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The race to EU integration: How many and how high are the hurdles?

Audra I. Mockaitis *

Vilnius University Department of Marketing, Sauletekio 9, II-817, LT-10222 Vilnius, Lithuania

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Abstract

Since the accession of the new member countries to the EU, the issues of regional growth and competitiveness have received wide attention by academics, governments and practitioners, and the benefits and drawbacks of EU membership are more and more the topics of public debate in the CEE region. It is not surprising that these questions sparked lively discussion at the conference "Catalysts and Impediments of Economic Development in Central and Eastern Europe," hosted by Vilnius University in October, 2004. This introductory note to the special issue overviews a selection of papers presented at the conference. The papers fall under any of six main themes: fiscal and monetary policy, competitiveness of the CEE region, social policy and public sector economics, economic theory, prospects for business and marketing.

Keywords: EU integration; EU membership; Economic development

In the early 1990s, like a deck of cards, one after another the communist regimes and economic systems in the Central and East European (CEE) countries fell to an abrupt halt. Paths to economic reform and democracy-based systems took on different forms, as Hungary, Poland and the Czech Republic went ahead with rapid transformation processes, while many of the Eastern European countries entered less constructive cycles of economic reform. Europeanization quickly became the driving force, which is still being implemented

* Tel.: +370 5 236 6146; fax: +370 5 236 6150.
E-mail address: Audra.I-Mockaitis@ef.vu.lt.

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to differing degrees in the countries throughout the region. And despite the diverse and sometimes turbulent paths toward this goal, on May 1, 2004, the paths of 10 CEE countries converged at the doorstep of the European Union.

But what does EU membership mean for the Central and Eastern European (CEE) countries? What are the impacts of policy changes for the economies of these countries? Will EU membership result in a shift in competitiveness in the region? Which countries will benefit most and why? What are the benefits and challenges associated with the enlarged European Union and how will these affect the direction of investments, labor, and the public sector, for example?

In answer to these questions, and in commemoration of its 425th anniversary, Vilnius University, one of the oldest universities in the CEE region, hosted an international conference entitled “Catalysts and Impediments of Economic Development in Central and Eastern Europe,” held on October 14–16, 2004. The anniversary could not have come at a better time. With the accession of the new member states to the European Union, scholars and practitioners throughout the region had much to consider and debate. Approximately, 100 participants from 25 countries gathered to discuss the impact of EU membership on the economies of the newly admitted countries.

Lively discussion centered on six main themes:

- Fiscal and monetary policies: impacts on growth.
- Competitiveness: changes, trends and factors of influence.
- Social policy and economics of the public sector.
- Influence of economic sciences on economic development.
- Prospects for business.
- Marketing theory and practice.

Attendance by scholars from throughout the world illustrated the importance of EU enlargement, not only for the CEE countries. Among distinguished guests at the conference was the Lithuanian Prime Minister, Algirdas Brazauskas, who provided a thorough overview of Lithuania’s road to EU integration, the obstacles already hurdled and the challenges that still lie ahead. Key speakers included Professor Erik Berglöf of the Stockholm Institute of Transition Economics, who stressed the importance of the financial sector in fostering transition, with his paper entitled “Convergence Revisited—Lessons from ‘New European’ Capitalism,” Professor Jørgen Drud Hansen, University of Southern Denmark, who highlighted the institutional aspects of EU integration in his paper “A Political Economy Analysis of the Eastward Enlargement,” Professor Michael Thomas of Strathclyde University, “Measuring Performance in Marketing,” and Professor Povilas Gylys, with a paper entitled “Two Paradigms of Economic Development in CEE countries.”

A wide range of high-quality presentations and vibrant discussions under each of the conference themes focused on relevant issues of integration. Among the main policy topics were the influence and consequences of uniform taxation policies on the growth of the transition economies and means for attaining stability in the financial sectors of the CEE countries. Sustainable agriculture, labor issues and health sector reforms were the focus of the social policy track. The competitiveness theme welcomed high-quality papers on foreign investment trends, entrepreneurship, competitiveness of industries and the internationalization of firms and attractiveness of the CEE countries. Information technologies, high-technology SMEs and financial services were the focus of the track "Prospects for Business." And of course, EU integration brings with it new challenges for reaching and attracting consumers through adapted advertising strategies and an understanding of the environment of each potential market, which were the highlighted themes of the Marketing track.

This special issue includes seven papers under the main conference themes.

The positive and negative aspects of EU membership are discussed by Hallett et al. (this issue) in their paper "The European Economy at the Cross Roads: Structural Reforms, Fiscal Constraints and the Lisbon Agenda." The authors compare the pros and cons of joining the rigid EU structures for both flexible economies, such as Britain, and less flexible economies, such as Germany and the Eastern countries, as well as the reasons behind the slow moving market reform throughout Europe. The authors suggest that incentives for joining the EU are not uniform for all countries and likely resemble a give and take scenario, with more of the giving, or absorption of the negative effects of reforms being the burden of flexible economies.

The paper "Former Soviet Union as the World Champion in Cheapness" by Raim (this issue) provides an overview of the relationship between income and price levels throughout the transition period in the countries of the former Soviet Union. The results illustrate the differences in starting points of the CEE countries, with Poland, Hungary and the Czech Republic consistently in the forefront throughout the period 1991–2000. However, the catching up of the Baltic State economies, both in terms of income and price levels is clearly evident, as Lithuania, Latvia and Estonia were ranked among the "cheapest" countries at the beginning of the 1990s and gradually, but consistently, converged to levels similar to those countries which had a head start, while countries such as Russia, the Ukraine and Belarus still lag behind. It is interesting to note that the Baltic States have had the highest growth rate in Eastern Europe, reaching 7.3% in 2003 compared to 4.3% in South Eastern Europe.[1] Raim's data illustrate the steady paths that some of the new EU member states have taken, and allow for inferring some of the causes for lagging economies.

One of the primary goals of the new EU member countries is to reign in inflation. Masso and Staehr (this issue) concentrate on the inflationary dynamics of the Baltic States in their paper entitled "Inflation Dynamics and Nominal Adjustment in the Baltic States." Among the questions the authors explore are whether membership in the European Monetary Union will not pose more problems for the economies of the transitioning countries than benefits, whether relatively rapidly increasing productivity in the Baltic States might cause inflation rates to increase, and most importantly, if the exchange rates and inflation in Estonia, Latvia and Lithuania, although stable, are flexible enough to withstand economic shocks. The authors seek answers in the estimation of Phillips curves for the three countries.

The European population is inevitably growing older, which also places a burden on the EU, as pension reforms are only beginning to take a definite form in the new member

[1] United Nations Economic Survey of Europe, No. 1, Economic Commission for Europe, New York and Geneva, 2004.

countries. In discussing the reforms needed to funded pension systems in the new member countries, in his paper "Contribution Rates into Funded Pension Systems in the Accession Countries," Kubíček (this issue) argues that contribution rates by the employed should be significantly higher in accession countries than in established economies in order to reach an adequate savings level upon retirement. This, he argues, is because of the rapid initial growth rates of these countries, which will gradually slow and reach the levels of established European economies, as well as differences in price levels and inflation rates. According to the author's calculations, the contribution of employees to social security must be higher than the Western European average by 30% in Slovenia, 57% in the Czech Republic, 70% in Lithuania and to up to 77% in Latvia.

In her paper "Corporate Income Taxation in Lithuania in the Context of the EU," Budrytė (this issue) discusses the influence of EU legislation on the income tax policies and competitiveness of the member states through a comparative analysis of their national corporate income tax policies. More specifically, the paper also explores the corporate income tax system in Lithuania in terms of both legislation and the actual tax burden. Although national tax systems exhibit significant divergence and are difficult to compare, the author argues that recent corporate income tax reforms in Lithuania have resulted in a system more similar to those of other EU member states and have improved the country's competitiveness in terms of statutory taxation. The author estimates measures of the effective profit tax burden (based on a macro backward-looking approach) for the enlarged EU and shows that Lithuania is in good competitive shape in this respect as well.

Two papers in this issue address foreign direct (FDI) and portfolio (FPI) investment in the CEE region. In their paper "Analysis of Foreign Investment Impact on the Dynamics of National Capitalization Structure: Computational Intelligence Approach," Plikynas et al. (this issue) explain international investment patterns in the CEE, the link between foreign investment and the development of economic sectors, and the influence that the distribution of FPI will have on the economies of the CEE countries in general (through a comparison between Lithuania and Poland versus EU and global averages). They propose a universally appropriate method aimed at the nontraditional estimation of sectoral indices weights according to the relative capitalization of economic sectors. The novelty of the proposed method lies in the application of neural network methods, which were thoroughly designed for the estimation of sectoral indices weights. Kippenberg (this issue) provides empirical evidence of the influence of FDI on employment in her paper "Sectoral Linkages of Foreign Direct Investment Firms to the Czech Economy." FDI may influence the domestic industrial structure and the economy as a whole, either positively or negatively. Specifically, Kippenberg seeks to explore the extent to which FDI is linked to the Czech economy and on what this depends through an analysis of data in 18 sectors. Results reveal that FDI has more of an influence on certain sectors over others.

Although reforms in the CEE countries have been ongoing for over a decade and a half, it is apparent that we have still only scratched the surface and have much yet to learn about and from one another. It still is not clear to what extent EU membership will positively or negatively influence the domestic economies of the newly acceded countries; the papers in this issue attest to the fact that there are still many unexplored avenues, which are undoubtedly important for and will influence policy development in the future.

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