbalances in the medium term.[14]

Romania's most severe economic problem is that it has the lowest absorption rate of Structural and Cohesion Funds in the EU – less than 10%. Romania is already receiving some external help to spend EU money and enjoys the technical assistance of several experts from the EIB, the EBRD, the World Bank and the International Monetary Fund in order to increase the absorption capacity of the country. Boosting the use of the available EU funds would substantially contribute to the recovery of the Romanian economy.[15]

2. General economic analysis

2.1. Overview of main macroeconomic developments

Romania suffered a severe recession in 2009; gross domestic product shrunk by 6.6% consequently, radical fiscal consolidation was implemented with a significant improvement of the structural deficit. Fiscal consolidation consisted of both revenue and expenditure side measures. In 2010, the contraction of the gross domestic product was 1.6% and recovery began in 2011 when Romania reached a 2.5% growth rate. The Romanian government calculates with a 1.7% growth this year, and the Eurostat projection

11 *Consulate General of Romania in Sydney (2012a)*
12 *Government of Romania Ministry of Foreign Affairs (2012)*
13 *Ghinea, C. – Chirilă, V. (2010)*
14 *European Commission (2009): Economic Crisis in Europe: Causes, Consequences and Responses. Director-General, DG Economic and Financial Affairs, European Commission*
15 *EurActiv (2012b)*

of July 2012 shows a similar, 1.4% rate in 2012 and nearly 3% in 2013. As can be seen from Table 1, the Romanian revival is driven by investments and exports while private and especially public consumption is declining.

According to Eurostat external trade statistics Romania's exports amounted to over 52 billion euros in 2011, registering an 18.2% increase, as compared to 2010. Import increased at a similar pace and reached some 59 billion euros. Romania's trade deficit thus stood at about 7 billion euros (close to the level registered in 2010 and 2009) and is expected to grow further in 2012. The intra-EU trade is slightly above 70% of the total volume of trade. Romania's most important export items are machinery and vehicles, the largest exporter company is Automobile Dacia Groupe Renault.

In 2011, the Romanian export to non-EU countries continued to follow an upward trend. Canada's importance as export destination has increased significantly, especially in the field of machinery, electrical devices, boilers, nuclear equipment and spare parts for planes. The volume of exports to the US, Brazil, the Russian Federation, Ukraine and Turkey was also on the rise. The closure of the Nokia plant in Cluj county can negatively impact on the export potential, however the place left by Nokia can be filled by the Italian company DeLonghi. The latter took over some of the production units previously held by Nokia in Cluj county.[16]

16 *According to Radio Romania International (2012)*

Table 1, Main macroeconomic indicators of Romania

	2009	2010	2011	2012 (f)	2013 (f)
Real GDP growth rate (annual change, %)	-6.6	-1.6	2.5	1.4	2.9
GDP/capita, EU27=100	47	47	49	n.a.	n.a.
Gross fixed capital formation/GDP (%)	24.4	24.0	24.6	25.9	26.6
FDI inflow (BEUR)*	3.5	2.2	1.9	1.5	n.a.
Private consumption/GDP (%)	62.1	64.0	62.0	61.9	61.3
Public consumption/GDP (%)	18.5	16.4	14.4	14.2	13.9
Exports of goods and services (BEUR)	36.2	44.0	52.3	55.1	60.8
Imports of goods and services (BEUR)	43.3	50.5	59.4	63.7	69.5
Current account balance/GDP (%)	-4.2	-3.9	-4.1	-5.0	-5.0
Unemployment rate (%)	6.9	7.3	7.4	7.2	7.1
Inflation (HICP)	5.6	6.1	5.8	3.1	3.4
Interest rates (10y)	9.69	7.34	7.29	n.a.	n.a.

*Eurostat, European Commission, * WIIW (f=forecast)*

In Romania, the recession and the austerity measures have drastic consequences on the labour market. Most austerity measures (amounting to 7% of GDP in the period of 2008 and 2011) had far-reaching impacts on public employment levels, pensions and other transfer payments and public sector wage levels. Employment rate is around 63%, after a continuous rise recorded during the period 2005-2008, employment began – as a consequence of the crisis – to decrease in 2009, reaching its lowest value in 2010, meaning 9.24 million persons. The most accentuated falls in employment were registered in manufacturing, construction and trade. The unemployment rate is relatively low however, since 2008 the number of registered unemployed increased to 7.4% in 2011. At the same time, a reduction of this level is predicted for the coming years.

2.2. Fiscal stability, economic and social competitiveness

Fiscal stability has been reached by both revenue and expenditure side measures. Revenues have been increased by raising the VAT rate and eliminating VAT loopholes, the expenditure side cuts have been carried out by reducing salary and wage expenditures in the general government budget. Public debt rose sharply, by 21 percentage points of the GDP between 2008 and 2011. Persistent reduction of the public debt is predicted until 2016 however this level is far below the 60% threshold. The forthcoming elections in the end of 2012 and in 2014 (parliamentary and presidential) will be a test of public support for fiscal consolidation, once the immediate threat of the fiscal crisis has passed.

In April 2011, the Romanian government prepared its Convergence Programme[17] for the period of 2011-2014. The current Convergence Programme confirms Romania's intention to reduce the structural deficit to less than 2% of the GDP until 2014, ensuring a sufficient buffer to avoid above 3% budgetary deficit. Romania's strong commitment for adopting the euro in 2015 is an important anchor of the fiscal policy and significant factor of promoting budgetary and structural reforms, however according to the Convergence Report carried out in May 2012, euro introduction date is to be revised.

Over the reference period from April 2011 to March 2012, the 12-month average rate of HICP inflation in Romania was 4.6%, well above the reference value of 3.1% for the criterion on price stability. Out of the five convergence criteria only the government debt ratio is far below the reference value, even with its slight projected increase to 34.6%. At present, Romania is under excessive deficit procedure, but as can be seen in Table 2 the figures show a fast declining trend. The Romanian leu is not a member of the ERM2 system yet, in 2010 the national currency was broadly stable, then appreciated modestly in the first half of 2011, and has since then gradually depreciated against the euro.[18]

Table 2, Public finances in Romania

	2009	2010	2011	2012 (f)	2013 (f)
Public budget balance (% of GDP)	-9.0	-6.8	-5.2	-2.8	-2.2
Public debts (% of GDP)	23.6	30.5	33.3	34.6	34.6

Eurostat, European Commission (f=forecast)

Considering the Europe 2020 strategy, the Euro Plus Pact, and the financial assistance agreement with the EU and the IMF, the Government Programme agreed upon four key issues. First objective is to promote competitiveness, which is a relevant shortcoming if we take into account the different competitiveness rankings in which Romania lags behind. There is actually much room for improvement, through a frame of lifelong learning, strengthening R&D&I potential and developing European cooperation in this area, as well as attracting foreign investments among others. Second objective of the government programme is the promotion of employment with the main aim of increasing flexibility on the labour market. The third key issue is ensuring the sustainability of public finances with continuing fiscal consolidation and implementing structural reforms. Reaching financial stability has been defined as a fourth objective with regulations on foreign currency borrowing, consolidation of the banking system and applying new prudential rules to loan institutions.

17 *Convergence Programme of Romania 2011-2014*

18 *European Central Bank (2012)*

Table 3, Europe 2020 targets of Romania

Europe 2020 targets	Situation in Romania in 2010	Romanian Europe 2020 targets
Employment rate – 75% of 20-64 year-olds	63.3%	70%
R&D – 3% of GDP to be invested in R&D	0.5%	2%
Climate change / energy		
Reducing greenhouse gas emissions by at least 20%	52% of the 1990 level	-19% compared to the 2005 level
Covering 20% of energy consumption from renewables	20.5%	24%
Energy use in Mtoe (2009) Increasing energy efficiency by 20%	35.43 Mtoe	-10 Mtoe
Education		
Reducing school drop-out rates below 10%	18.4%	11.3%
Reaching tertiary education attainment by at least 40% of 30-34 year-olds	18.1%	26.7%
Poverty / social exclusion Reducing the number of people in or at risk of poverty or exclusion by 20 million	41.4% of the population	-580,000

European Commission

3. Position and potential impact of Romania on current key issues

3.1. EU budget: the multiannual financial framework for 2014-2020

Romania finds the Commission's June 2011 proposal, calling for a moderate overall cut in spending and the maintenance of the structure of the CAP and cohesion policy, quite acceptable. However, the overall shift of emphasis from support for agriculture towards R&D is less desirable, as are the initiatives to relocate funds from the least developed regions towards more consolidated areas of the net contributor states.[19] Romania as a net recipient country is satisfied with the magnitude of the proposal. On the revenue side the Commission would like to introduce two resources: a new form of VAT and the financial transaction tax (FTT) on shares, bonds and derivatives. With regard to the introduction of the FTT, Romania shows no particular support, however would not block it as long as it is collected EU-wide, with the purpose of flowing into the EU budget and being redistributed among all member states – a long-term vision of the FTT in contrast to alternative proposals to utilise it as a crisis-stabilisation mechanism useful to indebted, individual states.

Table 4, Romania's reactions to the Commission's MFF 2014-2020 proposal

Level of agreement with Commission Proposal							Media coverage
Expenditure			Size of the Budget		Own resources		
Cohesion Policy	CAP	R&D	Size of MFF	Outside the MFF	VAT	FTT	
largely agrees	agrees	n.a.	agrees	largely agrees	not in favour, nor against	n.a.	low

Mijs, A. – Schout, A. (2012), p. 3.

Romania – alongside Hungary, the Czech Republic or Bulgaria – is likely to oppose new taxes, but only after an impact assessment. In net beneficiary countries, such as Romania, the media reaction towards the MFF 2014-2020 was relatively low; obviously in net payer countries the reactions were harsh. Romania considered the proposal as a starting point for further negotiations, and in general is in favour of changes which contribute to the improved

19 *Sobják, A. (2012)*

transparency of the EU budget.

3.2. Common agricultural policy after 2013

When analysing economic output by activity, it can be concluded that in Romania agriculture is an important sector. According to Eurostat "agriculture, hunting and fishing" made up around 6.7% of GDP in 2010. A sharp reduction in the share of agriculture in GDP occurred, from 12.1% in 2000 to 6.7% in 2010. However, the Romanian value is the highest in the EU, far above the EU27 average of 1.7% of GDP.[20] Romania agrees with the changes of the CAP because there is substantial difference in direct payments, particularly affecting Central and Eastern European member states.[21] Currently, direct payments are based on historic entitlements rather than definitive need for social welfare in agriculture. For example, Belgium receives 462 euros per hectare whilst Romanian farmers only receive 190 euros per hectare. The draft proposes to increase the direct payments for CEE farmers by approximately 26% by 2020. The countries concerned (namely receiving the lowest payments) are Bulgaria with 56%, Romania with 54%, Latvia with 48% and Lithuania with 45%.[22]

Despite the progressive increase in payouts for Romania, the total amount of direct payments will not grow significantly.[23] Concerning the proposal that establishes rules for direct payments to farmers, the Romanian chamber of deputies argues that the increment of direct payments does not fully meet the objective of equity and convergence set out by the European Commission in the debate on the future of the CAP. According to a preliminary memorandum relating to the Position of Romania on the Commission communication "The CAP towards 2020", the Romanian government is also raising reservations vis-à-vis the capping: „Romania is not considered appropriate to the Commission's proposal to introduce an upper limit (capping) the level of direct payments to large farms allocated".[24] Furthermore, in the case of capping direct payments for large beneficiaries, there may be a risk that well performing farms are affected.

The consideration of the Romanian senate on the reform of the CAP is that it is necessary to have a further analysis on the implementation of a more ambitious approach to the equity principle and convergence objective as regards direct payments, in order to ensure a faster reduction of differences between the levels of those payments. The senate asks for a careful reanalysis of the direct payments' green component implementation, budget impact and specific requirements that farmers must meet to access it. Furthermore, the amount allocated for the green component should have the same value per hectare, across in the Union. The senate argues that it is necessary to investigate the implementation of direct payments capping for large beneficiaries, in order to avoid increasing the national budget co-financing effort. It proposes to exclude voluntary payments for areas facing natural constraints from all direct payments subject to capping. As Romania and Bulgaria are still in the phasing-in process, in their case capping should not be applied. The senate asks to increase the 2% percentage from the national ceiling as well as the eligible area for the young farmers.[25] Romania would welcome greater transferability of funds between the first pillar of CAP (direct payments to farms

20 *Eurostat (2011)*
21 *CAP expenditure on direct payments in the new member states will only reach its full level in 2013 and in 2016 in the case of Bulgaria and Romania.*
22 *Poulain, A. (2011)*
23 *Goşa, V. – Feher, A. – Goşa, C. – Raicov, M. (2012a)*
24 *Goşa, V. – Feher, A. – Raicov, M. – Goşa, C. (2012b)*
25 *Interparliamentary Committee Meeting, European Parliament – National Parliaments (2012)*

for production support) and the second pillar (application-based rural development).[26]

3.3. Cohesion policy after 2013

The Commission's proposal on a Budget for Europe 2020 recommends modest reduction of the cohesion policy budget, mainly via some decrease in convergence spending. From the perspective of cohesion policy rules, Romania together with Hungary raised some concerns about the stronger conditionality provisions and about the measures proposed for strengthening the absorption of funds.[27] Having the lowest absorption level in the EU is defined as a crucial problem in the case of Romania. The coverage for convergence regions will be reduced, Romania would no longer have a convergence status in its entirety, and the capital region of Bucureşti-Ilfov would become a transition region. Romania as being one of the 12 'net beneficiaries' has demanded for an ambitious cohesion policy highlighting the importance of EU funds helping to exit from the crisis, boosting competitiveness and strengthening internal cohesion.[28]

The Prime Ministers and representatives of the "Friends of Cohesion"[29] all agreed in their statement on 1 June 2012 that the EU's cohesion policy needs reform and they welcome the proposals submitted by the Commission. The country representatives raised the importance of the effectiveness of policies co-financed from the EU budget to be a fundamental part of negotiations on the multiannual financial framework 2014-2020. The reduction of

26 *Sobják, A. (2012)*
27 *Molino, E. – Zuleeg, F. – Chiorean-Sime, S. (2011)*
28 *Mendez, C. – Bachtler, J. – Wishlade, F. (2011)*
29 *Bulgaria, Czech Republic, Croatia, Estonia, Greece, Hungary, Latvia, Lithuania, Malta, Poland, Portugal, Romania, Slovak Republic, Slovenia and Spain*

development gaps should continue to play a crucial role in the funding, therefore the balance between simplification of the implementation mechanisms of cohesion policy and the effectiveness of expenditure for cohesion must be ensured. In case of cohesion policy flexibility and ease of use are essential.

Similarly to the other "Friends of Cohesion" states, Romania backs the maintenance of the higher EU co-financing rate of 85% (the savers' group insists on reducing it to 75%) for both CAP second pillar and cohesion policy, and refuses the limitation of assistance at 2.5% of GDP. Romania is also against the establishment of so-called transition regions. This would re-orient considerable sums from poor Romanian areas to more developed regions in other member states with a GDP per capita of between 75% and 90% of the EU average.[30]

As a new instrument of cohesion policy the Connecting Europe Facility is proposed to finance projects aiming to fill the missing links in Europe's energy, transport and digital networks. The new fund would make available 31.7 billion euros for transport infrastructure for the next financial period. 80% of this money is to be used to (1) support core network projects priority projects along the 10 implementing corridors on the core network and (2) fund IT-related horizontal projects.[31] Romania supports the new initiative, because of the salient potential benefits. In the field of energy Romania is concerned in three priority corridors of ten, Bulgaria and Romania will work together to utilise funding from the Connecting Europe Facility of the Commission, especially on projects to give Danube shipping and navigation a boost.

30 *Sobják, A. (2012)*
31 *Permanent Representation of Romania to the European Union (2012)*

3.4. Energy Policy

Based on the data of the EU's energy portal,[32] in Romania gross energy consumption was 35.43 million tonnes oil equivalent in 2009. The energy dependency rate (imports divided by gross consumption) is around 20% which puts Romania to the second best position among the EU27 after the net energy exporter Denmark.

The greatest consumers of energy are households (36%), industry (29%) and transport (24%) while the services and the agriculture sector have a smaller share (8 and 2% respectively). Analysing the energy sources used, the most important ones are petroleum products (29%) and gases (27%) while electricity accounts for 15%. The share of renewable energy is 18% in Romania which is significantly above the EU average (6%).[33] However, there is a shift towards nuclear energy:[34] in the period between 2016-2020 two new nuclear units will come into operation. Currently nuclear energy production accounts for 11% of the total production. The greatest share of domestic production of energy comes from gases (31%) followed by solid fuels (23%), renewables (18%) and petroleum products (17%).

In June 2011, a new National Energy Strategy 2011-2035[35] was published by the Romanian ministry in charge, updating the previous one because of the effects of the economic crisis and new law packages adopted in the European Union in the field of energy and climate change. The new Energy Strategy opened the debate by setting the following objectives: (1) energy security, (2) domestic and regional competitiveness, (3) sustainable development,

32 *Energy Portal of the EU containing all energy-related statistics used here: http://energy.eu*
33 *Energy Portal of the EU: http://www.energy.eu/country_overview/Romania_2011.pdf*
34 *EU Climate Policy Tracker 2011: http://www.climatepolicytracker.eu/sites/all/files/Romania2011.pdf*
35 *Minister of Economy, Trade and Business (2011a)*

(4) environmental protection and mitigating the effects of climate change, (5) attracting capital for modernisation and development of the sector and (6) further development of a competitive market characterised by competition, transparency and liquidity.

Romania is strongly involved in three important regional energy projects: AGRI, Nabucco and the Pan-European Oil Pipeline (PEOP). The AGRI project[36] (the Azerbaijan-Georgia-Romania Interconnector for gas) represents a new way for Romania to accede to the energy sources of the Caspian Sea region. After the establishment of the project in 2010, Energy Ministers of Azerbaijan, Romania and Hungary signed in Bucharest a Joint Declaration approving the participation of Hungary's state-controlled electricity company, MVM (Hungarian Electricity Works) in the AGRI project in 2011.[37] Nabucco will be constructed from the Georgian/Turkish and the Iraqi/Turkish border to Baumgarten in Austria, connecting five transit countries, Austria, Hungary, Romania, Bulgaria and Turkey.[38] The development of the Southern Gas Corridor remains of particular importance for Romania, with the Nabucco project being the key part of it, considering its scale and ambition. The PEOP is a joint cooperation between Italy, Croatia, Slovenia, Serbia and Romania which will connect the Black Sea to the Western European markets. The agreement envisages a 1,400-kilometer pipeline from the port of Constanta in Romania to Trieste in Italy, transporting up to 90 million tons of oil annually.[39]

36 *Minister of Economy, Trade and Business (2011b)*
37 *EKEM European Energy Policy Observatory (2011)*
38 *Official website of the Nabucco Pipeline: http://www.nabucco-pipeline.com/portal/page/portal/en*
39 *SEECAP*

3.5. External relations, enlargement, neighbourhood policy

Romania has been actively involved in the EU's common foreign and security policy as well as in security and defence policy missions. The country has recently been part of six civilian missions – including EUMM Georgia and EULEX Kosovo – and two military operations, including EUFOR Althea in Bosnia and Herzegovina.[40]

Romania supports the "open doors" policy for those countries that have the will and capacity to meet the EU membership criteria.[41] Romania does not support EU expansion to countries whose entrance is not conditioned upon implementation of cooperation and verification mechanisms (CVM) with which Romania must comply. Croatia's status is controversial, because the enlargement process is not linked to the CVM. Instead of blocking Croatia's EU accession directly, Romania rather focuses on its entry to the Schengen zone. Romania fully supports Iceland's application for EU membership with highlighting the need for an impact assessment on fisheries – a factor that will certainly influence the outcome of the Icelandic referendum on the Accession Treaty.[42] Romania supports Turkey's accession to the EU, mainly due to the longstanding historical, political, economic and cultural relations of the two countries. Moreover Turkish EU membership is supported by 78.3% of the Romania citizens which is by far the highest among the EU27 countries (second highest is in Bulgaria: 58.5%, against the EU average of 34.4%).[43]

The European Council agreed to grant Serbia candidate status in 2012, but Romania threatened to veto the decision on grounds that Serbia is mistreating a Romanian minority

40 *Ministry of Foreign Affairs of Romania (2012a)*
41 *Ministry of Foreign Affairs of Romania (2012b)*
42 *Ministry of Foreign Affairs of Iceland (2012)*
43 *Gerhards, J. – Hans, S. (2011)*

group in the country. Behind the surface of this step might be the fact that Romania wanted to recall the problematic issue related to its accession to the Schengen zone which is still blocked by the Netherlands, a country otherwise one of the greatest supporters of Western Balkan integration.[44]

Romania is interested in fostering a common space of stability, security and progress in the EU neighbourhood, in deepening relations between the EU and its eastern and southern neighbours, based on common interests and values. Romania pays special attention to the Black Sea region, by having launched "The Black Sea Synergy", in 2007. This initiative is meant to strengthen cooperation in the region, by establishing partnerships in main sectors: respect of human rights, migration management, security improvement, frozen conflicts, environment, regional development and energy.[45]

As it was mentioned, for Romania it is an essential policy objective to improve its relationship with Moldova. The promotion of the Eastern Partnership is a good tool to reach this aim. Romania is an unconditioned and active supporter of Moldova's EU membership, offering assistance and financial support for fulfilling EU accession criteria.

3.6. Special issues for Romania

The accession to the Schengen zone is a key issue for Romania. According to the opinion of the European Parliament of 8 June 2011, Romania and Bulgaria are technically prepared to participate fully in the Schengen cooperation. It was expected that during the Polish presidency both countries would be enabled to accede to the area without internal

44 *More information on the debate: EUobserver (2012a) and EUobserver (2012b)*
45 *Ministry of Foreign Affairs of Romania (2012c)*

border controls.[46] In March 2012, EU leaders agreed on a roadmap asking the Justice and Home Affairs Council to adopt a decision. However, during the EU Summit, Dutch Prime Minister Rutte declared that Bulgaria and Romania are still not ready to join the Schengen area. Rutte informed his peers that the Dutch government would not agree to the accession of Bulgaria and Romania before the publication of the results of the Commission's annual monitoring report on the fight against corruption and organised crime. Upon this report the issue should be settled in autumn 2012. It is the first time that EU leaders have agreed on a concrete date for a decision on this highly contentious topic, thereby increasing the pressure on the Dutch government.[47]

4. Summary and conclusions

Until the next parliamentary elections – due to be held in December 2012 – the status of the Romanian government is really uncertain. This year, after the resignation of the Boc and Ungureanu cabinet, acting Prime Minster Victor Ponta's plagiarism scandal has been making headlines recently and following clashes between the Prime Minister and the President, the existence of democracy itself has been questioned internationally. The global economic crisis triggered severe recession in Romania and after the successfully introduced fiscal consolidation measures it is a challenge for the new government not to diverge from the general policy direction of the former government. Romania is now enjoying a relatively fast recovery as a consequence of the implemented austerity measures.

Romania as a net beneficiary country is satisfied with the size of the proposed EU budgetary framework. Romania considered the draft of the MFF 2014-2020 as a starting point for further negotiations, and in general it is in favour of changes that would result in improved transparency of the EU budget. Romania, similarly to several other EU10 countries, is likely to oppose new taxes, but only after an impact assessment. However, currently it is neither in favour nor against the proposed new resources of the EU budget. On the expenditure side, Romania agrees with the changes of the CAP, because there are substantial gaps in direct payments. From the point of view of cohesion policy developments, Romania together with Hungary raised some concerns about the stronger conditionality provisions and about the measures proposed for strengthening the use of funds. However, the extremely low absorption rate and the opaque use of EU funds, as well as the overall corruption problems, the slow pace of judicial reform, and the current internal political instability are all factors weakening the Romanian bargaining position on the EU's upcoming MFF.

In the field of energy, Romania is involved in three important regional energy projects: AGRI, Nabucco and the Pan-European Oil Pipeline. The development of the Southern Gas Corridor remains of particular importance for Romania, with Nabucco project being the key part of it, considering its scale and ambition. As regards enlargement, Romania supports Turkey's and Iceland's accession, however it raised some reservations about Croatia's EU membership and Serbia's candidate status. Romania is interested in remaining a strong and serious partner for the promotion of Eastern Partnership with special attention to Moldova.

46 *TEPSA (2011)*
47 *European Policy Centre (2012)*

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SLOVAKIA

Darina Malová – Martin Pašiak

1. Domestic political framework, EU strategy of the government

1.1. Overview of internal politics

The latest parliamentary election in Slovakia took place on 12 March 2012. It followed the fall of Prime Minister Iveta Radičová's centre-right coalition led by the Slovak Democratic and Christian Union – Democratic Party in October 2011, over Slovakia's contribution to the European Financial Stability Facility. After a confidence vote, Ms. Radicová's government had lost support because one of the coalition partners – the Freedom and Justice Party – disapproved the decision. The election was won by SMER – Social Democracy (Smer-SD) which received 44.4% of the votes and was able to form a single party government with 83 seats out of 150. The current opposition includes parties that passed the 5% threshold: the Christian Democratic Movement (KDH with 8.8%), the party called Common People and Independent Personalities (OLaNO with 8.6%),

the Bridge (Most-Híd with 6.9%), the Slovak Democratic and Christian Union – Democratic Party (SDKÚ-DS with 6.1%) and the Freedom and Solidarity (SaS with 5.9%).

1.2. EU strategy of the government

Ever since Slovakia became a member of the EU, it has been strongly supporting European integration in the broad sense. This is given by the structural conditions of its economy coupled with turbulent political developments till the end of the 1990s. Beyond its general commitment however, Bratislava has already openly objected to a few issues pertaining to tax and social policy harmonisation, justice and home affairs, cultural issues and restrictions on nuclear energy.

Slovakia is a supporter of the European Financial Stability Facility (EFSF), however not all parliamentary parties were and are in favour of it. In October 2011, Prime Minister Iveta Radičová (Slovak Democratic Christian Union – SDKÚ) linked the Slovak national assembly's vote on the boosting of the EFSF to a vote of confidence, after her coalition partner (Freedom and Solidarity – SaS) started a public campaign against Slovakia's participation in the scheme. On 9 October 2011, after losing the vote, the government was dismissed and the early elections were scheduled for next March. The bill on the EFSF finally passed a few days later, supported only by three coalition parties of the outgoing government and by the strongest opposition party Smer-Social Democracy. Two parties: the coalition member SaS and the opposition Slovak National Party (SNS) voted against.

At the EU summit of December 2011, Slovakia was in favour of measures aimed at the immediate introduction of fiscal discipline as well as automatic sanctioning mechanisms and monitoring. Slovakia supports a strong and independent position of the European Central Bank and would like to see the implementation of the European Stability Mechanism as soon as possible. With regard to the countries with excessive deficits, Slovakia's preference is to put them under surveillance by the European Commission. Despite the change of government as a result of the March 2012 elections, the new government continues to support the EFSF and ratified the ESM Treaty as well. Moreover, the new Prime Minister Robert Fico several times backed up publicly the leading role of the German-French tandem in managing the crisis of the euro area.[1] Overall, Slovakia is aiming to be in the inner core of the currently forming multi-speed European Union.

2. General economic analysis

2.1. Overview of main macroeconomic developments

In 2011, the Slovak economy grew by 3.3%. Growth was mainly fuelled by accelerated industrial production in the sectors sensitive to the economic cycle (vehicles, electronics and machinery). In terms of the structure of demand, Slovakia's economic growth was primarily driven by net exports and fixed investments.

1 *See an interview by EurActiv.sk 2011*

Table 1, Main macroeconomic indicators of Slovakia

	2009	2010	2011	2012 (f)	2013 (f)
Real GDP growth rate (annual change, %)	-4.9	4.2	3.3	1.8	2.9
GDP/capita, EU27=100	73	73	73	n.a.	n.a.
Gross fixed capital formation/GDP (%)	20.7	22.2	22.4	22.7	23.3
FDI inflow (BEUR)*	0.0	0.4	1.5	1.0	n.a.
Private consumption/GDP (%)	61.0	58.5	57.5	56.9	56.1
Public consumption/GDP (%)	19.9	19.4	18.1	18.1	17.8
Exports of goods and services (BEUR)	44.5	53.4	61.5	65.7	71.0
Imports of goods and services (BEUR)	45.0	54.3	59.7	63.8	68.6
Current account balance/GDP (%)	-3.6	-3.6	0.1	0.2	0.2
Unemployment rate (%)	12.1	14.5	13.6	13.2	12.7
Inflation (HICP)	0.9	0.7	4.1	2.9	1.9
Interest rates (10y)	4.71	3.87	4.45	n.a.	n.a.

*Eurostat, European Commission, * WIIW (f = forecast)*

Slovakia is a small and open economy, with a rate of openness (exports and imports/GDP) that reached 138% in 2010 and 163% in 2011. The Slovak economy is also strongly export-oriented: in 2011 85% of the goods and services were destined for export. Recently, the trade balance shows a clearly improving trend. The 2011 balance of the current account achieved a surplus of 0.1% of GDP, compared to a deficit of 3.6% both in 2009 and 2010. The less favourable development in the balance of goods was partially compensated by the improved balance of services. A good performance can be expected in 2012 and 2013 too.

Despite the gradual economic recovery in 2010 and 2011, the labour market in Slovakia continued to be influenced by its structural weaknesses (collapse of the economy in early 1990s, weak transport infrastructure and considerable regional disparities) as well as the consequences of the economic crisis. More than 50,000 people lost their jobs in 2009 and a further 30,000 became unemployed in 2010, pushing the unemployment rate up to 14.5%. This however seemed to be the peak, and since then the rate of joblessness is going down steadily, although it is still expected to remain at a two-digit level. Moreover, according to EU statistics, nearly 11% of the population lives below the poverty line and a further 12% lives at risk of being below the poverty line.

The low level of inflation in 2010 was influenced by the weakening of global demand which caused a diminished rate of imported inflation. The decline of unit labour costs also had a favourable impact on inflation, thus in 2010, the rate of annual inflation in Slovakia reached 0.7%. The harmonised index of consumer prices went however up in 2011 to 4.1%, mainly due to rising fuel prices. Since then, inflation has been taking a downward trend.

In the most recent National Reform Programme, Slovakia considers the consolidation of its public finances to be a prerequisite to re-launch sustainable economic growth in the long run. In order to accomplish this, the government launched a “3S” strategy that is based on three pillars: stabilisation, structural reforms and sustainability. *Stabilisation* includes across-the-board measures designed to reduce the general government deficit in order to underpin Slovakia’s credibility with the financial markets. The stabilisation measures need to address specific revenue and expenditure items of the budget; Slovakia attaches greater importance to those measures on the expenditure side which have a less negative impact on economic growth. In order to foster economic performance in times of consolidation, *structural reforms* are required to boost the growth potential of the economy. This is of particular importance at present since the external environment is unlikely to grow. As regards achieving *sustainability,* no fiscal consolidation can be successful in the long run without the

adoption of systemic changes designed to render public spending more efficient and to achieve a better functioning of fiscal institutions.[2]

The adopted measures respond to the recommendations contained in the Annual Growth Survey in which the European Commission assessed – in the framework of the European semester – major economic challenges faced by the EU and defined priority measures to address them. Based on these recommendations, the Slovak government has defined the following structural policy priorities: healthy and sustainable public finances; zero tolerance for corruption and ensuring access to justice; enough job opportunities that reduce social risks; encouraging business environment; educated people and innovative society; access to quality healthcare. [3]

The European Commission issued a paper on macro-structural bottlenecks to growth in Slovakia. These include:

- *reducing the high general government structural deficit and ensuring long-term sustainability of public finances in view of the ageing population;*
- *ensuring reallocation of public spending towards growth-enhancing items, including education, R&D and infrastructure;*
- *implementing the necessary reforms to ensure better quality of public spending and in particular that the additional expenditure for education and R&D are used efficiently;*
- *ensuring wage and price adjustment to sustain competitiveness, while improving the business environment;*

2 *Ministry of Finance of the Slovak Republic 2011a*
3 *Ibid.*

- *ensuring full utilisation of the economy's labour potential, by tackling the long-term unemployed and marginalised groups.*[4]

As one of the main problems it must be highlighted however, that the Slovak government has not been able to address the structural problems of the economy resulting from its vulnerability and dependence on a small number of industrial sectors.

2.2. Fiscal stability, economic and social competitiveness

The general government debt, previously on relatively low levels, rose significantly as a result of the economic crisis and expansionary fiscal policies. In 2011, it reached 43.3% of GDP and is still expected to rise up to over 50% in 2012-2013. The official deficit target of the Slovak government for 2010 – according to the budgetary planning for 2010-2012 – was 5.5% of GDP, the final outcome was however 7.7% of GDP. In nominal terms, public deficit was 1.5 billion euros higher than budgeted. On the revenue side, the dominant negative factor was the shortfall in tax revenues by the total amount of 637 million euros.[5] The public budget in 2012 anticipates a deficit at 4.7% of GDP. The government led by Iveta Radičová initiated an ambitious reform agenda aiming at fiscal consolidation and reduction of the budget deficit in 2011 by 2.5% of GDP. The consolidation package included spending cuts (a reduction in public sector wages and savings in public procurement) and revenue increases, notably a "temporary" rise in the VAT rate from 19% to 20%, higher excise duties and the phasing out of some tax exemptions. The care-taker government (in office until March 2012) abandoned the rest of planned structural

4 *Directorate-General for Economic and Financial Affairs 2010*
5 *Ministry of Finance of the Slovak Republic 2011b*

reforms (e.g. unification of income taxes, customs duties and mandatory payroll levies systems, or revision of the municipalities funding system). It only managed to impose an additional tax on the banking sector to increase the state revenues. The newly formed Fico government adopted a fiscal package consisting of 22 measures, with the aim of bringing down the deficit to the prescribed 2.9% in 2013. However, the European Commission expressed doubts[6] on whether the expenditure cuts constituting the bulk of the fiscal consolidation measures will be sufficient and sustainable: „The expected moderation in the public wage bill can be difficult to achieve, given the worse than budgeted outturn in 2011 and increasingly reduced scope to resort to easier options such as the cancellation of unfilled posts, the use of early pension schemes and incentives for the retirement of those above the statutory retirement age."

Table 2, Public finances in Slovakia

	2009	2010	2011	2012 (f)	2013 (f)
Public budget balance (% of GDP)	-8	-7.7	-4.8	-4.7	-4.9
Public debts (% of GDP)	35.6	41.1	43.3	49.7	53.5

Eurostat, European Commission (f=forecast)

The fiscal policy objectives for the following years have been set so as to ensure that Slovakia reduces its general government deficit below 3% of GDP by 2013 in a permanent and sustainable manner, which would lead to the abrogation of the excessive deficit procedure. Public finance consolidation will also continue beyond 2013 in order to bring Slovakia closer to achieving its medium-term budgetary objective, i.e., structural deficit of 0.5% of GDP.

6 *European Commission 2012, p. 7*

The first step towards reducing government borrowing to the planned 2.9% of GDP in 2013 was the 2011 fiscal consolidation. The consolidation effort reached 3.4% of GDP. The public budget for 2012, approved in the pre-election period, contained a deficit of 4.6% of GDP instead of the previously proclaimed deficit target of 3.8% of GDP. In order to meet the target set for 2013, a consolidation effort amounting to 2.7% of GDP on a cumulative basis will be required in the upcoming period. Beyond 2013, the annual consolidation effort is envisaged at 0.5% of GDP, in compliance with the provisions of the preventive arm of the Stability and Growth Pact. At the same time, the Commission is more sceptical and forecasts a deficit of 4.7% this year followed by 4.9% next year.

The reform of the second (fully-funded) pension system pillar came into force on 1 November 2011, with some changes only applicable as of 1 April 2012. The reform introduced the fourth type of pension fund, the so-called index-linked one, whose performance will replicate developments in one or more stock market indices. The proposed change enables savers to channel their savings into two pension funds, one of which must be a bond pension fund. In connection with this change, a gradual transfer of personal savings to a bond pension fund has been introduced, depending on the age of savers. The scope of insurers was defined anew, based on the principle of automatic entry, while the pension savers have the possibility to unilaterally opt out from the second pillar any time during the first two years after their entry to the old-age pension saving scheme. A modification was also made to one of the eligibility criteria for old-age pension payments from the second pillar, namely that savers must participate in the old-age pension saving scheme for at least 10 years, compared to the original 15-year limit.

The practice which entitled employees to both severance

pay and full wage over the course of the notice period was cancelled; the notice period was cut from two months to one month for employment contracts shorter than one year; the maximum duration of fixed-term employment contracts was extended and the maximum number of their renewals was increased from two to three. Changes concerning working time and new provisions on overtime work without prior consent from employee representatives gave the employers a better possibility to flexibly respond to changing economic conditions.

A healthy and sustainable economic growth and enhanced competitiveness of the Slovak economy can primarily be achieved through a healthy business environment, innovation and qualified workforce.[7] In the field of labour market policy, the individual instruments will be subject to a review based on their actual use and efficiency. Slovakia will primarily focus on educational programmes and counselling. These rank among the “most effective instruments, particularly in times marked by high unemployment.”[8] One of the tools of the active labour market policies – known as “internships for graduates” – is to be modified to place greater emphasis on the professional skills and practical experience of graduates. Financial incentives for the employers that create the conditions to improve graduates’ abilities are to be established.

Gross domestic expenditure on R&D in percent of GDP was 0.6 in 2010. A marginal progress has been made towards the achievement of the target of 1% recently. Employment grew by 0.5% in 2011, the national target is 72%. Out of structural reforms that could help achieve the target as indicated in the NRP, only the Labour Code revision was successfully completed. Slovakia is the top performer in the area of early leavers from education and training (4.7% in 2010) and is doing better than the EU average for both males and females and migrants and natives. In particular, males have a lower drop-out rate than the EU average. Despite the progress made since 2000, Slovakia still has a low tertiary education attainment rate compared to the EU average (22.1% versus 33.6% in 2010). In the period of 2007-2010, there have been positive developments for both males and females and migrants and natives. Data for 2011 are not yet available. The rate of those in or at risk of poverty or social exclusion could moderately increase due to the impact of the crisis on the most vulnerable groups of the society.

7 *Ministry of Finance of the Slovak Republic 2012*
8 *Ibid.*

Table 3, Europe 2020 targets of Slovakia

Europe 2020 targets	Situation in Slovakia in 2010	Slovakian Europe 2020 targets
Employment rate – 75% of 20-64 year-olds	64.6%	72%
R&D – 3% of GDP to be invested in R&D	0.6%	1%
Climate change / energy		
Reducing greenhouse gas emissions by at least 20%	59% of the 1990 level	-13% compared to the 2005 level
Covering 20% of energy consumption by renewables	8.3%	14%
Energy use in Mtoe (2009) Increasing energy efficiency by 20%	16.81 Mtoe	-1.65 Mtoe
Education		
Reducing school drop-out rates below 10%	4.7%	less than 6%
Reaching tertiary education attainment by at least 40% of 30-34 year-olds	22.1%	40%
Poverty / social exclusion Reducing the number of people in or at risk of poverty or exclusion by 20 million	20.6% of the population	-170,000

European Commission

3. Position and potential impact of Slovakia on current key issues

3.1. EU budget: the multiannual financial framework for 2014-2020

Slovakia supports the budgetary reform in general, but with a caveat that it should not affect the current financial perspective. With regard to the underlying principles of forming the EU budget, Slovakia calls for a balanced approach, and puts emphasis on the solidarity principle. As to the size of the budget, there is no special position of the government, however it has stressed that there is a general need to keep the budget size at least at the present level.[9] Slovakia supports a strong and competitive European Union. According to the government officials, achieving this goal is impossible without strengthening the economic and financial accountability, promoting education and innovation, enhancing energy security and effectively implementing the European neighbourhood policy.

Slovakia will support expenditures with the maximum possible added value for the Slovak Republic and the EU, including increased competitiveness, innovation and education, reform of the common agricultural policy, energy security, the strengthening of the EU's role on a global scale and the reinforcement of its neighbourhood policy. Keeping the cohesion policy among the priorities on the expenditure side of the EU budget will be paramount. The top priority for the Slovak government is to preserve the funds allocated to structural and cohesion policy at least at 35% of the EU budget. The government also supports an increase of allocations for the following policies: energy security, Europe

9 *Government of the Slovak Republic 2010*

2020 strategy, education, second pillar of the CAP, new challenges (climate change, bioenergy, water management, biodiversity), asylum and migration (European Fund for Refugees, European Return Fund), police cooperation and external relations – especially pre-accession funds and neighbourhood policy funds.

At the EU summit in June 2012, Slovakia stressed that there is a need to reform the system of own resources of the European Union. Slovakia supports the GNI resource and own revenues of the EU budget, and due to its complicated nature, favours the abolishment of the VAT source. The country can accept the proposed reduction of collection costs in the area of traditional own resources from 25% to 10%. The government is against the creation of the new European VAT, because this could lead to the harmonisation of taxation in the EU. At the same time, the new Slovak government backs up the Commission's idea of a financial transaction tax. The government disagrees with any compensation mechanism, such as the British rebate, as they represent non-equal treatment of member states.[10]

Slovakia participates in the regional cooperation of the Visegrad Group (V4) to support its positions vis-à-vis the MFF 2014-2020. The representatives of the V4 met in Prague in October 2011 and agreed on several key messages: the overall size of the EU financial framework proposed by the Commission guarantees adequate financing of the Union's key policies; the future EU budget must contribute to strengthening the Union's competitiveness and growth while ensuring its internal cohesion; and a strong and effective cohesion policy primarily focused on the less developed regions and member states can significantly contribute to achieving both of these goals and should not be therefore

10 *European Policies Initiative 2009*

weakened by any instrument of sectoral policies.[11] The Visegrad countries committed themselves to continue their close coordination in this matter.

3.2. Common agricultural policy after 2013

The economic crisis had a negative impact on Slovak farm production, leading to decreased contribution of agriculture to GDP and also to increased volatility in cash-flow for the farms. Slovakia prefers the reformed common agricultural policy to remain a strong common policy while maintaining its present structure. In the current CAP framework, the Slovak government "struggles" for the CAP with two main priorities: preservation of the Single Area Payment Scheme (SAPS) for new EU member states until 2013, and disapproval of the Commission proposal on progressive modulation. Slovakia also supported the "flat rate model" instead of the current historic model for the Single Farm Payment which would in future be more beneficial for Slovakia.[12] The Slovak government succeeded with the preservation of SAPS and also with lowering the Commission proposal for progressive modulation of payments for farms receiving more than 300,000 euros from 45% to only 4%, and abolishing the progressive modulation for farms receiving between 100,000 and 300,000 euros. However, Slovakia voted against the compromise version of the CAP Health Check because of the preservation of the differences in amount of payments between new and old EU member states. In fact, Slovakia would like to see a fair and balanced system of direct payments to farmers across the EU.

In the upcoming budgetary framework Slovakia supports preserving the direct payments as a basis of the

11 *Visegrad Group Presidency Communication 2011*

12 *European Policies Initiative 2009*

CAP's first pillar, but insists on withdrawing the historical principle. Slovakia shares these essential requirements with the majority of EU10 which (except for the Czech Republic and Slovenia) in February 2010 agreed that direct payments should remain the CAP's primary tool, but the criterion of intensity of production shall be replaced by criteria that reflect current and future objectives. These countries also argue that the direct payments after 2013 are justified only if they do not discriminate any member states. Slovakia's position on the size of the CAP spending is not explicit. It supports arguments for a CAP reform based on a liberal economic approach.[13] Specific national demands in this and related areas include: the need to strengthen rural development given its important role in combating regional disparities and strengthening social cohesion, minimal (or no) national co-financing in agricultural policy, and the creation of a level playing field for farmers of 'old' and 'new' member states.

To sum up, Slovakia would like to decrease or at least stabilise the share of administrative expenditures and stresses that „CAP first pillar funds should be primarily used for increasing the competitiveness of the agriculture sectors" of EU member states.[14] Slovakia favours a fair and equitable distribution of direct payments and underlines that the Commission proposal is still based on the historical principle which is not fair and well-grounded anymore. Slovakia argues that there is no reason for any kind of phasing-in period (transition period) for a longer time as the countries that joined in 2004 and 2007 have actually been phasing in since accession. Therefore, a solution must be found which will have a much stronger accent on convergence of direct payments in terms of scope and time.

13 *See: http://www.visegrad.info*

14 *European Policies Initiative 2009, p. 26*

As to the greening, Slovakia perceives the proposed 30% too high. Slovakia is not in favour of capping assistance for large farms either, which is counterproductive and could jeopardize competitiveness of the EU farms in general.

3.3. Cohesion policy after 2013

The goal of the Slovak Republic is to reach such a form of cohesion policy which would create a balance between the individual principles of the cohesion policy, i.e. economic, social and territorial cohesion. Slovakia's aim is to ensure transparent and the simplest possible rules for the implementation of cohesion policy and to create appropriate conditions for reducing the existing regional disparities. Slovakia considers cohesion policy as a powerful tool for the implementation of socio-economic priorities, and therefore is in favour of at least maintaining the current share of cohesion assistance in the overall expenditure of the EU budget, i.e. approximately 35 to 36%.[15]

Slovakia puts emphasis on those priorities for the next programming period which it deems crucial for the development of the Slovak economy and which require considerable financial resources: (1) basic infrastructure; (2) human resources, employment and social inclusion; (3) science, research and innovation and (4) focus on green growth.[16] Due to slow improvement till now, the priorities of cohesion policy remain almost unchanged: mostly narrowing the gap between regions, improving the infrastructure and fighting unemployment.[17] There is also a political will to enhance the cooperation among neighbouring countries – mainly through the Danube strategy – and to comply

15 *Ministerstvo dopravy, výstavby a regionálneho rozvoja SR 2010*
16 *National Reform Programme 2011*
17 *Geist (2010)*

with the targets of the Europe 2020 strategy. According to Bratislava, cohesion policy should have a privileged position among other EU policies, including a separate subheading in the MFF. Its traditional orientation aiming at reducing regional disparities should be preserved.

The position of Slovakia concerning cohesion policy derives from the Government Resolution no. 295 of 12 May 2010. The starting positions of the Slovak Republic on various aspects of the future EU cohesion policy include maintaining of the current support of cohesion policy, promoting the reduction of economic and social disparities between member states and EU regions by keeping the minimum of the current ratio of cohesion assistance for the total EU budget expenditure. Bratislava prefers strengthening multi-level governance and puts more emphasis on the principle of partnership with the involvement of regional and local actors to use their knowledge and experience in the process of planning and carrying out activities in a particular territory.[18] Slovakia aims to promote an integrated approach in developing regions favouring mutual inter-connectedness of towns and villages in the direction of the effective functioning of poly-centric settlement.[19] It would also prefer a more result-oriented cohesion policy in order to gain accurate identification of its added value in different regions and to compare the results among the regions. The Slovak Republic wants to maintain the current objectives of cohesion policy while allocating the highest proportion of expenditure to the Convergence objective. Besides that, Slovakia supports the creation of a new intermediate status for regions that exceed the 75% level of GDP per capita, i.e. which are not eligible for the support from the Convergence

18 *Košický samosprávny kraj 2010*
19 *Ibid.*

objective.[20] Such regions should be able to implement structural measures through all the objectives of cohesion policy with an increased level of co-financing from their own resources. The NUTS3 level in Slovakia affected by this measure would be the Bratislava and the Trnava regions.

The latest Slovak position on cohesion policy is in line with its previous stances. As far as the overall size of cohesion allocations, it is perceived that the Commission proposed a balanced compromise (between a sufficient financing of European policies and limited resources of national budgets). Slovakia supports the Commission's proposal on capping assistance at the level of 2.5% of the national GDP as well as the proposed allocation criteria. At the same time, the allocation proposed for transition regions is deemed to be too high: cohesion funding should remain concentrated on less developed regions. Slovakia favours keeping a separate sub-heading for cohesion policy and leaving the Connecting Europe Facility (CEF) outside of the cohesion sub-heading. It takes a sceptical view of the proposed transfer of 10 billion euros from the Cohesion Fund to CEF, because the real value added in transferring a part of Cohesion Fund money into a centrally managed facility is questionable.

3.4. Energy policy

The total electricity production in Slovakia in 2010 was 27,720 GWh, with a 53% share of electricity produced by nuclear power plants, 20% share of electricity produced by hydro power plants and 18% of electricity produced by thermal power plants.[21] Nuclear energy was defined in the Energy Security Strategy of the Slovak Republic until 2030 as the main guarantee of secure energy supply in the electricity sector and was clearly highlighted as a priority. The development of production capacities is based on the equality between different types of production sources and the balance of the fuel mix, therefore nuclear energy will form the basis for the production of electricity also in the future as an important component for maintaining security of supply and sustainable development.

Total energy use is expected to rise in the coming decades, with total primary energy supply reaching nearly 22 million tonnes of oil equivalent (Mtoe) by 2020 and 23.6 Mtoe by 2030.[22] Coal is the only fuel source expected to decrease from its current level, while supplies of all other fuels are expected to rise substantially to meet the country's energy needs. In terms of shares in the supply mix – based on this outlook – oil will continue to represent 20% of total primary energy, while the share of gas is expected to rise gradually to 31% in 2020 and 33% in 2030. The start up of two additional nuclear units in 2012 and 2013 will contribute to the fuel's share in the supply mix reaching nearly a quarter of the total by 2020. This would comply with one of the Slovak government's goals, i.e. maintaining the share of nuclear power in electricity generation at over 50% in the period to 2030. Taking into account the fact that Slovakia imports more than 90% of its primary energy sources, nuclear energy represents a long-term component in having stability in the field of energy security. Renewable energy, principally biomass, but also wind and hydro, is projected to rise to just over 11% of total primary energy supply by 2020[23] which would still be below the official national target of 14%. Furthermore, the Slovak Republic has already enacted most of the European Union's energy efficiency-

20 *Ministerstvo dopravy, výstavby a regionálneho rozvoja SR 2010*
21 *Ministry of the Economy of the Slovak Republic 2011*
22 *IEA 2011*
23 *Ibid.*

related regulations and directives. Despite a sharp decline in greenhouse gas (GHG) emissions in recent years, the Slovak Republic remains a GHG-intensive economy, with energy-related carbon dioxide emissions accounting for more than 70% of total GHG emissions.

The Slovak Republic imports virtually all of its natural gas and crude oil from a single supplier, the Russian Federation. The government is aware of the inherent risks of such dependence and has learned valuable lessons from the gas supply disruption in 2009. Energy security is therefore a dominant theme in Slovak energy policy. Slovakia, as well as the other V4 countries, is supportive of finding alternative routes for oil supplies for its market. In case of a shortage of supplies from the "Druzhba" pipeline, it is currently the pipeline Adria (which starts at the Croatian shore) that is able to supply Slovakia with 3.5 million tonnes of oil annually. However, this volume is not sufficient and therefore Slovakia seeks to secure other routes. A strategic alternative is the reverse flow of oil from the Czech IKL pipeline into Družba on Slovak territory. The Czech Republic has stared with its diversification of energy sources well before Slovakia and therefore today the country is also able to import oil from Germany and Italy.

In order to create a diversification of gas supplies Slovakia aims at signing various contracts with European gas companies. For example, in 2009 Slovak SPP has signed important agreements with the German company E.ON Ruhrgas, the French company GDF SUEZ, as well as with the company Verbundnetz Gas. Yet another important source of diversification is the connection between Slovakia and Hungary. If the gas pipeline is finished in 2013 (as it is scheduled) it could pump up to 5 billion m^3 of gas each year. Furthermore, the Slovak government supports the international initiatives for creating diversification of energy supplies, such as the Nabucco project which would be an alternative to the Russian gas. Greater regional cooperation, particularly in gas and electricity interconnections, plays an essential role in enhancing energy security and market competition**.** The Slovak Republic has coupled its electricity market with the Czech Republic, and it supports the construction of a North-South gas pipeline via its own territory that would link planned LNG terminals in Croatia and Poland, and would include an interconnector to Hungary.

Slovakia assumes that enhanced regional cooperation would have a positive impact on the process of setting up EU gas and electricity markets, as well as on ensuring security through enhanced regional resilience to potential supply disruptions. There is a need to combine top-down approach as exemplified by subsequent liberalisation packages with bottom-up activities as reflected for instance by strengthened energy cooperation between the Czech Republic, Hungary, Poland and Slovakia in the framework of the Visegrad Group. Having in mind regional plans to develop cross-border infrastructure, the ownership structure of energy industries within the region and the need for harmonising regulatory policies, it is important to ensure that all V4 countries belong to one region with the participation of Romania and Bulgaria, and with Croatia as an observer. Such a step would reflect achievements of V4+ cooperation, and would help improve coordination of V4 projects using already existing institutions and mechanisms. Moreover, these achievements have already been appreciated by the Commission in its initiative to establish a High-Level Group based on energy cooperation of V4+ countries to devise an action plan for North-South gas, oil and electricity interconnections. Common opportunities, risks and challenges require a common framework to be set up.

The Slovak government also supports the creation of a common European energy policy which should effectively react to the three main challenges: limiting external dependence on energy transmitters, supporting growth and employment and fighting climate change. Bratislava continues its efforts to strengthen the energy security of the Slovak Republic and that of the EU, which includes continued support for the Nabucco gas pipeline project.[24] Slovakia takes an active approach to the finalisation of the new Energy Strategy for Europe 2011-2020.

3.5. External relations, enlargement, neighbourhood policy

Slovakia builds its image as a 'good European' especially by promoting further enlargement and by fostering EU common foreign and security policy. Its main territorial and institutional priorities include integration of the Western Balkans, advancement of European neighbourhood policy and Eastern Partnership (EaP). Within the ENP and EaP its activities focus on support for democracy and transformation in Eastern Europe, energy security, service to citizens and crisis management. Slovakia is actively involved in two common security and defence policy (CSDP) missions: EUFOR operation ALTHEA in Bosnia and Herzegovina and EUMM mission in Georgia.

Probably the main policy initiative in which the Slovak government attempted to actively shape the agenda of the EU is tied to the Eastern Partnership initiative, designed to develop institutionalised relations between the EU and neighbouring countries of Eastern Europe. Even though the project was a direct result of the Polish-Swedish initiative of June 2008, a similar political priority had been put forward by Slovak diplomats during Slovakia's presidency of the

24 *Nosko et al (2010)*

Visegrad group. The commitment to the Eastern Partnership illustrates a rare long-term and consistent policy priority of the Slovak government in the EU-level policy-making.[25] Slovakia actively supports the project; the most important activities include bilateral assistance in the modernisation and reform endeavours of the six partner countries and passing on experience. Slovakia places a special emphasis on the continuation of the visa liberalisation process and on the adoption of association agreements and free trade agreements. Within the on-going revision of the European neighbourhood policy, Slovakia will promote an increased differentiation of political relations and instruments for the individual partner countries.[26]

Slovakia declared the relationship with Ukraine as its foreign policy priority right after its accession to NATO and the EU. Slovakia's interest lies in a stable, democratic and prosperous Ukraine which remains its only neighbour outside the European integration circle. Rapprochement of Ukraine and other Eastern European countries, as well as the creation of new opportunities for the development of bilateral relations represent a priority of the foreign policy of the Slovak Republic.[27] Slovakia's top priority is to further develop the Eastern Partnership as a policy based on the principles of democracy, human rights and the rule of law. Sectoral integration with the Eastern Partnership members in the fields of energy, transport, environment, education, research and development, business and trade belong to the highest ranked on the priority scale.[28] In addition to Ukraine – with which Slovakia had complicated relations, marked by the so-called gas crisis in early January 2009 – the Slovak diplomacy, since the fall of 2009, engaged in contacts with

25 *Rybář (2011)*
26 *Ministry of Foreign Affairs of the Slovak Republic 2011*
27 *Duleba (2010)*
28 *Ježovica (2011)*

EaP states with which it previously did not have closer ties. The Slovak Republic prepared for each country participating in the Eastern Partnership programme a special non-paper containing an offer of cooperation.

During the Slovak presidency of the V4 (July 2010 – June 2011) in Bratislava, it was agreed to set up a special programme V4-EaP (Visegrad Group for the Eastern Partnership) with a separate budget within the International Visegrad Fund with the intention of pursuing co-funded projects based on Eastern Partnership goals. This programme is being launched in 2012 and will help improve the funding policy of the Eastern Partnership programme. At the same time however, there is a feeling that the eastern partners – despite the policy of the Eastern Partnership to converge values – have not made significant progress toward respecting the European Union's values and integrating them into their own policies and practices. Slovakia repeats its position that economic reforms without basic long-term democratic changes are neither sufficient nor sustainable.

Slovakia supports further enlargement of the European Union. The country promoted the granting of candidate status to Serbia at the March 2012 European Council meeting and by the same token will promote the opening of accession negotiations with this country. Slovakia will support Albania's as well as Bosnia and Herzegovina's efforts to meet the criteria of European integration. As a member of the EU and NATO, Slovakia will encourage solutions to on-going challenges in the region, such as initiating a dialogue between Belgrade and Pristina, as well as progress in Bosnia and Herzegovina. At the same time, Slovakia will contribute to the strengthening of regional cooperation in the Western Balkans. Slovakia will make sure that the high-level bilateral political dialogue with the countries concerned encourages economic cooperation while opening up new opportunities for Slovak businesses.

4. Summary and conclusions

Slovakia benefited from global economic 'good times' since the beginning of the decade. However, the economic crisis fully exposed the structural vulnerabilities of the export-oriented economy. These shortcomings have not been addressed systematically and, as a result, Slovakia has suffered from the weakened external demand. The economy has been affected by a slowdown in Germany, one of its largest trading partners. Currently fiscal consolidation has become a priority together with structural reforms.

With regard to forming and defending its priorities, Slovakia has fallen into the habit of formulating broad priorities in order to create a room for manoeuvre to avoid the potential failure of negotiating priorities that would be too specific. Nevertheless, being part of the Eurogroup meetings, Slovakia now strongly aspires to be a member of the inner group in the multi-speed European Union. It has an ambition to lift its status up to the core member states, so far without a clear strategy.

Slovakia supports the EU's budgetary reform in general, however does not clearly specify its preference. It is clear that the Slovak government considers contributions received from the Structural Funds as an important source of financing its domestic priorities, therefore it is a member of the group of countries called "Friends of Cohesion". Regarding the proposal for CAP financing, Bratislava articulates its preferences more straightforwardly as it wishes to see a fair and balanced system of direct payments to farmers across the EU. The country's strong preference for nuclear energy as the main – secure and clean – energy

supply may generate tensions with some member states, particularly Germany, which is considered by Slovak officials as the key partner within the EU. Furthermore, Slovakia backs strengthening economic and financial accountability, promoting innovation, enhancing energy security, and is also in favour of further enlargement and effective implementation of the European neighbourhood policy.

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SI

SLOVENIA

Miklós Somai

1. Domestic political framework, EU strategy of the government

1.1. Overview of internal politics

In Slovenia, the winner of the 4 December 2011 early general elections was (against all expectations) Ljubljana's centre-left mayor, Zoran Janković and his brand new Positive Slovenia (PS) party backed by the retired but still influential first President of Slovenia, Milan Kučan. They got 28 seats out of 90 in the new parliament. On the second place, there were the Democrats (SDS) of Janez Janša, with 26 seats, having ranked as the firm favourites in all public opinion polls ahead of the vote. Third came the Social Democrats (SD), followed by the Civic List of Gregor Virant (DLGV), the Pensioners' Party (DeSUS), the People's Party (SLS) and the New Slovenia (NSi). The extreme nationalist Slovenian National Party (SNS) and two liberal parties (LDS and Zares) won less than the margin of 4% of the votes and hence lost their position in the national assembly. Due to the proportional electoral system, none of the parties had

gained a dominant position: the left-leaning combination of Positive Slovenia and SD got 38 seats, while the right-leaning bloc of SDS, SLS and NSi got 36 seats, so the centrist Virant party and/or DeSUS were to play the role of king-makers.

In spite Zoran Janković, the winner party's (PS) candidate for Prime Minister faced serious difficulties on his way to set up a governing coalition, on 5 January 2012, President Danilo Türk gave him the mandate to put together a government coalition. Two days later, although some 10-20% of the text still remained to be decided upon, a coalition agreement had been signed by the representatives of PS, SD, DLGV and DeSUS. However, another two days were enough to Virant's party (DLGV) to make a 180 degree turn and to opt against a coalition with Janković. Virant's last-minute rejection of Janković's coalition invitation led to the unprecedented situation whereby, for the first time in the history of Slovenia, the winner of the elections could not ally with enough MPs to form a parliamentary majority.

In this situation, the most obvious option was Janša's attempt to form a coalition by inviting the Social Democrats (SD) and the Pensioners' Party (DeSUS), as one of them was indispensable for building a majority that would be strong enough. While the SD could not "overcome ideological divisions for the first time in history" as Janša said and rejected the invitation, DeSUS did not have major problems with entering the right-leaning coalition. Janez Janša, the leader of the Democrats (SDS) was nominated for Prime Minister by the newly-formed centre-right coalition featuring his SDS alongside the Virant List (DLGV), the People's Party (SLS), the Pensioners' Party (DeSUS) and New Slovenia (NSi).

1.2. EU strategy of the government

Slovenia has been a member of the European Union since 1 May 2004. One of the four strategic goals of Slovenia's development strategy has always been to become a recognisable and distinguished country in the world.[1] The EU has proven to be a positive environment for Slovenian ambitions. Since membership, the country has become a dynamic and successful member state and it has already made an important contribution to the strengthening of its position in the international arena. Slovenia was the first among the new member states to introduce the euro in 2007 and also to holding the presidency of the Council of the European Union in the first half of 2008. On the other side, the EU has been listening to Slovenia's positions on the stabilisation of the situation in Western Balkan countries and their development and Slovenia has extended the scope of influence of its foreign policy and is now an active participant in discussions and initiatives that concern other world regions.

EU membership provides Slovenia with benefits and advantages. First of all, it brings positive financial and economic effects. In the 2007-2013 financial perspective, Slovenia has been allocated a considerable amount of European funds: more than ever before, opportunities for important investments and rapid development are arising. As for the common agricultural policy (CAP), of all new member states only Slovenia was able to obtain an equal footing for its farmers with their EU15 homologues as early as of 2007. On this basis, their farmers have access to direct payments at exactly the same level as their colleagues in the EU15.[2]

1 *Šušteršič et al. (2005)*
2 *Potočnik – Lombardero (2004)*

In such a small country like Slovenia, the strategic usefulness of EU membership has never been questioned: being part of a greater integration means external security, stability, the possibility of incorporating Slovene interests and ideas into the law- and decision-making process on the one side, and having access to a fully liberalised market of 500 million consumers on the other. There is a high degree of consensus among all important political groups to support the country's EU membership and its interest in a strong European Union. Slovenia was among the first to vote for the rescue packages to assist Greece in order to ensure the stability of the euro area, the destabilisation of which would be particularly detrimental to its vital economic and export interests.[3]

2. General economic analysis

2.1. Overview of main macroeconomic developments

Due to the relatively high degree of openness, the structure of exports and the spillover effect of the collapse of external demand on domestic production, investments and private consumption, the Slovene economy has been hit much harder by the international financial crisis (a fall of 8% of GDP in 2009) than the euro area as a whole. Supported by economic stabilisation in Europe and a counter-cyclical fiscal policy, the recession turned into modest, export-led recovery in 2010 (+1.4%). In 2011, however, because of a new decline in the euro area in the second half of the year and a drop in domestic consumption, Slovene GDP shrank by 0.2%. Under these circumstances, merchandise exports, which had been slowing steadily throughout the whole

3 *Szilágyi (2011a)*

2011, declined slightly in the fourth quarter of the year. At the same time, merchandise imports stagnated due to lower exports and continued weak domestic demand. What is a real worry is that while imports of both intermediate and consumer goods have already more or less reached their pre-crisis level, imports of investment goods seem to have been frozen at about two thirds of it.

The international slowdown has thus been hitting Slovenia hard through both the shrinking external and depressed domestic demand. The declining household incomes combined with precautionary savings keeps real consumption flat, while the continued contraction in construction causes gross fixed capital formation to fall sharply. Against this backdrop, many domestically oriented companies are struggling to service debts which results in banks suffering from substantial further losses in their loan portfolios. As a consequence, credit growth remained negative in 2011. As for the year 2012, a prolonged and even deeper recession is expected. The interim forecast of the European Commission places Slovenia amongst those nine member states where GDP growth would be negative. This is caused by the fact that gains from net exports cannot counterbalance the weakening domestic demand.[4]

4 *European Commission (2012)*

Table 1, Main macroeconomic indicators of Slovenia

	2009	2010	2011	2012 (f)	2013 (f)
Real GDP growth rate (annual change, %)	-8.0	1.4	-0.2	-1.4	0.7
GDP/capita, EU27=100	87	85	84	n.a.	n.a.
Gross fixed capital formation/GDP (%)	23.4	21.6	19.5	18.9	18.9
FDI inflow (BEUR)*	-0.5	0.27	0.8	0.9	n.a.
Private consumption/GDP (%)	55.8	56.0	56.8	57.8	57.3
Public consumption/GDP (%)	20.3	20.8	20.6	19.9	19.3
Exports of goods and services (BEUR)	20.6	23.2	25.8	27.0	28.9
Imports of goods and services (BEUR)	20.1	23.0	25.4	26.5	28.0
Current account balance/GDP (%)	-1.3	-0.8	-1.1	-0.4	0.7
Unemployment rate (%)	5.9	7.3	8.2	9.1	9.4
Inflation (HICP)	0.9	2.1	2.1	2.2	1.7
Interest rates (10y)	4.38	3.83	4.97	n.a.	n.a.

*Eurostat, European Commission, * WIIW (f = forecast)*

The number of employed persons had been declining throughout the whole year of 2011 and was 0.9% lower on a year-on-year basis in December. Employment declined most notably in construction and market services, while the drop in manufacturing was smaller than in the preceding two years. On the other hand, employment increased in agriculture, education, professional, scientific and technical activities, and in health services and social work. The labour market situation remained tense at the turn of the year 2011/2012. The registered unemployment rate was as high as 11.9% in the 4th quarter of 2011. At the end of January 2012, a total of 115,965 persons were registered as unemployed. A weak labour market is also expected for 2012, resulting in shrinking real private consumption, but the overall negative impact of sluggish domestic demand is likely to lessen as conditions in the construction sector are expected to gradually stabilise.

Inflation, which picked up to as high as nearly 7% on a year-on-year basis in the middle of 2008 (due to a quick increase in both food and energy prices at that time) and fell to a historical depth of 0.6% in July 2009, seems to have settled at a level of 2% since the end of 2009. Measured with the harmonised index of consumer prices (HICP), in 2011 the annual inflation in Slovenia was 2.1% – lower than both the euro area (2.7%) and the EU27 average (3%) average. Prices grew most for housing, food, beverages and tobacco, while they fell for communication, clothing, recreation and culture. 2011 was characterised by frequent changes in taxes and excise duties. As for the latter, those on petroleum products changed every month, while those on tobacco changed twice. As regards taxes, rates on motor vehicles changed in January, whereas some postal services became VAT exempt.[5] Overall, in the short term, consumer price movements were and continue to be mainly influenced by prices of liquid fuels and food, while in the long term they are affected by subdued economic activity. Due to both a weak domestic demand keeping the prices of services in check and an expected lowering of commodity prices, HICP inflation is forecast to remain below the euro area average, reaching 2.2% this year and 1.7% in 2013. In this regard, Slovenia's excise duty policy delays and mitigates the inflationary impact of world oil price movements.

2.2. Fiscal stability, economic and social competitiveness

In Slovenia, the combined effects of the crisis and the government's anti-cyclical policy resulted in rapidly deteriorating public finances: deficit grew from 1.8% of GDP in 2008 to slightly over 6% for the next three years, while gross public debt levels more than doubled (from nearly 22% in 2008 to 47.6% in 2011). Slovenia has been formally

5 *Statistical Office of the Republic of Slovenia (2012)*

under excessive deficit procedure since 2 December 2009. Slovenia's Stability Programme last updated in April 2012, plans to bring general government deficit below 3% of GDP by 2013, while the structural balance is to be reached in 2015 after the reduction in structural deficit by 0.9 percentage points on average annually. Government debt as a share of GDP increased substantially in 2009 and was on the rise both in 2010 and 2011. Even though the government calculates with a gradual decline, the European Commission still forecasts another ten percentage points of deterioration of the public debt ratio reaching 58.1% in 2013. The debt dynamics will be driven primarily by the central government as the local government sector is expected to remain on the very low indebtedness level of below 2% of GDP.

Table 2, Public finances in Slovenia

	2009	2010	2011	2012 (f)	2013 (f)
Public budget balance (% of GDP)	-6.1	-6.0	-6.4	-4.3	-3.8
Public debts (% of GDP)	35.3	38.8	47.6	54.7	58.1

Eurostat, European Commission (f=forecast)

Other key fiscal objectives for the programme period include the strengthening of the financial sector through bank recapitalisation, structural reforms of the labour market, pension and health insurance as well as the setting up of a favourable environment for economic activity and job creation by reducing administrative restrictions, actively supporting domestic and foreign investments and reducing the relatively high tax burden on labour and economic activity. In order for these objectives to be achieved, measures are to be taken in the area of both general government expenditure and of stimulating economic activity and competitiveness.

Expenditure savings envisaged for the period 2012-2015 mainly affect the public sector wage bill, social transfers (including pensions) and public investment. The concrete measures include:

- *reducing of the number of government institutions and other organisational changes, better efficiency of public procurement and informatics, better management of public real estate holdings and lowering transfers from the state budget to the local governments;*
- *lowering of the wages effectively by 5% across the entire public sector and cutting certain benefits and reimbursements to employees;*
- *reduction of expenditures for certain programmes and policies (infrastructure and housing), lowering subsidies to the real economy and to other activities, temporary reduction of pensioners' bonuses not based on paid contributions, cuts in some entitlements related to labour market, social and family policies, and cuts in certain reimbursements from public health insurance.*

Changes in the unsustainable pension system must be gradual regarding the recent rejection of its reform in a referendum (causing the falling apart of the previous governing coalition). Even if negotiations with the social partners are already to be started in 2012, implementation of a new reform is not foreseen before the end of 2013. The main changes of the reform should relate to higher effective retirement age than the current one. The new scheme is to be based on a multi-pillar system providing better links between paid contributions and the pensions themselves. It also has to ensure adequate allowance for those not being in a position to save enough money.

As for stimulating economic activity and competitiveness, certain tax burdens are being reduced. The Slovene parliament already adopted tax relives for research and development (from 40% to 100%) and for investments (from 30% to 40%). Corporate income tax was reduced from 20% to 18% with further decreases of 1 percentage point down to 15% planned for each year until the end of the programme period. In order to increase budgetary revenues, the government drew up a set of solidarity changes in taxation with a view of placing a larger portion of the fiscal consolidation burden on the wealthier population. The changes include the introduction of a financial transaction tax, additional tax on high-value real estate, an additional tax on high-value movable property (high price and high capacity vehicles and vessels), an increased tax on capital income (from 20% to 25%) and the possible introduction of an additional tax bracket (between 45% and 50%) for personal income tax on annual income of 70,000 to 100,000 euros. In order to further improve the competitiveness of the economy, broadening of tax bases, improvement of the tax collection system and systemic as well as structural measures are to be introduced in order to reduce the scope of informal economy.

Table 3, Europe 2020 targets of Slovenia

Europe 2020 targets	Situation in Slovenia in 2010	Slovenian Europe 2020 targets
Employment rate – 75% of 20-64 year-olds	70.3%	75%
R&D – 3% of GDP to be invested in R&D	2.1%	3%
Climate change / energy		
Reducing greenhouse gas emissions by at least 20%	105% of the 1990 level	-4% compared to 2005 level
Covering 20% of energy consumption from renewables	15%	25%
Energy use in Mtoe (2009) Increasing energy efficiency by 20%	6.99 Mtoe	n.a.
Education		
Reducing school drop-out rates below 10%	5%	less than 5%
Reaching tertiary education attainment by at least 40% of 30-34 year-olds	34.8%	40%
Poverty / social exclusion Reducing the number of people in or at risk of poverty or exclusion by 20 million	18.3% (366,000)	-40,000

European Commission

The new governing partners made it also clear in the coalition agreement that they intend to achieve fiscal consolidation and to comply with the requirements of the EU Stability and Growth Pact based on a more streamlined functioning of the public sector. Enhancing economic growth and employment, improving the institutional framework and creating an environment conducive for domestic and foreign investment, striking a balance between the welfare state and a more competitive market economy are mentioned among the main objectives of the new government. In order to achieve these goals, the coalition agreement puts forwards a lot of concrete measures about how to support creativity and reduce the cost of labour (e.g. by limiting the

level of social security contribution for the employers, or increasing tax relief for research and development), how to support entrepreneurs (e.g. by introducing a flat-rate tax for micro-enterprises and sole proprietors and a 40% investment tax relief for all, or gradually decreasing the corporate tax to 15%). Simplification and minimisation of red tape for both citizens and businesses and elimination of tax secrecy of data in case of tax evaders are also on the agenda.[6] In parallel with these efforts Slovenia has also set itself ambitious targets in the framework of the Europe 2020 strategy, especially as regards the high levels of employment rate, spending on research and the coverage of energy consumption by renewables.

3. Position and potential impact of Slovenia on current key issues

3.1. EU budget: the multiannual financial framework for 2014-2020

As for the overall amount proposed by the European Commission for the next multiannual financial framework (MFF) – i.e. 1.05% of the EU27 GNI as commitment appropriations – it is in Slovenia's opinion realistic and represents a good starting point for negotiations. With regard to the revenue side of the budget, Ljubljana welcomed the Danish presidency's proposal to make the discussion on revenues an integral part of negotiations, embraces the suggested simplification of the system and approves the abolition of the current correction mechanism. Moreover, Slovenia agrees on the elimination of the current VAT-based resource, while showing clear reluctance to

6 *Coalition partners (2012) pp. 3-4 and 9-10*

accept the introduction of a new VAT regime. At the same time, Slovenia supports the idea of introducing a financial transaction tax at European level.

In the field of security and citizenship Ljubljana wishes to render efficient the protection of the EU's external borders. As far as the external action budget is concerned, it would like to pay more attention to the enlargement issue. With regard to the administrative expenditure, Slovenia welcomes the intention of the three largest EU institutions (the Commission, the Parliament and the Council) to reach an agreement on cutting back European staff by 5%, which is to be applied to all EU institutions.

Slovenia supports the Commission's proposal for establishing a close link between key EU policies – as are the cohesion policy and the common agricultural policy (CAP) – on one side and the implementation of the Europe 2020 strategy on the other. Ljubljana considers the cohesion policy and the rural development pillar of the CAP to be solid instruments crucial in facilitating economic growth and the achievement of Europe 2020 targets. It agrees that expenditure on research, innovation and education, including funds for environmental protection and efficient energy supply is of central importance for boosting competitiveness of the EU and these aims should be reflected in all key policies. It also supports the creation of a Connecting Europe Facility to accelerate the infrastructure development in Europe, as Slovenia is one of the European countries which implements projects for the promotion of railway transport both nationally and internationally. After the finalisation of the freight transport corridors, the country will be crossed by 3 corridors that will be put in service in the period of 2013-2015.[7] As regards the revenue side of the EU budget, Slovenia regrets that there is

7 *RailwayPRO.com (web-2012)*

no ambitious proposal for a solution to avoid the problem of "juste retour" whereby EU members tend to maintain their net financial positions in relation to the budget.

At this point, it is to be noted that, even if Slovenia has been an overall net recipient of EU funds since the beginning of its membership, its cumulated net position for the period of 2004-2010 amounts to a mere 500 million euros. This was the consequence of an important difference which occurred between the planned and realised revenue flows from the EU budget to the Slovene budget, in other words the result of poor drawing on EU funds (63.8%), while the opposite flows (i.e. Slovenia's payments to the EU budget) have been realised as planned (99.2%). Hence, Slovenia is interested in simplifying the procedures and alleviating the administrative obstacles inherent to the system of drawing and monitoring of EU funds, especially in the framework of cohesion policy.

3.2. Common agricultural policy after 2013

Slovenia's overall considerations on the EU's post-2013 CAP are founded on ensuring that the spirit of the reforms undertaken since 1992 and its current two-pillar structure with common rules and mechanisms be retained and that the post-2013 CAP continue to boost competitiveness of the European agriculture. The Slovene cabinet thinks that CAP objectives can only be attained if adequate funding is ensured at the European level at least by 2020. Ljubljana several times expressed its concern about the planned reduction in real terms of funds available under the next MFF which would jeopardize the achievement of the CAP objectives. This would particularly touch on rural development where any reduction of allocations would be unacceptable for Slovenia.

As between 30 to 65% of home-grown basic food (with some exceptions like beef, milk and poultry) is produced in the country, the government is of the opinion that CAP subsidies must result in an increase in the quantity of home-grown food, which in turn increases self-sufficiency in Slovenia.[8] So, the government attaches great importance to direct payments for which sufficient funds should be earmarked in the future CAP, too. In addition, even if Slovenia is in favour of greater uniformity of the direct payments system, it advocates that specific natural and structural as well as economic characteristics of individual member states and their agricultures be reflected in the level of payments. The country thinks that the direct payments envisaged by the CAP should be more flexible than planned in the Commission proposals. Such flexibility would enable member states to solve problems caused by the reform in terms of producer income in different subsectors. Slovenia's key demand is to preserve the possibility of introducing different amounts of direct payments depending on soil use and that a transitional period for the introduction of the new system be extended beyond the proposed deadline. The Slovenians also expressed support for schemes encouraging young people to become farmers. In Slovenia the share of farmers under 35 is as low as 4.1%, while the EU average is at 6%. Last but not least, Ljubljana believes clear eligibility criteria are needed to ensure that direct payments be only received by those who are really engaged in agricultural production.

As for the so-called greening of the CAP, the measures proposed by the Commission (i.e. crop diversification, maintenance of permanent grassland area and reserving of 7% of farmland for "ecological focus area") are not welcomed in Slovenia given the vast preponderance of small plots (a

8 *Coalition partners (2012) p. 48*

mere 4% of the farms operate on more than 20 hectares) and the domination of permanent grasslands (ca. 60% of utilised agricultural area). If one takes into account that forests cover more than 1.2 million hectares (i.e. more than 60% of the national territory, whereby Slovenia ranks third in Europe after Finland and Sweden), it is obvious that the proposed greening measures would have negative effects on not only agriculture and landscape, but on national independence based on local food supply as well. Hence, by the Slovene cabinet, instead of greening, much more care ought to be given to field crop biodiversity and intercrops.[9]

The proposed capping would hardly really affect Slovenia as only about two dozen farms get direct payments of more than 150,000 euros a year and the overwhelming majority of them would probably be exonerated once the costs of salaries are deducted.[10]

Concerning the market management measures, Slovenia believes that the existing market intervention mechanisms in the form of a safety net need to be adequately upgraded and member states should in exceptional circumstances be allowed to introduce certain specific measures in compliance with existing internal market and WTO rules. As for rural development policy, it should retain its focus on fostering competitiveness and value-added, delivering agriculture-related public goods as well as promoting vitality of rural communities by enforcing sustainable local food supply and diversification of economic activities. As for the latter, the coalition government will, in order to shorten the food chain, promote shops selling locally produced food and farmers' markets in Slovene cities and towns and the restructuring of farms into a new social and economic model: the so-called "Community Supported Agriculture"

9 *Bavec et al. (2012)*
10 *European Commission (2011)*

(CSA) systems. Ljubljana thinks that the future CAP should pay more attention to small farms and to the issue of growing rural poverty in less favoured areas like hilly and mountainous regions and also in nature protection areas.

3.3. Cohesion policy after 2013

Even if Slovenia scores favourably within the EU27 in terms of social cohesion indicators (among other things: ranking first in EU27 with the lowest income inequality, the lowest share of jobless households with dependent children and the lowest share of early drop-outs in 2008) Slovenia agrees to that cohesion policy should remain one of the main European policies covering the entire territory of the Union. Slovenia was among those twelve member states which – in a common letter sent to Budget Commissioner Janusz Lewandowski in May 2010 – defended the share of the cohesion policy and stressed the need to use the EU budget as a leverage to exit from the crisis.[11] Also Ljubljana, in a joint statement with the four Visegrad Group countries, raised its voice against a possible reduction of cohesion funding available for the European regions during the next multiannual financial framework. It also contests, together with the other signatory countries, the future introduction of conditionality between the progress made in the national reform programmes and the transfer of EU support to the member states. In the discussion on cohesion policy under the Danish presidency, Slovenia supported the idea of preserving a safety net for the former convergence regions which would be equivalent to at least two thirds of their current budget allocations (i.e. those available for the period of 2007-2013).

Under the current MFF (2007-2013), Slovenia has been

11 *Sebag (2011)*

allocated 4.1 billion euros within the framework of three operational programmes (the Operational Programmes for Strengthening Regional Development Potential, for Human Resources Development and for the Development of Environment and Transport Infrastructure). The country is complementing the EU investment with an annual contribution expected to reach 957 million euros on average. The whole of Slovenia is eligible under the Convergence objective, the same as it was under the previous 2004-2006 programming period.

According to Commission proposals, during the next MFF (2014-2020) Slovenia would only partly be covered by convergence status with coverage falling from 100% to 53.8% following its split into two NUTS2 regions, East Slovenia and West Slovenia, the latter becoming a transition region – i.e. where GDP per capita (at PPS) is between 75 and 90% of the EU27 average.[12] As for the proposed change in capping of the cohesion allocations at 2.5% of GDP, Slovenia would not be affected, similarly to what has been the case under the current MFF. By the planned method, between 2014 and 2020 the country could apply for 2.712 billion euros under the cohesion policy, while 2.5% of its calculated GDP will for the same period of time reach about 6.4 billion euros.[13]

Because of the administrative systems of Slovenia being a bit complex with a number of different divisions with many of them without any administrative functions, the drawing on Structural and Cohesion Funds has traditionally been well below expectations. In 2007 and 2008, the net position of the Slovene national budget to the EU budget was even negative (drawing on cohesion policy funds being at 24.4% for Structural Funds and at 31.7% for the Cohesion Fund). Even if in 2011 there was a substantial improvement with

12 *KSH (web) and European Commission (2007)*
13 *Mendez et al. (2011)*

regard to drawing on funds, Slovenia supports Commission proposals to focus cohesion assistance and efforts on a small number of strategic priorities, well targeted programmes and projects delivering the highest possible European added value.

3.4. Energy policy

Slovenia exhibits an energy import dependency close to the EU27 average and mainly imports oil and natural gas. The country produces nuclear energy, solid fuels and renewable energy, all of which are also used in electricity generation in almost equal shares. The share of renewable sources in primary energy supply is steadily increasing. In the framework of the Europe 2020 strategy, Slovenia committed itself to cover one fourth of its total energy consumption by renewables by the end of the decade, however it is much more cautious vis-à-vis the energy efficiency and emission targets. In general, the Ministry of Economy endorses the common goals, but stresses that member states have varying potentials for reaching these targets. Action Plans need to be drawn up before setting compulsory targets in a new Directive. The National Energy Programme sets out Slovenia's long-term developmental goals and trajectories of energy systems and energy supply. It defines the goals of energy policy and the strategic measures to be implemented in order to achieve these goals.

The Ministry supports efforts to accelerate the development of cleaner coal and gas technologies, but sees energy saving measures to have greater chances for success. As for the debate over nuclear energy it is of the opinion that individual members should decide on its use individually. Slovenia supports the complete liberalisation of the internal market for electricity and natural gas which it considers to

be beneficial for consumers and the whole energy sector. The priority tasks of international energy policy are very significant for Ljubljana, as they ensure diversification of supply, transport routes and energy sources. Regarding the EU's external energy policy, the Ministry urges that emphasis be put on improved and equal energy dialogue with Russia and on increased investment in energy connections with neighbouring regions.

3.5. External relations, enlargement, neighbourhood policy

Ljubljana's foreign policy has come a long way in the past 20 years. From being an object of worries, suspicions, even threats with economic sanctions by top diplomats of the largest EU states, Slovenia evolved into a full-fledged EU member. It is and active participant both in the common foreign and security policy (CFSP) as well as in the common security and defence policy (CSDP).[14] The most important achievements include international recognition, as well as membership and participation in key international organisations (UN, NATO, OSCE, Council of Europe, EU, etc.). Slovenia's foreign policy must guarantee two fundamental values: security and welfare of both the state and its citizens. The policy is based on maintaining Slovene national identity and openness to the world.

Slovenia's key foreign policy priorities are the promotion of the country's interests and human rights and stronger economic diplomacy. Besides the traditional Slovenian interests in its immediate neighbourhood and the Western Balkans, the Minister of Foreign Affairs recently called

14 *In order to preserve Yugoslavia in one piece the largest states of the European Community at the time had been exerting strong diplomatic pressure against and even threatened the first non-communist coalition government of Slovenia with heavy economic sanctions which would have included a full trade boycott, if the republic was to break away. (See: Bebler, 2009)*

for "consolidated strategic partnerships and economic cooperation with France, Germany, Turkey, the BRICS countries and the US". Apart from this, growing attention is paid to economic diplomacy which is tasked with both assisting companies to enter foreign markets and operate abroad and attracting new investors creating new jobs on the Slovene territory. In this respect the recently established Strategic Council for Economic Cooperation – which unites the Foreign Ministry, the Ministry of Economic Development and Technology, the Chamber of Commerce and Industry, the Chamber of Craft and Small Business of Slovenia, and the Slovenian Chamber of Commerce – represents a united and unified approach within the Slovenian economy destined to assist foreign investors.

As for Slovenia's general attitude towards CFSP, one has to understand that tensions within the EU related to CFSP and CSDP bolstered by transatlantic differences on a growing number of issues pushed the Slovene political elite to adopt a tactic of often lacking principles, clarity and consistency in order to avoid spoiling its relations both with leading EU members and the USA. As a consequence, Slovenia has seen no need of investing heavily into developing the EU military infrastructure separate from the European pillar of NATO. Not surprisingly, and even if from the Slovene government's point of view a more balanced commitment to both organisations would be preferable, out of the total of 434 Slovenian solders involved in various military missions abroad (data of 1 August 2012) 398 contributed to NATO-led operations (mostly in Kosovo and Afghanistan), while only 18 to EU-led ones (exactly the same number as to UN-led operations).

Wide discrepancy between major security threats to the EU as contained in its pivotal document (EU Security Strategy – 2003) and the attitudes of the Slovene public,

which reflects a major general problem of CFSP/CSDP – low democratic legitimacy and very weak accountability due to the practically absent control by the European Parliament, by national parliaments and by public opinion – combined with lack of knowledge and underestimation of these two EU policies are behind the visible indifference towards them in Slovenia. The only exception to the rule happens to be Slovenia's growing involvement in international endeavours to stabilise the Western Balkans which has been receiving considerable support and understanding from the Slovenian public. This support has its strategic, political, economic and cultural underpinnings. It makes more sense in the eye of Slovenians to deploy their soldiers and policemen in the Western Balkans than somewhere much further afield, i.e. in Asia or Africa. Such policy indirectly promotes trade, enhanced general cooperation with the region and benefited also the Slovenian economy. The transformation of the neighbouring Western Balkan countries into a zone of peace, healthy economic and social development and prosperity, contributes also to furthering Slovenia's national interests.[15]

The EU enlargement, and especially its expansion to the Western Balkans, remains a priority foreign policy issue for Slovenia. A stable, democratic and economically viable Western Balkan region is of vital interest for Slovenia. As a consequence, Slovenia will continue to work towards the convergence and integration of, above all, Western Balkan countries (Croatia, Macedonia, Montenegro, Albania, Serbia, Bosnia and Herzegovina, Kosovo), but also Turkey and Iceland into the EU. Slovenia expects that, in the next enlargement round, the new member states of the EU will be Croatia and Iceland.

Slovenia supports European neighbourhood policy (ENP) for reasons of principles and legitimacy. It sees direct interest in (energy) security as well as more structural reasons in terms of human rights policy and general consistency of EU's policies towards its southern and eastern neighbours. A clear example of this is its support for continued talks with Ukraine and for a necessity of closer relations with Belarus, provided there is a satisfactory move in that country towards respect for rule of law, democracy and human rights.

It can be said that issues such as the ENP and the enlargement of the EU and NATO, are of a high salience in Slovenia, but as seen in the media coverage, only with a regional focus and preference towards the permanent expression of Slovenian foreign policy priorities, namely the neighbouring countries, especially Croatia, and the Western Balkans.

4. Summary and conclusions

Compared to its population, economic size, political strength, its capacity as a new and, for the common budget, net recipient member state of the European Union, Slovenia has become a fully recognised and organic element of European integration. Slovenia was the first among the new member states to introduce the euro (in 2007) and hold the presidency of EU Council (in the first half of 2008). It was able to successfully shape EU policies (e.g. issues regarding the Western Balkans). All the above successes rested on the solid basis of its national economy which has since the middle of the 1990s proved to be one of the most competitive among the new member states. The economic and financial crisis triggered – as everywhere in Europe – major macroeconomic imbalances, caused a serious

15 *Bebler (2009)*

derailment of public finances and revealed some important structural weaknesses, of which the unsustainability of the pension system. Considering the recent political events – the entering into office of the new cabinet backed by a comfortable majority in parliament – there is at last a chance to overcome the crisis, reform the pension system and consolidate the public finances which in turn will strengthen Slovenia's capacity to defend its national interests within the EU.

In order to achieve the above objectives, Slovenia needs to focus mostly on the improvement of its competitiveness, increasing growth and other measures for overcoming the economic crisis. In this respect, decisions on how to allocate funds from the EU budget will be very important, in particular the funds for development, cohesion policy, agriculture as well as environmental protection. It is of particular importance for Slovenia to maintain the concept of transitional arrangements in cohesion policy after 2013, and to continue with the common agricultural policy reform oriented towards the promotion of competitiveness, sustainable agricultural production and strengthening of the rural development policy. Also, the next multiannual financial framework should enable the preservation of the country's positive net financial position comparable with positions of other member states with a similar degree of development.

As a country with strong economic and other ties with the Western Balkan countries, Slovenia will continue to participate intensively in the process of integration of these countries into the EU. It will strive for the Union to pay adequate attention to the entire region and initiate accession negotiations with the countries fulfilling the conditions. Slovenia will make every effort that the amount of assistance the EU is going to provide to the Western Balkans in the next MFF enable these countries to make more rapid progress towards integration into the European Union.

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Summary

Krisztina Vida

1. Internal politics, EU strategy of the governments

Overview of internal politics

In a general approach it can be stated that (paradoxically?) the crisis seems to have consolidated public politics in the EU10 region. The sole exception is Romania, where the demonstrations triggered by the painful crisis management measures undermined the stability of the government. The situation became highly complicated in 2012, with the formation of a new coalition government (without elections) and with clashes between the President and the new Prime Minister. While the position of the President – after an invalid referendum on impeachment – was reinforced until the end of his initial term (end of 2014), parliamentary elections in December 2012 may result in the setting up of a stable government. The only country where the crisis provoked pre-scheduled elections was Slovakia in which the coalition parties were split over the country's contribution

to the European Financial Stability Facility. This however did not destabilise internal politics there, and the March 2012 pre-scheduled elections brought about a new single-party government. Regular elections have recently been held in Lithuania and the next ones will take place, as mentioned, in Romania, followed by Bulgaria in the summer of 2013. Government terms in the rest of the region will end in 2014 (Czech Republic, Hungary), in 2015 (Poland, Estonia, Latvia), or in 2016 (Slovakia, Slovenia). Currently, the predominant political orientation in the region is centre-right: there are centre-right governments in all reviewed countries with the exception of Slovakia and Romania, while in Lithuania the conservative government will now be replaced by a leftist one, too. Furthermore, there is only one minority government, namely in Bulgaria, which has so far proved to be stable.

Table 1, Internal political scene of the EU10
(as of 15 October 2012)

	State President	Term of office	Prime Minister	Political orientation	Term of office
PL	Bronislaw Komorowski	2010.07 2015.07	**Donald Tusk**	centre-right	**2011.10 2015.10**
CZ	Václav Klaus	2008.02 2013.02	**Petr Nečas**	centre-right	**2010.05 2014.05**
SK	Ivan Gašparovič	2009.04 2014.04	**Robert Fico**	centre-left	**2012.04 2016.04**
HU	János Áder	2012.05 2017.05	**Viktor Orbán**	centre-right	**2010.05 2014.05**
SI	Danilo Türk	2007.12 2012.12	**Janez Janša**	centre-right	**2012.02 2016.02**
EE	Tooma Hendrik Ilves	2011.09 2016.09	**Andrus Ansip**	centre-right	**2011.04 2015.04**
LV	Andris Bērziņš	2011.06 2015.06	**Valdis Dombrovskis**	centre-right	**2011.10 2015.10**
LT	Dalia Grybauskaité	2009.07 2014.07	**Andrius Kubilius**	centre-right	**2008.11 2012.11**
RO	Traian Băsescu	2009.12 2014.12	**Victor Ponta**	centre-left	**2012.05 2012.12**
BG	Rosen Plevneliev	2012.01 2017.01	**Boyko Borisov**	centre-right	**2009.07 2013.07**

It is also important to highlight that despite the difficult economic and social situation aggravated by recession and austerity measures, the crisis did not spark general social

discontent. The region cannot be characterised by strikes, demonstrations and social unrest. Nevertheless, there have been signs of dissatisfaction and resistance to reforms by the society. A striking example has been the strong lobbying of Czech, Slovak and Hungarian doctors for the significant upward correction of their wages (otherwise many of them were determined to leave, or indeed left the country). Another example of social resistance was the case of a negative referendum in Slovenia on the restructuring of the pension system.

EU strategy of the EU10 countries

When looking at the EU strategy of the ten member states it must be underlined that not all of them have an official written strategy as a member state of the European Union. However, their behaviour and articulated position in the most topical issues tell a lot about their approach to integration matters and their image about the future of the EU. Most of them have a pragmatic approach: they show interest in the well functioning internal market, in the development of infrastructure, in interconnections of energy networks, or in a stronger role for the EU as a global player.

Another common point is that most of these countries are interested in taking part in deepening of integration processes rather than remaining outside. These countries would not like to see the EU become more fragmented and would like to avoid a Europe of several circles and speeds. This is the reason why Romania and Bulgaria are so keen on joining the Schengen area as soon as possible, and this explains why most of the non-eurozone countries preferred to accede to the Euro Plus Pact and to the Fiscal Compact too. However, the EU10 countries (as mostly small and medium sized countries) prefer the EU framework coupled

with the Community method of decision-making instead of the intergovernmental approach marked by the leadership of some big member states. The only exception here was Poland which actually welcomed these developments and, in November 2011, the Polish Foreign Minister even asked Germany to take the lead in solving the euro area crisis.

At the same time, the Czech Republic seems to be the most eurosceptic country in the group often siding with the United Kingdom in shaping the future of the EU. As regards the mentioned two documents initiated by Germany and France and signed by most member states, the Czech government decided not to join them. Hungary was also rather reluctant in joining both initiatives but then opted for signing the Fiscal Compact (which will be fully binding only upon eurozone membership) and for voluntarily cooperating in all areas of the Euro Plus Pact with the exception of harmonising the corporate tax base. The other eight countries did accede formally to both pacts even if most of them are concerned about the increasing loss of sovereignty in budgetary policies and even if they are against any kind of tax harmonisation. But this stance is inferior to the strong wish of being part of policy formulation.

In close connection to tackling the euro area debt crisis, the 17 countries using the single currency decided to set up the European Stability Mechanism. Its legal basis is the ESM Treaty which was ratified by all 17 member states concerned, including Slovenia, Slovakia and Estonia. However, the new rescue fund can only be operational if the ratification of the amended Article 136 of the Treaty on the Functioning of the EU (TFEU) is completed by all 27 member states. By mid-October 2012 this process has still not come to an end, as Poland and the Czech Republic, as well as the United Kingdom and Malta have not deposited the ratification document yet (which is just a formality).

Table 2, Participation in EU-level crisis management: joining to and ratification of relevant legal documents
(as of 15 October 2012)

	Euro Plus Pact	Fiscal Compact	ESM Treaty	Art. 136 of TFEU
PL	✓	✓	not applicable	not yet
CZ	-	-	not applicable	not yet
SK	✓	✓	✓	✓
HU	-	✓	not applicable	✓
SI	✓	✓	✓	✓
EE	✓	✓	✓	✓
LV	✓	✓	not applicable	✓
LT	✓	✓	not applicable	✓
RO	✓	✓	not applicable	✓
BG	✓	✓	not applicable	✓

2. General economic analysis

Overview of main macroeconomic developments

The crisis broke extremely dynamic growth and catching up trends in most of the EU10, while in 2009 recession was deeper in nine out of the ten countries than the EU average. In the Baltic states – after the overheated growth – GDP plummeted by two-digit figures, but the other countries also suffered from substantial contraction (see Table 3). Solely Poland did not experience recession, thanks to its big internal market and lower dependence on external demand. Moreover, in 2010 and 2011 there was a dynamic expansion there thanks also to investment projects financed from EU funds. In 2010, only two countries' GDP change remained in the negative (that of Romania and Latvia) while the mentioned Polish, but also the Czech, Slovak and Estonian development outpaced the EU average. In 2011, only one country, Slovenia saw GDP contraction, the other nine countries were above the modest, 1.5% EU average growth rate.

Table 3, Real GDP growth in percent of the previous year

	2009	2010	2011	2012 (*f*)	2013 (*f*)
EU27	-4.3	2.0	1.5	0.0	1.3
Poland	1.6	3.9	4.3	2.7	2.6
Czech Republic	-4.7	2.7	1.7	0.0	1.5
Slovakia	-4.9	4.2	3.3	1.8	2.9
Hungary	-6.8	1.3	1.6	-0.3	1.0
Slovenia	-8.0	1.4	-0.2	-1.4	0.7
Estonia	-14.3	2.3	7.6	1.6	3.8
Latvia	-17.7	-0.3	5.5	2.2	3.6
Lithuania	-14.8	1.4	5.9	2.4	3.5
Romania	-6.6	-1.6	2.5	1.4	2.9
Bulgaria	-5.5	0.4	1.7	0.5	1.9

Eurostat, European Commission (f=forecast)

The year 2012 seems to have checked the promising recovery trends. According to Eurostat forecasts (of August 2012) the EU as a whole will see stagnation, just like the Czech and practically also the Bulgarian economy. Recession returns to Hungary and Slovenia while the other six countries would grow between 1.4 and 2.7% (above EU average). 2013 may however bring about better results; there should be no GDP contraction any more and most growth rates would again be above the 1.3% EU average. Thus, 2013 could be the first year after accession when the pace of economic development would be relatively even without any big discrepancies within the EU10.

It is worth taking a closer look at the factors influencing growth after 2009. In the case of Poland, Slovakia, Romania

as well as the Baltic states, growth since 2010 or 2011 has been driven – in parallel to exports – by recovering domestic demand, within that especially gross fixed capital formation. Due to budgetary austerity, public consumption is practically stagnating or decreasing while private consumption is picking up very slowly across the region (especially in Hungary, Slovenia and Bulgaria). At the same time, shrinking demand on external markets had a negative impact on these countries' exports throughout the past years. In 2011, only the Czech Republic, Slovakia, Hungary and Bulgaria had export-led growth, while in 2012 net exports are expected to play an exclusive role in the otherwise weak economic performance of the Czech Republic, Hungary, Slovenia and Bulgaria (while it will contribute to the revived internal demand in Poland and Slovakia). At the same time, the Romanian and the Baltic economies will primarily be driven by domestic demand, emphatically by investments. The shift from external to internal factors of growth might be even more pronounced in 2013 when exports will play an exclusive role in recovery only in Slovenia and Hungary. In the other three Visegrad countries exports would complement internal dynamism while the latter will drive the expansion of the two Balkan and the three Baltic member states' economies. So, the structure of growth in the EU10 is varied; there is no single regional pattern for catching up.

Development levels continue to be heterogeneous too. Most of these countries had a very dynamic closing up performance after accession and prior to the crisis, while the Hungarian rate of GDP per capita showed hardly any convergence to the EU average. The crisis slowed these trends down and brought about some deterioration in the highest developed Slovenia. However, its first place is not challenged (84% in 2011) and neither is the second place of the Czech Republic (80% in 2011). The two least developed countries, namely Romania and Bulgaria (with 49% and 45%

respectively) came somewhat closer to the middle range led by Slovakia and followed by Estonia, Hungary, Poland, Lithuania and Latvia (between 73% and 58% in 2011).

Fiscal stability, economic and social competitiveness

The situation of public finances in nine out of the EU10 countries has been good prior to the crisis. In 2007, only Hungary had a greater than 3% per GDP budget deficit and only the Romanian trend was a deteriorating one. In 2008, however, already five countries of the group exceeded the 3% limit and in the year of deepest recession, in 2009, only the Estonian figure remained below the threshold. At the same time, despite having avoided recession, Poland has accumulated a huge deficit due to the smaller growth rate (by 3.5 percentage points) impacting on the revenue side of the national budget. Thus, eight out of the ten countries came under excessive deficit procedure while Hungary has been subject to it ever since 2004. The traditionally disciplined Estonia was the only country to avoid it. The other successful country was Bulgaria which was under this procedure for two years only (between mid-2010 and mid-2012).

The correction deadlines[1] are close: for Poland, Romania, Latvia, Lithuania and Hungary it is 2012 while for the Czech Republic, Slovakia and Slovenia it is 2013. As it can be seen from Table 4, in 2010-2011 budgetary positions have clearly improved in most of the EU10 and this trend is largely continuing in 2012 too. As a result, for 2013 the European Commission forecasts a greater-than-allowed public deficit only in two countries: Slovakia and Slovenia.

1 *http://ec.europa.eu/economy_finance/economic_governance/sgp/deficit/index_en.htm*

Table 4, Public budget balance as percent of GDP

	2009	2010	2011	2012 (*f*)	2013 (*f*)
EU27	-6.9	-6.5	-4.5	n.a.	n.a.
Poland	-7.4	-7.8	-5.1	-3.0	-2.5
Czech Republic	-5.8	-4.8	-3.1	-2.9	-2.6
Slovakia	-8.0	-7.7	-4.8	-4.7	-4.9
Hungary	-4.6	-4.2	4.3	-2.5	-2.9
Slovenia	-6.1	-6.0	-6.4	-4.3	-3.8
Estonia	-2.0	0.2	1.0	-2.4	-1.3
Latvia	-9.8	-8.2	-3.5	-2.1	-2.1
Lithuania	-9.4	-7.2	-5.5	-3.2	-3.0
Romania	-9.0	-6.8	-5.2	-2.8	-2.2
Bulgaria	-4.3	-3.1	-2.1	-1.9	-1.7

Eurostat, European Commission (f=forecast)

It is worth mentioning what types of measures are being used by the EU10 to implement budgetary consolidation. Even though there is no single model, governments seem to pursue very similar strategies in many aspects. On the revenue side, VAT hikes occurred in the Visegrad countries and Romania, excise duties were raised in Hungary, Slovenia and Romania while the base for personal income tax and corporate tax was widened in Slovakia. As a new type of tax the banking tax was introduced in Hungary and Slovakia and the tax on lottery in the Czech Republic.

All in all however, the EU10 countries do not put emphasis on increasing revenues but rather on cutting back expenditure. Bulgaria took the lead in this respect: the role of the state in redistribution has been reduced significantly compared to the pre-crisis period. The Bulgarian government did not raise taxes while it froze pensions and public sector wages and cut back state aid. The “self-restriction” of the

public sector, the freezing of wages and the shrinking of public consumption is also typical for Poland, the Czech Republic, Slovakia, Latvia, Lithuania and Romania. In Estonia there are opposite tendencies however: the quickly restored confidence and good growth outlook make the upward modification of pensions and public wages possible while the budget deficit will continue decreasing. In contrast to this, in Slovakia the austerity measures do not seem to bring about the expected results in 2013.

The Hungarian strategy is “unorthodox” in the sense that the government decided to decrease both personal income tax and corporate tax for SMEs, thereby encouraging consumption/savings and economic activity. The holes caused by these measures on the revenue side should be filled by the banking tax, some (temporary) sectoral taxes, taxation on telephone conversations, a levy on financial transactions or the electronic road toll. On the expenditure side (while there are steps to streamline the public administration and maximise top level wages), the government is rather focusing on reforming and restructuring the social redistribution system including the health sector, education, transport and pensions.

Table 5, Public debt as percent of GDP

	2009	2010	2011	2012 (*f*)	2013 (*f*)
EU27	74.8	80.0	82.5	n.a.	n.a.
Poland	50.9	54.8	56.3	55.0	53.7
Czech Republic	34.4	38.1	41.2	43.9	44.9
Slovakia	35.6	41.1	43.3	49.7	53.5
Hungary	79.8	81.4	80.6	78.5	78.0
Slovenia	35.3	38.8	47.6	54.7	58.1
Estonia	7.2	6.7	6.0	10.4	11.7
Latvia	36.7	44.7	42.6	43.5	44.7
Lithuania	29.4	38.0	38.5	40.4	40.9
Romania	23.6	30.5	33.3	34.6	34.6
Bulgaria	14.6	16.3	16.3	17.6	18.5

Eurostat, European Commission (f=forecast)

The serious destabilisation of the public budgets caused by the crisis brought about an immediate increase of public debts in most of the EU10. It is important to highlight that this region has been characterised by low debt levels in the pre-crisis period, except for Hungary. The other nine countries have always been well below the 60% Maastricht threshold and they still are, despite the mounting problems. The best performer in the EU10 (as well as in the EU27) is Estonia which, thanks to its disciplined fiscal policy accumulated hardly any public debt. The second best performer is Bulgaria, where public debts were above 70% in 2000 which then have been pushed back to enviable levels thanks to stringent fiscal policy and dynamic growth. In both countries the recent slight increase of debts should take a reversed trend soon, in parallel with their lowering deficits.

At the other edge can be found Hungary where – in contrast to the other nine countries – EU accession did not induce growth and catching up while public finances have continuously been worsening. Hungary joined the EU with by far the biggest debt ratio which peaked in 2010 (81.4%) and has been reversed since then. The other country where the trend has recently been positive is Poland where the nearing to 60% triggered immediate measures to cut back the debt level (in accordance with the constitution). In the other six countries, the rise of debts is very substantial compared to the pre-crisis years. While this quickly deteriorating trend seems to slow down in most of them, the case of Slovakia and Slovenia might be alarming. These are the two countries where public deficits are predicted to be the highest too. The reasons for that are different in the two countries. In Slovakia, government expenditure rose suddenly in 2009-2010 to mitigate the effects of the crisis and this level seems to persist coupled with the same level of revenues. In Slovenia, the main reason is the weak economic performance and the resistance of the population to structural reform (see the negative referendum on the pension reform).

In terms of selected social and competitiveness indicators the region is heterogeneous. As can be seen from Table 6, only four countries out of ten had one-digit unemployment rates last year, of them Poland was at the EU average level while the Czech Republic, Romania and Slovenia had by far the lowest rates. The crisis had a negative impact on the other key labour market indicator too. Employment rates (which were not bad before the crisis, except for the Hungarian figure) have deteriorated everywhere as a consequence of the crisis. According to 2011 data, the farthest from the EU average is Hungary, but the Romanian and Bulgarian figures are also low. In the latter two countries (beyond structural challenges) labour outmigration plays an important role as well. Despite all

difficulties, the EU10 countries pledged to reach rates of 70% or above by 2020: target figures vary between 70% for Romania and 76% for Estonia and Bulgaria – according to their National Reform Programmes.

Table 6, Selected social and competitiveness indicators of the EU10 (2011)

	Unemployment %	Employment %	Early school leavers %	GERD* as % of GDP (2010)	Innovation index
EU27	9.7	68.6	n.a.	2.0	0.539
PL	9.7	64.8	5.4	0.7	0.296
CZ	6.7	70.9	4.9	1.6	0.436
SK	13.6	65.1	4.7	0.6	0.305
HU	10.9	60.7	10.5	1.2	0.352
SI	8.2	68.4	5.0	2.1	0.521
EE	12.5	70.4	11.6	1.6	0.496
LV	16.2	67.2	15.2	0.6	0.230
LT	15.4	67.2	8.1	0.8	0.255
RO	7.4	62.8	18.4	0.5	0.263
BG	11.3	63.9	13.9	0.6	0.239

*Eurostat, European Commission[2] (*Gross expenditure on research and development)*

Early school leaving is extremely high in Romania, Latvia and Bulgaria, and these are the three countries in the group of EU10 which did not even pledge to push this rate below 10% by the end of the decade as proposed by the Europe 2020 strategy. At the same time, a really good performance is shown by Poland, the Czech Republic, Slovakia and Slovenia. In terms of innovation performance Slovenia leads the group (having a record at around the EU average) followed by Estonia. The rest of the group is among the so-called moderate or modest innovators. Therefore the 3% of GDP expenditure on research, development and innovation is unrealistic for most of these countries: only Slovenia and Estonia set these Europe 2020 targets in their national strategies.

3. Position and potential impact of the EU10 on current key issues

EU budget: the size of the multiannual financial framework for 2014-2020

According to the European Commission's June 2011 proposal, the total amount of the commitment appropriations for the period of 2014-2020 would be 1,025 billion euros (without the items outside the MFF, or 1,083 billion including those items). Table 7 compares the size of the current and the upcoming multiannual financial frameworks at 2011 prices.

2 *European Commission: Europe 2020 webpage: http://ec.europa.eu/europe2020/index_en.htm*
European Commission (2012): Innovation Union Scoreboard, available at: http://ec.europa.eu/enterprise/policies/innovation/files/ius-2011_en.pdf

Table 7, EU budget in billion euros at 2011 prices

	2007-2013	2014-2020
Smart and inclusive growth	439	491
of which cohesion policy	*355*	*336*
Natural resources	413	383
of which direct payments	*330*	*281*
Security and citizenship	12	18
Global Europe	56	70
Administration	56	63
Total commitments	**976**	**1,025**
As percent of EU GNI	**1.12**	**1.05**
Total payments	926	972
As percent of EU GNI	1.06	1.00

European Commission[3]

According to the Commission proposal, in the upcoming seven years financial framework there would be a modest 5% increase of the total amount in terms of both commitments and payments, as compared to the 2007-2013 cycle. Even though this caused some disappointment, in the midst of the eurozone's debt crisis the EU10 countries – as net beneficiaries – have a realistic approach to the issue of the size of the upcoming MFF. At the same time, most of them insist that this should be the "negotiating minimum" and many of them, especially Poland, openly reject any further reduction of the sums proposed. However, Estonia might be ready to accept a small cut while the Czech Republic joined six net payer member states (Germany, the United Kingdom, the Netherlands, Austria, Sweden and Finland) which signed a non-paper stating that "the Commission

3 *For 2007-2013: http://ec.europa.eu/budget/figures/fin_fwk0713/fwk0713_en.cfm#cf07_13*
For 2014-2020: http://ec.europa.eu/budget/library/biblio/documents/fin_fwk1420/MFF_COM-2011-500_Part_I_en.pdf

proposal is significantly in excess of what is needed for a stabilisation of the European budget."[4] This group emphasises that a "higher quality of spending" is needed and that EU money in general should focus on investments improving the Union's competitiveness. In fact, Poland and Hungary also underline that the EU budget should not be seen as a simple redistribution mechanism with winners and losers but rather as a major investment tool that leads to greater cohesion and contributes to the implementation of the Europe 2020 strategy.

EU budget: the revenue side of the multiannual financial framework for 2014-2020

The EU10 countries agree with the European Commission that the revenue side of the EU budget should be made more transparent. They actually support the GNI source as a fair one reflecting every country's economic weight. The traditional own resources (TOR) should also be maintained while positions are either divided, or not yet available regarding the shrinking of the 25% national share (to cover the costs of customs duties and sugar levies collection) to 10% as proposed by the Commission. For example, Slovakia and Hungary can accept this change while Latvia would be against it. Furthermore, the EU10 countries support the idea to abolish the current VAT contribution system and they would also prefer the complete elimination of correction mechanisms. The Czech Republic, Hungary, Slovenia, Romania and Bulgaria have been explicit in this regard at the General Affairs Council meeting in the end of May 2012.

The European Commission – encouraged and supported by the European Parliament – proposed two new own

4 *Non-paper from AT, CZ, DE, FI, NL, SE, UK – May 29, 2012 http://www.euractiv.de/fileadmin/images/MFR_non-paper_May_29.pdf*

resources of the EU budget as well. On the one hand, a new European VAT should be introduced, namely 1 percentage point of the standard rate VAT income of member states would be transferred to the EU. This new resource has been received with scepticism by most of the member states including most of the EU10. By mid-2012 only Poland expressed its support openly while many other countries voiced their opposition. On the other hand, a new type of revenue, the financial transaction tax (FTT) was also put forward by the Commission. According to the concept, exchange of bonds and stocks would be taxed at the rate of 0.1% and derivatives trades at 0.01%. One third of this revenue would remain with the member states while two thirds would go to the EU budget. This is intended to become an important leverage on the national (GNI-based) contributions to the EU budget while also creating a brand new source for national governments. This has been perceived as an idea worth considering. However, the first reaction of most of the EU10 was to have impact assessments before taking a clear position on it. By mid-2012 only Poland, Slovakia and Slovenia signalled their approval while most of the others remained undecided. The Czech Republic, Hungary and Bulgaria seem to be most hostile to this new own resource. Their underlying argument is (similarly to the case with the European value added tax) that the EU has no taxation competence – this is a prerogative of the member states.

Thus, the EU10 are on the same platform as regards maintaining the GNI-based resource and the traditional own resources as the main revenue items of the EU budget and also as regards abolishing the old VAT source and preferably eliminating all correction mechanisms. At the same time, they are obviously divided over the two new own resources as proposed by the European Commission.

Common agricultural policy after 2013

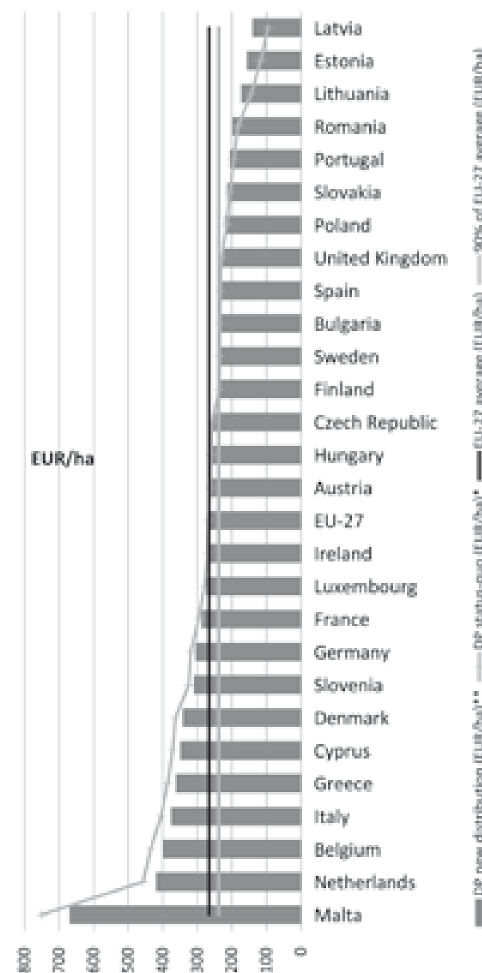
As can be seen from Table 7, in the upcoming MFF there would be less money earmarked for "natural resources" and within that for first pillar expenditure (direct payments and market measures) than in the period between 2007 and 2013. According to the Commission proposal, the share of agriculture and rural development in the EU budget would shrink from 42% to 37%. Given the fact that both key policy areas, common agricultural policy (CAP) and cohesion policy, would be hit by cuts in the new financial perspective, the EU10 can rather accept a smaller budget in the former than in the latter case.

The most important reform initiatives of the European Commission in terms of financing the CAP are the following. First, the level of direct payments should be more equitable across the EU, therefore the payments received per hectare should be evened out gradually. The Commission proposes to complement the direct payments to those member states where these payments are below 90% of EU average. The gap should be decreased by one third of the difference between the given level and the 90% level by the end of the decade (via shrinking assistance to those above the average). The second innovation would be the so-called greening whereby 30% of the direct payments envelope would be conditional on a range of environmental criteria (i.e. crop diversification, permanent pastures, and ecological farming on 7% of the given farm). Non-compliance with greening would entail sanctions. The third element of the proposal is the so-called capping, namely limiting assistance to the big farms (with a ceiling of 300,000 euros). This would mean an increasing share of direct payments to be deducted from the total amount given to large farms. Payments of above 150,000 euros per annum would be capped progressively, up to 300,000 euros above which 100% would be taken

away. The money “spared” on capping would remain in the recipient member state but would be channelled to the second pillar, to be used for innovation purposes. Further important elements of the CAP after 2013 include stronger links between direct payments and farming activities, as well as support for small farms and young farmers.

As regards the issue of more equitable direct payments across the EU, all EU10 agree with the principle, however they are in very different positions. At the moment, only Slovenia is above the EU average in terms of direct payments per hectare but compared to the status quo, the country would receive just a little bit less by 2020 (while still remaining above the average). Hungary and the Czech Republic are close to the average level which means they would practically preserve their status by the end of the decade. Bulgaria is around 90% consequently their payments per hectare will not change significantly either. The other six countries are and will remain below 90% of EU average even in 2020 according to the proposed scheme. Poland and Slovakia would come somewhat closer to the 90% level while Romania and especially the Baltic states would remain in the worst position despite some improvement. Latvia would be the most disadvantaged with reaching just around half of the EU average in 2020. This is the reason why Latvia actually proposed to thoroughly revise this plan by simply setting the rule according to which by the end of the MFF period no member state would be entitled to get more direct payments per hectare than 120% or less than 80% of EU average. Poland in its turn also proposed to simplify the system by introducing an area-based flat rate that would be an objective and fair basis for payments calculations.

Level of direct payments: current situation and 2020 levels



European Commission, DG Agriculture and Rural Development

Second, as regards the concept of tying 30% of direct payments to new and strict greening conditions, it is not really welcome by the EU10. Although some of them welcome the idea, most of the countries of the group emphasise that on the one hand, there are already enough green components in the CAP on the other hand, they find the sanctioning mechanisms too severe. Losing the relevant 30% in case of non-compliance, plus losing out in the direct payments in general are seen as too strong sanctions. Another concern often voiced by some of these countries (especially Poland, the Czech Republic and Hungary) is increased bureaucracy involved for both the farmers and the member states. Furthermore, for countries with typically small farms, like Slovenia, the greening requirements could pose special challenges.

Third, the idea of capping assistance to big farms is seen rather differently in the EU10. Here in principle the least interested countries, with predominantly big farms would be the Czech Republic, Slovakia, Hungary and Bulgaria. However, the latter country does welcome the capping of payments to large farms as they have a dominant position in Bulgaria and tend to "monopolise" EU financial support. At the same time, the Czech Republic and Slovakia are against the idea while Hungary can accept such a reform. In reality however, the sums lost for the big farms would not be too significant and the money would remain within the country. Another issue is however to lobby for a more flexible approach to spending these amounts for rural development (preferably not exclusively for innovation purposes, as stressed by Hungary). On the other hand, capping does not seem to be a challenging issue e.g. for Poland, Romania or Slovenia where small and medium sized farms prevail.

All in all, regarding the Commission proposal, the EU10 are most united in criticising the greening concept, while

they represent different interests stemming from their different positions as regards direct payments or capping. Finally, with a view to the other elements of the proposed CAP reform, i.e. stronger links between direct payments and farming activities, or support for small farms and young farmers are welcome and endorsed by the EU10.

Cohesion policy after 2013

The total amount of money earmarked for cohesion policy would be reduced in the upcoming MFF compared to the current financial framework. As can be seen in Table 7, instead of the 355 billion euros committed for 2007-2013 only 336 billion would be available between 2014 and 2020. Even though Croatia will join in 2013 (and other Western Balkan countries might gain membership before the end of the decade), the share of the Convergence objective within this smaller amount would be substantially cut back from 57% to 48%. This is unacceptable to the EU10 which are net beneficiaries of cohesion policy. The EU10 together with Spain, Portugal, Greece, Malta and Croatia have actually formed the lobby group of "Friends of Cohesion" and have already issued a statement and a declaration (see Appendix) with a view to highlighting the key importance of this policy area and its financial background. In fact, the group underlines that cohesion assistance should be primarily targeted to underdeveloped regions and that no further cuts can be accepted in this policy field.

One of the reasons why assistance to convergence is smaller than between 2007 and 2013 is a new fund, the so-called Connecting Europe Facility which would have a framework of 50 billion euros of which 10 billion would be channelled away from the Cohesion Fund to the facility. The idea is that it would finance trans-European infrastructure

projects and any member states would be entitled to apply for funding such projects (the part of 40 billion would be open to any EU members while the part of 10 billion would be open for the "cohesion countries"). Such trans-European projects can be beneficial, however many of the EU10 see this with scepticism and fear they might be less successful in their applications.

However, the main reason for the shrinking of assistance to the least developed regions is another innovation of the Commission proposal, namely the introduction of a new category of regions, the transition regions. To this category would belong all regions where GDP per capita is between 75 and 90% of the EU average. This would obviously shift some assistance away from the least developed to some better developed areas which is not welcome by many of the EU10. Actually, only two of the EU10 would benefit from this: Poland and Romania where the regions surrounding the capital cities would become eligible. In the other eight countries the regions are overwhelmingly below 75% and in a few cases above 90%. Thus, there is no single position on this issue by the EU10 but most of them are critical vis-à-vis the idea.

Another point of concern for many of the EU10 is the planned introduction of a lower cap of cohesion assistance, namely a ceiling of 2.5% of GDP would be applied for the beneficiary states between 2014 and 2020. Actually, only Slovakia and the highest developed Slovenia are ready to accept it. The other eight countries are all against the proposal as they think such a reduction in the resources is unfair and is against the principle of economic, social and territorial cohesion. According to preliminary calculations, the worst off would be the Baltic states and Hungary. In all four cases the basis for GDP projections are very low to which the approximately 1 percentage point cut back

relative to GDP (i.e. from the ca. 3.5% level down to 2.5%) must be added. These two effects result in substantial losses in the next MFF compared to the current one. Moreover, these countries also emphasise the aspect of absorption capacity and say that good performance should be also taken into account when calculating national tranches. However, in that respect only Lithuania and Estonia have an excellent record, while that of Latvia and Hungary is lower.

When looking at the new regulatory framework for implementing cohesion policy, the European Commission actually proposes a system of better targeted assistance that would also be in line with the Europe 2020 strategy and with the EU's efforts to reach fiscal stability and macroeconomic balances across the Union. This is of course acceptable for the EU10, nevertheless many of them are anxious because of the increased bureaucracy and the severe sanctions potentially involved with those new rules. In fact, the general fear is that between 2014 and 2020 there would be less money available for the least developed regions to catch up while the smaller amounts of assistance would be tied to stricter rules than ever before.

Energy policy

A common European energy policy is among the areas where the EU10 countries have strong shared interests. Even after 23 years of systemic changes, this region is still characterised by a predominantly unilateral dependence on oil and gas imports coming from Russia. In fact, the most dependent are Slovakia, Hungary, Latvia, Lithuania and Bulgaria, while the least dependent are Romania, Estonia, the Czech Republic and Poland. However, all of them are interested in the security of supplies, especially after some bitter lessons learned in 2009 due to disruption in the delivery. One of the

most important responses to this is the project of North-South Interconnections in Central and Eastern Europe with the participation of the Visegrad countries, Slovenia, Croatia, Romania, Bulgaria as well as Germany. The project covers interconnections of electricity networks, gas and oil pipelines stretching from the Baltic to the Adriatic and Black Seas. Another strategic goal, intimately linked to the previous one, is greater import diversification. This is the reason why most of EU10 countries are signatories to different alternative routes of energy supply such as the Pan-European Oil Pipeline, the Trans-Caspian Gas Pipeline System or the Nabucco project (even though the latter two are still in their initial phase and implementation seems to face considerable challenges).

A further shared strategic interest of the analysed countries is the establishment of a real single market of energy in the EU framework which would bring about greater competition among suppliers. Some bigger energy companies, especially the Hungarian MOL and the Czech CEZ can also profit from further liberalisation in line with the EU's third liberalisation package. A crucial step in the direction of interconnections and having a single gas and electricity market by 2014 was actually taken under the Hungarian presidency which put this issue very high on its agenda.

The EU10 countries are committed to reducing green house gas emissions and improving energy efficiency. Here they are facing very different challenges. In fact, in the region only Slovenia is above the Kyoto target in terms of CO2 emission, while the other nine countries are well below[5] (and have thus a good position in the quota trading system). In fact, these countries have a relatively good performance due to the fact that after the systemic

5 *http://www.energy.eu*

changes the outdated and highly polluting factories were mostly abolished, and via several important green field (or even brown field) investments in the manufacturing industry cleaner technologies have been installed. Another factor has recently been the crisis itself which slowed down economic activities compared to the pre-crisis years, thereby diminishing industrial pollution. Moreover, many of these countries launched programmes to modernise and insulate real estates and eight of them had also set clear targets in the field of lowering total energy consumption by 2020. Poland has a special problem in this regard: it has to reduce its overreliance on coal which is abundantly available in the country and which is used as the predominant source of electric power. But Poland needs more time for that therefore it currently resists faster carbon-dioxide cuts at the EU level.

Besides cutting back CO2 emissions by 20% and improving energy efficiency by 20%, the Europe 2020 strategy also set the target of covering 20% of total energy consumption from renewable energy sources by the end of the decade. In this respect the EU10 countries have a very heterogeneous performance. As can be seen from Table 8, Latvia, Romania and Estonia excel with their already high rates (above or nearly 20%) while the Visegrad countries have only a one-digit level of this figure. When looking at the national targets, the Visegrad countries and Bulgaria will make important efforts in this regard but will still remain below 20% in 2020. On the other hand, the Baltic states, Slovenia and Romania could reach impressive levels.

Table 8, Share of renewable energy sources in total energy use

	Situation in 2010 (%)	Europe 2020 target (%)
Poland	7.9	15.48
Czech Republic	8.5	13
Slovakia	8.3	14
Hungary	7.3	14.65
Slovenia	15.0	25
Estonia	18.9	25
Latvia	30.0	40
Lithuania	15.0	23
Romania	20.5	24
Bulgaria	12.6	16

European Commission

Finally, as regards nuclear energy, seven countries of the EU10 do use it and stick to it in the future too. Atomic energy plays an important role in all of them and is seen as a major tool for improving self-sufficiency in energy. Only Estonia, Latvia and Poland do not have any nuclear power plant but Poland is already on the way of planning one. Two plants of outdated technology had to be gradually decommissioned at the request of the EU, namely the Ignalina power plant in Lithuania and the Kozloduy power plant in Bulgaria.

External relations, enlargement, neighbourhood policy

For the EU10 – besides NATO – it is the European Union that guarantees security and a greater room of manoeuvre in international relations. These countries also participate in several common security and defence policy (CSDP) missions and operations of the EU. Their ratio of participation obviously shows a correlation with their size.

Table 9 represents a snapshot of EU10 involvement in selected missions as of April 2012 (but does not indicate these countries' earlier personnel or financial commitments which came to an end by that date).

Table 9, Actual participation of the EU10 in selected CSDP missions (as of April 2012)

	PL	CZ	SK	HU	SI	EE	LV	LT	RO	BG
EUFOR ALTHEA, BiH	✓	✓	✓	✓	✓	-	-	-	✓	✓
EUSEC DR, Congo	-	-	-	-	-	-	-	-	✓	-
EUJUST LEX, Iraq	-	-	-	✓	-	-	-	-	✓	-
EUBAM, Ukraine-Moldova	✓	-	✓	✓	-	-	-	✓	✓	✓
EUPOL COPPS, Palestine Terr.	-	✓	-	-	-	-	-	-	-	-
EUPOL, Afghanistan	✓	✓	✓	✓	-	✓	✓	✓	✓	✓
EULEX, Kosovo	✓	✓	✓	✓	✓	✓	✓	-	✓	✓
EUMM, Georgia	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
EUNAVFOR ATALANTA, Somalia	-	✓	-	-	✓	-	-	-	✓	✓

http://www.csdpmap.eu/mission-personnel

Beyond the general commitment of the EU10 to CSDP missions they broadly share interest and position in two topics that are important for them in the framework of the EU's external relations. One is Eastern Partnership and the other one is enlargement.

Due to their geographic position it is understandable that the EU10 insist on a more balanced approach of the EU in the framework of its neighbourhood policy. According to the EU10, the European Union should dedicate equal attention and financial support to this policy's southern and eastern dimension. Actually, the Eastern Partnership (EaP) idea originated in Slovakia, which put the issue forward during its presidency of the Visegrad group. Then it was

officially proposed to the EU27 by Poland and Sweden, two countries which became successful agenda-setters at the EU level in this regard. Later on, the first Eastern Partnership summit was held in Prague in 2009 and the next one in Warsaw in 2011. For different historical, geographic, economic and political reasons there is a "varied geometry" as regards the country preferences of the EU10 within Eastern Partnership. Consequently, a special relationship between Romania and Moldova, or between Poland, Slovakia, Hungary on the one hand, and Ukraine on the other can be seen as natural. However, the EU10 seem to be on the same platform as regards the Eastern Partnership's meaning and content. These countries would like to see a more pragmatic approach on the EU side with more added value and stronger cooperation. Thus, the EU10 would primarily promote democracy, rule of law, human rights accompanied with closer economic integration via free trade, or deep and comprehensive free trade agreements with the countries prepared for it (currently mainly Ukraine, Moldova and Georgia). Another concrete area where relations should strengthen is gradual and mutual visa liberalisation. Most of the EU10 would be in favour of prospective EU membership of those EaP countries that would be interested and prepared. As a sign of commitment, the Visegrad countries also decided recently to open a new section in the Visegrad Fund that would sponsor cooperation projects that are in line with the Eastern Partnership goals.

As regards further enlargement of the EU, the countries in analysis are all in favour of it. To underpin this argument it is enough to mention that the Hungarian presidency worked extremely hard to speed up and conclude accession negotiations with Croatia – a country which can finally become a member state on 1 July 2013. Actually, the membership of all Western Balkan countries is supported by the EU10 mainly for reasons of security in the region.

Icelandic membership would be welcome and the EU10 is probably the most positive group of countries in the EU27 as regards Turkish accession to the Union. This is not only an official stance of the political elite but is largely echoed by the population of the region as indicated by opinion polls. The basic approach of the EU10 is that any European country that meets membership criteria should be able to join the European Union. But emphasis is on meeting those preconditions, as the EU10 themselves had to make serious efforts to comply with all necessary criteria before entering the EU. Romania and Bulgaria recently have to meet extra conditions for their Schengen accession; this is the so-called cooperation and verification mechanism which involves justice and home affairs as well as border control and anti-corruption standards that have to be implemented. This is the reason why these two countries emphasise that any new applicant country (outside the Schengen zone) should also be subject to this mechanism. At the same time, none of the EU10 countries would veto any European country's accession.

4. Conclusions

Despite the protracted financial and economic crisis in the European Union, the EU10 countries can be generally characterised by political and social stability. Since 2009, the year of drastic recession in nine of the EU10, there has been a rather quick recovery in most of the countries concerned. The promising trends seem to halt in 2012 but the year 2013 could bring about a new impetus for growth. At the same time, all governments are making considerable efforts to bring public finances under control, to cut general government deficits, to restructure the public households

and to reverse the unfavourable trends in public debts. As a result, it is possible that by the end of 2013 only two of the EU10 will still be under excessive deficit procedure.

Being in general a less problematic region in political, social, economic and fiscal terms, the EU10 could become a lobby group within the European Union or at least could have the chance to make a stronger impact on policies and decisions. Due to diverse interests, positions and challenges however, the EU10 does not behave as a single lobby group which can also be seen as avoiding unwanted cleavages within the Union. Nevertheless, these countries have undoubtedly made a considerable contribution to having a genuine internal market of energy supply in the EU, or to intensifying relations with the Union's eastern neighbours in the framework of Eastern Partnership. The group – together with other member states – has also been lobbying strongly for preserving the budgetary commitments to cohesion policy in the next financial framework and to consider them as investment tools beneficial for the whole of the EU. Finally, the EU10 can be seen as perhaps the most pro-enlargement group of EU member states (at both the political and the public opinion level). As regards the different measures aimed at managing the debt crisis in the euro area, the three eurozone members adhered to all of them, as did many of the other seven however, the Czech Republic has been the least supportive. While the EU10 cannot be seen as an interest group within the EU (although the catalyst role of the Visegrad countries in this regard should not be underestimated), many policy areas can be detected where they – or most of them – have a common approach allowing them to make an impact on European integration.

Appendix

Appendix

Position of the EU10 on main points of the MFF for 2014-2020

	Size of MFF	Abolish old VAT	Correction mechanisms	EU VAT	EU FTT	CAP DP*
PL	OK, no further cuts	Yes	Abolish	Yes	Yes	OK
CZ	Should be smaller	Yes	Abolish	No	No	OK
SK	OK, no further cuts	Yes	Abolish	No	Yes	OK
HU	OK, no further cuts	Yes	Abolish	No	No	OK
SI	OK, no further cuts	Yes	Abolish	No	Yes	OK
EE	Could be smaller	Yes	Abolish	Undecided	Yes	N.a.
LV	OK, no further cuts	Yes	Abolish	No	Undecided	Not enough
LT	OK, no further cuts	Yes	Abolish	Undecided	Undecided	Not enough
RO	OK, no further cuts	Yes	Abolish	Undecided	Undecided	OK
BG	OK, no further cuts	Yes	Abolish	No	No	Not enough

	CAP greening	Ceiling for big farms	Cohesion total amount	Transition regions	CEF	2.5% capping
PL	Reservations	OK	No further cuts	OK	Scepticism	No
CZ	Reservations	No	No further cuts	N.a.	Scepticism	No
SK	Reservations	No	No further cuts	Not against	Scepticism	Can accept
HU	Reservations	Can accept	No further cuts	No	Scepticism	No
SI	Reservations	OK	No further cuts	Yes	OK	Not affected
EE	Reservations	OK	No further cuts	No	Scepticism	No
LV	Reservations	OK	No further cuts	N.a.	Scepticism	No
LT	Reservations	OK	No further cuts	N.a.	Scepticism	No
RO	Reservations	OK	No further cuts	No	OK	No
BG	Reservations	OK	No further cuts	Not against	Scepticism	No

*(*DP: gradual closing of the direct payments gap across the EU)*

“FRIENDS OF COHESION”

Joint Statement on the next Multiannual Financial Framework

2014-2020

WE, PRIME MINISTERS AND REPRESENTATIVES of “Friends of Cohesion” (Bulgaria, Czech Republic, Croatia, Estonia, Greece, Hungary, Latvia, Lithuania, Malta, Poland, Portugal, Romania, Slovak Republic, Slovenia and Spain) reunited at the Summit on the next multiannual financial framework 2014-2020, on June 1, 2012 in Bucharest:

WE DECLARE THE FOLLOWING:

EU efforts should be directed primarily towards measures which contribute significantly to economic growth and employment. This can be done, without reserves, through the Cohesion Policy, which is an important investment instrument available to the European Union to stimulate growth, employment and competitiveness in the regions, in line with Europe 2020 Strategy and the need for fiscal discipline.

We all agree that the Cohesion Policy has consistently shown its value added for the entire Union. According to European Commission estimates, over the last ten years, the Cohesion Policy has been instrumental for creating 2.4 million jobs at EU level.

The Cohesion Policy is important, particularly to reduce bottlenecks and boost the single market potential. Thus, it remains the most important financial instrument of Europe 2020 Strategy.

The Cohesion Policy has a major role in establishing a balance between economic growth and fiscal stability, which is a major challenge for the EU. In this context, it is absolutely necessary to ensure an adequate funding level for this European policy.

We all agree that the cohesion policy needs reform. In this context we welcome the proposals submitted by the Commission.

We strongly believe that the debate on the effectiveness of policies co-financed from the EU budget should be a fundamental part of negotiations on the multiannual financial framework 2014-2020.

The funding level provided for investments under the Cohesion Policy should take into account the priority objective of reducing development gaps among member states and among regions and it should provide adequate flexibility to ensure a better response to the specific individual needs of member states and regions. Therefore, there must be ensured the balance between simplification of the implementation mechanism of the Cohesion Policy and effectiveness of expenditure for Cohesion, therefore, flexibility and ease of use are essential.

We believe it is important to improve further on the quality of expenditure. However, “better spending” should not be a reason or a disguise for further reduction of the financial envelope dedicated to Cohesion Policy.

We INVITE

The European Council in June 2012 to consider the objectives set out in this Statement, when assigning the mandate for the multiannual financial framework to the future Cyprus Presidency of the Council of the EU.

Available at:

http://www.gov.ro/sessions-of-the-friends-of-cohesion-group-conference-on-eu-multiannual-financial-framework-2014-2020_l2a117305.html

“FRIENDS OF COHESION”

“FRIENDS OF COHESION”

Joint Statement on the next Multiannual Financial Framework

2014-2020

The Prime Ministers and Representatives of the “Friends of Cohesion” (Bulgaria, the Czech Republic, Croatia, Estonia, Greece, Hungary, Latvia, Lithuania, Malta, Poland, Portugal, Romania, Slovakia, Slovenia and Spain) met in Bratislava on 5 October 2012 in order to discuss common issues related to the MFF 2014-2020. The Prime Ministers and Representatives welcomed the presence of the President of the European Parliament and the President of the European Commission.

We RECALL

JOINT DECLARATION of Prime Ministers and Representatives of the Friends of Cohesion adopted on 1 June 2012 in Bucharest;

EUROPEAN COUNCIL CONCLUSIONS of 28-29 June 2012 which stated that "within the future MFF, spending should be mobilized to support growth, employment, competitiveness and convergence, in line with the Europe 2020 Strategy" and that "the reformed cohesion policy offers an opportunity to invest out of the crisis as it is a major tool for investment, growth and job creation at EU level and for structural reforms at national level".

We DECLARE

The European Union is facing an unprecedented crisis and needs to mobilize all available instruments to stabilize the economy, while restoring the conditions for sustainable growth and jobs. The European budget, and the Cohesion policy in particular, should play a strong role in this regard.

The Cohesion Policy remains a key investment tool for our countries. Furthermore, it benefits the entire union by strengthening the internal market and increasing economic convergence as well as channelling investments to areas of potential growth and supporting structural reforms in Member States.

Further decrease of the Cohesion policy funding - on top of the current Commission proposal - would not match the ambitions repeated in successive European Council conclusions nor the Treaty and the Europe 2020 Strategy objectives.

We sign up to better quality of spending and welcome measures already taken in the current course of negotiations. This creates the right framework for an effective use of the Cohesion policy as from 2014. At the same time we have to avoid increasing administrative burden.

We AGREE

The overall level of resources allocated to the Cohesion policy should be in line with the Commission proposal in order to achieve our common European goals. There is no room for further reduction following the Commission proposal.

The cohesion funding should remain concentrated on less developed regions and Member States, while recognising the need to help regions exiting convergence and phasing out regions to reach a higher level of development.

The current level of co-financing rates should be maintained or even increased in case a Member State is facing severe economic difficulties. In addition, we should respect - and extend to all Common Strategic Framework's funds - current provisions related to the eligibility of the non-recoverable VAT. The current pre-financing rates should also be maintained.

As an integral part of the Common Strategic Framework as well as the Europe 2020 Strategy, rural development should remain strong EU policy.

We need to secure that all programmes and instruments are operational from the first day of the new multiannual

financial framework being in place. A timely agreement is also important in the light of our ambition of better spending. Therefore, EU institutions and leaders should use all their efforts to conclude negotiations by the end of 2012 in order to demonstrate their ability to properly address current and future challenges and find solutions to citizen's benefit.

Available at:

http://www.vlada.gov.sk/friends-of-cohesion-joint-declaration-on-the-multiannual-financial-framework-2014-2020/

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The present report is displaying and analysing the attitudes of the ten Central and Eastern European member states (EU10) in the formulation of some of the most topical issues under discussion in the European Union. The countries in focus are Bulgaria, the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, Slovakia and Slovenia. The study attempts to identify the key EU-related priorities of these countries, their abilities to influence European Union policies alone or jointly and to look at the impact they make on the processes of European integration. The key issues discussed are the management of the eurozone crisis, the multiannual financial framework for 2014-2020, the reform of common agricultural policy and of cohesion policy after 2013, energy policy, external relations, enlargement and neighbourhood policy. The report concludes that – due to diverse interests, positions and challenges – the EU10 does not behave as a single lobby group, which can also be seen as avoiding unwanted cleavages within the Union. At the same time, many policy areas can be detected where they have a similar approach (e.g. in the field of energy security, enlargement, neighbourhood policy or cohesion policy financing and reforms) allowing them to make an impact on European integration.

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