

EUROPEAN UNIVERSITY INSTITUTE  
**Department of Political and Social Sciences**

**Mediating Membership: Sectors, States,  
and Strategies: EU Enlargement  
Negotiations (1998-2003)**

**Constructive and Destructive Interference**

**Wim Van Aken**

Thesis submitted for assessment with a view to obtaining the degree of  
Doctor of Political and Social Sciences of the European University Institute

March 2007



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*For Ann and my parents*

*'[...] eine Wissenschaft vom Menschen, und das ist die Volkswirtschaftslehre, vor allem nach der Qualität der Menschen fragt, welche durch jene ökonomischen und sozialen Daseinsbedingungen herangezüchtet werden. [...]*'  
(translation)

*'[...] a science concerned with human beings – and that is what political economy is – is concerned above else with the quality of the human beings reared under those economic and social conditions of existence. [...]*'

Max Weber, *Der Nationalstaat und die Volkswirtschaftspolitik*, p. 19, Freiburg, May 1895.

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## ABSTRACT

Why is it that when economic sectors have strong preferences and mobilise politically on a national and international level one does not always find the respective policy outcomes as ‘demand side’ international political economic theory predicts? In concentrating on the role national and international institutions play in an open polity model I argue that states (governments) and international organisations (negotiations) and the strategies of actors occupying these institutions mediate societal interests according to what I call *the logic of destructive and constructive interference*. States and international organisations act as constraints upon societal preferences at the negotiating table when their interests are not aligned. This is ‘destructive interference’. Conversely, when societal interests and institutional preferences are aligned states and strategies sustain or amplify societal preferences at the negotiating table. This I refer to as ‘constructive interference’.

I apply this conjecture to the fifth EU enlargement process (1998-2004) and the negotiated exemptions to the EU accession treaties. First, I quantitatively compare the universe of cases, i.e. 44 economic sectors across the ten applicant states according to their trade, factor and asset specificity. Subsequently, I subject the theory to a qualitative analysis in three economic sectors, i.e. pharmaceuticals, basic iron and steel and the international road freight transport, across four applicant states, i.e. the Czech Republic, Hungary, Poland and Slovakia. The case studies have been based on sector and country-specific literature and 82 positional and structured interviews.

The theoretical framework on the demand side has been provided by insights from modern political economy. The study finds that enlargement had a redistributive influence on sectoral incomes that resulted in preference formation and political mobilisation along sectoral lines. On the supply side, veto players and negotiation theory, combined with assumptions about political preference formation, provided hypothetical guidance. It finds that governments observed sectoral interests when their demand for protection reduced government expenditure and did not damage popular support for EU entry. On an international level, government negotiators found it easier to extract concessions from the EU when constrained by at least one domestic veto player. The EU would extend these concessions to other countries under the banner of equality and reciprocity.



## List of Abbreviations

AA	Association Agreement
CAP	Common Agricultural Policy
CEECs	Central and Eastern European Countries
COMECON	Council for Mutual Economic Assistance
COREPER	Committee of Permanent Representatives
CP	Common (negotiation) Position
DCP	Draft Common (negotiation) Position
EA	Europe Agreement
EC	European Commission
ECMT	European Conference of Ministers of Transport
ECSC	European Coal and Steel Community
EP	European Parliament
EU	European Union
FDI	Foreign Direct Investment
GATT	General Agreement on Tariffs and Trade
GMP	Good Manufacturing Practice
IISI	International Iron and Steel Institute
IO	International Organisation
M&A	Mergers and Acquisitions
MoE	Ministry of Economy
MoEN	Ministry of Environment
MoET	Ministry of Economy and Transport
MoFA	Ministry of Foreign Affairs
MoFI	Ministry of Finance
MoH	Ministry of Health
MoI	Ministry of Interior
MoT	Ministry of Transport
MoTI	Ministry of Trade and Industry
MP	Member of Parliament
NTBs	Non Tariff Barriers
PM	Prime Minister
PMO	Prime Minister's Office
R&D	Research and Development
M&As	Mergers and Acquisitions
SU	Soviet Union
TA	Transition Arrangement
TPR	Transition Period Request
V-4	Visegrad Four Countries (Czech Republic, Hungary, Poland and Slovakia)



## **Executive Summary**

Three building blocs make up the structure of the dissertation.

Part I concerns the puzzle, the research questions, the alternative accounts and the theory (chapter 1). It subsequently provides a detailed analysis of the dependent variable (chapter 2).

Part II has been devoted to sectoral demands to ease the adjustment costs of EU membership. It deals with preference formation and political mobilisation of economic sectors in the enlargement process. Chapters 3, 4 and 5 analyse the pharmaceutical, basic iron and steel and international road freight industries respectively.

Part III has analysed the institutional supply of adjustment to EU membership. Its analysis centres on the aggregation of sectoral preferences in the domestic arena in the applicant states (chapter 6). It also evaluates the ensuing domestic constraints and strategies in the EU entry talks (chapter 7).



## List of Figures

Figure 1: Number of TAs by country .....	17
Figure 2: H.O. and R.V. at the extremes of factor and sector specificity .....	26
Figure 3: Causal Diagram .....	36
Figure 4: Detailed Partial Mediated Model .....	37
Figure 5: The Theoretical Framework: Constructive and Destructive Interference .....	53
Figure 6: Factor Specificity, Asset specificity and Political Mobilisation .....	65
Figure 7: Number of Sectoral Transitional Arrangements .....	74
Figure 8: Number of TAs by Country .....	76
Figure 9: Number of TAs Weighed by Duration and by Country .....	76
Figure 10: Number of TAs per Sector Weighed by Duration .....	77
Figure 11: National Coverage Ratio (per cent of the economy affected by TAs) .....	78
Figure 12: Trade Balance in Pharmaceuticals (1992-2004).....	118
Figure 13: Exports in Pharmaceuticals (1997-2004) .....	119
Figure 14: The Czech Pharmaceutical Market (1999).....	120
Figure 15: The Hungarian Pharmaceutical Market (1990-2000) .....	121
Figure 16: The Polish Pharmaceutical Market (1996).....	122
Figure 17: R&D and Investment in Pharmaceutical Industry (1998-2002).....	123
Figure 18: Sectoral Concentration in the Drugs Industry (1998-2002).....	126
Figure 19: Sectoral Comparison of the V-4 Pharmaceutical Industry .....	144
Figure 20: Output crude steel over GDP (mmt, 1992-2004).....	167
Figure 21: Trade Balance in Basic Iron and Steel (1992-2004).....	169
Figure 22: Exports World and EU (1997-2004).....	170
Figure 23: R&D and Investment in Basic Iron and Steel (1999-2002) .....	172
Figure 24: Sectoral Concentration in the Basic Iron and Steel Industry (1998-2002) .....	173
Figure 25: Sectoral Comparison of the V-4 Basic Iron and Steel Industry .....	185
Figure 26: Sectoral Cohesion of the Road Transport Industry in the V-4 (1998-2002).....	209
Figure 27: Sectoral Cohesion of the Road Transport Industry in the V-4 (1998-2002).....	210
Figure 28: Sectoral Comparison of the V-4 International Road Freight Industry .....	219
Figure 29: Cross Sectional Comparison Czech Republic .....	222
Figure 30: Cross Sectional Comparison Hungary.....	224
Figure 31: Cross Sectional Comparison Poland .....	226
Figure 32: Cross Sectional Comparison Slovakia .....	227
Figure 33: Policy Process for the Preparation of the Czech Republic's Negotiation Position.....	252
Figure 34: Policy Process for the Preparation of Hungary's Negotiation Position .....	262
Figure 35: Policy Process for the Preparation of Poland's Negotiation Position (Before September 2001) ....	274
Figure 36: Policy Process for the Preparation of Poland's Negotiation Position.....	277
Figure 37: Policy Process for the Preparation of Slovakia's Negotiation Position .....	287
Figure 38: Distribution of power among EU Decision Making Institutions of the V-4 (1998) .....	294
Figure 39: Distribution of power among EU Decision Making Institutions of the V-4 (2000-2001).....	295
Figure 40: Preference Formation of EU Decision Making Institutions.....	295
Figure 41: The Formal EU Enlargement Negotiation Framework.....	306
Figure 42: Bargaining under the absence of a domestic veto player .....	325
Figure 43: Bargaining in the presence of a domestic veto player .....	326
Figure 44: Domestic Constraints at the EU Entry Talks for the V-4 .....	335





## List of Tables

Table 1: Total TAs per country and selected indicators.....	13
Table 2: Correlations TAs and GDP/capita.....	13
Table 3: Correlations intensity of TAs and GDP/capita.....	14
Table 4: Correlations the TAs national coverage ratio and GDP.....	14
Table 5: Vertical TAs per Sector and Country (NACE Rev 1.1.).....	73
Table 6: TAs per country and sector weighed by duration.....	75
Table 7: Sectoral TAs by Substance.....	75
Table 8: Cross sectoral or Horizontal TAs by Domain and Country.....	79
Table 9: TAs per sector (Nace 1.1 1-digit) measured by presence, number and number by time.....	91
Table 10: Trade in Pharmaceuticals (per cent, 1992-2004).....	115
Table 11: Specificity of the Pharmaceuticals Sector (1998-2002).....	124
Table 12: Economic and Political Market Structure.....	141
Table 13: Economic and Political Strength.....	143
Table 14: Trade in Basic Iron and Steel (per cent, 1992-2004).....	166
Table 15: Selected Asset Specificity Indicators (1998-2002).....	173
Table 16: Economic and Political Market Structure (1998-2002).....	182
Table 17: Economic and Political Strength.....	183
Table 18: ECMT Mulilateral Licence Indicators (1998).....	201
Table 19: Mode of International Transport V-4-EU-15 (2002).....	203
Table 20: Road Transport V-4-EU-15 (2002 and 2004).....	204
Table 21: Bilateral Transport in the V-4 (1999-2004).....	205
Table 22: Economic and Political Strength.....	217
Table 23: Cross Sectional/Country Comparison.....	221
Table 24: Governments and Parliamentary Majorities in the V-4.....	336
Table 25: Duration of the Accession Negotiation Rounds (March 1998-December 2002).....	337



# TABLE OF CONTENTS

<b>Acknowledgements.....</b>	<b>I</b>
<b>Abstract.....</b>	<b>III</b>
<i>List of Abbreviations .....</i>	<i>V</i>
<i>Executive Summary .....</i>	<i>VII</i>
<i>List of Figures .....</i>	<i>IX</i>
<i>List of Tables.....</i>	<i>XI</i>
<b>Table of Contents .....</b>	<b>XIII</b>
<b>PART I: MEDIATING MEMBERSHIP .....</b>	<b>1</b>
<b>Chapter 1: The Argument.....</b>	<b>3</b>
<i>1.1. The Puzzle: Joining the EU under Varying Conditions.....</i>	<i>3</i>
<i>1.2. Alternative Accounts: Institutions, Readiness and Closed Polities .....</i>	<i>7</i>
1.2.1. Historical Institutionalism .....	7
1.2.2. Adjusting to the EU: Who Was Ready? .....	11
1.2.3. Closed Polities .....	14
1.2.3.1. (Neo-) Realism.....	15
1.2.3.2. (Neo-) Liberalism .....	17
<i>1.3. Interest Groups, Constructive and Destructive Interference.....</i>	<i>20</i>
1.3.1. Defining Interests and Deriving Preferences .....	21
1.3.2. Limitations: Political Action and Accommodation of Preferences.....	24
1.3.3. The Theoretical Framework: Sectors, States and Strategies.....	25
1.3.3.1. Sectors.....	26
1.3.3.2. States.....	29
1.3.3.3. Strategies.....	31
<i>1.4. Application of the Theory.....</i>	<i>32</i>
1.4.1. Independent and Dependent Variables .....	32
1.4.2. Research Design and Hypotheses.....	34
1.4.2.1 Demand Side: Sectors and EU Enlargement.....	41
1.4.2.1 Supply Side: States and Strategies and EU Enlargement.....	45
<i>Conclusion.....</i>	<i>50</i>
<b>Chapter 2: Transitional Arrangements.....</b>	<b>55</b>
<i>Introduction.....</i>	<i>55</i>
<i>2.1. A Combined Strategy.....</i>	<i>56</i>
2.1.1 A Variable-oriented Approach.....	57
2.1.2. A Case-oriented Approach.....	58
2.1.3. A Combined Strategy.....	58
<i>2.2. Selection of the Cases.....</i>	<i>60</i>
2.2.1. Sectors .....	62
2.2.2. States.....	67
2.2.2.1. The Applicants and the EU .....	68
2.2.4. Time Dimension .....	69

2.3. Operationalisation and Specification of the Variables .....	70
2.3.1. Dependent Variable .....	70
Sectoral TAs .....	71
Horizontal TAs .....	78
2.3.2. Demand Side: Independent Variables .....	80
2.3.2.1. Factor and Asset specificity .....	80
2.3.2.2. Collective Action .....	84
2.3.2.3. Insider Status .....	86
2.3.3. Supply Side: Independent Variables .....	86
2.3.2.4. Veto players .....	87
2.3.2.5. Delegation and Insulation of the Policy Process .....	87
2.3.2.6. Executive Preferences .....	88
2.3.2.7. State Preferences .....	88
2.3.2.8. International Negotiations .....	89
Conclusion .....	90
<b>PART II: SECTORS.....</b>	<b>93</b>
<b>Introduction.....</b>	<b>95</b>
Notes on Data.....	96
1. Defining sectors.....	96
1.1. Pharmaceuticals .....	97
1.2. Basic Iron and Steel .....	97
1.3. Road Freight Transport.....	98
2. Data Availability and Reliability .....	98
2.1. Pharmaceuticals .....	98
2.2. Basic Iron and Steel .....	99
2.3. Road Freight Transport.....	99
<b>Chapter 3: The Pharmaceutical Industry .....</b>	<b>101</b>
3.1. Industry Concerns: Intellectual Property Rights.....	101
3.1.1. The Sector in the EU .....	101
3.1.2. The Sector in the Applicant States.....	102
3.2. Historical Overview .....	105
3.2.1. 1945-1989.....	105
3.2.2. Transition and Consolidation (1989-2004).....	107
3.2.2.1. Czechoslovak Pharmaceuticals (Czech and Slovak Republics).....	108
3.2.2.2. Hungarian Pharmaceuticals .....	109
3.2.2.3. Polish Pharmaceuticals .....	110
3.3. Characteristics and Preferences: A Divided Industry.....	112
3.3.1. Trade.....	112
3.3.1.1. World Pharmaceutical Markets (1992-2004).....	112
3.3.1.2. EU-V-4: Eastern Exports and Western Imports.....	114
3.3.2. Asset Specificity: A High Technology Manufacturing Industry?.....	123
3.3.4. Sectoral Cohesion: A Split Political Organisation .....	125
3.3.4.1. National Associations .....	127
3.3.4.2. European Federations .....	138
3.3.4.3. A Special Insider: Economic and Political Strength.....	143
3.4. Conclusion.....	143
<b>Chapter 4: The Basic Iron and Steel Industry.....</b>	<b>147</b>
4.1. The Industry's Concerns: Restructuring and Market Access.....	147

4.1.1. The Sector in the EU .....	147
4.1.2. The Sector in the Applicant States.....	149
<b>4.2. Historical Overview .....</b>	<b>152</b>
4.2.1. 1945-1989.....	152
4.2.2. Transition and Consolidation (1989-2004).....	154
4.2.2.1. Czechoslovak Basic Iron and Steel (Czech and Slovak Republics).....	155
4.2.2.2. Hungarian Basic Iron and Steel .....	158
4.2.2.3. Polish Basic Iron and Steel Sector .....	159
<b>4.3. Characteristics and Preferences: A Sunset Industry.....</b>	<b>162</b>
4.3.1. Trade.....	162
4.3.1.1. World Steel Markets (1992-2004) .....	162
4.3.1.2. The EUs Steel Trade Regime (ECSC and EAs).....	163
4.3.1.3. From Trade Surplus to Deficit .....	166
4.3.2. Asset Specificity: Medium Low Technology Industry .....	170
4.3.3. Sectoral Cohesion: A Highly Concentrated Industry.....	173
4.3.3.1. National Associations .....	174
4.3.3.2. European Federation: Eurofer.....	179
4.3.4. Insider Status: Economic and political Strength.....	183
<b>4.4. Conclusion.....</b>	<b>183</b>
<b>Chapter 5: International Road Freight Industry .....</b>	<b>187</b>
<b>5.1. The Industry's Concern: Competitiveness and Market Access .....</b>	<b>187</b>
5.1.1. The Sector in the EU .....	187
5.1.2. The Sector in the Applicant States.....	190
<b>5.2. Historical Overview .....</b>	<b>191</b>
5.2.1. 1945-1989.....	191
5.2.2. Transition and Consolidation (1989-2004).....	193
5.2.2.1. Czech and Slovak Trucking services .....	194
5.2.2.2. Hungarian Trucking Services .....	196
5.2.2.3. Polish Trucking Services .....	198
<b>5.3. Characteristics and Preferences: A Sunrise Industry .....</b>	<b>199</b>
5.3.1. Trade.....	199
5.3.1.1. European Trade in Trucking Services (1992-2004).....	200
5.3.1.2. EU Trade Regime in Trucking Services (1992-2004) .....	202
5.3.1.3. The Figures .....	203
5.3.3. Asset Specificity: Low Entry Barriers .....	207
5.3.4. Sectoral Cohesion: A Highly Fragmented Sector.....	208
5.3.4.1. National Associations .....	210
5.3.4.2. European Federation: International Road Transport Union (IRU) .....	215
5.3.5. Insider Status: Economic and Political Strength.....	217
<b>5.4. Conclusion.....</b>	<b>218</b>
<b>Cross Sectional Comparison .....</b>	<b>221</b>
<i>Czech Republic</i> .....	222
<i>Hungary</i> .....	223
<i>Poland</i> .....	225
<i>Slovakia</i> .....	226
<b>Conclusion Part II.....</b>	<b>229</b>

<b>PART III: STATES and STRATEGIES.....</b>	<b>235</b>
<b>Introduction.....</b>	<b>237</b>
<b>Assumptions.....</b>	<b>238</b>
<i>Two Levels of Analysis .....</i>	<i>238</i>
<i>An Open Polity .....</i>	<i>238</i>
<b>Chapter 6: States.....</b>	<b>241</b>
6.1. <i>Institutional Processes .....</i>	<i>241</i>
6.1.1. Constitutionally Mandated Number of Veto players .....	242
6.1.1.1. Czech Republic .....	242
6.1.1.2. Hungary .....	243
6.1.1.3. Poland .....	243
6.1.1.4. Slovakia .....	244
6.1.2. Policy Processes and Delegation .....	245
6.1.2.1. Czech Republic .....	245
6.1.2.2. Hungary .....	256
6.1.2.3. Poland .....	267
6.1.2.4. Slovakia .....	282
<i>Institutional Comparison.....</i>	<i>293</i>
<i>Conclusion.....</i>	<i>299</i>
<b>Chapter 7: Strategies .....</b>	<b>301</b>
<i>Introduction.....</i>	<i>301</i>
7.1. <i>Institutional Characteristics of the Accession Negotiations.....</i>	<i>303</i>
7.1.1. Institutions .....	303
7.1.2. Procedures .....	307
7.1.2.1 The Common Position .....	307
7.1.2.2. Level of Delegation .....	311
7.1.3. General and Idiosyncratic Aspects .....	312
7.1.3.1. Sequencing.....	312
7.1.3.2. Group Dynamic.....	313
7.1.3.3. Uncertainty .....	319
7.1.3.4. Equality and Reciprocity.....	320
7.2. <i>Second Image Constraints.....</i>	<i>322</i>
7.2.1 The Model .....	322
7.2.2. External Impact of Domestic Constraints in the V-4.....	327
7.2.2.1. Czech Constraints .....	327
7.2.2.2. Hungarian Constraints .....	329
7.2.2.3. Polish Constraints .....	330
7.2.2.4. Slovak Constraints .....	332
<i>Conclusion.....</i>	<i>337</i>
<b>Analytical Summary .....</b>	<b>339</b>
<b>Conclusions.....</b>	<b>351</b>
<b>Bibliography .....</b>	<b>355</b>
<i>Annex 1: TAs per Chapter of the Acquis and Country .....</i>	<i>371</i>

*Annex 2: Interviews*..... 373





**PART I: MEDIATING MEMBERSHIP**  
**The Puzzle, Alternative Accounts and Theory**



## CHAPTER 1: THE ARGUMENT

In the first half of the 1990s the European Union (EU) decided to embark on its fifth enlargement. Between the end of 1998 and 2003 the Central and Eastern European Countries (CEECs), Malta and Cyprus negotiated the terms of joining the EU. The negotiations took the form of bilateral talks between the EU, representing the 15 member states, and the individual future member states, i.e. Cyprus, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovakia, and Slovenia. The negotiations dealt primarily with the application of the *acquis communautaire*, the body of EU legislation, in the acceding countries. During the process the applicant states enacted, integrated, and implemented all EU related legislation. The exceptions permitted were transitional arrangements (henceforth TAs) and derogations, respectively temporary and permanent exemptions from the *acquis*.

TAs are the distributional outcome of the EU enlargement process. Their variation tells something about the EU accession negotiations and the sectors and countries to which they apply. For the comparativists they are an opportunity. They provide us with a handle on the otherwise conceptually and analytically elusive phenomenon of EU enlargement, its causes and consequences. Treating TAs as *explanandum* allows us to rigorously test hypotheses pertaining to the behaviour of sectors, states and their respective strategies in the enlargement process. An accurate test of theoretically informed hypotheses under clear assumptions has all too often been absent in the enlargement literature.

### 1.1. The Puzzle: Joining the EU under Varying Conditions

During the EU accession negotiations 292 TAs were agreed in sectors covered by 29 chapters of the *acquis communautaire*<sup>1</sup>. These arrangements delay the application of the *acquis communautaire* (henceforth *acquis*) and constitute different sectoral conditions under which the EU enlarges. They are the main flexibility in the negotiations<sup>2</sup>. TAs ease the adjustment costs of EU enlargement and may provide for

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<sup>1</sup> European Commission, *Report on the results of the negotiations on the accession of Cyprus, Malta, Hungary, Poland, the Slovak Republic, Latvia, Estonia, Lithuania, the Czech Republic and Slovenia to the European Union*, Brussels, 2002. The chapters of the *acquis* covering 'institutions' and 'miscellaneous' are not calculated because they essentially do not affect sectors.

<sup>2</sup> A. MAYHEW, *Enlargement of the European Union: an analysis of the negotiations with the central and eastern European candidate countries*, Brighton: University of Sussex, 2000, pp. 14-15; G. AVERY, *The Commission's Perspective on the EFTA Accession Negotiations*, Brighton: University of Sussex, 1995.; P. NICOLAIDES, *et al.*,

a temporary competitive advantage as the cost for joining the European single market can be deferred until some years after EU membership. EU entry presupposes full application of the *acquis* on EU accession while the presence of TAs indicates varying levels of EU legislative application.

TAs can be requested by both the EU and the candidate countries, however, the EU emphasises that they should be kept at a minimum and as short as possible<sup>3</sup>. As such, their presence is not surprising. They have been on the agenda in the past four EU enlargements. Moreover, for the current enlargement process country practitioners and academics generally agreed that immediate and strict application of the entire *acquis* in the applicant countries would be damaging for the reform and transition processes underway<sup>4</sup>.

Nevertheless, during the bilateral negotiations between the EU and the individual future member states the EU did not agree on all transition period requests (henceforth TPRs) where the future member states encountered difficulties. In some cases TPRs were completely or partially accepted, while in others they were entirely rejected. Consequently, instead of finding TAs across the board for those sectors where applicant countries requested them, one finds variation. Furthermore, TAs do not only vary between sectors within countries, but also across countries in similar sectors, and sometimes also in form and content.

Taking in account that: (a) TAs were designed to ease the adjustment cost of EU enlargement; and (b) applicant countries request TAs when they encounter difficulties when applying the *acquis*, the variation of the TAs is puzzling for three reasons.

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*A guide to the enlargement of the European Union (II): a review of the process, negotiations, policy reforms and enforcement capacity*, Maastricht: Institut Europeen d'Administration Publique, 1999.

<sup>3</sup> Commission of the European Communities, *Agenda 2000: For a stronger and wider union*, Luxembourg, 1997., pp. 51-52.

<sup>4</sup> H. GRABBE and K. HUGHES, *Eastward enlargement of the European Union*, London: Royal Institute of International Affairs (RIIA), 1998., pp. 55-65; G. AVERY and C. FRASER, *The enlargement of the European Union*, Sheffield: Sheffield Academic Press, 1998., p. 246; L. BALCEROWICZ, Europe Growing together in: A. LANDAU, R. WHITMAN and V. CURZON PRICE, *The enlargement of the European Union: issues and strategies*, London; New York: Routledge, 1999, pp. pp. 6-9.; A. SMITH, Integration into the Single Market, in: R. DEHOUSSE, *An Ever Larger Union?, the Eastern enlargement in perspective*, Baden: Nomos Verlagsgesellschaft, 1998, pp.104-105; A. MAYHEW, *Recreating Europe: the European Union's policy towards Central and Eastern Europe*, Cambridge; New York: Cambridge University Press, 1998., p. 389; U. SEDELMEIER and H. WALLACE, Eastern Enlargement, in: H. WALLACE and W. WALLACE, *Policy Making in the EU*, Oxford: Oxford University Press, 2001, pp. 455; EBRD, *Transition Reports*, London, 2000, 2001, 2002.; R.E. BALDWIN, *Towards an integrated Europe*, London: Centre for Economic Policy Research, 1994., pp. 197-203.

First, one would expect sectoral TAs across the board when the candidate country requests them, rather than the EU granting a TA for a particular sector, while excluding another. For instance, in Hungary sectoral TAs can be observed for pharmaceuticals and international road haulage, but not for steel. The Hungarian basic iron and steel industry was making heavy losses at the time of the EU enlargement negotiations. Application of EU legislation complicated matters for the industry.

Second, and more contentious, one would expect similar sectoral TAs across all candidate countries that request them; rather than the EU granting one applicant country a sectoral TA and excluding another, particularly for sectors facing similar problems. For instance, the Czech Republic, Poland and Slovakia negotiated sectoral TAs for the steel industry, whereas Hungary failed to do so.

Finally, enlargement literature as well as IR and negotiation theory expects that the applicant states are unable to obtain different sectoral conditions upon EU entry. A central tenet of its assumptions is the power asymmetry between the EU and the applicant states works against the applicant countries interests in the process. They are supplicants and dependants particularly when confronted with the EUs dominating power in the EU accession negotiations.

Obviously, one could ascribe the variance of TAs between similar sectors in different applicant countries to the bilateral nature of the accession negotiations. Each applicant country negotiates individually with the EU while all applicant countries vie for EU membership. As a result, applicant states appear to compete among each other for EU membership strengthening the bargaining position of the EU. Consequently, the EU would be less inclined to grant TAs whereas applicant countries would soften their negotiation position to speed up the EU entry talks to surpass their competitors in the number of closed chapters of the *acquis*<sup>5</sup>. As a result, one would expect few TAs *ex post* and little variance of the sectoral conditions under which the EU enlarges. Such is not the case (see annex 1). Moreover, the simultaneous bilateral negotiations and the competition element favours the generalisation of concessions by EU and the applicant countries. Negotiating EU membership simultaneously with 12 applicant

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<sup>5</sup> E. BERGLOF and G. ROLAND, *From Regatta to Big Bang, Impact of EU accession strategy on reforms in central and eastern Europe*, Washington: IMF Working Paper, 2000. EU accession can be seen as a “tournament” prize where only the best can win. Perceiving entry as a tournament could explain why countries speed up their negotiations and drop TPRs in order to obtain EU membership. The best pupil in the class will then not necessarily obtain the best result.

countries, including Romania and Bulgaria, suggest that an overburdened EU would harmonise the criteria for granting TAs, which would reduce the impact of the bilateral form accession negotiations take. Applicant countries would be inclined to drop TPRs because EU membership would override particular or special interests.

This brings me to the first research question: *'How and why do sectoral conditions for joining the EU, i.e. the presence of TAs, vary for the individual applicant states?'* Accession negotiations on a sectoral level concern the sectoral conditions under which the candidate countries join the EU, and more specifically the single European market. In other words, how can one explain the presence of TAs under which the EU enlarges?; and, what accounts for their sectoral variation across the different applicant states?

The enlargement literature provides several insights to answer this question. Actors are central to its analysis. Essentially, it follows three broad approaches each with a different focus pointing to a different actor and explanation. The first approach looks at the traditional method of the EU enlargement in the sense of an historical institutionalist theory. EU institutions are central in its analysis. The second approach considers the candidate countries' readiness for EU membership and also concentrates on the bargaining aspect of the negotiations. States under a closed polity, the EU-15 and the applicants, are the main explanatory variables. The third approach, which this research project adheres to, focuses on the underlying motives of interest groups and their response to the challenges and opportunities posed by the enlargement process. This approach is largely to be found in the realm of political economy. Interest groups, and more specifically firms, understood as factors, i.e. labour and capital, are essential to its perspective. The second research question is therefore: *'What do the transitional arrangements reveal about sectoral interests' ability to influence the enlargement process?'*

This chapter comprises four sections. First, it presents three alternative explanations from the literature on EU enlargement and international relations, i.e. historical institutionalism, the readiness argument and the closed polity argument in the form of (neo-)realism and (neo-)liberalism. The second segment discusses interest groups and the theoretical framework of the present research, which falls partly in the realm of

‘demand side’ modern political economy and ‘supply side’ institutionalism. The third section applies the theory to the EU enlargement process and the presence of TAs.

## **1.2. Alternative Accounts: Institutions, Readiness and Closed Polities**

### **1.2.1. Historical Institutionalism**

The historical institutionalist approach largely explains the presence of sectoral TAs and their variation within and across countries as the result of a set of established rules and principles. They have been maintained over the past four enlargements and are embedded in the classical EU enlargement method, which is furthered by EU institutions.

Historical institutionalists define institutions by and large ‘as the formal or informal procedures, routines, norms and conventions embedded in the organisational structure of the polity’<sup>6</sup>. They accept the contention that conflict among rival groups for scarce resources lies at the heart of politics<sup>7</sup>. Explanations for political outcomes of these conflicts can be found in:

(a) The institutional organisation of the polity as the principal factor structuring collective behaviour and generating distinctive outcomes, emphasising ‘structuralism’ implicit in the institutions of the polity. As such, institutional development underlines path dependence;

(b) The way the institutional organisation of the polity and economy structures conflict to privilege some interests while demobilizing others. Historical-institutionalism tends to emphasise the asymmetries of power associated with the operation and development of institutions. Institutions are capable of structuring the character and outcomes of group conflict rather than being neutral brokers among competing interests<sup>8</sup>;

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<sup>6</sup> P.A. HALL and R.C.R. TAYLOR eds, *Political science and the three new institutionalisms*, Koln: Max Planck Institut für Gesellschaftsforschung, 1996., p. 938; S. STEINMO and K. THELEN, Historical Institutionalism in comparative politics, in: S. STEINMO, K. THELEN and F. LONGSTRETH, *Structuring politics: historical institutionalism in comparative analysis*, Cambridge[England]: Cambridge University Press, 1992, pp.

<sup>7</sup> P.A. HALL and R.C.R. TAYLOR, Political Science and Three New Institutionalisms, in: *Political Studies*, 1996, XLIV, pp. 936-57., pp. 937-942.

<sup>8</sup> For the definition of power see S. LUKES, *Power: a radical view*, Houndmills, Basingstoke, Hampshire: New York: Palgrave Macmillan, 2004.

(c) The way institutions affect behaviour primarily by providing actors with greater or lesser degrees of certainty about the present and future behaviour of other actors. By placing actors in an institutional context, institutions affect individual action by altering the expectations an actor has about the actions that others are likely to take. More specifically, institutions provide information relevant to the behaviour of others. Individuals adhere to these patterns of behaviour because deviation will make the individual worse off in terms of a decreasing certainty and predictability. It follows that the more an institution contributes to the resolution of collective action problems the more robust it will be.

Within the enlargement literature, *Christopher Preston* and *Phendon Nicolaidis* (*et. al.*) represent the historical-institutionalist perspective.<sup>9</sup> Both emphasize the traditional ‘Community Method’ of EU expansion. Central in their argument is the ‘classic’ method of EU enlargement. It is based on experience and considered as an integral component of the underlying Community integration method. The six enlargement rounds to date have followed a consistent pattern for the formal accession procedures adopted<sup>10</sup>. The method’s major strength has been to establish at the outset of the negotiations what the key outcomes should be. The classical method has endured over time. The growing diversity within the EU due to previous enlargements has not changed this; it merely added new policy instruments without fundamentally altering the classical enlargement method.

Not only has the formal method endured over time, but the procedures of the process based upon implicit assumptions and principles too. Six underlying principles are identified, of which two stress the power asymmetry between the negotiating parties, i.e. the EU and the applicant states<sup>11</sup>. First, the EU prefers to negotiate with groups of

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<sup>9</sup> C. PRESTON, *Enlargement & integration in the European Union*, London; New York: Routledge, 1997., p. 4.; The first EU enlargement (UK, Denmark and Ireland; 1973); the second EU enlargement (Greece; 1981); the third EU enlargement (Spain and Portugal; 1986); the ‘EFTA’ enlargement (Austria, Sweden and Finland; 1995); P. NICOLAIDES, *et al.*, *A guide to the enlargement of the European Union (II): a review of the process, negotiations, policy reforms and enforcement capacity*, Maastricht: Institut Europeen d’Administration Publique, 1999.; P. LUIF, *On the Road to Brussels, The political Dimension of Austria’s Finland’s and Sweden’s Accession to the European Union*, Vienna, 1995.; I.S. TSALICOGLU, *Negotiating for Entry, The accession of Greece to the European Community*, Aldershot, 1995., pp. 29-78.

<sup>10</sup> C. PRESTON, *Enlargement & integration in the European Union*, London; New York: Routledge, 1997., p. 9.

<sup>11</sup> *Ibid.*, p. 19-22. Helen Wallace describes the power asymmetry as a core assumption of the enlargement literature as follows: (a) Enlargement is an asymmetrical process in which the incumbent members, in the driving seat, engage with the candidates, which are supplicants and dependants; (b) the issue for the incumbents is whether or not the candidates are desired or desirable partners in terms of their fit with the existing and established patterns of



states, which creates economies of scale allowing the EU to defray the adjustment costs of enlargement more widely among the applicants for EU membership. Second, the existing member states draw on the enlargement process to pursue their own interests and collectively externalise internal problems. The dynamics and methods of the accession negotiations also shape the expectations of the participants and progress of the negotiations. Here another key principle of the classical EU enlargement method maintains that applicants must accept the *acquis* in full and that no permanent opt-outs are available, but TAs are. As such, the method sets the parameters of the negotiations, defines the limits of the compromises and shapes mutual expectations of both parties in the negotiations. The principle has acted as a discipline on the potential members and reduced the uncertainty of upsetting the accession negotiations.

The main explanatory variable for the presence of sectoral TAs and their variations across the candidate countries in the historical-institutionalist theory lies in the institutional provisions that are reflected in a set of established rules and principles. These rules and principles have been maintained over the past four enlargements and are embedded in the classical EU enlargement method. More specifically, the number of TAs is influenced by the institutional parameters, and the power asymmetry, between the member states on the one hand and the applicants on the other, embedded in the classical method of EU expansion. Finally, the enlargement policy affects the strategic interaction among the negotiating parties by setting the general framework in which the negotiations take place that ultimately agree on the sectoral conditions under which the EU enlarges.

Although the historical-institutionalist approach draws attention to the role of institutions in political and economic policy outcomes, their approach falls short on three accounts.

First, the approach has difficulty in explaining why actors react differently in a similar institutional realm. For instance, the historical institutionalist approach fails to account for Warsaw's relative tough bargaining position in the first phase of the negotiations and became more lenient from November 2001 onwards. Another case in

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integration, in: H. WALLACE, EU enlargement: A neglected subject, in: M. G. COWLES, *The State of the Union: Risks, Reform, Resistance, and Revival*, Oxford: Oxford University Press, 2000, pp. 149-63.

point is the flexibility of Czech negotiators at the outset of the process. They changed their strategy over the last six months of the negotiations.

Second, an historical institutionalist view of institutions is somewhat static and fails to account for institutional evolution over time. The EU is in constant motion and as integration advances so does the EU enlargement policy. The growing number of directives and regulations at a European level embodied in the *acquis communautaire* has profoundly changed the nature of EU enlargement process. It has not only made accession negotiations more complicated and extensive, but also raised the threshold for EU membership. Two developments had just taken place at the time of the EU membership applications of the CEECs (1994-1996) which would make the fifth enlargement – or the second since the creation of the EU – far more complicated: a) the completion of the single European market; and, b) the negotiation of the Maastricht Treaty establishing the European Union. Both events have spurred regulatory innovation<sup>12</sup>. The fifth enlargement negotiations included acceptance by the candidate countries of the traditional *acquis communautaire* and the extensions provided for in the Single European Act and the Treaty of the European Union – both excluded from previous accession negotiations<sup>13</sup>.

Along this view, the EU would act more lenient when negotiating EU accession since the burden of EU membership has become heavier for the newcomers. The EU enlargement policy would therefore allow for more TAs and derogations than in the previous four accessions<sup>14</sup>. Nevertheless, the progress reports of the European Commission (EC, 1998, 1999, 2000, 2001, 2002 and 2003) do not support this view. The EC emphasised the complete transposition of the *acquis* and gave the applicant states bad marks when transposition stalled. Moreover, this explanation cannot

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<sup>12</sup> These two developments extended the *acquis communautaire* massively – currently accounting for 80.000 pages of rules and legislation – and making preparation for EU membership far more difficult for the CEECs.

<sup>13</sup> F. GRANELL, The European Union's Enlargement Negotiations with Austria, Finland, Norway and Sweden, in: *Journal of Common Market Studies*, 1995, 33(No. 1), pp. 117-41., pp. 117-118. For a more extensive overview of the increasing rule book of the EU see: G. MAJONE ed, *Deregulation or re-regulation?: regulatory reform in Europe and the United States*, London: Pinter; St. Martin's Press, 1990, G. MAJONE ed, *Regulating Europe*, London: New York: Routledge, 1996.

<sup>14</sup> P. NICOLAIDES, et al., *A guide to the enlargement of the European Union (II): a review of the process, negotiations, policy reforms and enforcement capacity*, Maastricht: Institut Europeen d'Administration Publique, 1999., pp. 37-45. There might be a possibility that the length of the TAs has gradually increased over the past enlargements; Richard Baldwin makes a comparison between the EFTA and Iberian enlargement, in: R.E. BALDWIN, *Towards an integrated Europe*, London: Centre for Economic Policy Research, 1994., pp. 197-200.

account for sectoral differences among the candidate countries, as well as the fact that regularly the EU did not accept TPRs while allowing for others.

The presence of TAs might be much more related to the scope of the fifth enlargement. The EU never carried out accession negotiations with more than four countries at once nor has it been endowed with the administrative capacity to manage the gargantuan task of handling simultaneous negotiation with 12 applicants<sup>15</sup>. As a result, the EU appeared to be forced by this state of affairs to adopt a fairly uncompromising stance on the interpretation of the *acquis*. Moreover, the lack of funding, ring fenced by Agenda 2000, even for the formally approved enlargement policy might have had a strengthening effect on the uncompromising stance of the EU in the negotiations<sup>16</sup>.

Finally, the institutionalist analysis is less illuminating as to the specifics of the TAs. The historical institutionalist approach falls short in clarifying what is more specific to the method of enlargement, the country, the EU, the sector or actors when addressing the different conditions under which candidate countries achieve EU membership. Hence, historical-institutionalists rarely insist that institutions are the only causal force in politics and seek to locate institutions in a causal chain that accommodates a role of other factors.

### **1.2.2. Adjusting to the EU: Who Was Ready?**

One explanation why sectoral conditions for joining the EU vary is that applicant countries were simply not ready to join the EU. Some candidates needed and obtained more TAs relative to others. Particularly the poorer ones would need more time to adjust as their economies were less robust. The burden of applying EU legislation falls on the national budgets and economies of the applicant countries. Wealthier countries would probably be able to bear more of the costs than the poorer ones. Hence one would expect wealthier countries to be both better prepared; and in need of fewer TAs. Evidence does not bear this out. The progress reports of the Commission evaluating the preparedness of the candidate countries almost consistently celebrated

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<sup>15</sup> V. BILCIK, EU enlargement after the Helsinki summit and Slovakia at the start of the negotiations, in: *Slovak Foreign Policy Affairs*, 2000, 1(1), pp. 57-71.

<sup>16</sup> L. CSABA, Ostpolitik and Enlargement of the EU: The Challenge of the Millennium, in: *CEU Working Papers IRES*, 2000, (2), pp. 37., pp. 24-25.

progress in Estonia and Slovenia – respectively one of the poorest and wealthiest countries amongst all the candidates by several measures – in its Progress Reports Towards Accession<sup>17</sup>. Table 1, table 2 and table 3 show that wealth (expressed in GDP per capita) is not a good indicator to explain the presence of TAs neither their intensity.

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<sup>17</sup> EC, *Regular Report from the European Commission on the Czech Republic's, Hungary's, Poland's and the Slovak Republic's Progress towards Accession*, Brussels, 1998-2002.

**Table 1: Total TAs per country and selected indicators**

country	total TAs (1)	total TAs weighed (2)	coverage ratio (3)	GDP (4)	population (5)	GDP /capita
Cyprus	27	250	0.12	9480.47	748800	12660.88
Czech R.	30	312	0.13	59137.83	10294373	5744.68
Estonia	26	178	0.11	5658.29	1449712	3903.04
Hungary	29	258	0.11	48883.15	10266570	4761.39
Latvia	33	212	0.26	7393.39	2448924	3019.04
Lithuania	29	181	0.08	11941.95	3702380	3225.48
Malta	49	330	0.46	3618.53	377516	9585.10
Poland	53	391	0.33	173887.16	38663481	4497.45
Slovakia	25	236	0.09	21573.56	5390516	4002.13
Slovenia	24	194	0.27	20365.76	1981629	10277.28
total/average	325	2542	0.20	36194.01	75323901	6167.65

Source: (1) and (2) Accession Treaties for all ten candidate countries: Total TAs are coded per country according to economic sectors affected and weighed by duration  
(2) Eurostat: own calculation of coverage ratio (here a figure between one and zero approximating the lowest proportion of the GDP affected by Total TAs). The country weight is based on the coverage ratio or the proportion of GDP exempted by a TA calculated as follows:  $(\sum_i l_i * GVA_i) / GDP = \text{national coverage ratio} [1,0]$ .  
(4) Eurostat: Average current annual GDP 1998-2002  
(5) World Bank indicators (2002)

**Table 2: Correlations TAs and GDP/capita**

		total TA	GDP current (mn. euro/capita)
total TA	Pearson Correlation	1	-.009
	Sig. (2-tailed)		.980
	N	10	10
GDP current (mn. euro/capita)	Pearson Correlation	-.009	1
	Sig. (2-tailed)	.980	
	N	10	10

Furthermore, when correlating wealth of the candidate countries expressed in GDP per capita (average euro current for the period 1998-2002) with the intensity of TAs (number of TAs weighted in terms of their length expressed in number of years) no significant correlation appears.

**Table 3: Correlations intensity of TAs and GDP/capita**

		total TA w	GDP current (mn. euro/capita)
total TA w	Pearson Correlation	1	.133
	Sig. (2-tailed)		.715
	N	10	10
GDP current (mn. euro/capita)	Pearson Correlation	.133	1
	Sig. (2-tailed)	.715	
	N	10	10

Both wealthier and poorer countries equally are endowed with TAs. Furthermore, when correlating the share of the economy that is affected at the lower end by the total number of TAs on economic strength only a weak correlation appears (table 4).

**Table 4: Correlations the TAs national coverage ratio and GDP**

		national coverage ratio	GDP current (mn. euro)
national coverage ratio	Pearson Correlation	1	.222
	Sig. (2-tailed)		.537
	N	10	10
GDP current (mn. euro)	Pearson Correlation	.222	1
	Sig. (2-tailed)	.537	
	N	10	10

Finally, when comparing the number of TAs with those of the previous enlargement (the enlargement towards Austria, Finland and Sweden) all countries that exceed the wealth of the candidates of the fifth wave at the moment of accession by a wide margin, the argument that more advanced economies would require less time and less TAs to adjust does not hold up<sup>18</sup>. The readiness argument neither provides for a necessary nor a sufficient explanation for the presence of TAs. Countries obtained TAs regardless of their relative economic wealth.

### 1.2.3. Closed Polities

Complementary to the historical-institutionalist and the readiness argument is the approach that concentrates on the state as the prime actor in the enlargement negotiations. State-centred approaches explain the presences of TAs and their

<sup>18</sup> P. NICOLAIDES, *et al.*, *A guide to the enlargement of the European Union (II): a review of the process, negotiations, policy reforms and enforcement capacity*, Maastricht: Institut Europeen d'Administration Publique, 1999., p 40-45.

variation on the basis of relative and absolute power of the negotiating states in the enlargement process<sup>19</sup>; the negotiation positions of the applicant states and the EU; and the strategic calculus of the bargaining process on a EU level. Two state-centred perspectives are discussed below: the (neo-)realist power-based and the (neo-)liberal interest-based approach. Both differ on several theoretical assumptions and expectations, but share some basic premises, such as the premise of rationality and utility maximisation of the state.

### **1.2.3.1. (Neo-) Realism**

Three basic elements characterise (neo-)realism in international relations theory<sup>20</sup>. Realists treat states as unitary actors and the most important unit of analysis of action; states seek power, either as an end in itself or as a means to other ends; and states behave in ways that are, by and large, rational, and therefore comprehensible to outsiders in rational terms<sup>21</sup>.

Within the realist tradition international relations are characterised as an anarchical society and a struggle for power because of the inherent logic of the competitive realm in world politics. A realist power-based approach assumes that relations among nation-states are therefore inherently competitive. States care deeply about the status of their power position relative to other states and approach international co-operation with concern for the impact on their relative power position. Subsequently, realists explain states' support for economic international agreements as a function of their efforts to enhance their relative economic positions vis-à-vis competitors: 'Realists and neo-realists view international politics as the arena where states attempt to organise ever-shifting balances of power'<sup>22</sup>.

Additionally, realists contend that states act rationally. They have consistent, ordered preferences, and they calculate the cost and benefits of all alternative policies in order to maximise their welfare in the light of their preferences and perceptions of reality. The balance of power between states and their rational calculation in the international

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<sup>19</sup> I define power as the ability to make people do what they would not otherwise have done, *ceteris paribus*.

<sup>20</sup> K.N. WALTZ, *Man, the state and war: a theoretical analysis*, New York: Columbia University Press, 1959, K.N. WALTZ, *Theory of international politics*, New York: Random House, 1979.; See also R.O. KEOHANE ed, *Neorealism and its critics*, New York: Columbia University Press, 1986a.

<sup>21</sup> R.O. KEOHANE, Realism, Neorealism and the Study of World Politics in: R. O. KEOHANE, *Neorealism and its critics*, New York: Columbia University Press, 1986b, pp. 1-26., pp. 6-7.

<sup>22</sup> H. BULL, *The anarchical society: a study of order in world politics*, Basingstoke; New York: Palgrave Macmillan, 2002., p. 102-107.

arena are the main explanatory variables for a specific outcome among all the possible outcomes of international negotiations.

The (neo) realist theory would have difficulties in explaining EU eastward enlargement. Eastern enlargement does not necessarily represent the strengthening of the power of the EU-15 member states individually or as group. It could be argued, albeit in a narrow sense, that instead of increasing the EU's common power, the economies of the CEECs will likely impose relative costs on the EU's resources for some time to come. All applicant states are relatively poor and will have access to the EU's common budget. Enlargement might also upset the balance of power within the EU as the individual voting power of the EU member states has been re-weighted. Moreover, the EU did not have to fear that the CEECs could come under control of its perceived competitors. It is rather unlikely that the region's economic dependence on the EU-15 could be replaced with that of distant economies: 'neo-realism cannot explain the EU's interest in eastward enlargement because it is neither necessary nor useful for balancing purposes'<sup>23</sup>.

Second, a realist theory would have difficulties to account for the existence of TAs on the CEECs behalf in the enlargement process. TAs do not serve the economic competitive position of the EU member states. Not applying the *acquis* would give the applicant states a competitive advantage in the enlarged EU.

Realists would also expect that the relative more powerful applicant states would be more capable of extracting TAs relative to their less powerful neighbours. It must be surprising for realist to find that Malta, an island in the Mediterranean with an economy at an annual GDP of € 3618 mn. and a population of about 377.516 obtained just four TAs less relative to Poland. The latter is by far the leading country amongst the candidate countries in terms of population (mn. 38,663) and economic power (€ mn. 173887,16). More often than not small as well as large states endowed with different intensity of economic powers appear to obtain TAs (see Figure 1). Structural power derived from the economic weight and population is neither a necessary nor a sufficient condition to explain the presence of TAs and their distribution among the

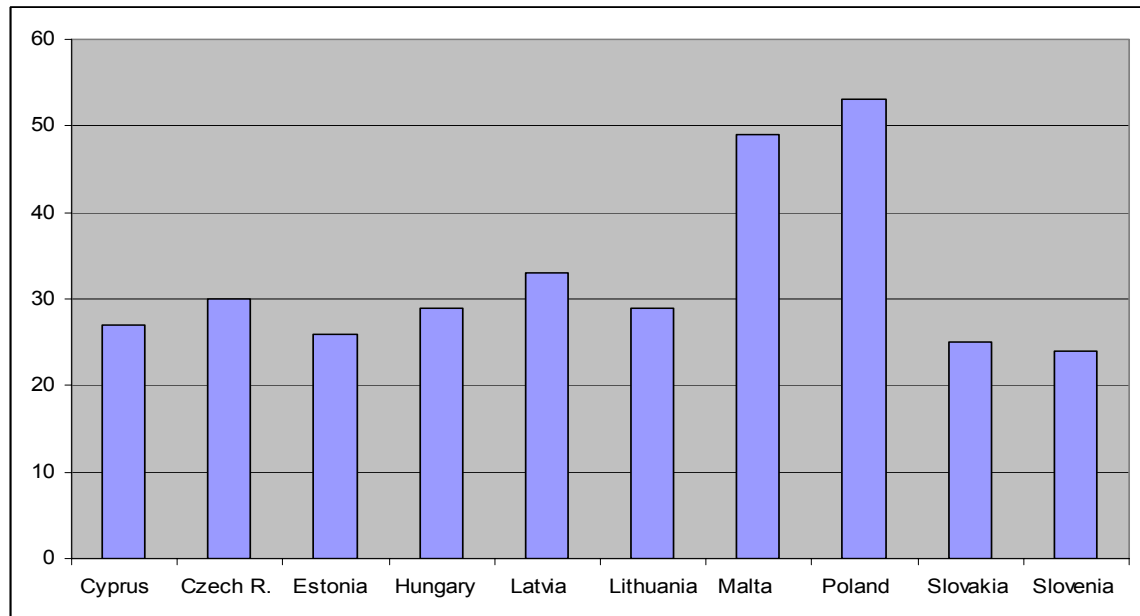
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<sup>23</sup> F. SCHIMMELFENNIG, The Community Trap: Liberal Norms, Rhetorical Action, and the Eastern Enlargement of the European Union, in: *International Organization*, 2001, 55(1), pp. 47-80.



applicant states. Consequently, a (neo-)realist approach appears not able to offer a satisfactory explanation.

**Figure 1: Number of TAs by country**



### **1.2.3.2. (Neo-) Liberalism**

A (neo-) liberal interest-based approach shares to a certain extent the realist focus on the state as a unitary actor. It does not refute the role of domestic politics. As (neo-) realism, it tries to understand what role states actually play. States represent the aggregated interests of the domestic arena and act strategically and instrumentally in the international arena to achieve their overall material self-interests. They are concerned mostly about maximizing their absolute (economic) interests under conditions of (economic) interdependence in a variety of issue areas<sup>24</sup>. In the international arena states make a strategic calculus about costs and benefits consistent with their preferences. The state's expectations about how others are likely to behave in international negotiations deeply affect this strategic calculus. States respond to each others decisions until each is in a position from which no improvement is possible, the *Pareto optimum*. As such, liberals characterise the international system by a complex of (economic) interdependence and seek to explore the role of strategic interaction of states in the determination of political outcomes<sup>25</sup>.

<sup>24</sup> R. GILPIN, *The political economy of international relations*, Princeton, N.J: Princeton University Press, 1987., pp. 26-31.

<sup>25</sup> R.O. KEOHANE and J.S. NYE, *Power and interdependence: world politics in transition*, Boston; Toronto: Little, Brown, 1977.

In the debate on EU integration, *Alan Milward* and *Andrew Moravcsik* have presented the liberal state centred approach<sup>26</sup>. From an historical perspective, the former argues that EU integration has been the result of the purposes and national will of the nation-states. Likewise, Moravcsik argues that the EU can be understood by analyzing state behaviour, their preferences, the power of its individual members and their economic interdependence. Therefore, ‘the first stage in explaining the outcome of international negotiations is to account for national preferences’<sup>27</sup>. It predicts outcomes of intergovernmental negotiations through the strategic interaction of the member states. This strategic interaction is in turn shaped by national interests influenced by economic interdependence, the relative bargaining power and the intensity of preferences in interstate negotiations. The main explanatory variables of the sectoral TAs and their variations across the candidate countries are states, their negotiating position and the strategic calculus of the bargaining process on an EU level.

In the enlargement literature, the writings of *Alan Mayhew* and *Graham Avery* take a similar viewpoint<sup>28</sup>. Their analysis is essentially state-centred, intergovernmentalist, and liberal while taking in account the traditional method of EU enlargement. They clarify the nature of the EU enlargement process by focusing on the bilateral negotiations between the EU-15 and the individual applicant countries. They take into account the positions of the negotiating states, the national preferences, the strategic calculus, and their relative bargaining power. They equally consider the institutional and procedural structures and the explicit and implicit constraints on the negotiations<sup>29</sup>.

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<sup>26</sup>A.S. MILWARD, *The European rescue of the nation-state*, London; New York: Routledge, 2000.; A. MORAVCSIK and M.A. VACHUDOVA, National Interests, State Power, and EU Enlargement, in: *East European Politics and Societies*, 2003, 17(1), pp. 42-57, A. MORAVCSIK, Preferences and Power in the European Community: A liberal intergovernmentalist Approach, in: *Journal of Common Market Studies*, December 1993, Vol. 31 (4), pp. 476

<sup>27</sup>A. MORAVCSIK, *The choice for Europe: social purpose and state power from Messina to Maastricht*, Ithaca, N.Y: Cornell University Press, 1998., p. 24.

<sup>28</sup> Both authors might find the label of a neo-liberal interest based approach for their writings out of place.

<sup>29</sup> Most analysis of the association policy of the EU, which preceded the enlargement policy and lead to the association agreements with CEECs, are also based on state centered assumptions and use implicitly a liberal intergovernmentalist approach. See S. HAGGARD and A. MORAVCSIK, The Political Economy of financial assistance to Eastern Europe 1989-1991, in: R. O. KEOHANE, N. J.S. and S. HOFFMANN, *After the Cold War: Institutions and State strategies in Europe, 1989-1991*, Cambridge: Harvard University Press, 1993, pp. 246-85.; S. HAGGARD, Integrating the Two Halves of Europe: Theories of Interest, Bargaining and Institutions, in: R. O. KEOHANE, J. S. NYE and S. HOFFMANN, *After the Cold War: Institutions and State strategies in Europe, 1989-1991*, Cambridge: Harvard University Press, 1993, pp. 173-95.

A state-centred approach goes a long way in explaining how divergence from the *acquis* takes place. The main explanatory variables for the sectoral TAs and their variations across the candidate countries are states, their negotiating position and the strategic calculus of the bargaining process on an EU level, embedded in the classical method of EU expansion<sup>30</sup>.

Theoretically, a neo-liberal state-centred perspective is attractive for its parsimony and straightforward analysis. However, it falls short to explain the sectoral conditions under which the EU enlarges on three accounts. First, it remains unclear whether a national negotiation positions reflect solely the states' preferences and how these preferences come about. The emphasis on states as unitary actors makes it difficult to spell out why individual states' preferences diverge across issue areas; and why they have different preferences amongst all possible outcomes. States as unitary actors conceal the reality that they might prefer individually different positions across issue areas that are not necessarily consistent with their overall position. Second, it is not necessary so that states' preferences, seen as an aggregate of multiple interests, at the negotiating table are in fact real. Preferences could be *cheap talk* and part of the strategic bargaining rather than any *revealed preferences*<sup>31</sup>.

Third, national preferences might be in conflict with other actors' preferences such as interest groups operating both nationally and internationally. On a sectoral level, for instance, sectoral interests might not coincide with national ones. Sectoral interests may be well transnational and articulated in EU institutions; different EU member states; the candidate countries; or a combination of all these levels. Interests do not necessarily come about within the vacuum of the national boundaries. In sum, taking national preferences for certain neglects preference formation and draws attention away from areas that may contain more explanatory power, in which the present research is interested.

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<sup>30</sup> A. MAYHEW, *Recreating Europe: the European Union's policy towards Central and Eastern Europe*, Cambridge; New York: Cambridge University Press, 1998., p. 16; p. 19.; see also D. TOSI, Les négociations sur l'élargissement de l'Union Européenne: développements, problèmes, scénarios de perspectives, in: *Est-Ovest*, 1999, 3, pp. 209-37.. Dario Tosi's perspective on the negotiations focuses on the decisions of the EU-15 that lead to the accession negotiations. He focuses on the Copenhagen Council (June, 1993), the Essen Council (December, 1994), and the Madrid Council (December, 1995).

<sup>31</sup> Cheap talk is a term used in game theory. It is a form of credible speech that is neither costly nor binding. It is pay-off irrelevant and has no credibility cost. The players in the game may or may not tell the truth, may or may not believe each other. Revealed preferences are preferences of rational people that are revealed by the choices they make.

The account that the sectoral conditions under which the EU enlarges is due to the preferences of the EU member states and the candidate countries that filter through the classical enlargement method is valuable. Nevertheless, it fails to account for the sectoral interests, or the micro foundations of state preferences, that are not necessarily constraint by national boundaries, and might well be the underlying motive of national preferences. Consequently, it is prudent to look at theories that elicit the state and regard national strategic decision-making as aggregates of sub-state preferences. Hence, I will turn to a political-economic approach of the EU enlargement process and the effect it has on economic actors, such as firms represented by the factors labour and capital; and whether and how institutions aggregate their preferences in the public arena.

### **1.3. Interest Groups, Constructive and Destructive Interference**

Central in the political economic perspective are interests of individuals aggregated in groups. These interests are assumed to be rational and self-interested. They rationally calculate their policy preference as a function of their goal of maximizing their incomes given their position in the economy. Generally, political economy starts its analysis by defining interests, specifying their objectives, and identifying their preferences in respect to a given trade policy. It does this by providing a general theory. Political economy tries to answer the central research questions in two steps. It identifies whose material interests are affected by the presence of sectoral TAs; and it derives their policy preferences in respect to TAs. Traditional political economy generally pays little attention to collective action problems of interest groups and the ensuing acquisition of political influence.

Modern political economy takes the analysis one step further<sup>32</sup>. On the basis of factor and assets specificity it formulates a theory that also allows for the prediction of the likelihood of political mobilisation and the likelihood of its success. States (governments) and international organisations (negotiations) and the strategies of actors occupying these institutions are endogenous to its analysis. International outcomes are assumed to be an automatic reflection of sectoral preference formation and political mobilisation.

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<sup>32</sup> J.A. FRIEDEN, *Debt, development and democracy: modern political economy and Latin America, 1965-1985*, Princeton, New Jersey: Princeton University Press, 1991., pp. 15-16.

The theoretical framework the present research adheres to considers states and international organisations as exogenous to sectoral interests. While sectoral interests are assumed to be necessary conditions – the demand side for TAs – states and international organisations are assumed to mediate sectoral interests along what I call *the logic of destructive and constructive interference*<sup>33</sup>. States and international organisations act as constraints upon sectoral preferences at the negotiating table when their interests are not aligned, i.e. destructive interference. Conversely, when societal interests and institutional preferences are aligned states and strategies sustain or amplify sectoral preferences at the negotiating table, i.e. constructive interference – the supply side of TAs. In other words, supply for TAs comprises the sufficient condition for the presence of TAs.

### **1.3.1. Defining Interests and Deriving Preferences**

Classic political economic theories use a set of restrictive micro foundations that specify some characteristics of interest groups in society and their preferences<sup>34</sup>. The basic starting point is that actors are rational and self-interested, i.e. they attempt to maximise their utility given the circumstances and the means at their disposal. Actors are largely distinct in terms of relationships to the means of production (labour and capital); relationships to the economic sector in which they are employed according to the level of international competition they face (tradables and non-tradables); relationships to the mobility of their assets in the economy (fixed and mobile assets); relationships to their capital and labour ratios associated with production (capital or labour intensive); and the relationships to the main site of their markets (domestic and foreign). Largely different classes of models follow the above-described distinctions and generate predictions about preferences of different interest groups on trade policy. Each predicts different welfare and preferences of interest groups concerning TAs.

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<sup>33</sup> Interference is the phenomenon in physics which occurs when two sound waves meet while travelling along a similar medium. The interference of waves causes the medium to take on a shape which results from the net effect of the two individual waves upon the particles of the medium. Constructive interference occurs where two interfering waves have a displacement in the same direction. In contrast, destructive interference is where the two interfering waves have a displacement in the opposite direction. The two interfering waves do not need to have equal amplitudes in the same or opposite directions for constructive/destructive interference to occur.

<sup>34</sup> See A.L. HILLMAN, *The political Economy of Protection* London, 1989.; S.P. MAGEE, W.A. BROCK and L. YOUNG, *Black hole tariffs and endogenous policy theory, Political economy in general equilibrium* Cambridge, 1989 , D.M. SHAFER, *Winners and losers: How sectors shape the developmental prospects of states* New York, 1994.

Traditionally, political economists are inclined to emphasise the classic *Heckscher-Ohlin* model (H.O.), its *Stolpher-Samuelson* variant of international trade, the *Ricardo-Viner* (R.V.) and the more recent *Increasing Returns to Scale* model (IRS)<sup>35</sup>. The first two models (H.O and R.V.) are endowment-based models of trade patterns and are polar opposites on the continuum of factor specificity. Factor specificity is a central determinant for the composition of interest groups and trade policy coalitions. It indicates the ease with which factors, i.e. labour and capital, can move between sectors in the economy<sup>36</sup>.

More accurately, endowment based models predict the ‘costliness’ with which factors move from their current use to an alternative one when affected by a changing trade policy. The H.O. model assumes no factor specificity and expects theoretically and empirically that interest groups form coalitions along the lines of factor or class<sup>37</sup>. The R.V. model assumes that some factors are highly specific and predicts-industry or sector based cleavages on trade policy<sup>38</sup>. The fortunes of the specific factor in an industry then rise and fall together whether they are the same type of factor or not. Hence, interest group coalitions tend to form along the lines of exporting versus import-competing industries. Sectors and preference formation is hypothesised theoretically according to sectoral positions<sup>39</sup>.

The H.O. and R.V. models are not sufficient to account for the increasing importance of the vast majority of trade, i.e. *intra*-industry trade between regions of similar factor endowments as opposed to inter-industry trade taken as the basis of the H.O. and R.V.

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<sup>35</sup> R. ROGOWSKI, *Commerce and coalitions: how trade affects domestic political alignments*, Princeton, N.J: Princeton University Press, 1989.; W. STOLPER and P. SAMUELSON, Protection and Real Wages, in: *Review of Economic Studies*, 1941, 9, pp. 58-73. For a broad overview of these models see International trade theory in: P.R. KRUGMAN and M. OBSTFELD, *International Economics, Theory and Policy*, New York, 1997., , pp. 14-180.

<sup>36</sup> Given the economic reform process in the candidate countries factor specificity is a highly important concept coinciding with the productivity crunch immediately after the economic transition took off in the early 1990s, in: P. BOONE, S. GOMULKA and P.R.G. LAYARD eds, *Emerging from communism: lessons from Russia, China and Eastern Europe*, Cambridge, Mass.: MIT Press, 1998.; EBRD, *Transition Report*, London, 2001

<sup>37</sup> R. ROGOWSKI, *Commerce and coalitions: how trade affects domestic political alignments*, Princeton, N.J: Princeton University Press, 1989. Rogowski applies the variant of the H.O. model, the Samuelson-Stolper model of comparative advantage.

<sup>38</sup> P. SWENSON, *Fair Shares: Unions, Pay and Politics in Sweden and West Germany*, London, 1989.

<sup>39</sup> P.A. GOUREVITCH, International Trade, Domestic Coalitions, and Liberty: Comparative Responses to the Crisis of 1873-1896, in: *Journal of Interdisciplinary History*, 1977, 8(2), pp. 281-313. P.A. GOUREVITCH, *Politics in hard times: comparative responses to international economic crises*, Ithaca: Cornell University Press, 1986., J.R. KURTH, The Political Consequences of the Product Cycle: Industrial History and Political Outcomes, in: *International Organization*, 1979, 33(1), pp. 1-34.; T. FERGUSON, From Normalcy to New Deal: Industrial Structure, Party Competition, and American Public Policy in the Great Depression, in: *International Organization*, 1984, 38(1), pp. 41-94.

models<sup>40</sup>. It predicts theoretically that EU enlargement will not be as contentious as an issue as the endowments-based models predict it will be. The IRS model shows how both labour and owners can be threatened by a ‘tipping’ of regional advantage that moves a whole sector from one location to another under a changing trade policy. As a result, it is reasonable for sectors to have clear preferences and act as sectors.

Most scholars of trade theory would deny that either the H.O., R.V. or IRS model are panacea for deriving preferences. They constitute different set of spectacles through which preferences of interests are inferred. The character and composition of interest constellations will depend on the model. Each appears to explain some things the others do not, and the phenomena each emphasises are likely to be at work to some degree. For those that emphasise the politics of international political economy, the R.V. or sector specific model has generally been regarded as a *short-run* version of the long-run H.O. model. In the long run there are no factors that are specific to anything, whereas in the short run very few factors are without costs. This implies that the analysis using the H.O. assumptions are correct when analysis runs over a long time span<sup>41</sup>. Equally, positions in the short run probably are better predicted by the sector-specific or R.V. model. The time horizon may well be the key determinant of the appropriateness of the two models<sup>42</sup>.

The enlargement literature that takes a political economy approach explains the sectoral agreements and their variation under which the EU enlarges by means of a balance of interests groups in the EU as well as the applicant states. Material interests and preference formation within states and the EU are central to their analysis<sup>43</sup>. These interests affect the preferences of the member states, aggregated in the Council of the EU, and the applicant countries as well as other European institutions such as the EC. The actors include labour unions and employers. Different models, implicit and

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<sup>40</sup> P.R. KRUGMAN and M. OBSTFELD, *International Economics, Theory and Policy*, New York, 1997. Intra-industry trade is two-way exchanges of goods within standard industrial classifications.

<sup>41</sup> R. ROGOWSKI, *Commerce and coalitions: how trade affects domestic political alignments*, Princeton, N.J: Princeton University Press, 1989.

<sup>42</sup> This is, however, not an uncontroversial view. If economic agents can secure protection for a declining industry from the government, then they would have no reason to move to another industry.

<sup>43</sup> F. LAURSEN ed, *The political economy of European integration*, The Hague: Kluwer Law International, 1995. M. MARESCAU and E. LANNON eds, *The EU's enlargement and Mediterranean strategies: a comparative analysis*, Basingstoke; New York: Palgrave Macmillan, 2001.; H. TANG ed, *Winners and losers of EU integration: policy issues for Central and Eastern Europe*, Washington, D.C.: World Bank, 2000.; A. MAYHEW, *Recreating Europe: the European Union's policy towards Central and Eastern Europe*, Cambridge; New York: Cambridge University Press, 1998.

explicit, follow H.O., R.V., IRS. The approach has dominated the analysis of the Association Agreements (AAs) between the EU and the candidate countries, and that of the emerging and increasingly interdependent trade patterns between the EU and the CEECs. It is valuable to identify the groups that are likely to lose out or profit from the EU enlargement process within a margin of error.

According to the political economic perspective, TAs would be explained by interest groups and how their material interests are affected by EU enlargement. The nature of the interests groups, and more precisely firms, characterised by capital and labour, are affected differently by TAs depending on their position within the economy. Factor specificity of these interest groups suggests the likelihood of political mobilisation in favour or against TAs; and would account for the different preferences of the candidate countries and the EU member states in the negotiation position papers and the bargaining process. Compared to institution and state centred approaches an interest group approach has the advantage that it sheds light on specifics of TAs. It adds useful insights by indicating how and why preference of both member states and candidate countries come about. It opens the state as an actor and shifts the focus of attention to the role of multiple interest groups and their impact on the form and content of EU membership agreements, particularly on a sectoral level.

### **1.3.2. Limitations: Political Action and Accommodation of Preferences**

The political economic analysis is limited for the present research question in at least three ways. First, the theoretical choices (H.O., R.V., IRS) to infer preference formation restrict the researcher's conclusions. The results of the analysis are sensitive to the economic theories used to specify the material interests of the relevant actors. The choice of the theory also appears to depend on the time horizon.

Second, despite the centrality of coalitions and preference formation to the political economic perspective, it pays little attention to the likelihood of political mobilisation and success of interest groups. The collective action problems associated with coalition formation and the ensuing acquisition of political influence in the policy process are either overlooked or regarded as endogenous<sup>44</sup>.

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<sup>44</sup> 'Every lobby obtaining a general change in legislation or regulation thereby obtains a public or collective good for everyone who benefits from that change. Some might benefit from these collective goods, but free ride and not



The models provide the tools to identify and infer specific preferences of interest groups in the enlargement process, however, they do not appreciate how these preferences are articulated and find expression in the political arena. The political mobilisation and accommodation of interest groups is not automatic. Simply having a particular set of preferences will not motivate to take political action and imply the accommodation of those preferences in the enlargement process<sup>45</sup>. In many respects, it raises the question how one should understand the way in which interest groups decide that they should influence the enlargement policy and how they go about it?

A third limitation is related to the mediating role of national and international public institutions between sectoral interests and international outcomes. As chapter 3, 4 and 5 show the relationship between political mobilisation and accommodation of preferences on a national or international level is not automatic. Political mobilisation does not necessarily imply accommodation of those preferences in the enlargement process. It raises the question how one should understand the interactive effects between sectoral preferences and their political mobilisation (demand side for TAs); and national and EU institutions in the enlargement process (supply side for TAs).

### **1.3.3. The Theoretical Framework: Sectors, States and Strategies**

This study opts on the demand side for a combination of so called ‘modern political economy’ developed by *Alt, Frieden, Gilligan, Rodrik, and Rogowski*; and the insights of *Olson* about interest group behaviour. On the supply side of the argument I analyse the mediating role of states (governments) using *Tsebelis’* theory of veto players combined with insights from *Milner* and *Lange*. The argument is complemented by the use of a two level game and *Schelling’s* paradox of weakness to analyse the accession negotiations.

Crucial in the theoretical framework is the relationship between the supply and demand side of TAs. I assume the relationship to be one of *destructive and constructive interference*. States and international organisations act as constraints

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carry the costs of obtaining them’, in: M. OLSON, *The logic of collective action : public goods and the theory of groups*, Cambridge, Mass; London: Harvard University Press, 1971.

<sup>45</sup> J.E. ALT and M. GILLIGAN, The Political Economy of Trading States: Factor Specificity, Collective Action Problems, and Domestic Political Institutions, in: *Journal of Political Philosophy*, 1994, 2(2), pp. 165-92.

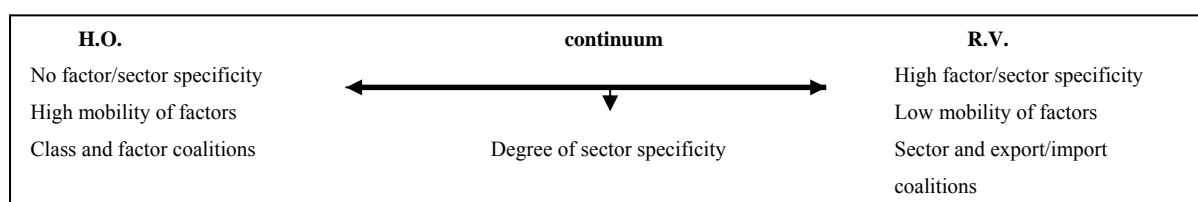
upon sectoral preferences and their political mobilisation at the negotiating table when their interests are not aligned, i.e. destructive interference. Conversely, when societal interests and institutional preferences are aligned states and strategies sustain or amplify sectoral preferences at the negotiating table, i.e. constructive interference – the supply side of TAs.

### 1.3.3.1. Sectors

#### Degree of Specificity

*Alt et al.* address the limitations of choosing between different political economic theories by combining their assumptions. They propose a model that balances between H.O. and R.V. that aims to treat factor specificity as a matter of degree. They take a continuum that ranges from no cost of factor mobility to prohibitive cost of factor mobility with high gradations between them. Once the extreme assumptions of both the H.O. and R.V. are lessened, their predictions about coalition formation, although probably superior empirically, no longer are as clear-cut (fig. 1)<sup>46</sup>.

**Figure 2: H.O. and R.V. at the extremes of factor and sector specificity**



The interpretation of degrees of specificity among factors allows for the combination class-based coalitions (H.O.) as well as cross-class coalitions (R.V.). Labour and capital in an industry or sector can be conceptualised according to their degree of specificity along sectoral lines (henceforth sector specificity). Taking a degree of factor specificity would predict empirically that owners of an abundant general factor would be more susceptible to having strong policy preferences the more specific their present investments or skills happen to be. They are likely to suffer more from changing economic conditions, such as trade liberalisation, than those that are less sector specific.

### Political Mobilisation

<sup>46</sup> J.E. ALT, *et al.*, The political Economy of International Trade, Enduring Puzzles and an agenda for Inquiry, in: *Comparative Political Studies*, December 1996, Vol. 29(6), pp. pp. 689-717., pp. 697-698; J.A. FRIEDEN, *Debt, development and democracy: modern political economy and Latin America, 1965-1985*, Princeton, New Jersey: Princeton University Press, 1991.

Subsequently, theory addresses the issue of the likelihood of political mobilisation. Political action involves a cost and benefit calculation. The preferences derived from the degree of factor specificity can be thought of as the ‘benefits’ side, i.e. the goods that individuals hope to receive or the ills they hope to avoid from trade policy by taking political action. However, interest groups also take in account the ‘costs’ side of political action<sup>47</sup>. The greater potential loss facing the owner of a specific factor on the cost side, accrued to the trade policy (EU enlargement policy and TAs) rationalises greater expenditure of resources on activities that offer the prospect of averting the loss or reaping the gain. The crucial determinant of incentives for an interest group to influence decisions pertaining to his or her economic activity is then the degree to which the agent’s factors are specific to his activity. At the limit, if the factor is completely mobile from use to use, then there is less incentive to spend resources to lobby for TAs, whereas if the factor is completely specific to its current use, then the owner has a strong incentive to engage in political action.

### **Organisational Strength**

Interest groups must also have the ability to organise in order to exert effective political pressure and increase the likelihood of their success. Success translates in the accommodation of preferences of interest groups that are politically active. The returns on political lobbying are increasing with the specificity of the factor. As a result, one would expect the more factors are specific to an industry, and the less mobile they are, the more likely they hold political and economic assets, *i.e. institutionalised political aggregations*, specific to their current use. Two complementary theories are used to predict the organisational strength of interest groups. Modern political economy argues that factor specific industries tend to hold stronger institutional political organisations than industries with highly mobile or diversified interests. The literature on the logic of collective action argues that interest groups that have fewer collective action problems and can overcome the free rider problem are likely to be more successful.

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<sup>47</sup> J.E. ALT, *et al.*, The political Economy of International Trade, Enduring Puzzles and an agenda for Inquiry, in: *Comparative Political Studies*, December 1996, Vol. 29(6), pp. 689-717., pp. 700-702; J.E. ALT, *et al.*, Asset Specificity and the Political Behaviour of Firms: Lobbying for Subsidies in Norway, in: *International Organization*, 1999, 53(1), pp. 99-116. pp. 103-104; J.E. ALT and M. GILLIGAN, The Political Economy of Trading States: Factor Specificity, Collective Action Problems, and Domestic Political Institutions, in: *Journal of Political Philosophy*, 1994, 2(2), pp. 165-92.; M.J. GILLIGAN, Lobbying as a Private Good with Intra-Industry Trade, in: *International Studies Quarterly*, 1997, 41(3), pp. 455-74., p. 457.

Modern political economy argues that factor specific industries tend to be better organised than industries with highly mobile or diversified interests. The latter are rather unlikely to enter in long term organisations; the former are more likely to do so. Perfectly mobile asset holders have incentives to lobby generally for protection for all industries that use them intensively, specific asset holders' real incomes will vary much more with the fortunes of the particular industry to which they are specific. Therefore, specific asset holders generally have more incentives to lobby than do owners of mobile factors<sup>48</sup>.

For instance, unskilled labour that can move readily from job to job will be less likely to act together politically than skilled workers tied to their particular industry. Equally, industries producing a wide range of goods – that is, those whose physical and human capital are suited to many industrial uses – will be less likely to organize than those in highly specialized industries. However, if a particular group has long since paid up fixed costs of creating political organisations and if it has well-worn channels of access to policy makers, then it may defend its trade-related interests even when little is at stake because the marginal costs are low. *Rogowski* observes in a more historical context that workers and managers develop ever more specialized skills, their political aggregations should become ever more specific to particular industries and activities<sup>49</sup>. The theory therefore expect that those with more specific assets to be both better organised and more likely to engage in political activity than those with less specific assets<sup>50</sup>.

Better organisation generally refers to the capacity of an interest group to overcome the contradictions of collective actions problems, particularly the free-rider problem<sup>51</sup>. Actors might enjoy the benefits of a group without incurring the costs of joining it. Some groups are able to overcome this problem. Generally, several factors affect interest groups' ability to organise for the provision of collective goods. These are the size of the group, the ability to provide selective benefits to its members, the provision

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<sup>48</sup> J.E. ALT, *et al.*, The political Economy of International Trade, Enduring Puzzles and an agenda for Inquiry, in: *Comparative Political Studies*, December 1996, Vol. 29(6), pp. pp. 689-717., pp 700-702.

<sup>49</sup> R. ROGOWSKI, *Commerce and coalitions: how trade affects domestic political alignments*, Princeton, N.J: Princeton University Press, 1989.

<sup>50</sup> J.E. ALT and M. GILLIGAN, The Political Economy of Trading States: Factor Specificity, Collective Action Problems, and Domestic Political Institutions, in: *Journal of Political Philosophy*, 1994, 2(2), pp. 165-92.

<sup>51</sup> M. OLSON, *The logic of collective action : public goods and the theory of groups*, Cambridge, Mass; London: Harvard University Press, 1971.

of information and effective enforcement mechanisms. The strength of an interest group largely depends on the concentration of the industry or sector and the entry and exit barriers. The theory assumes that the more concentrated the industry, the easier it would be to exert political pressure. The greater the entry barriers, the more easily the industry will be able to avoid free riding by new entrants.

The writings on lobbying comes to similar conclusions. It argues that accommodation of economic interest in the EU policy process is contingent upon their capacity to successfully influence political decisions. This in turn depends on the organisational characteristics of the interest group. The character of an interest group is embodied in its operational resources such as economic muscle, sources of information, expertise to outside policy-makers, and its function as a signpost within its specific operational environment for implementing regulations<sup>52</sup>. The latter is referred to as insider status of the interest group. Insider status, defined as the governing mechanism for the domain in which sectoral interests are involved, renders sectoral interests indispensable to policy-makers. It implies that interests groups can perform services to policymakers or the broader public interests and equally promote their own interests. The services interest groups can perform relate to the bargaining chips they hold.

### **1.3.3.2. States**

The capacity of producer group interest to influence the policy process depends additionally on the institutional configuration that either facilitates or impedes their progress vis-à-vis the policy-making apparatus<sup>53</sup>.

### **Veto Players and Delegation**

This study departs from the assumption that states are unitary actors. Crucial to our argument is the opposite supposition that domestic elements, i.e. sectors and domestic politics in the applicant states, bear heavily on the prospects of countries joining the EU, the related TPRs and the ensuing TAs. The state is an open polity composed of central decision makers, legislatures, and domestic groups. These actors have varying

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<sup>52</sup> Eight characteristics define operational resources, in: J. GREENWOOD, *Representing interests in the European Union*, Basingstoke: Macmillan, 1997., p. 18-20.

<sup>53</sup> J. GREENWOOD, *Representing interests in the European Union*, in: J. GREENWOOD, J. R. GROTE and K. RONIT, *Organized interests and the European community*, London: SAGE Macmillan, 1992, pp. 1-26; S. MAZEY and J. RICHARDSON, *Interest groups and EU policy making, Organizational logic and venue shopping*, in: J. RICHARDSON, *European Union, Power and Policy-making*, London, 2001, pp. pp 217-37.

preferences and share formal decision-making authority according to their national constitutions. Formal political institutions distribute power among these actors in the policy making process and contribute to policy formation.

Differences among states in the selection of political institutions and the preferences of the actors that inhabit these institutions are assumed to have important effects on domestic and international politics. According to *Tsebelis'* theory on political institutions the distribution of decision-making power among these actors and the extent to which their preferences diverge defines the number of veto players in a country and the likelihood of policy change. Institutional receptiveness to a change in societal preferences and political pressure is inversely related to the formal number of veto players in the political system that is the number of institutional actors whose assent is required for a change in policy<sup>54</sup>. *Milner* applies this argument at an international level. She argues that 'differences among states in their internal preferences and political institutions have important effects on international politics'<sup>55</sup>.

Policy outcomes do not only vary depending on the identification and number of institutional veto players but also on partisan veto players and their preferences relative to the status quo. Therefore, I need assumptions to derive the preferences of these actors. Governments negotiate foreign treaties, not states. The state's interest, such as joining the EU, enters into a government's preference function, however, governments are expected to act above all to their direct political benefit and to factor in national interests in that context.

Nevertheless, should states delegate and insulate decision-making authority from societal pressures the number of veto players and their preferences might well be irrelevant or their influence decline. Governments have the power to delegate authority to bureaucracies or independent agencies to negotiate treaties with foreign powers. These bureaucracies might not share preferences of elected politicians or societal actors. As administrative bodies gain more autonomy it is likely that

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<sup>54</sup> G. TSEBELIS, *Veto players: how political institutions work*, Princeton: Princeton University Press, 2002.

<sup>55</sup> H.V. MILNER, *Interests, institutions, and information: domestic politics and international relations*, Princeton, N.J.: Princeton University Press, 1997., p. 10.; see also E.D. MANSFIELD, H.V. MILNER and J.C. PEVEHOUSE, *Vetoing Co-operation: The impact of Veto Players on International Trade Agreements*, s.l., 26 January 2005, 46., p. 3.

governments' or principals' preferences are less reflected in effective policy. The accommodation of sectoral preferences assumed to be additionally related to government's delegation of authority.

### **1.3.3.3. Strategies**

While domestic institutions are assumed to play an important role one cannot neglect the role of international institutions such as international organisations (negotiations) and actors' preferences and strategies in these institutions. I use the two-level game metaphor to analyse the interaction effects between the national and EU institutions.

### **International Organisations and Negotiations**

According to *Putnam*, 'the politics of many international negotiations can be usefully conceived as a two-level game. At a national level, interest groups pursue their interests by pressuring the government to adopt favourable politics. At an international level, governments seek to maximize their own ability to satisfy domestic pressures, while minimizing the adverse consequences of foreign developments. Neither of the two games can be ignored by central decision-makers, so long as their countries remain interdependent, yet sovereign'<sup>56</sup>.

Arguably Putnam's two-level game is a more general version of *Thomas Schelling's* thinking in the 1960s about interactive effects between domestic politics and international negotiations. For Schelling a possible mechanism for a two-level game is the paradox of weakness. The Schelling paradox rest on the assumption that weakness at the negotiating table, i.e. the 'power to bind one self' through for example a highly visible and inflexible negotiating mandate relative to the opposite party, may confer strength in negotiations on the basis of an inability to make concessions and meet demands of the opposite party<sup>57</sup>. In the words of *Putnam*, 'a small domestic win-set can be a bargaining advantage' because 'the larger perceived win-set of a negotiator, the more he can be pushed around' by other negotiators on a different level<sup>58</sup>. In short, a negotiator can obtain the best possible deal in negotiations, i.e. to obtain the most

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<sup>56</sup> R.D. PUTNAM, *Diplomacy and Domestic Politics: The Logic of Two-Level Games*, in: *International Organization*, 1988, 42(3), pp. 427-60., p. 434.

<sup>57</sup> T.C. SCHELLING, *The Strategy of Conflict*, Cambridge, Massachusetts: Harvard University Press, 1960., p. 19; See also H.V. MILNER and B.P. ROSENDORFF, *Democratic Politics and International Trade Negotiations: Elections and Divided Government as Constraints on Trade Liberalization*, in: *Journal of Conflict Resolution*, 1997, 41(1), pp. 117-46..

<sup>58</sup> A win set is defined as a set o potential agreements that would be ratified by domestic constituencies, in: R.D. PUTNAM, *Diplomacy and Domestic Politics: The Logic of Two-Level Games*, in: *International Organization*, 1988, 42(3), pp. 427-60., p. 440.

from its opponent while conceding the least, when she is most constraint among the negotiating parties by domestic ratification<sup>59</sup>.

Studies of two-level games have attempted to confirm Schelling's intuition. One needs to specify clearly under which conditions the Schelling conjecture can be confirmed.

## **1.4. Application of the Theory**

The first part of this section deals with the introduction of the theory in the context of the EU enlargement process. To enhance the model's predictions for the accession negotiations the design takes into account institutions, i.e. states (governments) and strategies (negotiations), as intervening variables for sectoral preferences and their ensuing mobilisation.

### **1.4.1. Independent and Dependent Variables**

This study focuses on the presence and variation of sectoral conditions under which the candidate countries join the EU. These conditions differ from the *acquis communautaire* for certain sectors, while not in others; within and between candidate countries. The first research question is therefore: Why and how do sectoral conditions for joining the EU vary for the individual applicant states?

The endeavour is to partially contest the conventional explanation for TAs by other actor based approaches that focus either on the EU institutions or on the participating states in the negotiations. Accounts that solely refer to the EU traditional manner of expansion and the strategic calculus of the negotiating parties are inconclusive.

Our main argument is that interest groups and more precisely firms, i.e. capital and labour, affected by EU enlargement, will have preferences about the presence of TAs. They are likely to assert their interest in the accession negotiations when particular terms of EU membership are debated. States and strategies mediate these interests at the negotiating table according to the logic of constructive and destructive Interference.

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<sup>59</sup> Putnam uses the term 'ratification' generically for "any decision-process at Level II that is required to endorse or implement a Level I agreement, whether formally or informally. It is sometimes convenient to think of ratification as a parliamentary function, but that is not essential. The actors at Level II may represent bureaucratic agencies, interest groups, social classes, or even 'public opinion', in: *Ibid.*, p. 436.



The research contends that the presence of *the dependent variable*, the sectoral conditions under which the EU enlarges (TAs) is due to sectoral interests' ability to influence the enlargement policy. Sectoral interests are defined as firms composed of labour and capital organised in associations and federations. While the ability of sectoral interests to influence these sectoral conditions would constitute our main *independent variable*, it is assumed that the dependent variable is not only determined by preferences of sectoral interests, but respectively mediated by two *intervening variables*, i.e. states and strategies – regarded as distinct of the underlying sectoral interests.

I define states in an open polity model. Of all the political actors that fill a state's political system I focus on two important categories, i.e. the executive and the legislature. The government and the administration make up the executive with the administration comprising the various working groups, committees, departments and ministries dealing with EU accession. The legislature encompasses parliament comprising political parties which, depending on the issue, oppose or support the executive's policy on EU accession. State level outcomes in an open polity model are the result of prevailing national institutions ingrained in a body of law or constitution and the manner in which they distribute power among political institutions and the amalgam of the actor's preferences that inhabit those institutions<sup>60</sup>.

In studying strategies the research design makes a distinction between actors and their institutional environments<sup>61</sup>. For instance, the strategies in the EU accession negotiations can be regarded as the strategic bargaining of the actors while the institutional setting can be different according to the level of analysis, i.e. state or the international level. Strategy or strategic interaction focuses on the interaction of two or more actors. It seeks to explain how the interaction unfolds.

States and strategies shape the dependent and independent variable in that they create pressures for adjustments of the respective interest. The absence of interest

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<sup>60</sup> G. TSEBELIS, *Veto players: how political institutions work*, Princeton: Princeton University Press, 2002., pp. 16-19.

<sup>61</sup> D.A. LAKE and R. POWELL eds, *Strategic choice and international relations*, Princeton, N.J.: Princeton University Press, 1999., pp. 3-6.

accommodation in the dependent variable is then assumed to be appropriated to either the inability of sectoral interests to influence the sectoral conditions under which the EU enlarges (demand side); or de facto accommodation where no influence has been exerted by sectoral interests (supply side). Such constitutes the *nil-hypothesis* under which no causal relationship between the sectoral interest's ability to influence the enlargement policy and the sectoral conditions under which the EU enlarges can be inferred. The central hypothesis of this study is then: Sectoral conditions under which the EU enlarges, i.e. TAs, is due to the influence of sectoral interests on states domestic cost and benefit calculation and their strategies at the international negotiation, which ultimately determines their EU accession policy.

#### **1.4.2. Research Design and Hypotheses**

The research design is structured around two building blocks to isolate the independent variables, i.e. sectors, states and strategies. Each has a logic of its own and relates to a different explanation: Are the sectoral conditions under which the EU enlarges influenced by sectoral interests – the demand side?; Or, do they reflect the underlying pattern of aggregation of those sectoral interests in the public arena and the strategic bargaining between states in the EU accession negotiations – the supply side (see Figure 3)?

Modern political economy expects that the presence of sectoral TAs and their variation is affected by sectoral interest of firms, nationally or internationally organised, and shaped by patterns of interdependence, i.e. their position in the national and international economy. The state and strategy centred approach contributes less importance to these groups and considers the explanatory variables to be state preferences under an open polity model and the strategic bargaining in the negotiations (see Figure 4).

Both explanatory variables are not mutually exclusive. They are assumed to operate following a logic of necessary and sufficient conditions for the presence of sectoral TAs under a partial mediated model. It allows identifying the intervening causal mechanism or process between the independent variables and the outcome of the dependent variable. In an attempt to limit equifinality each building block represents

all foreseen causally-relevant variables following the theoretical discussion of pages 18 to 28.

### **Selection of the Cases**

The phenomenon under investigation, TAs, refers to a universe of cases on the level of the sector and country. Chapter 2 shows that the universe of cases of the dependent variable comprises 47 sectors across 10 applicant countries providing for 470 observations on TAs. To augment the external validity of the research the case selection should be as representative as possible for the entire population. The dissertation focuses on 12 cases, i.e. three economic sectors across four applicant states permitting sectional and cross sectional analysis. The economic sectors are pharmaceuticals, basic iron and steel and international road transport. The Czech Republic, Hungary, Poland and Slovakia are the countries.

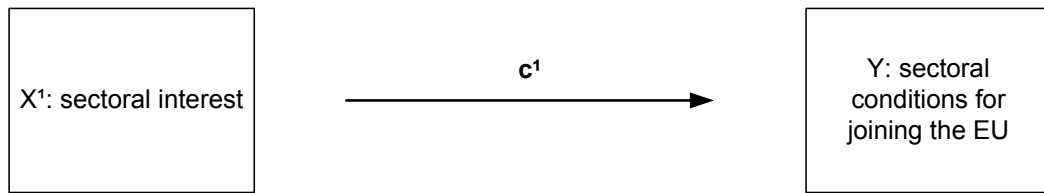
Under a partial equilibrium the EU is black boxed and held constant throughout the study. It is assumed to be a unitary actor that is independent, unelected and supportive of EU integration and enlargement. Simultaneously, the EU is assumed to be the guardian of the *acquis* signifying a unsupportive stance vis-à-vis legislative divergence between the EU and the national legislation of the member states and future member states<sup>62</sup>. These assumptions are uniform across the EU and all applicant countries.

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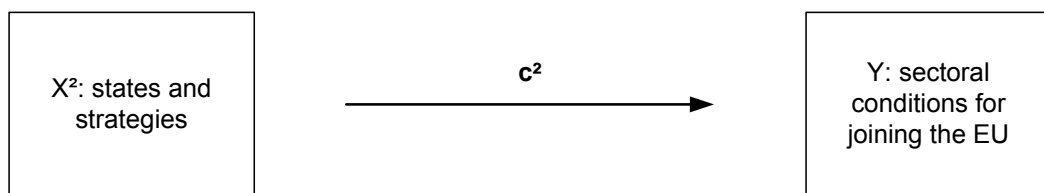
<sup>62</sup> I only touch upon the EU's internal decision-making process in Chapter 7 to describe its common position at the international negotiating table; and the concepts of pivots or break point countries as well as the theoretical logic for considering the EC the representative of the EU in the EU accession process.

**Figure 3: Causal Diagram**

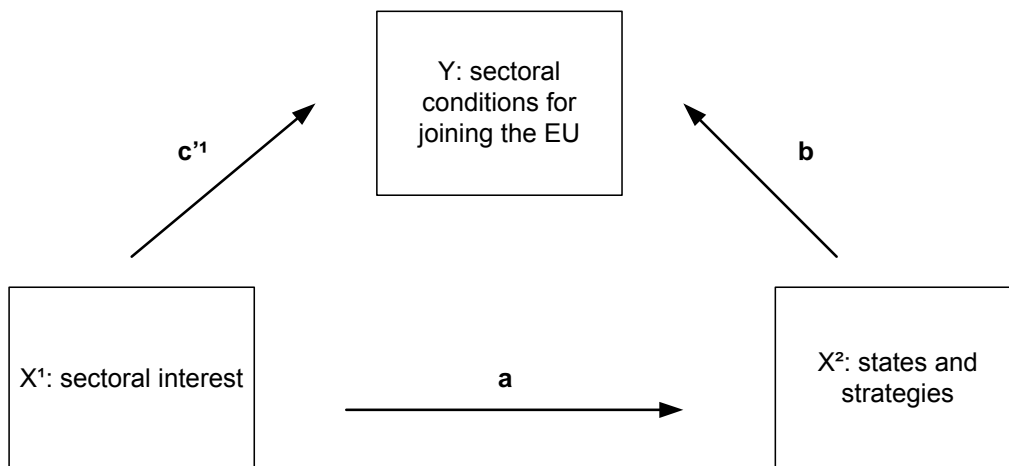
(1) a modern political economic approach



(2) a state centred approach

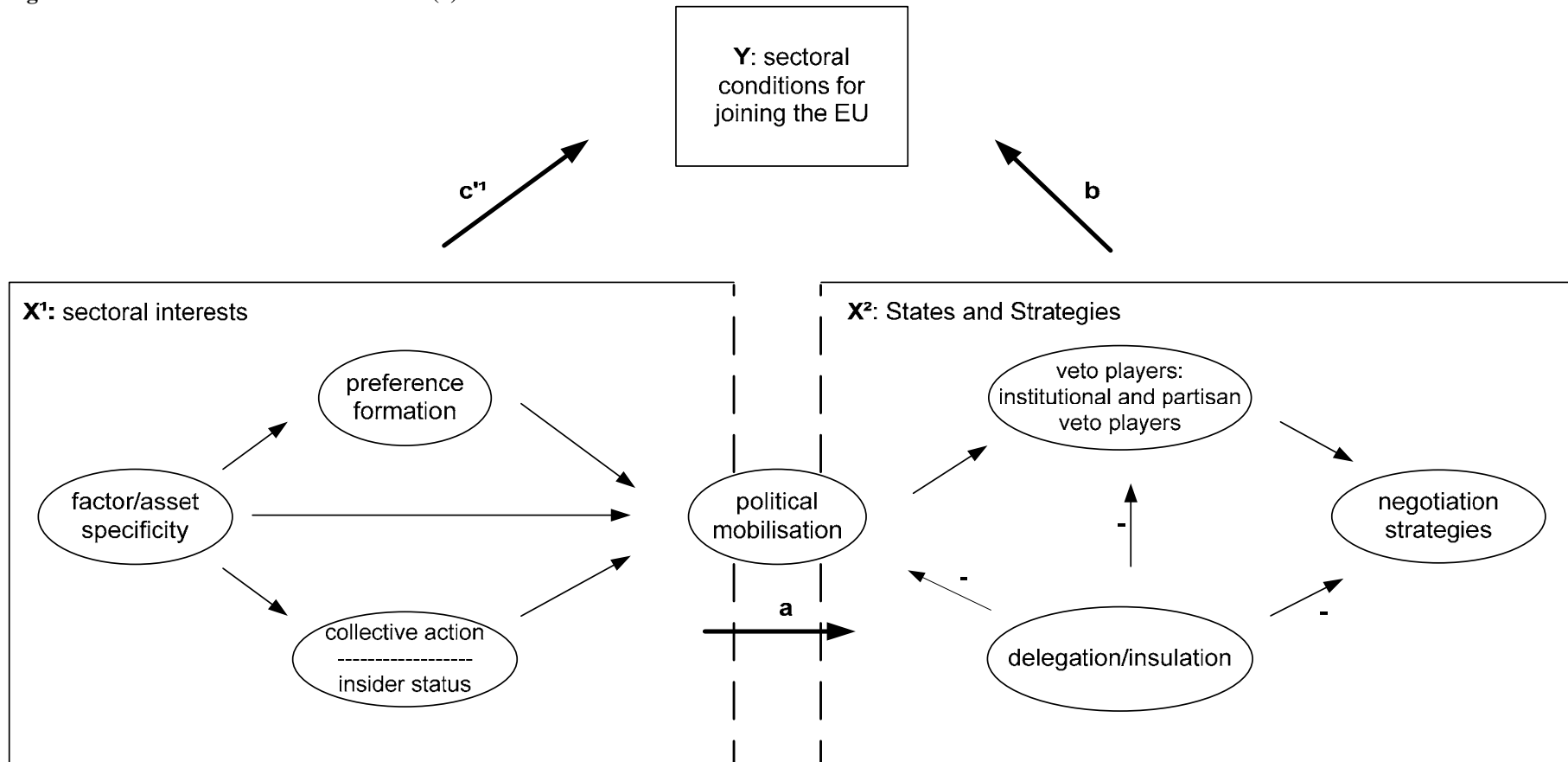


(3) a combined approach: partial mediated model



- Y = dependent variable
- X<sup>1</sup>, X<sup>2</sup> = independent variables whereby X<sup>2</sup> under a partial mediated model (3) is assumed to be a mediating cause, i.e. X<sup>2</sup> mediates the effect of X<sup>1</sup> on Y whereby Y ≠ 0 when X<sup>2</sup> is controlled
- c<sup>1</sup>, c<sup>2</sup> = direct effect
- ab ≈ indirect effect (c<sup>1</sup>-c<sup>1</sup>'), the reduction of the effect of the initial variable on the outcome

Figure 4: Detailed Partial Mediated Model (4)



Y = dependent variable

X<sup>1</sup>, X<sup>2</sup> = independent variables whereby X<sup>2</sup> under a partial mediated model (4) is assumed to be a mediating cause, i.e. X<sup>2</sup> mediates the effect of X<sup>1</sup> on Y whereby Y ≠ 0 when X<sup>2</sup> is controlled

c<sup>1</sup>, c<sup>2</sup> = direct effect

ab ≈ indirect effect (c<sup>1</sup>-c<sup>1'</sup>), the reduction of the effect of the initial variable on the outcome

While expedient for research purposes a partial equilibrium excludes a number of potentially valuable explanatory variables. For instance, domestic causes in the EU-15 member states might have had spill over effects in the EU enlargement negotiations. I acknowledge this methodological difficulty. Another confounding variable is logrolling or the presence of side payments. In the context of this study I assume issue linkages are of lesser theoretical importance. Moreover, I have found little evidence of their existence (see pages 49 and 310).

The study follows a most different system design (method of agreement) to choose the sectors and countries maximising leverage over the causal hypotheses<sup>63</sup>. On a sub-national level most different sectors increase the leverage of the theory to be tested over the outcomes. On a cross-country level the opposite logic holds for the sectors while not for the countries. Similar sectors are compared across different countries. The most dissimilar design allows inference on the basis of specificity of different sectors on a country level; and the specificity of a country across similar sectors on a cross-country level<sup>64</sup>.

### Sectors

The difficulty of tracing and understanding sectoral preferences and corresponding interest organisations calls for the use of as systematic an analytical method as possible. Economic sectors can be chosen according to several categories and definitions<sup>65</sup>. This research opts for defining economic sectors by output. They are selected on the basis of variables understood to be potential causes of the dependent variable, i.e. variables indicating a degree of asset/factor specificity (see Chapter 2, pages 60-65 and figure 6 for a detailed explanation).

The degree of factor and asset specificity is respectively lower for road transport compared to the basic iron and steel sector followed by the pharmaceutical industry. The pharmaceutical industry tends to have a higher degree of specificity on all levels. The steel sector is site specific involving

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<sup>63</sup> V. BUNCE, *Subversive institutions: the design and the destruction of socialism and the state*, Cambridge, UK; New York: Cambridge University Press, 1999. Cases are not matched on the dependent variable. They are matched on the main explanatory variables.

<sup>64</sup> D. COLLIER, *The Comparative Method: Two Decades of Change*, in: D. A. RUSTOW and K. P. ERICKSON, *Comparative political dynamics: global research perspectives*, New York, NY: HarperCollins, 1991, pp. 7-31., pp. 16-17. A. PRZEWORSKI, *Methods of Cross-National Research 1970-1983: An Overview*, in: H. N. WEILER, A. B. ANTAL and M. DIERKES, *Comparative policy research: learning from experience*, Aldershot, Hants, England: Gower, 1987, pp. 31-49.

<sup>65</sup> See Chapter 2, pp. 52-53 and Introduction, Part II, pp.84-89.

many dedicated assets. Despite lower factor specificity international road transporters' assets are well developed.

To locate these sectors in the Czech Republic, Hungary, Poland and Slovakia results in varying degrees of sectoral concentration and insider status.

The pharmaceutical sector is more concentrated in Hungary and Slovakia followed by the Czech Republic and Poland. The pattern is similar for sectoral economic strength and the degree of privatisation. The presence of private investment is higher in Hungary and the Czech Republic compared to Poland and Slovakia.

The basic iron and steel industry is relatively more concentrated in Slovakia, the Czech Republic, Hungary and Poland respectively. At the outset of the EU accession process (1998) the sector is predominantly state owned with varying levels of privatisation in subsequent years.

The international road transport sector was almost entirely in private hands except in Hungary, with the Czech and Slovak Republic leading the economic changeover. The market for international road transport is highly fragmented for labour and capital with the highest relative fragmentation in Poland followed by the Czech Republic, Slovakia and Hungary. Hence, no evident patterns of sectoral concentration and insider status emerge.

To test the theory two sectors would suffice to maximise leverage<sup>66</sup>. I included a third sector because it allows for more variance on factor specificity and augments external validity. Factor/asset specificity of capital and labour might have a different impact on the hypotheses despite the blind of defining sectors by output rather than factor endowments<sup>67</sup>. Sectors also are chosen from different structural sectors in the national economy to control for biases. Transport has relevance for the service sector while basic iron and steel relates to heavy industry and pharmaceuticals to manufacturing.

I match the selection of these three sectors on other potential structural explanatory factors. All three sectors – or 12 sectors taking into account the national differences – experience the economic transformation process after 1989. They are confronted with the EU accession process

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<sup>66</sup> G. KING, R.O. KEOHANE and S. VERBA eds, *Designing social inquiry: scientific inference in qualitative research*, Princeton, N.J.: Princeton University Press, 1994., p. 29.

<sup>67</sup> J.A. FRIEDEN, *Debt, development and democracy: modern political economy and Latin America, 1965-1985*, Princeton, New Jersey: Princeton University Press, 1991., pp. 31-32.

after 1998 with the possible exception of those located in the Slovak Republic, which starts the accession negotiations in 2000. The latter might have an effect according to the so-called 'readiness' explanation (see Chapter 1 pages 11-14). While Chapter 1 demonstrates the inconclusiveness of this explanation the location of sectors in Hungary, Poland and the Czech Republic – countries judged to be more advanced – should partially control for its influence. In addition, at the outset of the negotiations with the other V-4 (1998) Slovakia is not as much considered less advanced for economic than democratic reasons.

A similar logic applies for the cross sectional analysis. I compare similar sectors across relatively different countries in the cross sectional comparison. The examination of matching sectors in order to highlight the common elements sets the framework for interpreting how similar processes of change play out within different contexts<sup>68</sup>.

### **States and Strategies**

On a country level I observe variation in national institutions dealing with the EU accession process over economic sectors to gauge their influence on the dependent variable. These are institutional and partisan veto players, the level of delegation of decision-making authority or the insulation of the policy process and the international negotiating strategies.

At the outset of the negotiations institutional and partisan veto players vary for the Czech Republic, Hungary, Poland and Slovakia. The choice of the V-4 countries has the benefit that the variance of institutional and partisan veto players and their respective preferences evolve. The importance and the modalities for holding a referendum change for the individual countries. Executives in Prague, Budapest, Bratislava and Warsaw are confronted with different majorities in parliament and electoral cycles between 1998 and 2003. Likewise, the level of delegation and the insulation of the administrative frameworks for dealing with the transposition of EU legislation differ for the individual V-4 countries at the outset of the negotiations. In this context, the dynamic element between 1998 and 2003 for these variables is more important for Poland and the Czech Republic than for Hungary and Slovakia.

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<sup>68</sup> D. COLLIER, *The Comparative Method: Two Decades of Change*, in: D. A. RUSTOW and K. P. ERICKSON, *Comparative political dynamics: global research perspectives*, New York, NY: HarperCollins, 1991, pp. 7-31.



On an international level the preferences and the strategies of the chief negotiators and the progress in the negotiations differed noticeably. The Czech, Hungarian, Polish and Slovak chief negotiators advance at a different pace in the EU accession process depending on their respective strategies.

Apart from the aforementioned explanatory variables the V-4 countries are in many respects alike. All countries embark upon the transition process after 1989 and applied for EU membership between 1993 and 1996. They commenced EU accession negotiations in March 1998 with the exception of Slovakia. Bratislava started the EU entry talks in February 2000, however, the ‘readiness argument’ appears a less valuable explanatory variable as Chapter 1 has indicated. The inclusion of Slovakia in the case studies possibly contributes to the breath of the argument for the broader population.

On a cross sectional level the size of the country might have an influence on the presence of sectoral conditions. While Chapter 1 demonstrates that size is a less illuminating variable I control for it in the sectional comparisons by normalising the quantitative variables.

### **Time Dimension**

This study focuses on the period 1998-2003 during which the accession negotiations take place. Given the particular nature of the transition process snap shot measurement of quantitative data over these years causes bias. The economic reform process coincided with the productivity crunch immediately after the economic transition took off in the early 1990s. Afterwards the economy embarked upon a gradual modernisation<sup>69</sup>. As a result, some sectors are still recovering while others are going through restructuring; and still others are well on their way to become global competitors. A snapshot would therefore provide a biased picture of the state of certain sectors. Hence, I normalised sectoral quantitative data for the years 1989-2003 when possible.

#### **1.4.2.1 Demand Side: Sectors and EU Enlargement**

The demand side explores the effect of EU enlargement on sectoral preferences formation and ensuing sectoral political mobilisation (a preference driven approach). A theory on asset

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<sup>69</sup> P. BOONE, S. GOMULKA and P.R.G. LAYARD eds, *Emerging from communism: lessons from Russia, China and Eastern Europe*, Cambridge, Mass.: MIT Press, 1998.

specificity offers an approach that stresses the importance of firms or sectoral interest which are directly affected by EU enlargement and the presence of sectoral TAs<sup>70</sup>. It proposes three central building blocks that drive the explanation: (a) it allows for identifying sectoral interests and preferences on TAs in the enlargement process; (b) the likelihood of their political mobilisation on EU enlargement; and (c) the likelihood of their success in the enlargement policy.

Economic exchange is primarily driven by a return on factors. The greater the return on factors in a given activity, the more likely the industry will favour continuing activity as quasi rents, the difference between the rate of return in a factor's current use and its best alternative use, are higher. More asset specificity therefore implies larger quasi rents. Ergo, owners of factors of production have an incentive to lobby for policies that keep their rents high. Ceteris paribus, under threat of international competition – or the introduction of different market regulations ahead of EU membership – that result in rents and revenues to change, exit or entry of mobile factors in the industry may be expected. Therefore, an actor's policy preference on EU enlargement is a function of the susceptibility of the actor's factor to EU enlargement. The less EU enlargement changes the return on the factor – change the relative prices for instance – the less incentive the factor's owner has to try and affect policy. The higher the opportunity costs to a sector related to a TA the more likely the sector will seek to influence enlargement policy on TAs.

The theory on a degree of factor/asset specificity predicts empirically that owners of a factor are likely to exert more political pressure the higher the returns on the factor and the more specific factors are to their current use.

### **Hypothesis 1: Preference Formation**

The more factors are specific to an industry the more likely it will be affected by EU enlargement, i.e. full membership of the European single market and the more likely it will hold strong preferences on EU enlargement policy.

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<sup>70</sup> J.A. FRIEDEN, *Debt, development and democracy: modern political economy and Latin America, 1965-1985*, Princeton, New Jersey: Princeton University Press, 1991.

Holding preferences does not automatically mean political mobilisation. Modern political economy assumes that the more factors are specific to an industry the more likely they hold political and economic assets, i.e. institutionalised political aggregations specific to their current use. Sector specific industries tend to be politically better organised than industries with highly mobile or diversified interests. The latter are rather unlikely to enter in long term organisations; the former are more likely to do so. It is expected that those with more specific factors/assets are both better organised and more likely to engage in political activity than those with less specific assets. *Baldwin* adds that political economic forces driving preferences formation are strengthened by a peculiar tendency of special-interest groups. They usually mobilise politically to avoid losses rather than to secure gains. This form of political mobilisation is termed *asymmetric lobbying*<sup>71</sup>.

Factor and asset specific firms producing in the CEECs that face competition from EU based firms are more likely to oppose the application of the *acquis* to avert losses they may face from more stringent regulation. They are likely to support grace periods or TAs while securing benefits by having access to the EU market. These firms are likely to have greater incentives to mobilise politically to secure gains and avert losses in the EU enlargement process because they tend to hold well developed political assets.

### **Hypothesis 2: Political Mobilisation**

The higher the degree of factor and asset specificity of the sector in the applicant states, the more likely political mobilisation will occur; and the more likely it will occur along sectoral lines.

Simply having a particular set of preferences and the likelihood of political mobilisation does not necessarily guarantee the accommodation of sectoral interests and preferences. The literature on asset specificity, collective action and lobbying provides useful insights as to ‘how’ lobbying activities take place.

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<sup>71</sup> R.E. BALDWIN, *Towards an integrated Europe*, London: Centre for Economic Policy Research, 1994., pp. 70-71.

An asset specific theory expect that those with more specific assets to be better organised and more likely to be successful than those with less specific assets. The strength of an interest group largely depends on the concentration of the sector and the entry and exit barriers of firms. The literature on collective action expects that the stronger the interest groups cohesion the more influence it will have on the policy process; and, hence, the more successful it will be. As a result, the theory would assume that the more concentrated the industry, the easier it would be to exert political pressure. The greater the entry barriers, the more easily the industry will be able to avoid free riding by new entrants.

In other words, cohesive sectors in the CEECs that face competition from EU based firms and that are disadvantaged by the application of the *acquis* are likely to exert more political pressure on policy makers in the enlargement process. They also are assumed to be more successful in opposing the application of the *acquis* and obtaining exemptions from applying or enforcing regulations.

### **Hypothesis 3: Intensity of Political Pressure**

The greater the internal cohesion of a sector, the more political pressure it will exert to avoid losses or reap gains from the enlargement policy.

The writings on lobbying, and more precisely lobbying the EU, come to similar conclusions by arguing that accommodation of economic interest is contingent upon their capacity to successfully influence political decisions. To successfully influence political decisions organisational resources and the bargaining chips an interest group holds are crucial<sup>72</sup>. The latter implies that interests can perform services in the broader public interests at the same time as promoting their own interests. The interest group that holds these bargaining chips is likely to obtain more TAs<sup>73</sup>.

### **Hypothesis 4: Insider Status**

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J. GREENWOOD, *Representing interests in the European Union*, Basingstoke: Macmillan, 1997., pp. 11-12.

<sup>73</sup> Neo-corporatism in this sense argues that interest groups follow the logic of influence and that they hold particular types of resources, which predict access to particular types of governance mechanisms.

If sectoral interests have obtained insider status in the policy process it is more likely that their preferences on TAs are accommodated.

#### **1.4.2.1 Supply Side: States and Strategies and EU Enlargement**

Assuming that accommodation of sectoral preferences is not inevitably concomitant to asset specificity forces this study to be explicit about public institutions, i.e. states (governments) and strategies (negotiations). It makes an analytical distinction between national and EU institutions and the interaction between them.

On a national level it is concerned with the conditions under which authorities were responsive to sectoral interests' preferences in the EU enlargement process. On an EU level it concentrates on the conditions under which the EU was willing to accept temporary departures from the *acquis* when negotiating EU membership with the CEECs. Throughout the dissertation I black-box the EU, which corresponds to a partial equilibrium and the variation this study attempts to explain.

The supply side of the argument explores whether and how institutions aggregate and influence sectoral preferences in the public arena (an institutional driven approach)<sup>74</sup>. It concentrates on the mediating role national and EU institutions play between sectoral interests and outcomes in the EU enlargement negotiations. It proposes four central building blocks that drive the explanation: (a) it allows for identifying institutional veto players in the EU accession process; (b) the partisan veto players in the EU accession process; (c) the level of delegation in the enlargement process; and (d) the country strategies pursued at the negotiating table.

Following Tsebelis' theory on veto players, institutional receptiveness to a change in societal preferences and political pressure are inversely related to the formal number of veto players in the political system, that is the number of institutional actors whose assent is required for a change in policy. In the context of EU enlargement this means that the national market in which a sector operates is least likely to change the higher the number of veto players needed to endorse government policy on EU accession. The status quo represents the market *ex ante* EU membership.

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<sup>74</sup> P.A. GOUREVITCH, Squaring the Circle: The Domestic Sources of International Cooperation, in: *International Organization*, 1996, 50(2), pp. 349-73., p. 6.

Tsebelis' theory on political institutions also has an effect on the international level. *Mansfield, Milner* and *Pevehouse* hypothesise that it is difficult to forge international agreements when leaders confront an array of domestic groups with diverse preferences and the ability to block initiatives (second image effects). The authors argue that increasing the number of veto players never increases and usually reduces the range of agreements that would satisfy the countries involved in international negotiations. Veto players therefore tend to augment the limits upon international agreements particularly when they involve a policy change<sup>75</sup>.

In the context of EU enlargement this would mean that the market in which a sector operates is least likely to change the higher the number of veto players needed to endorse government policy on EU accession. The status quo represents the market *ex ante* EU membership<sup>76</sup>. In other words, the higher the numbers of veto players the more likely TPRs would be reflected in national enlargement policy.

#### **Hypothesis 5: Veto Players**

Institutions are likely to be more receptive to societal pressures the higher the number of institutional actors whose assent is required for a policy change.

The higher the number of institutional veto players the more likely TPRs would be reflected in national enlargement policy. Policy outcomes do not only vary depending on the identification and number of institutional veto players but also on partisan veto players or their respective preferences relative to the status quo in regard to policy change. To identify partisan veto players one needs to have an idea about assumptions to derive the preferences on EU enlargement of these actors<sup>77</sup>.

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<sup>75</sup> E.D. MANSFIELD, H.V. MILNER and J.C. PEVEHOUSE, *Vetoing Co-operation: The impact of Veto Players on International Trade Agreements*, s.l., 26 January 2005, 46., pp. 2-3.

<sup>76</sup> Note that many stakeholders did not necessarily oppose EU enlargement. People who vested in the status quo opposed certain economic consequences of EU enlargement.

<sup>77</sup> Alternatively, when all else fails, preferences need to be stated clearly.

The focus is on the executive because in the area of foreign policy, and particularly EU accession, the executive is often able to set the agenda and formulate proposals<sup>78</sup>. It must have foreign policy initiatives ratified by the legislature under a quorum and varying majorities depending on the voting rule. This is important as a government's main interest and preference is assumed to remain in office. Ergo, it cares about the political parties and the supporters of which it is composed<sup>79</sup>. As foreign policy choices have electoral ramifications government's need to heed the electoral consequences of these choices in addition to the political pressure of societal groups with conflicting interests. Ignoring the preferences of its supporters and interest groups could lead to exit from power. Therefore, supporters and interest groups have an opportunity to exercise influence on the government's policies.

The executive is reliant upon the confidence of his or her majority in Parliament. According to *Milner*: 'Parliament looms large in the deliberations of the executive, exercising its influence largely through the law of anticipated reactions but also through more overt expressions', such as parliamentary approval of government policy<sup>80</sup>. Government's with a comfortable parliamentary majority are less at the mercy of its composite political parties and supporters to carry forward policy – at least in the short run which it might benefit in the long run, a phenomenon that is called the *time inconsistency problem*. In addition, governments will base their strategic choices on the expected utility of maintaining or changing the institutional status quo only at the time when they are accountable to the citizenry. Hence, at least for a while they can ignore special interests relative to governments with narrower majorities.

### **Hypothesis 6: Executive Preferences**

The larger the executive's majority in Parliament and proximity to the next general elections the less likely societal preferences loom over governmental policy.

Should states delegate and insulate decision-making authority from societal pressures the number of veto players and their preferences might well be irrelevant or decline. Governments have the power to delegate authority to bureaucracies or independent agencies to negotiate treaties with

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<sup>78</sup> H.V. MILNER, *Interests, institutions, and information: domestic politics and international relations*, Princeton, N.J.: Princeton University Press, 1997., p. 14.

<sup>79</sup> P. LANGE, Maastricht and the Social Protocol: Why Did They Do It?, in: *Politics Society*, 1993, 21(1), pp. 5-36., pp. 14-15.

<sup>80</sup> H.V. MILNER, *Interests, institutions, and information: domestic politics and international relations*, Princeton, N.J.: Princeton University Press, 1997., p. 14.

foreign powers. These bureaucracies might not share preferences of elected politicians or societal actors. As administrations gain more autonomy it is likely that their principals' preferences are less reflected in effective policy.

I will test this hypothesis on the formal powers and preferences of the Czech, Hungarian, Polish and Slovak administrations responsible for negotiating EU membership.

### **Hypothesis 7: Delegation and Insulation of the Policy Process**

The more decision making authority over policy is insulated from societal and political pressure the less likely policy change should be associated with changes in societal preferences and their political mobilisation.

While domestic institutions are assumed to play an important role one cannot neglect the role of international institutions such as the setting of international negotiations and their conduct. In this sense domestic negotiations are a subset of international negotiations.

According to *Thomas Schelling* if one negotiator's constraint is strong relative to another, the former is likely to obtain a better deal than if neither side were constrained. For instance, on an international level a country could argue the unfeasibility of making concessions that involves untying accords that its negotiators agreed on a domestic level; or alternatively threaten the other negotiating party with the risk of a degenerative negotiation position relative to the proposed deal on the table. Domestic bargaining or a ratification constraint might provide for a pre-emptive bargaining advantage. The chief negotiator could project a credible constraint about his negotiation position that preceded difficult and protracted negotiations on a domestic level involving several veto players.

Two-level games have attempted to confirm Schelling's intuition that the constraints imposed by domestic institutions could prove a bargaining asset in international negotiations. However, there is a trade off, the higher the domestic constraint the more unlikely an international agreement.

Specifications under which conditions the Schelling conjecture can be confirmed centre on *ex post* ratification constraints and the level of complete information.

### **Hypothesis 8: International Negotiations**



The higher the domestic ratification constraint upon the chief negotiator among the negotiating parties the more likely the chief negotiator will be provided with a bargaining advantage.

As a result of the political intricacies of domestic and international politics governments might prefer not to reveal their negotiation positions. Such position might be strategic and the result of cheap talk, as opposed to credible speech, rather than a revealed preference. A TPR might be calculated and strategic with the executive not willing to fight for it<sup>81</sup>. Alternatively, it might prefer to do exactly the opposite and the respective position papers might reflect their position at the international negotiating table<sup>82</sup>. The executive has little to gain from an uncompromising stance when what it demands is in fact strategic. In this sense a TPR is an indication of the state's preference over the issues on the table. An uncompromising position reflected in protracted negotiations is then likely to reveal true preferences. The revealed national preference is assumed to be a litmus test for the preference formation of the aggregated preferences of economic sectors, executives, legislatures and administration.

### **Hypothesis 9: National Preferences**

The longer the duration of issue specific negotiations between states the more important the issue is likely to be for the negotiating parties and the more likely preferences reflect revealed preferences.

The real methodological difficulty for this study is logrolling, package deals or issue linkages with other agreements up for discussion in the enlargement negotiations. It is not naive to assume that governments have a limited amount of negotiation leeway. They might have to make deals that are compensated by others. At the outset of this study it is assumed that this is not the case. Sectoral negotiations take place in closed sectoral committees in the Council of the EU that bear little reference to each other<sup>83</sup>. Moreover, within the EC each DG is likely to regard its proper jurisdiction too important to compromise for another. Finally, in all but two out of 82 interviews the participants in the negotiations denied the existence of logrolling unless within similar

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<sup>81</sup> P. LANGE, Maastricht and the Social Protocol: Why Did They Do It?, in: *Politics Society*, 1993, 21(1), pp. 5-36., p. 32, footnote 29.

<sup>82</sup> In the EU enlargement negotiations the applicant countries initial position papers were available on a chapter by chapter basis. Subsequent position papers were secret and only occasionally available. The EU's common negotiation position remained secret.

<sup>83</sup> A. MAYHEW, *Recreating Europe: the European Union's policy towards Central and Eastern Europe*, Cambridge; New York: Cambridge University Press, 1998., pp.91-92.

sectors. Where logrolling was attempted it failed. Proposals were refused or the strategic calculus worked out otherwise. Package deals usually take place at the end of the negotiations when outstanding issues are resolved at once<sup>84</sup>. The December 2002 Copenhagen summit is well documented and does not appear to suggest the existence of package deals.

## **Conclusion**

In the first half of the 1990s the EU decided to embark upon its fifth enlargement. Between March 1998 and December 2002 the CEECs, Malta and Cyprus negotiated the terms of joining the EU. During the EU accession negotiations 292 transitional arrangements (TAs) were agreed in sectors covered by 29 chapters of the *acquis communautaire*. These arrangements delay the application of the *acquis communautaire* and constitute different sectoral conditions under which the EU enlarges.

TAs are the distributional outcome of the EU enlargement process. Their variation tells us something about the EU accession negotiations and the sectors and countries to which they apply. For the comparativists they are an opportunity. They provide us with a lever on the otherwise conceptually and analytically elusive phenomenon of EU enlargement, its causes and consequences. TAs allow for a rigorous test of hypotheses pertaining to the behaviour of sectors, states and their respective strategies in the enlargement process.

The presence of TAs is puzzling for three reasons. First, while EU membership expects full application of the *acquis* the presence of TAs indicates different sectoral conditions under which countries join the EU. Second, considering the transition process in the applicant countries TAs were negotiated for sectors and countries where least expected. Finally, IR and negotiation theory expects applicant states not to be able to obtain different sectoral conditions that would serve their interests upon EU entry when confronted with the EU's dominating power in the EU accession negotiations.

The enlargement literature based upon the assumptions of historical institutionalism and theories treating states as closed polities fails to explain the presence and specificity of TAs. In addition,

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<sup>84</sup> H. RAIFFA, J. RICHARDSON and D. METCALFE, *Negotiation analysis: the science and art of collaborative decision making*, Cambridge, MA, London: Belknap Press of Harvard University Press, 2002., pp. 90-91, 480-481.

the distribution of TAs across countries contradicts the argument that they are present because the countries were simply not ready for EU entry. This study proposes an alternative explanation that falls in the area of modern political economy. It takes a preference driven approach and explores the demand for TAs. It identifies whose material interests are affected by EU enlargement and their corresponding policy preference; the likelihood of their political mobilisation on EU membership; and the likelihood of the accommodation of their preferences in the EU enlargement policy.

Within the framework of modern political economy international outcomes are assumed to be inevitably concomitant to sectoral preference formation and political mobilisation. The role of states (governments) and international organisations (negotiations) and the strategies of actors occupying these institutions are endogenous to its analysis. The theoretical framework the present research adheres to inverts this assumption. It considers states and international organisations as exogenous and separate from sectoral interests. It complements the modern political economy analysis with an institutional driven approach and explores the supply side for TAs.

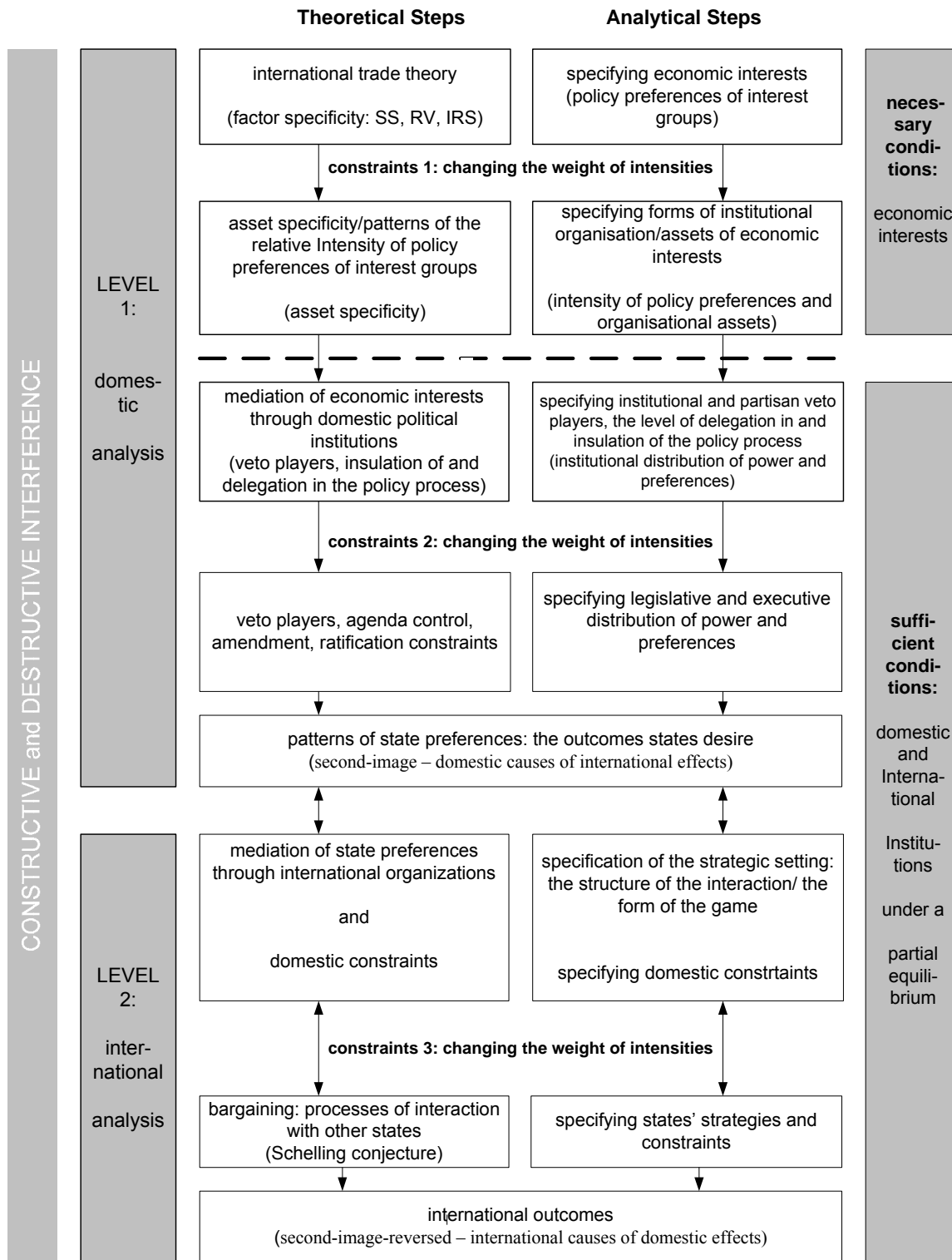
States and international organisations aggregate sectoral interests in the public arena. They might act as constraints upon sectoral interests. States and international organisations are assumed to mediate sectoral interests following *the logic of destructive and constructive interference*. States and international organisations act as constraints upon sectoral preferences at the negotiating table when their interests are not aligned, i.e. destructive interference. Conversely, when societal interests and institutional preferences are aligned states and strategies sustain or amplify sectoral preferences at the negotiating table, i.e. constructive interference.

More specifically, states' and international organisation's mediation of sectoral interests is assumed to be related to: the number of formal domestic veto players and their preferences; the level of delegation of authority in the policy process; and states' strategies at the international negotiating table.

In short, in the preference driven approach sectoral interests are assumed to be necessary conditions for the presence of TAs. In an institutional driven approach states and international

organisations are understood to provide for sufficient conditions for TAs presence and their distribution.

**Figure 5: The Theoretical Framework: Constructive and Destructive Interference**





## CHAPTER 2: TRANSITIONAL ARRANGEMENTS

### Introduction

The research questions and the puzzle direct the study towards two macro levels of analysis, i.e. the sectoral level within countries and across countries<sup>1</sup>. Therefore this study requires makes two crosscutting comparisons that address the sectoral level, i.e. why this particular sector instead of another, and the national level, i.e. why in this particular country instead of another, for its cases, which are sectors and countries<sup>2</sup>.

The theoretical framework integrates the domestic and the international level of analysis. A two-level game allows to test theory and hypothesis geared towards second-image (domestic causes of international effects) while not excluding the second-image-reversed (international causes of domestic effects)<sup>3</sup>. The theoretical model combines theories of domestic and international politics and formulates competing hypothesis in both directions. It lies at the crossroads of *international political economy*, *comparative politics* and *international relations*. TAs might be the result of sectoral interests and their preferences and/or the result of international negotiations.

The levels of analysis and the combination of theory drives the research in the direction of a combined variable- and case-oriented strategy, respectively complemented by quantitative and qualitative research techniques<sup>4</sup>. The former is guided by a theoretical informed comparison. The latter follows the logic of the cases as a whole. The variable-oriented strategy allows the researcher to test theory across a larger number of cases using many variables and focus on structural factors, i.e. factor and asset specificity (see this chapter, section 4). The case-oriented approach studies the impact of human agency tested in a small number of cases and allows for

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<sup>1</sup> T. LANDMAN, *Issues & methods in comparative politics: an introduction*, London and New York: Routledge, 2000., pp. 14-15.

<sup>2</sup> T. JANOSKI, *Synthetic Strategies*, in: C. C. RAGIN, *Issues and alternatives in comparative social research*, Leiden: Brill, 1991, pp. 59-81..

<sup>3</sup> For terminology see: K.N. WALTZ, *Man, the state and war: a theoretical analysis*, New York: Columbia University Press, 1959. P. GOUREVITCH, *The Second Image Reversed: The International Sources of Domestic Politics*, in: *International Organization*, 1978, 32(4), pp. 881-912, K.N. WALTZ, *Man, the state and war: a theoretical analysis*, New York: Columbia University Press, 1959.; J.A. CAPORASO, *Across the Great Divide: Integrating Comparative and International Politics*, in: *International Studies Quarterly*, 1997, 41(4), pp. 563-91.; R.D. PUTNAM, *Diplomacy and Domestic Politics: The Logic of Two-Level Games*, in: *International Organization*, 1988, 42(3), pp. 427-60. ,p. 434.

<sup>4</sup> C.C. RAGIN, *The comparative method: moving beyond qualitative and quantitative strategies*, Berkeley: University of California Press, 1987b., pp. 69-84.

counterbalancing the more abstract probabilistic conclusions of the variable-based approach (Chapters 3, 4, 5, 6 and 7).

The first two sections of Chapter 2 deal with the methodological choices covering the combined strategy in comparative politics and the selection of the cases. The third section presents the specification of the independent and dependent variables. The fourth section deals the main findings of the analysis of the dependent variable.

## **2.1. A Combined Strategy**

Triangulation of the research question according to *Lasswell* concerns the *what*, the *who*, the *when*, the *how* and the *why* of TAs<sup>5</sup>. To answer these questions this study applies the comparative method following a variable and a case-oriented approach. The comparative method is central to both variable and case oriented research and is used in both of them<sup>6</sup>.

The variable-oriented strategy allows the researcher to test the factor/asset specific theory and the state-centred approaches across a large number of cases, sectors and countries. It makes use of many well defined variables and focuses on structural factors, i.e. factor and asset specificity. Its conclusions are probabilistic and general and its attention is centred more strongly on the insight gained from a set of variables.

The case-oriented approach studies the impact of human agency, i.e. processes revolving around the EU accession negotiations tested in a smaller number of cases. It allows for counterbalancing the more abstract probabilistic conclusions of the variable-based approach. It tends towards complexity. Rather than arriving at a synthesis of both approaches that transcend the principles of generality and complexity, the present study attempts to combine both of them<sup>7</sup>.

An investigation that uses a combined strategy simply implies both major strategies to the research question. It pursues an internal and external analysis in comparative research, i.e. ‘why this sector and not another’ and ‘why these countries and not others’, to achieve both external and

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<sup>5</sup> H.D. LASSWELL, *Politics: who gets what, when, how*, New York: Smith, 1950.

<sup>6</sup> M. DOGAN and A. KAZANCIGIL, *Strategies in Comparative Research*, in: M. D. M. and A. KAZANUFI, *Comparing Nations*, Oxford: Blackwell, 1994, pp. 1-14.

<sup>7</sup> C.C. RAGIN, *Fuzzy-set social science*, Chicago: University of Chicago Press, 2000., pp. 35-38.



internal validity, i.e. the applicability to a whole class of instances and the descriptive inferences for the selected cases respectively.

### 2.1.1 A Variable-oriented Approach

A variable-oriented approach to comparative data offers several attractions<sup>8</sup>. First, a variable-oriented approach is theory centred, i.e. the asset/factor specific theory discussed in Chapter 1. Central is the ‘why’ questions in the analysis: ‘It is less concerned with understanding specific outcomes or categories of outcomes and more concerned with assessing the correspondence between relationships discernable across many countries, on the one hand, and broad theoretical based images of macro-social phenomena, on the other’<sup>9</sup>. Generality is given precedence over complexity and the interest goes to testing hypothesis derived from general theories. The implicit model of causation central to this strategy is structural.

Second, it allows to consider alternative explanations more carefully (state centred and interest based approaches. The statistical method inherent to a variable based perspective has the merit of assessing rival explanations through statistical control<sup>10</sup>. It allows us to test other theories on the dependent variable, i.e. state-centred approaches.

Third, a variable-based approach enables the study of more than a handful of cases at the time. A variable based approach allows testing propositions on the widest possible population of relevant observations. A systematic analysis of a well defined set of variables for the widest possible set of cases widens and deepens the breath of the argument and more exact testing.

Finally, a variable oriented makes the researcher more cautious in formulating empirical generalisations and counteracts the tendency to proffer particularistic explanations when faced with the complexity of empirical cases. Causal explanations are seen as probabilistic and outliers are expected. In sum, a variable-oriented strategy is best suited for assessing probabilistic

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<sup>8</sup> C.C. RAGIN, Introduction: The Problem of Balancing Discourse on Cases and Variables in Comparative Social Sciences, in: C. R. RAGIN, *Issues and Alternatives in Comparative Social Science Research*, Leiden: Brill, 1991, pp. 1-8. p. 1-2.

<sup>9</sup> C.C. RAGIN, *The comparative method: moving beyond qualitative and quantitative strategies*, Berkeley: University of California Press, 1987b., pp. 34-52.

<sup>10</sup> D. COLLIER, The Comparative Method: Two Decades of Change, in: D. A. RUSTOW and K. P. ERICKSON, *Comparative political dynamics: global research perspectives*, New York, NY: HarperCollins, 1991, pp. 7-31., pp. 8-9.

relationships between features of social structures, conceived as variables, over the widest possible population as observation.

### **2.1.2. A Case-oriented Approach**

In contrast to a variable based approach the case-oriented approach uses theory to aid interpretations and guide the identification of important causal factors, rather than test hypothesis<sup>11</sup>. Case-oriented research accommodates interest in specific cases and specific historical chronologies of processes<sup>12</sup>. The essential features of a case-oriented approach are interpretative and causally analytic. It attempts to account for significant outcomes or set of comparable outcomes or processes by piecing evidence together in a manner sensitive to chronology and offering limited generalisations which are sensitive to context. Case-oriented research also focuses on variables, however, it considers contextual characteristics of specific cases more thoroughly and how variables interact within the context of these cases. Thus, comparativists who use case-oriented strategies often want to understand or interpret specific cases because of their intrinsic value<sup>13</sup>. Such strategy is warranted in the present research since one objective is to trace the process of negotiating TAs through the different levels of analysis<sup>14</sup>.

Comparative case-oriented researchers see cases as complex configurations of events and structures. Case-oriented discourse speaks directly to the events and experiences of cases, abstracting from their histories and their special characteristics and circumstances to draw out their theoretical significance. Case-oriented discourse responds to the experiences of cases as singular entities and is capable of contributing directly to the discussion of issues and problems faced by individual cases and the elaboration and refinement of theory. The case-oriented approach is best suited for identifying invariant patterns common to one or a few cases.

### **2.1.3. A Combined Strategy**

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<sup>11</sup> C.C. RAGIN and H.S. BECKER, What is a case?: exploring the foundations of social inquiry, in: Cambridge (England); New York, NY, USA: Cambridge University Press, 1992, pp.4-5.

<sup>12</sup> H. ECKSTEIN, Case Study and Theory in Political Science, in: F. I. GREENSTEIN and N. W. POLSBY, *Handbook of political science*, Reading, Mass.: Addison-Wesley Pub. Co., 1975, pp. 79-138., p. 82.

<sup>13</sup> C.C. RAGIN, *Fuzzy-set social science*, Chicago: University of Chicago Press, 2000., p 57.

<sup>14</sup> The method of process-tracing attempts to trace the links between possible causes and observed outcomes, in: A.L. GEORGE and A. BENNETT, *Case studies and theory development in the social sciences*, Cambridge Mass: MIT Press, 2004., pp. 6-7.

The choice between variable- and case-oriented approaches appears to be between variables and cases – between the radically analytic, statistical techniques that obscure cases and qualitative-historical methods that immerse the investigator in cases<sup>15</sup>. *Ragin* argues that ‘the perception that researchers must choose between small-N, case-oriented strategies and large-N, variable-oriented strategies is unfortunate’<sup>16</sup>. The main weakness of a variable-oriented approach is its tendency towards abstract generalisations while a case-oriented approach strategy leans toward particularising. Both strategies are at the opposite end of the methodological continuum in comparative research and have clear methodological biases<sup>17</sup>.

However, a combination of both strategies allows the researcher to study both structural factors and factors reflecting processes and human agency, which is the objective of this study. The usage of both strategies in this pursuit checks the biases of the other. Understanding the ‘why’ of TAs and testing the asset/factor specific theory point in the direction of a variable based approach; while tracing the process of the accession negotiations and the influence of state institutions, international negotiations and human agency informs us about ‘what and how’ and directs us towards a case based approach.

A combination of both strategies allows for strengthening the variable based approach and the case-based approach through cross-checking the findings. The first objective in this study calls for a variable-oriented strategy in the study of competing theories. The second objective is to test the outcomes of the variable-based approach in specific cases. It provides a basis for verifying and refining the interpretation of TAs through the variable based approach. In the variable based approach the independent variables are identified on the basis of theory (asset/factor specificity and state-centred approaches). The quantifiable independent variables will be put together in a competition to explain the variation in the dependent variable, i.e. TAs. The statistical analysis provides probabilities as to which theory explains most of the variation in our dependent variable. Subsequently, the case-oriented approach provides a degree of assurance that the correlations

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<sup>15</sup> C.C. RAGIN, *Fuzzy-set social science*, Chicago: University of Chicago Press, 2000., p. 3.

<sup>16</sup> *Ibid.*, p. 7.

<sup>17</sup> C.C. RAGIN, *The comparative method: moving beyond qualitative and quantitative strategies*, Berkeley: University of California Press, 1987b., pp. 34-52.

observed in the statistical analysis are in some sense real and probable, and not the arbitrary results of measurement decisions. Comparative case studies deepen the investigation as a whole<sup>18</sup>.

Another reason that speaks in favour of a combined strategy is that it is more suitable for analysis on different levels. The research question draws attention to three levels of analysis, the sub-national level, the national level and the international level under a partial equilibrium. It pursues both internal and external validity. *Janoski* argues that a combined and more integrated methodological design is better suited for this type of analysis<sup>19</sup>. In the study the researcher will use a theory on asset and factor specificity to extract knowledge on interest groups from within the country. The theory at this level will be used to provide the causal mechanism that explains ‘changing levels of outcomes’ (sectoral) compared to state and international organisations centred theory used in the second step that refers to ‘different levels of outcome’ (national and international): ‘The internal analysis in the case studies produces data for the external analysis, and the internal analysis adds aspects of theory and evidence that the external analysis could not provide alone’<sup>20</sup>.

## 2.2. Selection of the Cases

Many two-level games analyses select their cases on the variance of an outcome. While attractive for purposes of analysis such approach amounts to sampling on the dependent variable. *Reverse reasoning* for reliable clarification after the outcome is established, is straightforward compared to selecting cases on variation in the independent variable. Selection of cases for study on the basis of outcomes, on the dependent variable, biases conclusions<sup>21</sup>. In the extreme case there may be no relation at all between independent and dependent variables: ‘One way the absence of a relationship may be in evidence is by the absence of change in the outcome variable’<sup>22</sup>. Selecting

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<sup>18</sup> C.C. RAGIN, Combined versus Synthetic Comparative Strategies, in: C. C. RAGIN, *The comparative method: moving beyond qualitative and quantitative strategies*, Berkeley: University of California Press, 1987a, pp. 69-84..

<sup>19</sup> T. JANOSKI, Synthetic Strategies, in: C. C. RAGIN, *Issues and alternatives in comparative social research*, Leiden: Brill, 1991, pp. 59-81., p 60. Internal versus external validity is also referred to the dichotomy of different research styles of a case- and variable-oriented analysis. Others, make reference to levels of analysis in comparative research. See A. PRZEWORSKI and H. TEUNE, *The logic of comparative social inquiry*, New York: Wiley-Interscience, 1970..

<sup>20</sup> T. JANOSKI, Synthetic Strategies, in: C. C. RAGIN, *Issues and alternatives in comparative social research*, Leiden: Brill, 1991, pp. 59-81., p. 71.

<sup>21</sup> B. GEDDENS, How The Case You Choose Affect the Answers You Get: Selection Bias in Comparative Politics, in: *Political Analysis*, 1990, 2, pp. 131-50., p. 131.

<sup>22</sup> J.A. CAPORASO, Across the Great Divide: Integrating Comparative and International Politics, in: *International Studies Quarterly*, 1997, 41(4), pp. 563-91., p. 571.

the cases for variation on the dependent variable reduces the number of outcomes that are consistent with the theory.

The reverse logic yields better results. Selecting observations for inclusion according to the categories of the key causal explanatory variable causes no inference problems<sup>23</sup>. I use the logic of *Mill's* comparative method and theory to choose sectors and countries. The study follows a most different system design (method of agreement) to choose the sectors and countries<sup>24</sup>. On a sub-national level most different sectors increase the leverage of the theory to be tested over the outcomes. On a cross-country level the opposite logic holds for the sectors while not for the countries as similar sectors will be compared across different countries. The most dissimilar design allows inference on the basis of specificity of different sectors on a country level; and the specificity of a country across similar sectors on a cross-country level<sup>25</sup>.

In contrast, a most similar system design encounters the problem of over-determination. It will fail to eliminate many rival hypotheses, leaving the researcher with no criteria for choosing among them. The most different system design based on a set of cases as diverse as possible in which the analyst traces similar processes of change forces the analyst to distil out of that diversity a set of common elements with great explanatory power<sup>26</sup>.

The phenomenon under investigation, TAs, refers to a universe of cases on two levels, i.e. sectors and countries. The universe of sectors and sectoral interests is infinite depending on the level of analysis and the definition of sectors. The number of observation ranges between three representing the structure of the economy (primary, secondary, and tertiary sectors) and an infinite number of sectors defined either by economic activity or output, i.e. product. On a country level the universe of the cases comprises 10 countries, i.e. the ten applicant countries. Under a partial equilibrium the EU is black boxed and held constant.

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<sup>23</sup> G. KING, R.O. KEOHANE and S. VERBA eds, *Designing social inquiry: scientific inference in qualitative research*, Princeton, N.J.: Princeton University Press, 1994., p. 137-138.

<sup>24</sup> V. BUNCE, *Subversive institutions: the design and the destruction of socialism and the state*, Cambridge, UK; New York: Cambridge University Press, 1999. Cases are not matched on the dependent variable. They are matched on the main explanatory variables.

<sup>25</sup> D. COLLIER, The Comparative Method: Two Decades of Change, in: D. A. RUSTOW and K. P. ERICKSON, *Comparative political dynamics: global research perspectives*, New York, NY: HarperCollins, 1991, pp. 7-31., pp. 16-17.

<sup>26</sup> A. PRZEWORSKI, Methods of Cross-National Research 1970-1983: An Overview, in: H. N. WEILER, A. B. ANTAL and M. DIERKES, *Comparative policy research: learning from experience*, Aldershot, Hants, England: Gower, 1987, pp.

The logic of a variable based approach and the statistical method requires that the entire universe of cases is taken into account to maximise control. If the universe becomes too large a representative sample should be drawn from it<sup>27</sup>.

In the variable oriented approach the constitution of negative cases, absence of TAs, is usually much more difficult than the constitutions of positive cases, TAs. Instead of clarifying and identifying instances of an empirical outcome, the researcher must identify relevant instances of its absence. Potentially this category is infinite, however, not for the present research since the widest possible population inevitably comprises negative cases. In the case oriented approach the position papers of the relevant countries clearly indicate where TPRs has been put forward. A comparison with the outcome TAs shows the positive/negative nature of the dependent variable (see cross sectional comparison, Part II). As a result, the constitution of positive cases provides clues for constituting negative cases. Thus, for the present research the specification of negative cases rests on the prior constitution of positive cases<sup>28</sup>.

### **2.2.1. Sectors**

Sectoral analysis requires strict definitions, classifications or concepts of economic sectors to prevent confusion when using quantitative and in particular qualitative data. When observing the political science and political economy literature sectoral definitions and conceptualisation are often implicitly assumed, discussed with a broad brush or absent. They are rarely explicitly mentioned. A strict conceptual idea of an economic sector prevents confusion between categories and subcategories particularly when moving up and down the ladder of abstraction; and when comparing output, employment, trade and firm level data across different statistical databases.

Economic sectors can be chosen according to several categories and definitions. The most basic categorisation is that of the three economic sectors in the economy, i.e. primary, secondary and

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<sup>27</sup> A. LIJPHART, The Comparable-Cases Strategy in Comparative Research, in: *Comparative Political Studies*, 1975, 8(2), pp. 158-77., p. 167; A. LIJPHART, Comparative Politics and the Comparative Method, in: *The American Political Science Review*, 1971, 65(3), pp. 682-93., pp. 686-688. Lijphardt defines the comparative method as the analysis of a small number of cases, entailing at least two observations, but less than about twenty.

<sup>28</sup> C.C. RAGIN, *Fuzzy-set social science*, Chicago: University of Chicago Press, 2000., pp. 60-61.

tertiary (agriculture, manufacturing and services)<sup>29</sup>. More sophisticated categories and definitions of economic sectors concern economic activity (NACE, CPA), product (CPC), occupation (ISCO) or a mix of the former based on the origin, the prevalent use, the providing institution and the required level of detail (ISIC, HS, SITC, NAICS and Prodcod from 1 to 8 digits). Correspondences between these different classification systems are established and regularly updated. I used NACE Rev. 1.1 and ISIC Rev.3.1 (1-3 digits) as the most basic categories using UN correspondences when the respective database required a different unit of observation (see also Introduction of Part II)<sup>30</sup>.

For sectoral interests a similar picture emerges. They are complex and crosscutting. Each sector can be divided in sub-sectors; each sub-sector can be further divided up to the level of the firm, specialisation or nature of the product<sup>31</sup>. The researcher particularly needs to pay attention to the use of qualitative data, including the use of interviews that pertain on political assets of economic sectors. For instance, does the analyst discuss the pharmaceutical sector or the chemical sector?; Or, does he deal with the manufacture of basic pharmaceutical products or the manufacture of pharmaceuticals, medicinal chemicals and botanical products? Quantitative data differ for each category and tend to do more so when pertaining to sectoral associations and trade unions. Does the association represent manufacturers of basic iron and steel; or manufactures of seamless steel pipes and tubes; or both? Does the trade union represent just steel workers or all the labourers in metallurgy, including those in engineering?

The quantitative analysis comprises the widest possible universe of sectors where TAs are presents across all 10 applicant countries. A sample from the universe of sectors serves the purpose of the qualitative analysis. The difficulty of tracing and understanding the relevant divisions and sectoral preferences calls for the use of as systematic an analytical method as possible to have a representative sample. Therefore, the theory of factor and asset specificity

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<sup>29</sup> OECD, Statistical Compendium; EIU, Country statistics; World Bank, World Development Indicators; Eurostat, National Country Data.

<sup>30</sup> The world matrix for sectoral economic data provides a good overview of the classification systems: [http://www.hwva.de/wmatrix/Technical\\_Description.html](http://www.hwva.de/wmatrix/Technical_Description.html); particularly useful is the UN website on classification systems at: <http://unstats.un.org/unsd/cr/registry/regct.asp?Lg=1>; For Eurostat see [http://ec.europa.eu/comm/eurostat/ramon/index.cfm?TargetUrl=DSP\\_PUB\\_WELC](http://ec.europa.eu/comm/eurostat/ramon/index.cfm?TargetUrl=DSP_PUB_WELC);

For a good overview of industry concordances see <http://www.macalester.edu/research/economics/PAGE/HAVEMAN/Trade.Resources/TradeConcordances.html> and the above mentioned UN website. For occupation classification look at: <http://www.ilo.org/public/english/bureau/stat/class/isco.htm>.

<sup>31</sup> See for more detail the UN Classification Registry at <http://unstats.un.org/unsd/cr/registry/default.asp?Lg=1>

describes the method used here to select the sectors. Moreover, sectors will be chosen from different structural economic sectors in the national economy to control for biases<sup>32</sup>. All sectors are confronted with EU enlargement.

Following the theory of factor/asset specificity the selection of the cases respects the variables indicating a degree of asset/factor specificity. Translating a degree of factor and asset specificity into a matrix with a two dimensional variance of high/low factor mobility and specificity the case selection becomes more clear-cut (see figure 6). The schematic reasoning indicates that sectors, firms and industries, find themselves in one of the four quadrants. They are likely to mobilise politically by an ordinal scale (1>2>3>4) when confronted by a changing economic environment, i.e. opening up the market under the EU enlargement process. Those with more specific factors are likely to engage in political action and tend to be better organised, i.e. asset specific, than those with less specific factors.

Because factor/asset specificity of capital and labour might have a different impact on our hypothesis (see selection of the independent variables), it is assumed that it will not affect the selection of the economic sectors, particularly if sectors are defined by output rather than factor endowments. In fact, blue-collar workers, technicians, managers, and owners of basic iron and steel works share an interest in the price of coal, even though they may be divided over how to allocate the returns to the firm among wages, salaries, and profits<sup>33</sup>.

To test the theory two sectors would suffice to explain as much possible with as little as possible<sup>34</sup>. One for quadrant (Q) 4 and one for Q1 given (1>2>3>4). Q1 and Q4 would guarantee that the variance on the degree of specificity would be sufficiently large to test the theory. An additional sector would not increase the leverage, unless Q1 and Q4 represent only capital and labour respectively as is the case. Therefore I selected a third sector that allows for more variance on either capital or labour in regard to asset and factor specificity.

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<sup>32</sup> The sectors are chosen on the basis of variables understood to be potential causes or effect of the dependent variable.

<sup>33</sup> J.A. FRIEDEN, *Debt, development and democracy: modern political economy and Latin America, 1965-1985*, Princeton, New Jersey: Princeton University Press, 1991., p. 31-32.

<sup>34</sup> G. KING, R.O. KEOHANE and S. VERBA eds, *Designing social inquiry: scientific inference in qualitative research*, Princeton, N.J.: Princeton University Press, 1994., p. 29.



A theory of asset/factor specificity will have diverse implications for labour and capital. For instance, in the steel sector capital might be highly factor/asset specific as it is completely tied to capital goods and location. Steel workers on the contrary might be relatively low on factor specificity, however, high on asset specificity. In other words, asset specificity might be related to the composition of skills<sup>35</sup>. Therefore this study would include a third sector.

**Figure 6: Factor Specificity, Asset specificity and Political Mobilisation**

capital/labour	high asset specificity	low asset specificity	
high specificity low factor mobility	1 pharmaceuticals capital steel capital	3 pharmaceuticals labour	high political mobilisation
low specificity high factor mobility	2 steel labour road transport capital	4 road transport labour	low political mobilisation
	high political mobilisation	low political mobilisation	

I propose to take three sectors: the pharmaceutical industry, basic iron and steel producers and international road transport sector. Steel and pharmaceuticals are overt in factor and asset specificity, and pharmaceuticals more so than steel. Following figure 6, it is assumed that the degree of factor and asset specificity is respectively lower for road transport compared to the basic iron and steel sector followed by the pharmaceutical industry respectively. Steel and pharmaceuticals producers are positioned in Q1, however, the relationship of labour in both sectors to asset specificity might be different. Labour in the steel sector is assumed to be lower on factor specificity, however, high on asset specificity. Labour in the pharmaceutical sector is assumed to be higher on factor specificity, yet, low on asset specificity. For the transport sector capital might be highly mobile but also specific to its current use depending on the nature of the

<sup>35</sup> T. IVERSEN and D. SOSKICE, An Asset Theory of Social Policy Preferences, in: *American Political Science Review*, 2001, 95(4), pp. 875-93., p. 875, p. 879.

company. The selection of sectors has several other advantages that might mitigate possible biases. Each sector represents a different part of the structure of the economy. Transport has a particular relevance for the service sector while our other two cases relate to heavy industry and manufacturing.

The pharmaceutical industry is complementary to steel and transport because of its internationalisation and tradition of collusion. The pharmaceutical industry tends to have a high degree of specificity on all levels. It depends on a highly skilled labour. High levels of research and development (R&D) indicate high levels of dedicated assets<sup>36</sup>. It is concentrated along company lines and in countries while not in others<sup>37</sup>. The largest producer of pharmaceuticals on the candidate countries side is Hungary and exceeds its neighbours in production. In Hungary, private investment dominated the market, while in neighbouring countries pharmaceutical industries were partly in state hands. This is useful as no evident patterns of insider status emerge in the applicant countries. The sector is highly relevant to the population at large in the realm of health care and is heavily regulated<sup>38</sup>. The EU-15 pharmaceutical industry has taken a tough stance on EU enlargement. Several applicant countries produced generic medicines and had low patent protection standards while having access to the EU market. Given the high sunk cost of the industry in R&D the sectoral organisation representing the pharmaceutical industry has politically mobilised on several occasions (see Chapter 3).

The steel sector represents the pinnacle of heavy industry. It is traditionally well known for its politicised nature in international trade, its problematic restructuring and its historical linkages to the EU. Steel tends to be site specific involving a lot of dedicated assets. Raw materials are important to its production. It has a high degree of dedicated assets<sup>39</sup>. The steel sector is concentrated in some countries, and more often in regions. It is highly concentrated in Poland, Slovakia and the Czech Republic. In the accession countries, the steel sector was still partly state owned and experienced a painful restructuring. It was heavily subsidised and had access to the

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<sup>36</sup> Global pharmaceutical expenditure on R&D was somewhat above US40bn in 2000., in: Survey on Pharmaceuticals, in: *Financial Times*, 30 April 2002. p. 11.

<sup>37</sup> Pharmaceutical companies consecutively rank among the top 50 largest companies in the world by value, by country, by sector, in: FT 500, in: *Financial Times*, 10 May 2002. p. 6.

<sup>38</sup> *Financial Times*, Survey on Pharmaceuticals, 30 April 2002.

<sup>39</sup> See OECD, Iron and steel outlook, The steel Market in 1997-1998, OECD, Paris CEDEX; OECD Steel Committee, 2000, Paris Cedex, Iron and Steel Industry in 1998, enterprises and industry.

European single market, which created conflicts between producers. These characteristics point out obvious insider status of the steel sector in the candidate countries. The steel sector compared to pharmaceuticals and international road transport is interesting because the role of labour was more pronounced particularly given the varying levels of the restructuring process in Hungary, the Czech Republic and Poland and Slovakia (see Chapter 4).

Cross country comparison reveals both similarities and differences in the road transport sector. The transport sector operated in heavy regulated national and international markets with pervasive international linkages, hence the influence of supranational interests. Despite their low factor specificity the assets of road transporters are highly developed. Because of the international outlook they were well informed about the enlargement process. The sector was almost entirely in private hands, except in Hungary. In contrast to steel and pharmaceuticals its market is highly fragmented both for labour and capital in the Czech Republic, Poland and Slovakia but less so in Hungary. The Hungarian freighters were competing in their exports markets (see Chapter 5) with the Czech, Polish and Slovak truckers dominating their respective international market.

### **2.2.2. States**

Cases need to be carefully selected and the criteria for grouping them together made explicit. There must be sufficient similarities to allow the case to be grouped together for a comparative analysis<sup>40</sup>. Cases can be chosen as basically similar examples in the transition and EU enlargement processes. All applicant states went through a transition process from Communism to a market economy between 1989 and 1998 with the exception of Cyprus and Malta. The economies of Central and Eastern Europe experienced a production crunch immediate after the changeover which lasted broadly up to the mid 1990s. All embarked on a privatisation process although with different strategies. Between 1993 and 1996 they all applied for EU membership – Malta re-activated its 1990 application in September 1998, which was frozen in 1996. They all commenced the EU accession negotiations between March 1998 and February 2000. They are most similar for the purpose of answering the research questions.

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<sup>40</sup> T. SKOCPOL, in: *States and social revolutions : a comparative analysis of France, Russia, and China*, Cambridge; New York: Cambridge University Press, 1979, pp., p. 40, 41, 42.

However, for the purpose of design it is useful to select countries on the basis of the method of agreement because in the cross sectional comparisons similar sectors are compared across different countries. Selecting countries on the basis of the method of agreement provides more explanatory power over the outcomes. The examination of two or more cases in order to highlight the common elements for the variable and case-based sets the framework for interpreting the way similar processes of change play out within different contexts. This contrast of contexts is more central to the more interpretative side of the study<sup>41</sup>.

#### **2.2.2.1. The Applicants and the EU**

I choose countries according to Mill's method of agreement. The general reference frame constitutes the candidate countries and the EU. For the applicant countries the universe of cases comprises Cyprus, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovakia and Slovenia. The selection follows relative economic size, the degree of concentration and insider status of the sectors to control for possible biases.

Poland, the Slovak and Czech Republics and Hungary are interesting for the steel sector. Steel is concentrated regionally, it was largely state owned in the Czech Republic, Hungary and Poland, while it was in private hands in the Slovak Republic. In Hungary the steel industry is smaller. For similar reasons Poland and Hungary are pertinent for pharmaceuticals which is less the case in the Czech Republic and Slovakia. Finally, road transport tends to be evenly spread over all the countries, although more fragmented in the Czech Republic, Poland and Slovakia.

On a country level it might be useful to see whether national preferences and strategies at the international negotiating table differ over similar sectors. Therefore I control for economic size and population. More importantly I control for progress in the negotiations. Slovakia was part of the less advanced countries applying for EU membership. In December 1997 the Luxembourg European Council agreed to open accession negotiations with the Czech Republic, Estonia, Hungary, Poland, Slovenia and Cyprus. The *Luxembourg Six* started negotiating the terms of EU enlargement at the end of March 1998. The Helsinki European Council in December 1999 agreed

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<sup>41</sup> D. COLLIER, *The Comparative Method: Two Decades of Change*, in: D. A. RUSTOW and K. P. ERICKSON, *Comparative political dynamics: global research perspectives*, New York, NY: HarperCollins, 1991, pp. 7-31.

to open negotiations with a further six countries, i.e. Bulgaria, Latvia, Lithuania, Romania, Slovakia and Malta. The *Helsinki Six* commenced the negotiations in February 2000.

Because this study is concerned with the variation of TAs in the applicant states it opted for a partial equilibrium. The EU as a unit is held constant and black boxed throughout the study. I only touch upon the EUs internal decision-making process in Chapter 7 to describe its common position at the international negotiating table; and the concepts of pivots or break point countries (see Chapter 7).

#### **2.2.4. Time Dimension**

Data on sectors provide a snapshot of instances of structural processes. Structural features and their interrelations can be represented in terms of variables and inter-correlations. By studying the patterns that emerge from such a snapshot of structural processes (that is by studying correlations between variables), it is possible to derive empirical generalisations about structural processes relevant to large numbers of macro-social units (sectors and countries).

The study focuses on the period 1998-2003 during which the accession negotiation took place. Given the particular nature of the transition process in the future member states, snap shot measurement of quantitative data over these years could cause bias. It could provide for a partial picture, particularly in regard to factor and asset specificity.

Factor and asset specificity were highly relevant concepts in the applicant states due to the reform processes underway. The economic reform process coincided with the productivity crunch immediately after the economic transition took off in the early 1990s. Afterwards the economy embarked upon a gradual modernisation<sup>42</sup>. As a result, some sectors are still recovering while others are going through restructuring; and still others are well on their way to become global competitors. A snapshot would therefore provide a biased picture of the state of certain sectors. Hence, it would be prudent to normalise the data for the years 1989-2003.

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<sup>42</sup> P. BOONE, S. GOMULKA and P.R.G. LAYARD eds, *Emerging from communism: lessons from Russia, China and Eastern Europe*, Cambridge, Mass.: MIT Press, 1998.

## 2.3. Operationalisation and Specification of the Variables

### 2.3.1. Dependent Variable

TAs are the dependent variable. They are an indicator that tells us something about the EU enlargement process, interest groups in the applicant states, the applicant states' preferences at the negotiating table and their negotiation strategies. Taking TAs as an independent variable allows us to test rigorously the nine hypotheses from Chapter 1. An accurate test of theoretically informed hypotheses under clear assumptions has been rare in the enlargement literature.

The EC presented TAs along 31 administrative Chapters of the *acquis*, such as competition or taxation policy (see Annex 1). Their presentation is misleading. The structure of the *acquis communautaire* is different from the Chapters presented in the EU accession negotiations. The *acquis* refers to the Treaties on the EU while in the enlargement negotiations the *acquis* is structured along chapters for the purpose of transparency and clarity.

One TA might have a broader impact than the chapter in which it has been negotiated. For instance, a TA can have an impact on a specific economic sector, such as a tariff and quota for the steel industry. I call TAs that exclusively affect an economic sector vertical TAs. Some TAs can have a partial impact on the economy because they apply to an administrative area rather than sectors. Examples are regional state aid or tax holidays in geographically defined economic zones. I call these horizontal or cross sectoral TAs.

Because of the different effects and impact horizontal and vertical TAs have on the economy they are difficult to quantify and compare. It is far from straightforward to quantify and measure sectoral and cross sectoral TAs under an equivalent indicator that represents its uniform variation across all countries<sup>43</sup>. One of the problems that occur when quantifying horizontal and vertical TAs is that they might affect similar sectors. For instance, an economic sector might receive a vertical TA that concerns a regulation, a tax holiday, a subsidy, or quotas and tariffs. The sector might also benefit from a horizontal TA in the form of regional fiscal state aid or a tax exemption. To compare both types of TAs one requires detailed firm level data in the countries

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<sup>43</sup> Other authors have encountered similar difficulties. For instance see F. MCGILLIVRAY, *Privileging industry: the comparative politics of trade and industrial policy*, Princeton, N.J.: Princeton University Press, 2004., pp. 32-35.

studied, which is not available for the universe of our cases and goes beyond the scope of the present study. Therefore, this study categorises TAs in two groups: vertical and horizontal TAs.

### **Sectoral TAs**

A sectoral or vertical TA is a temporary exemption from the *acquis communautaire* that has a direct impact on an industry or sector defined by economic activity, output or product such as the construction or automobile sector for example. The coding of the TAs represented in Table 5, 6 and 7 and Figure 7 is the broadest possible population across all ten candidate countries. In table 1 the 47 sectors represent the broadest possible population by economic sector defined according to economic activity following the NACE revision 1.1. classification of up to three digits for all the ten applicant countries<sup>44</sup>.

The 292 TAs counted by chapter of the *acquis* (see Annex 1) correspond to 325 TAs across 10 countries in 47 sectors (see table 5-7 and figure 7) plus those defined as horizontal TAs (see Table 8).

For the 470 observations (47 sectors x 10 countries) Figure 5 shows that TAs in the ten applicant states cover the primary, secondary as well as the service sector. The distribution among the applicant states across all 47 sectors is skewed towards the agricultural sector followed by utilities and land transport.

Poland and Malta obtained most TAs among the applicant countries followed by Latvia, the Czech Republic, Hungary and Lithuania, Cyprus, Estonia, Slovakia and Slovenia respectively (see Figure 8). Adding up the number of TAs does not enhance our understanding of the dependent variable. I coded TAs according to a variety of measures, i.e. by form, duration and country effect, to increase the analytical breath for analysing the dependent variable.

**Form:** TAs are categorised by substance following four criteria, i.e. regulation, taxation, subsidy, and tariffs and quotas (see Table 7). Of the total 325 TAs coded by economic sector 72.9 per cent concern regulations that directly affect one of the 47 sectors of table 1. Only 14.1 per cent concern tax measures with subsidies, and tariffs and quotas taking account for just 6.8 and 6.1 per cent. The least overt means of TAs, i.e. exemptions by regulation, prevail.

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<sup>44</sup> NACE or Classification of Economic Activities in the European Community

**Duration:** TAs are measured according to the number of years they are meant to last. One TA of 10 years is assumed to be more important to its beneficiary than one lasting just one year. Hence, TAs are multiplied according to the number of years (1=1 up to 10, >10=15, derogation=20). The descriptive statistics for TAs weighed by duration, frequency and variation of the dependent variable per country are presented in Table 5 and Figure 9 and 10. Poland and Malta continue to dominate the ten applicant countries followed by the Czech Republic, Hungary, Cyprus, Slovakia, Latvia, Slovenia, Estonia and Lithuania. The frequencies of TAs by duration per sector are presented in Figure 10 and show a declining dominance of agriculture overall with manufacturing, transport and utilities benefiting most from their presence.

**Country:** TAs are measured according to a country effect using a coverage ratio. The coverage ratio is defined as the share of the national GDP that is exempted from the acquis at the point of EU entry. It is a figure between 1 and 0 (see Figure 11) that provides an indication of the proportion of the economy affected by sectoral TAs. Based on Eurostat figures it is calculated as follows:

$$\text{Coverage ratio} = \sum_i l_i * GVA_i / \text{GDP}$$

The coverage ratio is probably the most accurate of all measures that provides an idea about the country effect. According to figure 11 Malta clearly emerges as the applicant country with at least 45.9 per cent of its economy exempted from one or another piece of EU legislation upon EU entry. It is followed by Poland with almost 33 per cent of its GDP. Slovenia (26.5 per cent) is third followed by Latvia (25.93 per cent), Czech Republic (13.3 per cent), Cyprus (11.86 per cent), Hungary (11.02 per cent), Estonia (10.86 per cent), Slovakia (8.7 per cent) and Lithuania (8 per cent).

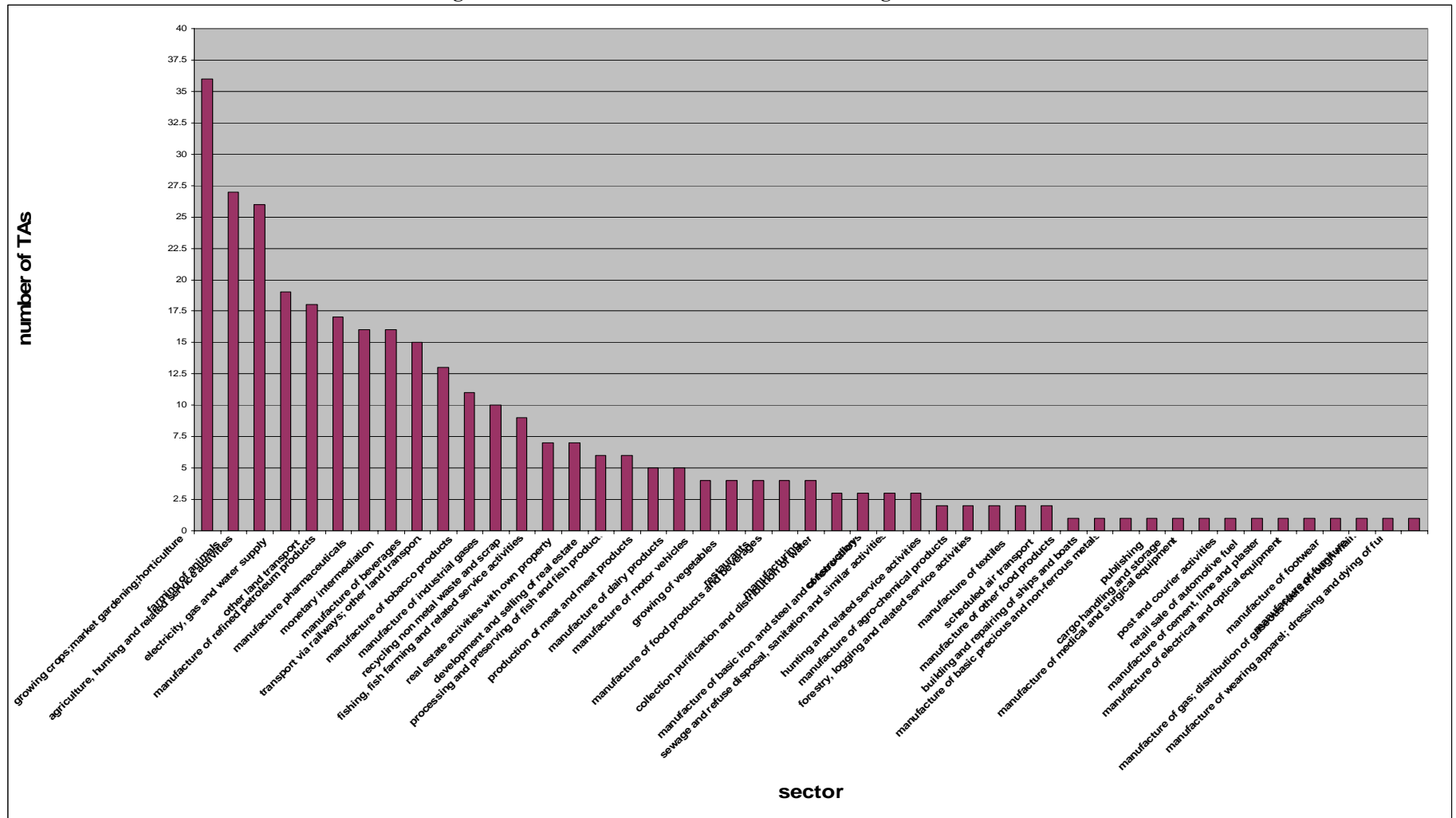


**Table 5: Vertical TAs per Sector and Country (NACE Rev 1.1.)**

sector nr.	sector (NACE rev. 1.1/1-3 digits)	Cyprus	Czech R.	Estonia	Hungary	Latvia	Lithuania	Malta	Poland	Slovakia	Slovenia	Total
1	agriculture, hunting and related service activities	4	0	3	0	6	4	7	0	0	2	26
2	building and repairing of ships and boats	0	0	0	0	0	0	1	0	0	0	1
3	cargo handling and storage	0	0	0	0	0	0	0	0	1	0	1
4	collection purification and distribution of water	0	0	1	0	1	0	1	0	0	0	3
5	construction	0	1	0	0	0	0	0	0	1	1	3
6	development and selling of real estate	1	1	0	1	0	0	1	1	0	1	6
7	electricity, gas and water supply	1	2	6	2	2	1	1	2	2	0	19
8	farming of animals	1	2	1	2	4	4	4	6	0	3	27
9	fishing, fish farming and related service activities	0	0	1	0	2	0	3	1	0	0	7
10	forestry, logging and related service activities	1	0	0	0	0	0	0	1	0	0	2
11	growing crops;market gardening;horticulture	6	5	0	4	1	2	2	9	3	4	36
12	growing of vegetables, horticulture specialities and nursery products	0	1	0	0	0	1	1	1	0	0	4
13	hunting, trapping and game propagation, including related service activities	0	0	1	0	0	0	1	0	0	0	2
14	manufacture of basic iron and steel and of ferro-alloys	0	1	0	0	0	0	0	1	1	0	3
15	manufacture of basic precious and non-ferrous metals	0	0	0	1	0	0	0	0	0	0	1
16	manufacture of beverages	0	6	0	3	0	0	2	1	2	1	15
17	manufacture of cement, lime and plaster	1	0	0	0	0	0	0	0	0	0	1
18	manufacture of dairy products	0	0	1	0	0	1	1	2	0	0	5
19	manufacture of electrical and optical equipment	0	0	0	0	0	0	1	0	0	0	1
20	manufacture of food products and beverages	1	0	0	0	0	0	2	1	0	0	4
21	manufacture of footwear	0	0	0	0	0	0	1	0	0	0	1
22	manufacture of furniture	0	0	0	0	0	0	1	0	0	0	1
23	manufacture of gas; distribution of gaseous fuels through mains	0	1	0	0	0	0	0	0	0	0	1
24	manufacture of industrial gases	1	1	1	1	1	1	1	1	1	1	10
25	manufacture of medical and surgical equipment and orthopaedic appliances	0	0	0	0	0	0	0	1	0	0	1
26	manufacture of motor vehicles	0	0	0	1	0	0	1	1	1	0	4
27	manufacture of other food products	0	0	0	0	0	0	1	0	0	0	1
28	manufacture of pesticides and other agro-chemical products	1	0	0	0	0	0	0	1	0	0	2
29	manufacture of pharmaceuticals, medicinal chemicals and botanical products	2	1	1	1	1	2	3	2	1	2	16
30	manufacture of refined petroleum products	2	1	2	0	2	2	2	3	2	1	17
31	manufacture of textiles	0	0	0	0	0	0	2	0	0	0	2
32	manufacture of tobacco products	0	2	2	1	1	1	0	2	1	1	11
33	manufacture of wearing apparel; dressing and dying of fur	0	0	0	0	0	0	1	0	0	0	1
34	manufacturing	0	0	0	0	1	0	1	1	0	1	4
35	monetary intermediation	1	0	2	3	2	2	0	2	1	3	16
36	other land transport	1	1	1	2	3	3	4	2	1	0	18
37	post and courier activities	0	0	0	0	0	0	0	1	0	0	1
38	processing and preserving of fish and fish products	0	1	0	0	1	1	0	2	1	0	6
39	production, processing and preserving of meat and meat products	0	1	0	1	1	1	0	0	1	0	5
40	publishing	0	0	0	0	0	0	0	1	0	0	1
41	real estate activities with own property	0	1	1	1	1	1	0	1	1	0	7
42	recycling non metal waste and scrap	0	0	1	1	2	0	0	2	2	1	9
43	restaurants	1	0	0	1	0	0	0	1	0	1	4
44	sale, maintenance and repair of motor vehicles and motorcycles; retail sale of automotive fuel	0	0	0	0	0	0	1	0	0	0	1
45	scheduled air transport	0	0	0	1	0	1	0	0	0	0	2
46	sewage and refuse disposal, sanitation and similar activities	0	0	0	0	0	0	1	1	1	0	3
47	transport via railways; other land transport	2	1	1	2	1	1	1	2	1	1	13
	Total	27	30	26	29	33	29	49	53	25	24	325

Source: Own calculation based on EU Accession Treaties with Cyprus, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovakia and Slovenia, Brussels, 2003.

Figure 7: Number of Sectoral Transitional Arrangements



Source: Own calculation based on EU Accession Treaties with Cyprus, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovakia and Slovenia, Brussels, 2003.

**Table 6: TAs per country and sector weighed by duration**

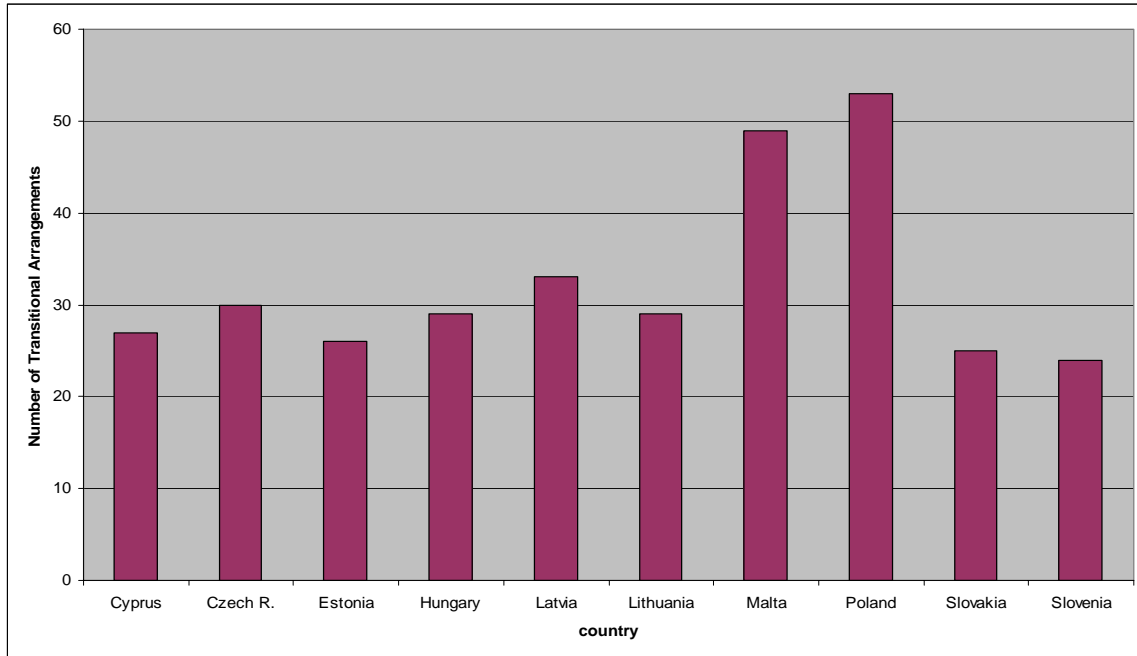
Variables	N	Minimum	Maximum	Mean	Std. Deviation
candidate countries	470	1	10		
economic sectors (Nace rev. 1.1 up to 1-3 digits)	470	1	47		
Presence/Absence TA	470	0	1		
Total nr. of TAs per country	470	24	53	32.50	9.625
Total nr. of TAs per country weighed by duration	470	178	391	254.20	66.954
Total nr. of TAs per sector	470	1	36	6.97	8.006
Total nr. of TAs per sector weighed by duration	470	1	595	54.09	99.178
Total nr. of TAs per sector and country	470	0	9	.69	1.159
Total nr. of TAs per country and sector weighed by time	470	0	120	5.41	13.416
Valid N (listwise)	470				

**Table 7: Sectoral TAs by Substance**

sector nr.	sector (NACE rev. 1.1/1-3 digits)	regulation	taxation	subsidy	tariffs and Quotas	total
1	agriculture, hunting and related service activities	17	0	9	0	26
2	building and repairing of ships and boats	0	0	1	0	1
3	cargo handling and storage	0	0	1	0	1
4	collection purification and distribution of water	3	0	0	0	3
5	construction	0	3	0	0	3
6	development and selling of real estate	6	0	0	0	6
7	electricity, gas and water supply	15	4	0	0	19
8	farming of animals	25	0	0	2	27
9	fishing, fish farming and related service activities	5	0	0	2	7
10	forestry, logging and related service activities	2	0	0	0	2
11	growing crops;market gardening;horticulture	31	1	2	2	36
12	growing of vegetables, horticulture specialities and nursery products	3	0	1	0	4
13	hunting, trapping and game propagation, including related service activities	2	0	0	0	2
14	manufacture of basic iron and steel and of ferro-alloys	0	0	3	0	3
15	manufacture of basic precious and non-ferrous metals	0	0	0	1	1
16	manufacture of beverages	12	3	0	0	15
17	manufacture of cement, lime and plaster	0	1	0	0	1
18	manufacture of dairy products	3	0	2	0	5
19	manufacture of electrical and optical equipment	1	0	0	0	1
20	manufacture of food products and beverages	1	3	0	0	4
21	manufacture of footwear	1	0	0	0	1
22	manufacture of furniture	1	0	0	0	1
23	manufacture of gas; distribution of gaseous fuels through mains	1	0	0	0	1
24	manufacture of industrial gases	0	0	0	10	10
25	manufacture of medical and surgical equipment and orthopaedic appliances	1	0	0	0	1
26	manufacture of motor vehicles	1	0	3	0	4
27	manufacture of other food products	1	0	0	0	1
28	manufacture of pesticides and other agro-chemical products	0	2	0	0	2
29	manufacture of pharmaceuticals, medicinal chemicals and botanical products	15	1	0	0	16
30	manufacture of refined petroleum products	17	0	0	0	17
31	manufacture of textiles	1	0	0	1	2
32	manufacture of tobacco products	1	10	0	0	11
33	manufacture of wearing apparel; dressing and dyeing of fur	1	0	0	0	1
34	manufacturing	4	0	0	0	4
35	monetary intermediation	16	0	0	0	16
36	other land transport	16	2	0	0	18
37	post and courier activities	1	0	0	0	1
38	processing and preserving of fish and fish products	6	0	0	0	6
39	production, processing and preserving of meat and meat products	5	0	0	0	5
40	publishing	0	1	0	0	1
41	real estate activities with own property	7	0	0	0	7
42	recycling non metal waste and scrap	9	0	0	0	9
43	restaurants	0	4	0	0	4
44	sale, maintenance and repair of motor vehicles and motorcycles; retail sale of automotive fuel	0	0	0	1	1
45	scheduled air transport	2	0	0	0	2
46	sewage and refuse disposal, sanitation and similar activities	3	0	0	0	3
47	transport via railways; other land transport	1	11	0	1	13
	total	237	46	22	20	325

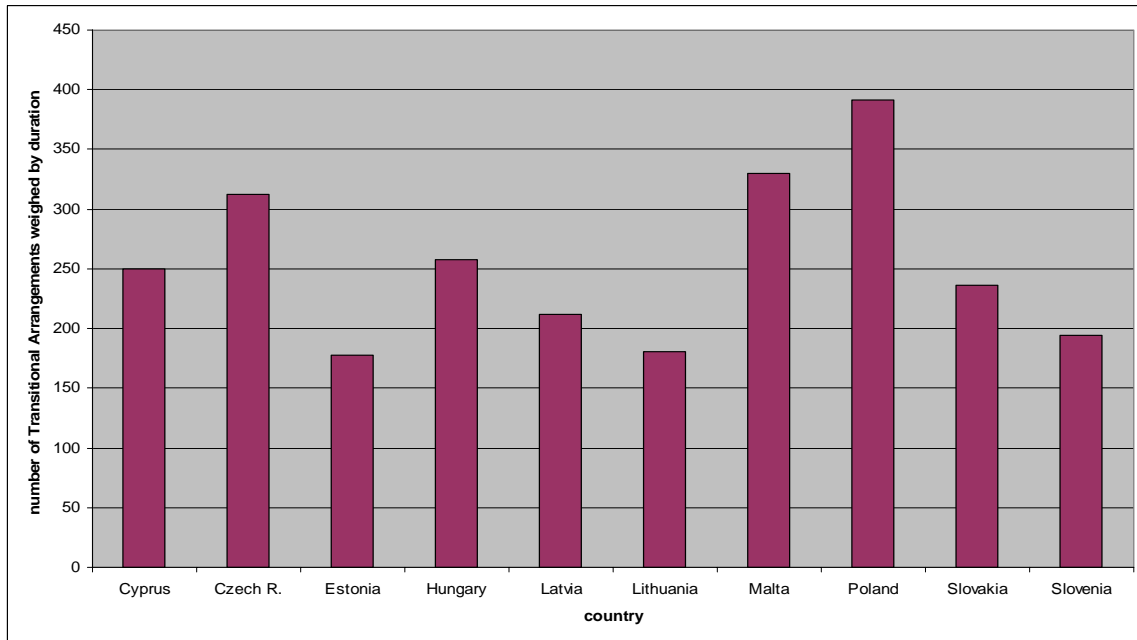
Source: Own calculation based on EU Accession Treaties with Cyprus, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovakia and Slovenia, Brussels, 2003.

**Figure 8: Number of TAs by Country**



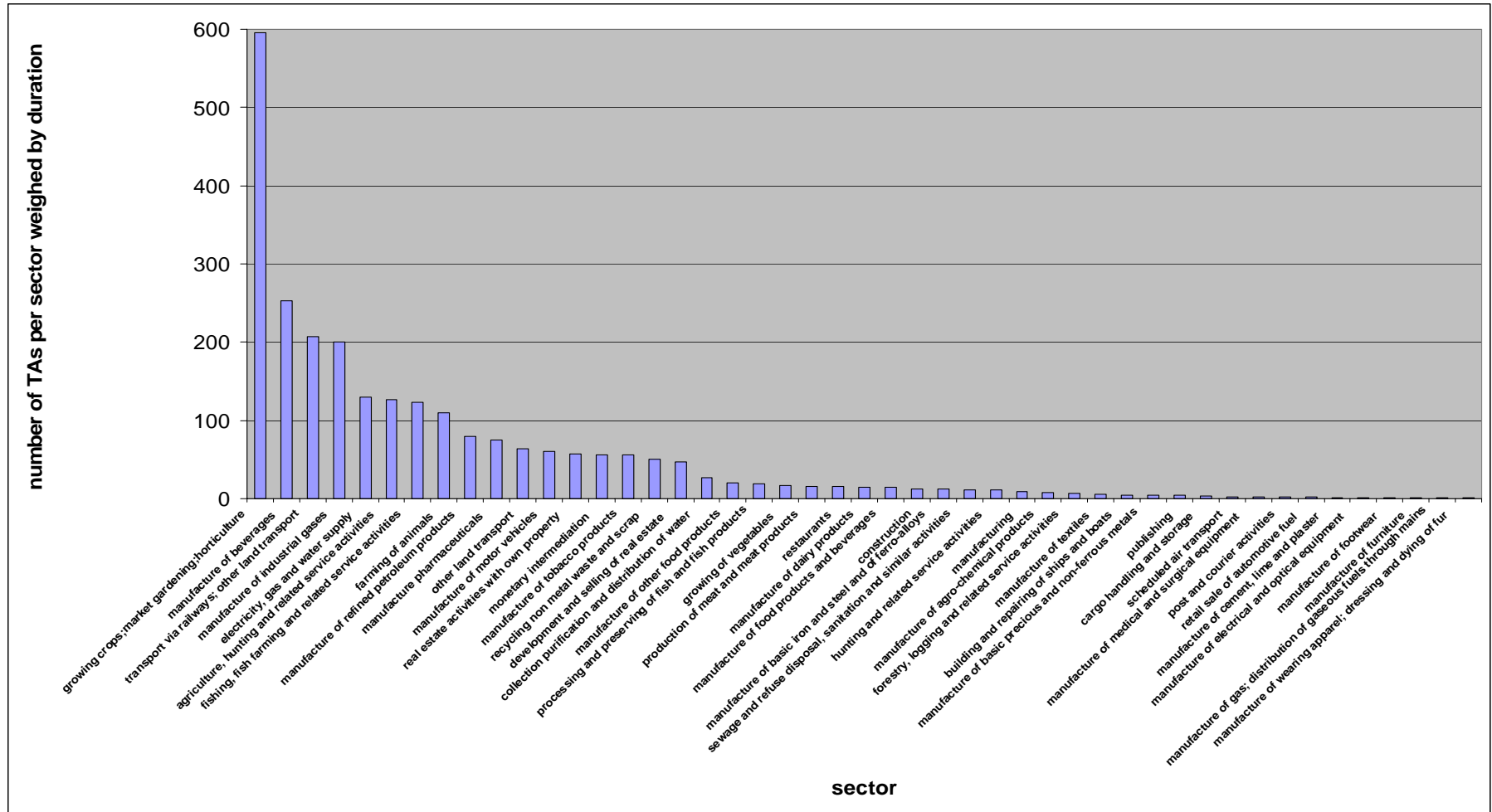
Source: Own calculation based on EU Accession Treaties with Cyprus, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovakia and Slovenia, Brussels, 2003.

**Figure 9: Number of TAs Weighed by Duration and by Country**



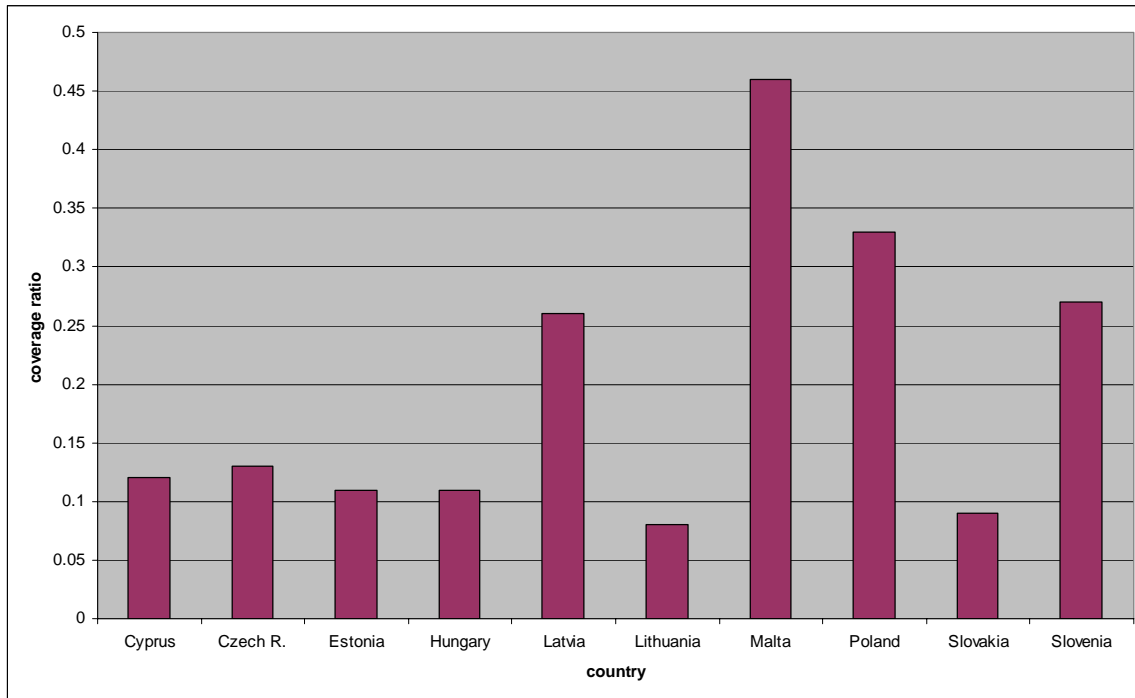
Source: Own calculation based on EU Accession Treaties with Cyprus, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovakia and Slovenia, Brussels, 2003.

Figure 10: Number of TAs per Sector Weighed by Duration



Source: Own calculation based on EU Accession Treaties with Cyprus, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovakia and Slovenia, Brussels, 2003.

**Figure 11: National Coverage Ratio (per cent of the economy affected by TAs)**



Source: Own calculation (Coverage ratio =  $\sum_i I_i * GVA_i / GDP$  with  $GVA_i$  from Eurostat detailed enterprise indicators normalised for the years 1998-2002 ) based on EU Accession Treaties with Cyprus, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovakia and Slovenia, Brussels, 2003.

### **Horizontal TAs**

A horizontal or cross sectoral TA is a temporary exemptions from the *acquis communautaire* that has a direct or indirect impact on an administrative part or section of the economy it is applied to. Examples are regional state aid, regional tax holidays, or the exemption from the application of regional environmental legislation for small and medium sized enterprises. I have coded the horizontal TAs according to nine different categories present in the accession Treaties for the countries to which they apply (see table 2). Because of methodological difficulties I have excluded horizontal from this research.

**Table 8: Cross sectoral or Horizontal TAs by Domain and Country**

Cross Sectional or Horizontal Tas	Cyprus	Czech R.	Estonia	Hungary	Latvia	Lithuania	Malta	Poland	Slovakia
Incompatible fiscal state aid for small and medium-sized enterprises by the end of 2011				x			x		
incomptatible fiscal state aid for small enterprises by the end of 2011								x	
incompatible fiscal state aid for medium sized enterprises by the end of 2011								x	
incompatible fiscal state aid for offshore companies by the end of 2005				x					
state aid granted by local authorities end 2005	x			x					
Operating aid under the business promotion act end 2008							x		
Conversion of incompatible fiscal state aid for large companies into regional investment aid (1)				x			x	x	
Environmental protection within the context of competition policy (2)								x	
Lower VAT levels for SMEs	x	x	x	x	x	x	x	x	x

Source: Own Compilation, EU, Accession Treaties with Cyprus, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovakia and Slovenia, Brussels, 2003.

Note: (1) - 75 % of the eligible investment costs if a company has started the investment/obtained the entitlement for the tax exemption before 1 January 2000.

- 50% if the company has started the investment/obtained the entitlement for the tax exemption after 1 January 2000.

(2) - Poland receives extra measures to 2010 and 2007.

### **2.3.2. Demand Side: Independent Variables**

To test the hypothesis on the demand side of the theoretical framework I make use of both quantitative and qualitative analysis. The indicators for pharmaceuticals, the basic iron and steel industry and the international road freight transport sectors for the quantitative test return in the case based analysis of Part II. The quantitative analysis (see Chapter 2, section 2.4. statistical analysis) is based on the measurement of three concepts approximated by 10 different indicators. The qualitative analysis evaluates seven concepts on the basis 15 indicators followed throughout Part II, chapters 3, 4 and 5.

The qualitative analysis includes 88 positional and structured interviews (see Annex 4 and 5). I supplemented interview data with sector specific literature, press articles on contemporary and retrospective market analysis, political commentary and scholarly studies on the sectors in the enlargement process.

#### **2.3.2.1. Factor and Asset specificity**

##### **Quantitative Indicators**

The measurement of asset specificity takes into account four different sources of specificity at a variety of levels of aggregation<sup>45</sup>.

##### **Trade Balance**

Usually the economic forces driving lobbying activity are inferred from the evolution of *import penetration ratios*, i.e. the share of imports in total domestic demand. Import penetration ratios are a proxy for policy preference and the likelihood of political mobilisation. For the period 1992-2004 output data are not available or comparable within and across industries for the V-4 countries. Industrial output, sales and market share and consumption data are limited and incomplete. It poses questions about the detailed basis of policy formation in the Central European countries over those years (I discuss the availability of data and sectoral enlargement impact studies in more detail in Chapter 6). It also is unpractical to record the sectoral *policy*

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<sup>45</sup> O.E. WILLIAMSON, Credible Commitments: Using Hostages to Support Exchange, in: *The American Economic Review*, 1983, 73(4), pp. 519-40.; P.L. JOSKOW, Asset Specificity and the Structure of Vertical Relationships: Empirical Evidence, in: *Journal of Law, Economics, & Organization*, 1988, 4(1), pp. 95-117., p. 107; J.E. ALT, *et al.*, The political Economy of International Trade, Enduring Puzzles and an agenda for Inquiry, in: *Comparative Political Studies*, December 1996, Vol. 29(6), pp. pp. 689-717., p. 705.



stance by country or association for 47 sectors across 10 countries. For similar reasons I excluded *expert surveys*<sup>46</sup>.

To remedy the lack of the aforementioned data I rely on indirect measures based on sectoral *trade balance*. I assume that unfavourable sectoral trade patterns, i.e. comparative disadvantage and advantage sectors, provide an indication of the sectors' preference. Sectors characterised by a comparative disadvantage are likely to be more inclined to have a protectionist policy stance than those experiencing a comparative advantage. The reasoning is in analogy to *Mayda* and *Rodrik's* argument. They find that people in comparative disadvantage sectors are likely to be more protectionist than those in comparative advantage sectors. The finding is supportive of a sector specific factors models<sup>47</sup>. Moreover, sectors that position themselves in export markets are likely to hold stronger preferences over EU enlargement than those exclusively focussed on the domestic market. They are likely to be better informed as the economic impact of enlargement is more forthcoming. As a result, they are also assumed to exert more political pressure.

It is possible to use trade data to define the 47 sectors of the dependent variable in terms of comparative advantage, comparative disadvantage and non-tradable sectors. The indicator exposes winners and losers in EU enlargement process. Losers from enlargement are likely to lobby more than winners, a phenomenon called asymmetric lobbying<sup>48</sup>.

Trade figures come from Eurostat's External Trade data base according to SITC Rev. 3 nomenclature obtained. I recoded the 47 economic sectors (table 1) for which TAs were obtained in at least one of all ten candidate countries (470 national sectors)<sup>49</sup>. I recoded the economic sectors by economic activity from NACE Rev. 1.1 (up to 3-digit level) into SITC Rev. 3 product codes in order to match the coding of Eurostat's External Trade database, containing trade flows from 1995 to 2005. The recoding of NACE Rev. 1.1 into SITC Rev. 3 followed United Nations

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<sup>46</sup> Regardless of OECD membership for the Czech Republic (1995), Hungary (1996), Poland (1996) and Slovakia (2000) the OECD's statistical compendium only lists consistent output data from 2000 onwards with the exception for the basic iron and steel industry. Import penetration ratios are only available for pharmaceuticals from 1998 onwards and are absent for Slovakia. Eurostat's applicant country statistics do not provide comparable output data on steel and pharmaceuticals. Output or domestic production data by the EU's prodcom codes only start in 2002 for the applicant states. The number of missing values is high. Trade data are available throughout the period in the Eurostat database.

<sup>47</sup> A.M. MAYDA and D. RODRIK, *Why are some people (and countries) more protectionist than others?*, London: Centre for Economic Policy Research, 2001., pp. 16-20.

<sup>48</sup> R.E. BALDWIN, *Towards an integrated Europe*, London: Centre for Economic Policy Research, 1994., pp. 71-72.

<sup>49</sup> Eurostat, EU Trade since 1995 by SITC, Luxembourg, 2005. The figures are to be found on Eurostat's website: <http://fd.comext.eurostat.cec.eu.int/xtweb/>. The trade figures for all 47 sectors and ten candidate countries were taken from EU intra and extra EU-15 trade expressed in euro for the years 1998-2003 and controlled by trade balance.

correspondences with intermediate steps from NACE Rev. 1.1 into CPC Ver. 1.1 then into HS 2002 and finally into SITC Rev. 3<sup>50</sup>.

As a result, I found sector-specific trade values in euro. For each new code, exports (imports) are the sum of exports (imports) of the sectors in the combination matching the NACE rev. 1.1 code. For example, exports of sector nr. 2 (building and repairing of ships and boats) according to economic activity (NACE Rev 1.1) equal to the sum of the exports of all corresponding products (essentially different types of boats and ships) under SITC Rev. 3.

Because of strong fluctuations and missing data of sectoral trade figures due to the transition process imports and exports are normalised per sector and country over the years 1998-2003. This results in respectively 32 and 33 (partly overlapping) sectors with trade figures for commerce between the candidate countries and the world, and with the EU-15. To eliminate the country effect I normalised all the trade figures per country. Subsequently, I treat the sectors with missing trade variable (non-manufacturing industries) as non-tradables (NT)<sup>51</sup>. I define two sector-specific variables, CA (comparative advantage sector) and CD (comparative disadvantage sector) for each sector correlated by trade balance as follows:

$$\begin{aligned} CA &= 0 \text{ if } \text{Exp} - \text{Imp} < 0 \text{ and } CA = 1 \text{ if } \text{Exp} - \text{Imp} > 0 \\ CD &= 0 \text{ if } \text{Exp} - \text{Imp} < 0 \text{ and } CD = 1 \text{ if } \text{Exp} - \text{Imp} > 0 \end{aligned}$$

A sector is defined as a comparative advantage sector if its adjusted net imports are less than zero; and as a comparative disadvantage sector if its adjusted net imports are greater than zero. Each individual sector per country is therefore assigned to one of three types (NT, CA, CD) for trade with the world and trade with the EU-15.

In Part II of the dissertation these data are cross checked by looking at the policy stance of the corresponding assets by country for each of our case studies, i.e. pharmaceuticals and steel producers and road haulage in the Czech Republic, Hungary, Poland and Slovakia.

## R&D, Investment and Skills

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<sup>50</sup> <http://unstats.un.org/unsd/cr/registry/regot.asp?Lg=1>

<sup>51</sup> I essentially followed a similar logic to A.M. MAYDA and D. RODRIK, *Why are some people (and countries) more protectionist than others?*, London: Centre for Economic Policy Research, 2001., pp. 17-18 and Appendix II p.33.

The test the hypotheses on asset specificity I propose the use of three measures, i.e. R&D, investment and human specificity or the sectoral skill level of labour.

*R&D* refers to physical asset specificity and is a proxy for the ability of an industry to capture quasi rents based on physical design characteristics. Physical specificity refers to investments that involve design characteristics specific to particular transactions Economists and political scientists have traditionally understood that R&D intensity creates asset specificity because firms that sell products with close substitutes are likely to do less R&D<sup>52</sup>. The firms that invest heavily in R&D introduce new products and technologies and are expected to have longer time horizons. These firms will make investments in machinery, products, and processes that are expected to be valuable in the future but may have little value today<sup>53</sup>. The R&D data comes from Eurostat Annual Detailed Enterprise Statistics. I consider three different R&D indicators for all sectors across all candidate countries<sup>54</sup>.

- **R&D1** represents share of R&D expenditure in value added. I normalised the data for the years 1998-2002.
- **R&D2** represents share of R&D employment in number of persons employed expressed in percentages. I normalised the data for the years 1998-2002.
- **R&D3** represents total number of R&D personnel. I normalised the data for the years 1998-2002.

Another indicator refers to *investment* as a proxy for dedicated asset, i.e. investment on the prospects of continuing sales in the future whereby the higher the investment the more likely factors are relatively immobile. The essence is to capture the ability of capital to move across industries relative to human capital. The more investment occurs per person the more likely it is to stay within the industry. Low mobility implies high specificity<sup>55</sup>. The indicator is investment per person employed per sector from Eurostat's detailed enterprise statistics (v94414) normalised for the years 1998-2002. The higher the investment the more likely capital will be dedicated.

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<sup>52</sup> J.E. ALT, *et al.*, Asset Specificity and the Political Behaviour of Firms: Lobbying for Subsidies in Norway, in: *International Organization*, 1999, 53(1), pp. 99-116., p. 107 and 108.

<sup>53</sup> J.K. CAVANAUGH and J. GAREN, Asset Specificity, Unionization and the Firm's Use of Debt, in: *Managerial and Decision Economics*, 1997, 18(3), pp. 255-69., pp. 40-43.

<sup>54</sup> Eurostat indicators v95110, v95120, v22120 respectively, on Eurostat's New Cronos, Annual detailed enterprise statistics on manufacturing, industry, construction and services at <http://epp.eurostat.cec.eu.int/portal>

<sup>55</sup> Ibid.

Finally, the *level of skills* to a particular industry concerns income derived from skills that can be either general or specific. Specific skills are valuable only to a single firm or group of firms (whether an industry or a sector), whereas general skills are portable across all firms. Workers with specific skills have more to fear if they lose their job than workers with general skills. Therefore, the level of skills can be used to approximate the specificity of human capital. The data is derived from the classification of occupations by the International Labour Office (International Standard Classification of Occupations, ISCO-88 Skill Levels). One drawback of these data is their limited variation and broad categorisation. To avoid bias due to economic fluctuations in the V-4 transition economies the data was averaged for the years 1998-2002 with the exception of the number of granted patents and skill levels.

### **Qualitative Analysis**

I derive the approximation for factor specificity and policy preference from the sectoral concerns related to the introduction of EU regulations in the applicant states. The approach exposes *de facto* winners and losers in Central Europe from the EU enlargement process. Like for the quantitative analysis I expect asymmetric lobbying. A detailed analysis of underlying economic motives, i.e. trade, output and prevalent market conditions are essential to the understanding of preference formation. Throughout the analysis sectoral statistical data from the quantitative part has been supplemented with sector specific literature and positional interviews with sectoral representatives and government officials in all the V-4. Note that referenced citations in the chapter are underscored by saturation for the interviews across countries and sectors (see Annex 2). For the inter-sectoral analysis of the pharmaceutical industry in the V-4 I added data on annual patent applications to gauge R&D activity (number of granted patents in the pharmaceutical industry from Eurostat and European Patent Office for 2001).

#### **2.3.2.2. Collective Action**

##### **Quantitative Indicators**

Approximating collective action and the ability to organise can be achieved by estimating the size of the interest group and its ability to provide selective incentives<sup>56</sup>. For this reason, members of larger groups will often have less incentive to take costly political action. To approximate

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<sup>56</sup> M.J. GILLIGAN, Lobbying as a Private Good with Intra-Industry Trade, in: *International Studies Quarterly*, 1997b, 41(3), pp. 455-74., p. 457.

collective action I use the size of the group in terms of concentration of the industry and the number of enterprises per sector<sup>57</sup>:

- **sectoral concentration** (v92100) or number of persons employed per enterprise. I normalised the data for the years 1998-2002.
- **group size** (v11110) number of enterprises per sector. I normalised the data for the years 1998-2002.

Following *Alt et. al.* we assume that collective action problems are inversely proportionate to the number of persons employed per enterprise and the number of enterprises per sector<sup>58</sup>. Larger firms would have anticipated a greater likelihood of success from lobbying and thus be more inclined to pursue political mobilisation. Larger firms should lobby more if the cost of contacting does not increase with firm size, or if the outcome is excludable and the probability of affecting it increases with firm size. If political support is exchanged for policy outcomes, the number of employees is a good indicator for firm size.

Note that collective action problems are likely to be less severe for costly political action when factors are not highly mobile as when they are. Factor specificity, then, determines in large part, individuals' stakes in a given trade issue and the size of the group to which they belong. In this way it affects their incentives to lobby given exogenous collective action problems.

### **Qualitative Analysis**

First, I use the indicators from the quantitative analysis. The hypothesis is tested by calculating a sectoral concentration ratio for the years 1998-2002. The ratio is further complemented data on membership of national associations and international peak associations and their respective role in the process of political mobilisation. The focus is on their ability to provide selective benefits to its members, the provision of information and effective enforcement mechanisms. For each case the representation of the interest group for the relevant sector in the economy is at least 50

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<sup>57</sup> - Eurostat indicators v92100 and v11110 respectively, on Eurostat's New Cronos, Annual detailed enterprise statistics on manufacturing, industry, construction and services at <http://epp.eurostat.ec.eu.int/portal>

<sup>58</sup> J.E. ALT, *et al.*, Asset Specificity and the Political Behaviour of Firms: Lobbying for Subsidies in Norway, in: *International Organization*, 1999, 53(1), pp. 99-116., pp. 108-110.

per cent of the market expressed in terms of employment or market share. Interviews complemented by primary literature reveal effective political action.

### **2.3.2.3. Insider Status**

#### **Quantitative Indicators**

I approximated insider status by sectoral employment and revenue for political strength. Sectors with high employment relative to those sectors with low employment are assumed to have more political power at the negotiating table. Governments in power are assumed to acquiesce to demands from high employment sectors because of the votes they represent. I averaged sectoral employment data from Eurostat and normalised the data per country.

I have used revenue representing political strength because of contributions these sectors could make and the importance they represent in the national economy. I used averaged sectoral gross value added (1998-2002) from Eurostat's detailed enterprise statistics.

#### **Qualitative Analysis**

The first measure for insider status is ownership structure, which I analyse at the firm level in the historical overview and the transition and consolidation sections of Chapters 3 to 5 (see table 12 and 16). Ownership structures are assumed to be important to the extent that they indicate access to policy makers. A state owned firm is likely to have a higher insider status compared to a private firm. Moreover, if the firm is owned by a foreign subsidiary it is assumed to be an outsider and hence less influential. I record the sectoral privatisation process and its completion.

I supplement the analysis by studying the relative national importance of the sector measuring its economic and political strength from the quantitative analysis<sup>59</sup>. Economic and political additionally is measured by the share of regional exports and export earnings. These measures provide an indication of the inter- and intra-sectoral economic weight in the V-4.

### **2.3.3. Supply Side: Independent Variables**

The supply side (Part III) engages with the national and international institutions dealing with EU accession. Throughout Part III the analysis centres on the dynamic of five empirical factors

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<sup>59</sup> Economic weight is measured by the share of value added and export earnings.

between for the period 1998-2003, i.e. the national distribution of decision making power for enlargement policy, the articulation of sectoral preferences within the national institutions, the formulation of national negotiation positions on EU enlargement, the international bargaining setting and the related domestic constraints.

The supply side limits the enquiry to qualitative data. These include 88 positional and structured interviews (see Annex 4 and 5). I supplemented interview data with sector specific literature, press articles on contemporary and retrospective market and political commentary and scholarly studies on the sectors, the states and their strategies in the enlargement process.

#### **2.3.2.4. Veto players**

For the present purpose it is necessary to identify the number of institutional veto players as well as partisan veto players. I derive the number of institutional veto players from the constitution of the applicant states and the array of laws, decrees, resolutions and regulations on the books that set the procedure for the national enlargement policy. The partisan veto players correspond to the actors that inhabit these institutions at the time of the accession negotiations. Because different veto players might not be equally important the researcher must ascertain their equivalence by identifying the critical constraints and opportunities in the policy process.

#### **2.3.2.5. Delegation and Insulation of the Policy Process**

The capacity of producer group interest to influence the policy process depends on the institutional configuration that either facilitates or impedes their progress vis-à-vis the policy-making apparatus<sup>60</sup>. The structure of the policy-making process has a bearing that it constitutes of opportunity structures or venues that interest will seek to exploit and which they believe will maximise their chances of public policy pay-offs. These opportunities structures – also called the channels of influence – are contingent on the centralisation of the policy structure shaping access points for interest groups<sup>61</sup>.

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<sup>60</sup> J. GREENWOOD, *Representing interests in the European Union*, Basingstoke: Macmillan, 1997., pp. 1-26; S. MAZEY and J. RICHARDSON, Interest groups and EU policy making, Organizational logic and venue shopping, in: J. RICHARDSON, *European Union, Power and Policy-making*, London, 2001, pp. pp 217-37.

<sup>61</sup> M.P.C.M. SCHENDELEN and R.J. JACKSON eds, *The Politicisation of business in Western Europe*, London; New York: Croom Helm, 1987., pp. 6-7; W. GRANT, *Business and politics in Britain* Basingstoke: Macmillan, 1987., pp. 213-235. The organization of Business Interest for European Community Representation; B.G. PEETERS, Agenda-setting in the European Union, in: J. J. RICHARDSON, *European Union: power and policy-making*, London: Routledge, 2001, pp. 78-94., pp. 78-94.

However, when the level of delegation of policy making authority is high and the policy process is heavily insulated the number of institutional veto players and their preferences might be well irrelevant. I will derive the level of delegation and insulation from (a) the formal powers and preferences of the Czech, Hungarian, Polish and Slovak administration responsible for negotiating EU membership; (b) the mechanisms that allowed for sectoral consultation and the formulation of TPRs in the enlargement policy.

#### **2.3.2.6. Executive Preferences**

To elicit executive preferences relative to the status quo I need to make assumptions about preference formation. Policy choices are likely to differ according to the degree of executive dominance since executives share decision-making power with other internal groups. Policy choices are the result of a strategic game among internal actors. I use the number of coalition partners and the parliamentary majority as a proxy for the responsiveness of governments to societal interest. The majority in parliament is a proxy for the fear of losing office. Government coalitions with a suitable majority are assumed to weigh less the policy preferences of lobbyist and interest groups. The proximity of elections functions as a proxy that public policy of the government will become more salient as they generate short-term negative/positive political evaluations. Hence, the executive also is assumed to be more susceptible to societal pressures as the prospect of general elections near.

#### **2.3.2.7. State Preferences**

When two parties negotiate a deal their respective position papers might reflect their position at the negotiating table<sup>62</sup>. In this sense a TPR is an indication of the state's preference over the issues on the table and an indication of the state's national interests. The EU applicants' position papers are available on a chapter by chapter basis.

However, a TPR might be strategic on the part of a national government. Its position might be the result of cheap talk rather than a revealed preference. It might not be willing to fight for it.

Conversely, an uncompromising position reflected in protracted negotiations might reveal true preferences. The executive has little to gain from an uncompromising stance when what it

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<sup>62</sup> In the EU enlargement negotiations the applicant countries initial position papers were available on a chapter by chapter basis. Subsequent position papers were secret and only occasionally available. The EU's common negotiation position remained secret.



demands is in fact strategic. The revealed national preference is assumed to be a litmus test for the preference formation of the aggregated preferences of economic sectors, executives, legislatures and administration. For the individual applicant countries I collected data on deputy and chief negotiator level for the different negotiation rounds for all the ten applicant countries. I subsequently compared the duration of each negotiation round to gauge the individual government's revealed preferences.

### **2.3.2.8. International Negotiations**

Before testing the Schelling conjecture on the EU applicant's strategies it is imperative to specify the strategic setting of the negotiation. The structure of the interaction of the negotiating parties and the form of the negotiation game are assumed to reveal the asymmetry of power between the parties. Power asymmetry is a central tenet of the enlargement literature whereby the applicant states are seen as dependents and suppliants. I will demonstrate the power asymmetry in the negotiations by drawing a picture of the institutional framework for the EU to arrive at its common negotiation position and how that affects the negotiation mandate at the negotiating table.

The position of the EU is unclear as a unit. The EU member states debate EU enlargement in the Council where EU preference formation takes place. The minutes of the Council are not open for consultation. The EU common negotiation position is not known. To find a way around this problem I take the EC as a proxy for the EU-15 common position. I assume that the position of the EC is close to that of the Council. It has agenda setting powers and formulates the Draft Common Position (DCP) to the EU in response to the position papers of the applicant states<sup>63</sup>. The EC is aware of the voting rule in the Council and the EU member states' preferences. Within that context it has to consider what the member states will be prepared to agree among themselves. As a result, it is unlikely to make proposals to the Council that are far of the mark of the Council's pivot(s). Otherwise it might risk further delays in the negotiations and lose the trust of the Council's members in the process<sup>64</sup>.

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<sup>63</sup> With the exception of issues relating to common foreign policy and security and third pillar issues.

<sup>64</sup> This is essentially an analogy of the argument on delegation on American trade policy made by M. Gilligan in: M.J. GILLIGAN, *Empowering exporters: reciprocity, delegation, and collective action in American trade policy*, Ann Arbor: University Of Michigan Press, 1997a., pp. 4-6 and chapter 3, pp. 35-57.

The common bargaining position adopted by the member states reflects the EU's collective interests and sets the limits of the mandate given to EU representatives in international negotiations. Subsequently the test of the Schelling conjecture draws on the empirical analysis of partisan the veto players in the applicant countries.<sup>65</sup>

## **Conclusion**

In the fifth EU enlargement process the negotiating partners agreed to allow adjustment to EU membership in 47 economic sectors. They chose predominantly exemptions from EU market regulations (72.9 per cent) followed by exemptions from EU tax (14.1 per cent) and state aid (6.7 per cent) law as means to redistribute income. Only 6.15 per cent represents traditional forms of market protection, i.e. tariffs and quotas.

Not taking in account derogations, 82 per cent of all transitional measures are no longer applicable after five years from the date the applicants joined the EU. Just 16 per cent of all TAs have a length of between 5 and 10 years. Only 2 per cent of the measures will allow exemption from the *acquis* for more than 10 years.

Poland and Malta, respectively the largest and the smallest of all the applicant countries received most TAs. Latvia, the Czech Republic, Lithuania and Hungary follow closely with Cyprus, Estonia, Slovakia and Slovenia respectively trailing the group.

The order of countries obtaining exemptions in the negotiations changes slightly when weighing TAs according to their duration. The period for not applying EU legislation is longest for Poland and Malta. The Czech Republic, Hungary, Cyprus and Slovakia are in the middle of the group. The Baltic countries and Slovenia come last.

Finally, the estimated national coverage ratio of exemptions from the *acquis*, i.e. the estimated national GDP that is touched by one or another exemption from the *acquis*, places Malta, Poland, Slovenia and Latvia far ahead of the other six countries. Malta's economy is for just more than an

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<sup>65</sup> S. MEUNIER, What Single Voice? European Institutions and EU-U.S. Trade Negotiations, in: *International Organization*, 2000, 54(1), pp. 103-35., footnote 3.

impressive 45 per cent of its GDP covered by one or another exemption from the acquis. It is followed by Poland with just over 30 per cent. Also here no clear pattern emerges based on traditional explanations as chapter 1 has showed.

Therefore, it is fruitful to dig a little deeper and look at the economic sectors to which TAs apply. Throughout chapter two I have used a more detailed analysis of economic sectors (NACE 1-3 digits). For the purposes of this conclusion it suffices to look at broader categories (see Table 9).

**Table 9: TAs per sector (Nace 1.1 1-digit) measured by presence, number and number by time**

Sector	Nace (1-digit)	Presence TA %	Tas per sector %	Tas per sector by time %
Agriculture, Hunting and Forestry	A	29.8	16.5	34.1
Fishing	B	2.2	2.1	4.8
Manufacturing	D	1.2	2.1	0.4
Manufacturing of food products, beverages and tobacco	DA	9.8	13.4	5.5
Manufacturing of textiles and textile products	DB	0.9	1.0	0.3
Manufacture of leather and leather products	DC	0.3	0.5	0.0
Manufacturing of pulp, paper and paper products; publishing and printing	DE	0.3	0.5	0.2
Manufacture of chemicals, chemical products and man-made fibres	DG	8.6	11.3	11.1
Manufacture of other non-metallic mineral products	DI	0.3	0.5	0.0
Manufacture of basic metals and fabricated metal products	DJ	5.8	5.2	10.6
Manufacture of electrical and optical equipment	DL	0.6	1.0	0.1
Manufacture of transport equipment	DM	1.5	2.6	2.6
Manufacturing n.e.c.	DN	3.1	3.6	2.0
Electricity, gas and water supply	E	7.1	6.7	6.2
Construction	F	0.9	1.5	0.5
Wholesale and retail trade; repair of motor vehicles, motorcycles	G	5.5	5.2	3.2
Hotels and restaurants	H	1.2	2.1	0.6
Transport, storage and communication	I	10.8	11.9	10.9
Financial intermediation	J	4.9	4.1	2.2
Real estate, renting and business activities	K	4.0	6.7	4.1
Other Community, social and personal activities	O	0.9	1.5	0.4
Total		100.0	100.0	100.0

Out of the total of 21 broadly defined economic sectors (NACE 1-digit) 29.8 per cent of all TAs have been negotiated for agriculture, hunting and forestry. Transport, storage and communication take second place with 10.8 per cent followed by manufacturing of food products, beverages and tobacco (9.8 per cent); manufacturing of chemicals and chemical products (8.6 per cent); electricity, gas and water supply (7.1 per cent); manufacturing of basic metals and fabricated metal products (5.8); construction (3 per cent), manufacture of transport equipment (1.5 per cent), etc.

TAs are more evenly distributed across the 21 sectors when counting their number per sector. Agriculture, hunting and forestry (16.5 per cent), Transport, storage and communication (11.9 per cent) manufacturing of food products, beverages and tobacco (13.4 per cent) and manufacturing

of chemicals and chemical products (11.3 per cent) continue to dominate. This is also the case when measuring TAs over time.

From these broad categories Part II takes three sectors at the level of 3-digits to whether a pattern emerges on the basis of our proposed theoretical framework.

**PART II: SECTORS**  
**(DEMAND FOR PROTECTION)**



## INTRODUCTION

Part II is devoted to preference formation and the likelihood of political mobilisation of economic sectors and their expression in Central Europe when confronted by the prospect of EU membership – demand for protection as opposed to supply for protection which is discussed in Part III.

Each chapter begins with an account of the sectoral regulations that need to be transposed in Central Europe ahead of EU entry. With the exception of a few cases where the EU set quotas or tariffs (see Chapter 2) these regulations consist of behind the border issues, which are a full integral part of the EU's internal market. These internal market regulations form the contours of the sectoral conflicts that emerged when integrating EU and Central European market operators. They provide the analyst with an overview of what is at stake when integrating two halves of the enlarged EU, i.e. the market of the applicant states and that of the EU-15.

Subsequently, I analyse the structure of the market in a brief historical overview whereby nationalisation and centralisation precede fragmentation, liberalisation and privatisation of the industry in Central Europe. The historical overview prepares the ground for a rigorous test of four specific predictions for the pharmaceutical industry, the basic iron and steel industry and the international road transport sector in the V-4.

A comparative intra-sectoral analysis across the Czech Republic, Hungary, Poland and Slovakia drives the argument that *sectoral preference formation and political mobilisation are necessary conditions for the presence of transitional arrangements or grace periods in the EU's enlargement process*. The underlying economic dynamic leading to sectoral preference formation is central to its analysis. It lays out the implications of EU integration for sectoral incomes: Who stood to win or lose and which sector held the strongest intensity of preferences over enlargement policy?

The analysis moves on to the socio-economic institutions underpinning sectoral preferences. It pinpoints the organisation strength of sectors: Which sector exerted political pressure and at what intensity? In other words, on the basis of the EU integration of pharmaceuticals, basic iron and

steel and international road freight transport I attempt to discover not just how EU enlargement policy played a distributive role in the integration process between west and eastern Europe but also why it did so.

Part II concludes with a cross sectoral or inter-sectoral analysis for the Czech Republic, Hungary, Poland and Slovakia. The focus gradually shifts towards the national likelihood of accommodation of sectoral preferences and prepares the ground for Part III, which concentrates on formal institutions – the supply side of protection.

## **Notes on Data**

### **1. Defining sectors**

Sectoral analysis requires strict definitions, classifications or concepts of economic sectors to prevent confusion when using quantitative and in particular qualitative data. When observing the political science and political economy literature sectoral definitions and conceptualisation are often implicitly assumed, discussed with broad a brush or just absent – they are rarely explicitly mentioned. A strict conceptual idea of an economic sector prevents confusion between categories and subcategories particularly when moving up and down the ladder of abstraction; and when looking for and comparing output, employment, trade and firm level data across different statistical databases.

The researcher particularly needs to be cautious when using of qualitative data, including the use of interviews, that pertain on political assets of economic sectors. For instance, does the analyst discuss the pharmaceutical sector or the chemical sector?; or does he deal with the manufacture of basic pharmaceutical products or the manufacture of pharmaceuticals, medicinal chemicals and botanical products? Quantitative data differ for each category and tend to do more so when pertaining to sectoral associations and trade unions. Does the association represent manufacturers of basic iron and steel; or manufactures of seamless steel pipes and tubes; or both? Does the trade union represent just steel workers or all the labourers in metallurgy, including those in engineering?



Economic sectors can be chosen according to several categories and definitions. They can be defined according to economic activity (NACE, CPA), product (CPC), occupation (ISCO) or a mix of the former based on the origin, the prevalent use, the providing institution and the required level of detail (ISIC, HS, SITC, NAICS and Prodcom). Correspondences between these different classification systems have been established and are regularly updated. For the present study I have used NACE Rev. 1.1 and ISIC Rev.3.1 as the most basic categories using UN correspondences when the respective database required a different unit of observation (see also Chapter 2)<sup>1</sup>.

For all sectors I have used the four-firm concentration ratio - the sum of the portions of sales, value added, assets, or employees held by the largest four firms in an industry – as the benchmark for a representative sample of the industry. Actually, for all three sectors that market share, employment, value added or political representative bodies approaches or exceeds 80 per cent.

### **1.1. Pharmaceuticals**

For Chapter 3 on pharmaceuticals I restricted the research to the manufacture of pharmaceuticals, medicinal chemicals and botanical products (NACE 24.40) and include the manufacture of basic pharmaceutical products (NACE 24.41) and the manufacture of pharmaceutical preparations (24.42) unless otherwise specifically mentioned. The chapter excludes the manufacture of basic chemicals (NACE 24.10) including for employment data. Finally, NACE 24.40 category and its respectively correspondences are used for output, employment, trade and firm level data across different statistical databases. The originating database is mentioned in each instance as well as the level of aggregation for the respective indicator.

### **1.2. Basic Iron and Steel**

For Chapter 4 on the basic iron and steel industry I restricted the study to NACE code 27.10 (Manufacture of basic iron and steel and of ferro-alloys) according to the definition of the ECSC Treaty, which involved the production of crude steel, semi-products, hot-rolled finished products,

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<sup>1</sup> The world matrix for sectoral economic data provides a good overview of the classification systems: [http://www.hwua.de/wmatrix/Technical\\_Description.html](http://www.hwua.de/wmatrix/Technical_Description.html); particularly useful is the UN website on classification systems at: <http://unstats.un.org/unsd/cr/registry/regct.asp?Lg=1>; For Eurostat see [http://ec.europa.eu/comm/eurostat/ramon/index.cfm?TargetUrl=DSP\\_PUB\\_WELC](http://ec.europa.eu/comm/eurostat/ramon/index.cfm?TargetUrl=DSP_PUB_WELC); For a good overview of industry concordances see <http://www.mcalester.edu/research/economics/PAGE/HAVEMAN/Trade.Resources/TradeConcordances.html> and the above mentioned UN website. For occupation classification look at: <http://www.ilo.org/public/english/bureau/stat/class/isco.htm>.

continuously cast products, cold-rolled sheets and plates, and coated sheets. According to this definition, the steel industry does not include the manufacture of steel tubes, which are included under NACE code 27.20, nor the initial cold processing of steel (mainly wire drawing, but also cold drawing, laminating, profiling and shaping), which are covered by NACE code 27.30. The ECSC Treaty excludes these processes, along with cast-iron foundry products and forged, pressed, deep-drawn and cup-packed products. Together, these three sub sectors represented by NACE 27.10, 27.20 and 27.30 constitute the ferrous metal sector. When Chapter 4 uses the term 'metal industry' it refers to a much wider sector, corresponding at least to NACE codes 27, 28 and 29, which is explicitly mentioned. Only when discussing EU-V-4 anti-dumping measures over the 1990s and early 2010s does the chapter include 27.20 and 27.30. Finally, the NACE 27.10 category and its respectively correspondences are used for output, employment, trade and firm level data across different statistical databases. The originating database is mentioned in each instance.

### **1.3. Road Freight Transport**

Chapter 5 on road freight transport is limited to freight transport by road (NACE 60.24) and more specifically international road freight transport. The statistics in the chapter are collected according to Eurostat and the European Conference of Ministers of Transport (ECMT - under the auspices of the OECD) road transport definitions which are collected according to transport equipment, enterprises, economic performance, employment, traffic and goods. The chapter excludes domestic and international passenger transport unless explicitly mentioned.

## **2. Data Availability and Reliability**

### **2.1. Pharmaceuticals**

Trade: OECD, Bilateral Trade Statistics; OECD, STAN Bilateral Trade Database

Output: Unfortunately no comparable output or volume trade data for the pharmaceutical sector in the V-4 is available for the 1990s and early 2010s.

Employment, value added, R&D, Investment, group size and sectoral concentration:

Eurostat, Annual Detailed Enterprise Statistics

Patents: European Patent Office and Eurostat, Annual Detailed Enterprise Statistics

Skills: ILO ISCO-88 Skill Levels and ISCED Categories

With the exception of skill levels no comprehensive comparable data is available to test the hypothesis on asset and factor specificity. In the annual detailed enterprise statistics of Eurostat several measures of R&D and investment for Poland and the Czech Republic are absent or confidential. Only Hungary and Slovakia provide full statistics. The only measure available for all four countries is investment per person employed. To remedy missing data the number of annual granted patents in pharmaceuticals and labour skill levels were added. Data were supplemented with sector specific information to attain a more comprehensive picture of the sector. Data is complemented by sector specific literature providing information at the sectoral and firm level. All positional interviews were carried out in the period January 2004-May 2004 – no positional interview for all the V-4 was left out.

## **2.2. Basic Iron and Steel**

Trade: OECD, Bilateral Trade Statistics; OECD, STAN Bilateral Trade Database

Output: Crude steel production data from International Iron and Steel Institute

Employment, value added, R&D, Investment, group size and sectoral concentration:

Eurostat, Annual Detailed Enterprise Statistics

Skills: ILO ISCO-88 Skill Levels and ISCED Categories

Data is complemented by sector specific literature providing information at the sectoral and firm level. All positional interviews were carried out in the period January 2004-May 2004 – two positional interviews for Poland were left out due to the EUI's ad hoc announced financial limitations for carrying out missions in April 2004. They were substituted by interviews published in sectoral literature.

## **2.3. Road Freight Transport**

Trade: Eurostat, road transport statistics including:

- Road freight cabotage 1999-2001, Statistics in Focus (Eurostat, July 2003);
- Road freight cabotage 1991-2001, Statistics in Focus (Eurostat, April 2001);
- Trends in road freight transport up to 2003, Statistics in Focus (Eurostat, July 2005);
- Trends in road freight transport 1990-1999, Statistics in Focus (Eurostat, February 2002);

Employment, value added, R&D, Investment, group size and sectoral concentration:

Eurostat, Annual Detailed Enterprise Statistics

Skills: ILO ISCO-88 Skill Levels and ISCED Categories

Trade statistics were collected via sample surveys, which by definition can sometimes result in over- or underestimation of road transport volumes. The problem of data reliability mainly concerns data from the period 1990-1998. From 1999 onwards data on road transport is considered to be reliable and available the Czech Republic and Hungary. Data for Poland and Slovakia are only reported from 2004 onwards. Data prior to 1999 come from two main sources:

- The Phare multi-country projects (and studies) on the costs and benefits of enlargement in the transport sector and on road transport charges;
- Eurostat, Road Transport: Enterprises, economic performance and employment; and Eurostat, Transport Measurement – goods.

## **CHAPTER 3: THE PHARMACEUTICAL INDUSTRY**

This chapter considers the economic issues affecting the pharmaceutical sector in the V-4 in the run up to EU membership. It analyses the most important industry concerns in the context of EU enlargement with a brief historical overview of the regional and national pharmaceutical manufacturers in Central Europe. The chapter then moves on to apply the theory of factor and asset specificity. It assesses four hypotheses specifying the industries' trade in pharmaceuticals, its factor and asset specificity, national cohesion and concentration as well as its insider status in the policy process. The focus is on the period 1992-2004 treating the actual years of the enlargement negotiations (1998-2004) in more detail.

### **3.1. Industry Concerns: Intellectual Property Rights**

Intellectual property rights on pharmaceutical products proved by far the biggest challenge for the industry in the EU enlargement process. The rules under which the Central European industry produced pharmaceutical products and their application differed markedly from those in the EU.

#### **3.1.1. The Sector in the EU**

For the EU the problematic areas for a liberalised market in pharmaceuticals emerged before the V-4 applied for EU membership. Regulations for the pharmaceutical industry were included in the EA's with Czechoslovakia, Hungary and Poland<sup>1</sup>. According to the EA's GATT TRIPS regulations should have been applied before the end of the fifth year from the entry into force of the agreements, i.e. 1999-2000<sup>2</sup>. In 1997 the dominant representative of the European pharmaceutical producers, the European Federation of Pharmaceutical Industries and Associations (EFPIA), argued in an EC memorandum that it would be detrimental to the EU's

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<sup>1</sup> The EAs were signed and entered into force as follows: Czechoslovakia (1991; entry into force 1995), Hungary (1991; entry into force 1994) and Poland (1991; entry into force 1994).

<sup>2</sup> According to article 66, nr.1 of the EAs the signatories 'shall continue to improve the protection of intellectual, industrial and commercial property rights in order to provide, by the end of the fifth year from the entry into force of this Agreement, a level of protection similar to that existing in the Community, including comparable means of enforcing such rights; nr. 2.2. By the end of the fifth year from the entry into force of this Agreement, [the Czech Republic, Hungary, Poland and Slovakia] shall apply to accede to the Munich Convention on the Grant of European Patents of 5 October 1973 and shall accede to the other multilateral conventions on intellectual, industrial and commercial property rights referred to in Annex XIII paragraph 1 to which Member States are Parties, or which are de facto applied by Member States'. See EAs Czech Republic, Hungary and the Czech Republic, 1991; 1993.

pharmaceutical industry ‘when countries with significantly lower levels of effective intellectual property protection and economic and market conditions [...] join the Union’<sup>3</sup>.

The industry feared that different market conditions could under the influence of free movement of goods, result in so-called parallel trade<sup>4</sup>. Therefore, EFPIA requested full application of the *acquis* upon accession of the applicant states. More specifically EFPIA stressed adequate patent protection, proper enforcement of legislation and data protection and confidentiality of dossiers<sup>5</sup>. In the run up to EU entry the EC agreed with EFPIA as far as enactment and enforcement of EU legislation in the areas of free movement of goods and company law was concerned. In its 1998, 1999, 2000, 2001 and 2002 regular reports the EC stressed the importance of intellectual property rights, their application and penalties for the violation of copyrights<sup>6</sup>.

### **3.1.2. The Sector in the Applicant States**

For the pharmaceutical industry in the applicant states EU membership became an important issue after 1998 when EU entry talks were firmly underway. The prospect of EU membership raised the spectre that all medicines that did not comply with EU regulations would disappear from the market for some time until they did comply<sup>7</sup>. Full implementation of European standards in drug production, certification and registration certainly gave rise to the danger that domestically made products would disappear for good from domestic pharmacies in the Czech Republic, Hungary, Poland and Slovakia.

Central European pharmaceutical manufacturers produced only a minority of original medicines and over 90 per cent of the locally produced pharmaceuticals were generics and copies of original

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<sup>3</sup> EFPIA, *The Accession of Central and Eastern European Countries (CEECs) to the European Union (EU)*, Brussels, July 1997, pp. 15.

<sup>4</sup> Parallel trade is the re-exporting of a product, on sale in one country at a lower price, to another.

<sup>5</sup> ‘Any new member state is bound to fully accept the aims and provisions of the European Treaties, and to fully adopt the common policies and various regulations and directives of the European Union (EU) as they stand at the time of accession [...] Alternatively, EFPIA proposed upon accession ‘an appropriate transition period providing for safeguard measures [...] until distortions are eliminated in the CEEC economies and operating environments reach EU standards and norms’, in: EFPIA, *The Accession of Central and Eastern European Countries (CEECs) to the European Union (EU)*, Brussels, July 1997, pp. 15., p. 6, p. 14.

<sup>6</sup> See: EC, *Regular Report from the European Commission on the Czech Republic's, Hungary's, Poland's and the Slovak Republic's Progress towards Accession*, Brussels, 1998-2002.

<sup>7</sup> See interview with Maria Glowniak, Poland's chief Pharmaceutical inspector, in: W. JELONKIEWICZ, *Preparing for EU Impact*, in: *Warsaw Voice*, Warsaw: 21/07/2001.

drugs<sup>8</sup>. Full application of EU market regulations would threaten the viability of the region's pharmaceutical industry.

As *Wojciech Kuymierkiewicz*, Vice President of the Polish pharmaceutical producing industry, *Polish Zakłady Farmaceutyczne Polpharma*, stated in 2001: 'the consequences for the Polish pharmaceuticals industry would be catastrophic'<sup>9</sup>. In Poland alone about 2,000 out of more than 3,000 drugs produced in 2001 would have to be registered anew in accordance with EU requirements. Furthermore, a majority of Polish generic drugs would have to be withdrawn from the market significantly reducing the Polish factories ability to manufacture generic pharmaceuticals<sup>10</sup>. The Polish Pharmaceutical Works produced up to 95 per cent cheaper generic medicines and copies of original medicaments. A similar situation existed in the Czech Republic, Hungary and Slovakia.

The domination of the generic medicine production base of generic medicines in the Central European market have much to do with a legacy of Communism, patent protection, intellectual property rights and their enforcement and state preferences for cheaper generics throughout the region. Regardless of the EA's patent laws in Central Europe usually allowed local manufacturers to launch generics and conduct research while a product was still under patent. It allowed local producers to get a head-start once the patent had expired – a practise uncommon in the EU<sup>11</sup>.

Prior to 1991 international patent law was not recognised in Czechoslovakia. The first patent law was introduced at the beginning of 1991. It provided for a patent term of 20 years for product claims. The law was not retroactive and patented drugs copied before 1991 were continued in local production. The US industry association, the Pharmaceutical Research and Manufacturers of America Foundation (PhRMA), criticised the industry for breaching patent laws and it cited the Czech 1991 patent law 'as a major cause for concern'. It urged the inclusion of the Czech Republic on the U.S. Trade Representative (USTR) 2000 Special 301 Watch List. PhRMA also

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<sup>8</sup> Business Eastern Europe: Eastern Europe regulations: EU enlargement will help combat piracy, in: *Economist Intelligence Unit*, 22/05/2000.

<sup>9</sup> J. SPARSHOTT, Poland to reopen EU chapter for drugs industry, in: *ISI Emerging Markets*, 11/02/2001

<sup>10</sup> J. OKRZESIK, *Poland by sectors: Production of Pharmaceuticals*, Warsaw: BOSS Informacje Ekonomiczne, 2001.

<sup>11</sup> N. SPIRO, Bitter Pill, in: *Economist Intelligence Unit*, 18/12/2001. . .

called the enforcement of existing patent rights problematic, with legal procedures being unwieldy, contradictory and time-consuming<sup>12</sup>.

Under Communism in Hungary making copies of western drugs was legal. Up to 1994 a process patent system had been in force which meant that if a Hungarian researcher found a new process – an independent one from the patented processes of the original manufacturer – he was free to manufacture the given product. The company subsequently could market it in every country in which a process patent system was in force. In other words, local manufacturers could effectively copy products just by slightly altering the production process. The 1990s brought profound changes. Under international pressure, Hungary shifted to a product patent system, whereby one has to wait 20 years until the patent expires and only then can a product be manufactured in generic form. The Hungarian law of 1994, however, provided for a transitory period. Those independent processes are accepted for which patent was applied before 1 January 1987. With such process patent the product is allowed to be developed<sup>13</sup>.

Hungary's patent protection at the end of the 1990s was still regarded as less than perfect by the international industry. In 1999 PhRMA recommended the Hungarian industry be placed on the Special 301 Watch List by the US government. PhRMA's concerns centred on the inadequacy of Hungarian pipeline protection and poor data exclusivity. It had doubts about the Hungarian court's inadequate legal enforcement of patent protection.

The situation was analogous in Poland. Until 1993 only process patents were available. From January 1993 onwards pharmaceutical companies were able to obtain product patents, although, not retrospectively. The amendments extended patent terms from 15 to 20 years from the date of application. Ahead of EU entry the Polish Parliament decided to retain a controversial provision in new pharmaceutical legislation that removed data exclusivity protection for companies filing marketing authorisation applications in Poland.

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<sup>12</sup> PhRMA, *PhRMA Special 301 Submission: Submission of the Pharmaceutical Research and manufacturers of America (PhRMA) for the National Trade Estimate Report on Foreign Trade Barriers (NTE)*, 27 November 2000, pp. 189., p. 87-89.

<sup>13</sup> PhRMA, *Submission of the Pharmaceutical Research and manufacturers of America (PhRMA) for the Special 301 report on Intellectual Property Barriers: country profile Hungary*, 16 February 1999.



PhRMA attacked a wide range of Polish manufacturing practices, with the most notable being data exclusivity. PhRMA claimed that Poland brought down prices through the existence of copycat products. The association also disparaged deficiencies in compulsory licensing, international exhaustion of patent rights, and the existence of Roche-Bolar provision and the weak enforcement of existing patent rights. PhRMA recommended Poland be included on the USTR 2003 Special 301 Priority Watch List<sup>14</sup>.

In Slovakia, despite the 1998 legislation designed to bring the country's regulatory system into line with the EU, patent protection remained patchy. The Slovak authorities were accused of openly discriminating in favour of local products. Slovakia passed new rules on data exclusivity in February 2000, however, the new regulations allowed for six years of protection, from the date of the first EU registration of the product in question. This meant in practice that many products had no data exclusivity protection since they were launched in the EU many years before being made available in Slovakia. PhRMA argued that this violated Slovakia's international agreements, including the TRIPS agreement<sup>15</sup>.

On the whole, under the prospect of EU membership Central European producers would find their share of domestic sales shrinking. More importantly, it would cause them to lose export markets in the CEECs and former S.U. as they would no longer be allowed to produce a large number of pharmaceutical products upon EU entry. As a result, one would expect that under full sectoral EU membership without any TA a significant repositioning of industrial players on the Central European pharmaceuticals market would ensue<sup>16</sup>.

## **3.2. Historical Overview**

### **3.2.1. 1945-1989**

Following the end of World War II the Central European Communist regimes over time introduced a more or less centrally planned economic system. The regional pharmaceutical

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<sup>14</sup> PhRMA, *Submission of the Pharmaceutical Research and manufacturers of America (PhRMA) for the Special 301 report on Intellectual Property Barriers*, 8 March 2003, pp. 217., pp. 71-81, pp. 8-15.

<sup>15</sup> Episcom Business Intelligence, *World Pharmaceutical Markets: Czech Republic, Hungary, Poland, Slovakia*, West Sussex, 1998-2003.

<sup>16</sup> S. DILOVA and L. MALYCHEVA, *Corporate Finance; Emerging Markets Special Report: Pharmaceuticals in Central and Eastern Europe*, FitchRatings, September 2002. pp. 1-2.

industry was no exception to this rule. Variation existed between the V-4 as to the level of independence of companies. By the end of the 1960s a majority of the sector's firms were nationalised and centralised.

For the Czech and Slovak lands of the Czechoslovak Federation (1918-1992) the economic policy resulted in the reorganisation of the pharmaceutical industry around one single production entity, the United Pharmaceutical Works of Czechoslovakia (*Spojené farmaceutické závody* or *Spofa*)<sup>17</sup>. All pharmaceuticals in the Czechoslovak market were free and the MoH defined its drugs portfolio<sup>18</sup>.

In Hungary the production of the long standing pharmaceutical sector was concentrated in six large enterprises with *Alkaloida*, *Biogal*, *Chinoin*, *Egis*, *Human* and *Gideon Richter* producing the majority of human medicines<sup>19</sup>. Similarly, the Polish industry was nationalised and reorganised around the state conglomerate the Polish Pharmaceutical Works also known as *Polfa*. The conglomerate comprised 16 large enterprises organised around 17 industrial sites throughout the country<sup>20</sup>. As much as 70 percent of the entire production came from the Polfa association.

The strong position of the Hungarian and Polish pharmaceutical sector in the CEECs was due to the fact that Poland and Hungary were assigned the role of the main supplier of medicines within the former Soviet bloc. The production of medicines in Central Europe was chiefly oriented towards the markets of the members of the Council for Mutual Economic Assistance (COMECON)<sup>21</sup>. Over the years 1949-1991 Czechoslovak, Hungarian and Polish pharmaceutical exports to COMECON countries grew considerably. Institutional factors and the nature of the COMECON market encouraged manufacturing of cheaper generic drugs mainly intended for export to the S.U. Many of the drugs produced were copies of those developed in the west. Patent laws in the region allowed wide scale drug copying. The Central European producers were immune to pressure from Western manufacturers<sup>22</sup>.

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<sup>17</sup> Espicom Business Intelligence, *World Pharmaceutical Markets: Czech Republic*, West Sussex, March 2001, pp. 46., p.36.

<sup>18</sup> *Interview by Author with Representative of the Czech Association of Pharmaceutical Companies*, Prague, 02/05/2004.

<sup>19</sup> MAGYOSZ, *The Pharmaceutical Market*, 2004.

<sup>20</sup> Espicom Business Intelligence, *World Pharmaceutical Markets: Poland*, West Sussex, April 2000, pp. 54., p.26.

<sup>21</sup> COMECON was the economic framework for co-operation among members of the Soviet Union. It was set up in 1949 and disintegrated in 1991 when the S.U. collapsed.

<sup>22</sup> Espicom Business Intelligence, *World Pharmaceutical Market: Hungary*, West Sussex, February 2001, pp. 46., p. 25.

### 3.2.2. Transition and Consolidation (1989-2004)

After the Berlin Wall came down (1989) Czechoslovakia, Hungary and Poland embarked upon a transition towards democracy and a market economy. Market reforms hit the industry hard and the pharmaceutical industry underwent significant changes. The most serious challenges of the transition process were the need to overcome the negative effect of market liberalisation, to adjust from a process patent to a product patent system, to recapture the COMECON market after the break up of the S.U., and to manage the privatisation of the industry.

Market liberalisation resulted in imports of modern produced pharmaceutical products and western competition. Global pharmaceutical enterprises set up local subsidiaries for the import and representation of more modern produced finished medical products. Over a short time span domestic companies unfamiliar with the new market rules were in competition with often superior products.

Simultaneously, the COMECON export market collapsed with powerful spill over effects on the trade flows and production of regional pharmaceuticals<sup>23</sup>. Russian roubles disappeared in Central Europe and trade in pharmaceutical products was accounted for in local currencies or US dollars. Local producers were left exposed as the biggest export market for the Central European producers, the S.U., collapsed (1991-1992).

International pharmaceutical companies based in the US and EU pressured Central European governments through trade negotiations to align pharmaceutical patents laws with international regulations<sup>24</sup>. The introduction of new legislation and standards such as Good Manufacturing Practice (GMP) required high investments and threatened the prospects of an industry that largely depended on the production of generic medicines – ahead of EU membership and largely before the EU entry negotiations had begun.

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<sup>23</sup> P. BOONE, S. GOMULKA and P.R.G. LAYARD eds, *Emerging from communism: lessons from Russia, China and Eastern Europe*, Cambridge, Mass.: MIT Press, 1998., pp. 14-41.

<sup>24</sup> The Europe Agreements with Czechoslovakia, Hungary and Poland were concluded in 1991. For an extensive overview see: J.I. TORREBLANCA PAYA, *The European Community and Central Eastern Europe (1989-1993): foreign policy and decision-making*, Madrid: Centro de Estudios Avanzados en Ciencias Sociales, 1997.

The Czechoslovak, Hungarian and Polish authorities embarked upon various privatisation programmes. The nature, method and timing of the privatisation programmes differed for each country<sup>25</sup>. Throughout the region centralised state owned pharmaceutical companies were broken up and privatised in the 1990s. The industry had consolidated by the end of the decade with the exception of Poland.

On the whole, the total number of companies in the industry remained fairly stable between 1989 and 2000. Initially the number went up because of the division of state owned companies and ensuing privatisation. The number of importing companies rose and many established a representation in the V-4. Few, however, established new production facilities through green field investments. The number of pharmaceutical workers declined and with the exception of Poland stabilised by 1995-1996. Subsequently, their numbers rose and so did salaries and productivity levels<sup>26</sup>.

### **3.2.2.1. Czechoslovak Pharmaceuticals (Czech and Slovak Republics)**

In Czechoslovakia the market leader, Spofa, which included all the Czechoslovak drug producers disintegrated into several independent companies. The new entities principally took the form of joint stock companies propped up with capital from foreign drug companies or private investment funds. The first foreign investment in the pharmaceutical industry took place in 1992. The largest domestic market player, *Leciva*, set up two joint ventures with foreign companies, *Interpharma* and *Ferring-Leciva*<sup>27</sup>. In turn, *Leciva* set up a Czech branch, *Leciva CZ*, in 1997 with support of an American investor, *Warburg Pincus*.

Following the break up in 1993 of the Czechoslovak Federation into the Czech and Slovak Republics the pharmaceutical industry split into Czech and Slovak branches. The majority of Czechoslovak assets went to the Czech Republic as the industry was concentrated in the Czech half of the country. In 1994 the second biggest Czech pharmaceutical company, *Galena*, was privatised to the US company *IVAX Corporation* and renamed *IVAX CR*. The third biggest player, the company *VUAB (Vyzkumny ustav antibiotek a biotransformaci)* was privatised in

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<sup>25</sup> O. BLANCHARD, *et al.* eds, *Reform in Eastern Europe*, Cambridge, Mass MIT Press, 1994., pp. 31-57.

<sup>26</sup> Seven interviewees involved in the regional pharmaceutical sector expressed similar views on the sector. Only the Polish representatives observed a declining number of firms and employment for the Polish industry.

<sup>27</sup> Ministry of Industry and Trade (Department of Chemistry and Pharmaceuticals) Czech Republic, *Perspectives of the Czech Pharmaceutical Industry*, Prague, 16 September 2002 .

1998 with the American company *ICN Pharmaceuticals* taking a majority stake. At the end of 1999 the Croatian generics medicines manufacturer, *Pliva*, purchased *Lachema*. It signified the last major privatisation deal in the Czech pharmaceutical industry. By the end of 1999 more than 80 per cent of the Czech pharmaceutical production capacity had passed into private and mostly foreign hands (see Table 12).

Following the creation of the independent Slovak Republic in January 1993 the underlying economic assets of the former Czechoslovak pharmaceutical industry were transferred to the new capital Bratislava<sup>28</sup>. The first foreign investor in the Slovak pharmaceutical industry established a joint venture between the German *Hoechst AG* and the local firm *Biotika* in 1992 with production starting in 1994. Slovakia's largest domestic producer, *Slovakofarma*, was re-organised as an independent entity in 1990. The company was privatised between 1992 and 1994 with *S.L.Pharma Holding GmbH* of Austria as the largest shareholder. The second largest manufacturing and distribution plant in Slovakia, *Leciva Sk* was established in Bratislava in July 1996 and formed part of the Czech company *Leciva Cz*<sup>29</sup>. In Slovakia the pharmaceutical industry was predominantly in private and foreign hands by 1998 (see table x).

### 3.2.2.2. Hungarian Pharmaceuticals

With the exception of Gideon Richter, all the large Hungarian producers were privatized between 1991 and 1996 to foreign pharmaceutical multinationals. Chinoin was the first company transferred into private hands when *Sanofi-Synthelabo* acquired a controlling share in 1993. Biogal was bought by Israeli generic manufacturer *Teva* in 1996. The State Privatisation and Holding Company (APV) allowed Human, formerly the *Hungarian Human Serum and Pharmaceutical Company*, to be reorganised in July 1992. Shortly afterwards, the Canadian pharmaceutical manufacturer, *Novopharm*, acquired a majority interest in the company. American pharmaceutical producer, *ICN*, took a majority stake in *Alkaloida*, the only remaining majority state-owned pharmaceuticals producer. By the end of 1996 Gideon Richter was the only major producer not owned by a multinational pharmaceutical company. In 1999, 62 per cent of the shares in the company were owned by a number of overseas investors while the Hungarian

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<sup>28</sup> S. DILOVA and L. MALYCHEVA, *Corporate Finance; Emerging Markets Special Report: Pharmaceuticals in Central and Eastern Europe*, FitchRatings, September 2002., p. 14.

<sup>29</sup> Espicom Business Intelligence, *World Pharmaceutical Markets: Slovakia*, West Sussex, May 1998, pp. 46., p. 20.

government, through the APV kept a 25.2 per cent share<sup>30</sup>. In April 2002 the government decided to keep the golden share of the state in Richter to ensure its independence and guarantee a continuing supply of cheaper pharmaceuticals on the Hungarian market. The Hungarian industry was the first to consolidate in the region (see Table 12).

### 3.2.2.3. Polish Pharmaceuticals

After 1989 the Polish MoI considered the pharmaceutical industry one of 18 Polish sectors with high development potential. About 66 Polish companies supplied the market in Poland with the Polfas dominating position.

The privatisation of Polish Pharmaceutical Works (Polfa) commenced relatively late compared to the other V-4<sup>31</sup>. A majority of domestic production capacity was still in state hands at the end of 2000. The sector was far from consolidated. The government had been reluctant to privatise Polfa to ensure a continuing influence over decisions regarding the range of pharmaceuticals produced. An early government commissioned report on the restructuring of the pharmaceutical industry was rejected. Only in 1994 was a restructuring programme for the industry approved.

It envisaged a restructuring to improve efficiency, profitability and production quality following a two step privatization plan. First, the Treasury would convert state-owned companies into joint-stock companies. By April 1997 three of the four largest pharmaceutical manufacturers in the country, i.e. *Polfa Krakow*, *Polfa Tarchomin* and *Polfa Poznan* had passed into joint-stock companies while the fourth largest company, *Polpharma Starogard Gdanski*, still underwent the process<sup>32</sup>. It was later privatised to Polish investors.

In the second phase the Treasury would divulge its remaining ownership. The first company of the Polfa conglomerate to be fully privatised was *Polfa Kutno*. It was listed on the Warsaw stock exchange and privatised for 49 per cent to *Enterprise Investors*, a US investment fund, and a number of national funds. Also a part of *Jelfa* was privatised via a share listing on the Warsaw stock exchange. Circa 60 per cent of the capital remained in state hands with 40 per cent owned

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<sup>30</sup> Espicom Business Intelligence, *World Pharmaceutical Market: Hungary*, West Sussex, February 2001, pp. 46., pp. 23-29.

<sup>31</sup> S. DILOVA and L. MALYCHEVA, *Corporate Finance; Emerging Markets Special Report: Pharmaceuticals in Central and Eastern Europe*, FitchRatings, September 2002., p. 11.

<sup>32</sup> J. OKRZESIK, *Poland by sectors: Production of Pharmaceuticals*, Warsaw: BOSS Informacje Ekonomiczne, 2001., pp 6-9.

by small shareholders. Majority shareholdings of *Polfa Poznan*, *Polfa Rzeszow* and *Polfa Krakow* were purchased by *Glaxo Wellcome* in 1998, ICN and Pliva in 1997 respectively<sup>33</sup>.

The opening of the Polish market to imported finished medicines preceded the protracted privatisation process of the industry by almost a decade, which in turn led to limited interest among investors from the sector. It was not surprising, therefore, that the remaining three state-owned pharmaceutical producers, i.e. *Polfa Tarchomin*, *Polfa Warszawa* and *Polfa Pabianice*, instead of being sold off, were consolidated in a holding structure<sup>34</sup>. After 2002 the government kept one pharmaceutical group, i.e. *Polski Holding Farmaceutyczny* (PHF) which included *Polfa Pabianice*, *Polfa Warszawa* and *Polfa Tarchomin*. PHF was still in state hands in 2004.

Foreign pharmaceutical companies had entered the Polish market much faster than the privatisation process would have allowed<sup>35</sup>. *Lek Polska* established a subsidiary of the Slovenian parent company as early as 1991. The second significant foreign pharmaceutical company to enter the Polish market was *Sanofi*. It signed a 50/50 joint venture agreement with *Biocom*, Poland's largest private pharmaceutical group. Slovenian pharmaceutical manufacturer, *Krka*, set up its first foreign factory near Warsaw and began production at the end of 2001.

By that time and unlike in neighbouring countries a substantial share of Polish pharmaceutical production capacity was still in state hands. It had resulted in a progressively declining domestic production capacity<sup>36</sup>.

### **3.3. Characteristics and Preferences: A Divided Industry**

In the next section I will consider the Global and EU pharmaceutical market, trade patterns (1992-2004), factor and asset specificity, sectoral cohesion and insider status for the industry across the region and the Czech Republic, Hungary, Poland and Slovakia individually.

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<sup>33</sup> Ibid., pp. 6-9.

<sup>34</sup> S. DILOVA and L. MALYCHEVA, *Corporate Finance: Emerging Markets Special Report: Pharmaceuticals in Central and Eastern Europe*, FitchRatings, September 2002., pp. 11-12.

<sup>35</sup> One of the reasons for a depleting market share of Polish drugs has been the inability of privatisation of pharmaceutical producers to boost sales. According to the Central Auditing Office (NIK), activities for the protection of the economic interests of producers of medicines and medical supplies failed to produce results, in: M. JEZIORSKI, *Pharmaceutical Market: Some Modest Proposals*, in: *The Warsaw Voice*, Warsaw: 25 August 2002.

<sup>36</sup> Espicom Business Intelligence, *World Pharmaceutical Markets: Poland*, West Sussex, December 2001, pp. 54., pp. 31-35.

A distinctive trait of the industry is the split along original and generic, and foreign and local pharmaceutical manufacturers respectively. The division had an influence on production, trade patterns and industry specificity and, therefore, on the intensity of preference formation and political mobilisation.

### **3.3.1. Trade**

#### **3.3.1.1. World Pharmaceutical Markets (1992-2004)**

Throughout the 1990s and early 2000s pharmaceutical companies were under intense pressure to develop new drugs while R&D development costs soared. Time to bring drugs to the market lengthened. The pharmaceutical industry is one of the most R&D-intensive sectors in the world economy. Worldwide the industry spent bn 39 US\$ on R&D in 1998. The average cost of bringing a new drug onto the market was estimated at above mn 300 US\$. Development and approval of new drugs generally takes more than a decade<sup>37</sup>.

To rein in R&D related expenditure and reduce risks many companies set up alliances and outsourced R&D activities as well as clinical testing of potential new drugs. The market witnessed a frenzy of new alliances and M&As. These occurred in three waves (1989, 1995 and 1999). The third wave was the most significant both in numbers and deal value<sup>38</sup>. While the first two waves involved large scale consolidation at national level the third upsurge took place on a more global scale. Large pharmaceutical companies, particularly in the US and the EU, acquired foreign holdings to expand their global market share and to exploit external resources for research and new product development purposes.

The nature of government regulation and oversight – particularly costs related to the time period and procedures for new drug approval – also influenced restructuring in the pharmaceutical industry, the size and geographical dimensions of the new alliances. Some manufacturing alliances reflected government requirements for local drug production.

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<sup>37</sup> OECD, *New Patterns of Industrial Globalisation Cross-border Mergers and Acquisitions and Strategic Alliances*, Paris, 2001 pp. pp. 1 - 175.

<sup>38</sup> *Ibid.*, pp. 78-81.



The countries with the world's leading pharmaceutical companies, i.e. the UK, France, Switzerland, Germany and the US experienced the largest deals. They became home to a relatively small number of global firms. These roughly 100 global firms performed most of the R&D of the world's pharmaceutical industry. They dominate the market for prescription drugs. It is also in their home countries that R&D remained concentrated with a large knowledge and research base.

The large research-based pharmaceutical companies, invest heavily in R&D, hold the bulk of the total patents and can often enjoy substantial market power. Returns on successful R&D are high. By and large, global firms rely on the revenues generated by a small number of products. For some major firms, three products alone can account for 70-80 percent of total pharmaceutical sales, and for most firms, these percentages are substantial. Therefore, they will protect their patents and property rights intensely against potential breaches of market regulations.

At the opposite end are a large number of smaller firms producing mostly for local or national markets. They undertake little R&D activity, hold fewer patents and rely primarily on manufacturing off-patent generic medicines or patent medicines under licence. These non-research firms will either produce drugs under licence for a local market which the licence holder does not want to serve. Alternatively, they produce out-of-patent drugs which do not require any large research facilities. Since the bulk of production as well as conversion into dosage forms involves little economies of scale these firms could be rather mobile and entry and exit from the industry relatively easy. Many of the manufacturing firms are located in the emerging Asian economies and in some countries in Eastern Europe such as Hungary, Poland and Slovenia<sup>39</sup>.

#### **3.3.1.2. EU-V-4: Eastern Exports and Western Imports**

Between 1992 and 2004 trade in pharmaceuticals in Central Europe doubled due to (a) growing domestic pharmaceutical markets; (b) rising exports of lower value and higher volumes of Central European produced generic medicines to the CEECs and the former S.U.; and (c) rapidly rising EU and US imports of higher value and lower volume of innovative drugs.

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<sup>39</sup> G. KLEPPER, Pharmaceuticals, in: P.-A. BUIGUES, A. JACQUEMIN and A. SAPIR, *European Policies on competition, trade and industry*, Aldershot, UK: Edward Elgar, 1995, pp. 329-66., p. 338; OECD, *Competition and Regulation Issues in the Pharmaceutical Industry*, Paris, 2000, pp. 401., p. 170.

## Growing Trade

At the outset of the EU enlargement process (1998) combined trade in pharmaceuticals in the Czech Republic, Hungary, Poland and Slovakia was worth between bn 4.2 and 4.3 US\$. When the V-4 joined the EU (2004) pharmaceutical trade had more than doubled reaching a total of approximately bn 9.9 US\$<sup>40</sup>. In 1998 exports of pharmaceuticals accounted for 27.8 per cent while imports took 72.2 per cent of total regional trade. At the end of 2004 imports as a share of regional trade had expanded to 75.3 per cent; exports had fallen to 24.6 per cent.

In 1998 Poland accounted for the biggest share of total regional trade in pharmaceuticals (42,5 per cent) followed by the Czech Republic (23.5 per cent), Hungary (23 per cent) and Slovakia (11 per cent). Differences in national population account for much of the variation, however, the capacity of the domestic industry accounts for most of the relative variations.

As Table 10 indicates Hungary's share of regional trade in pharmaceuticals rose by 7 per cent reaching a total of 29 per cent between 1998 and 2004. Poland's regional share of total trade weakened by equal measure and bottomed out at 35.6 per cent in 2004. The Czech Republic's share of total trade was 25 per cent in 1998 rising slightly over the entire period while Slovakia's share by and large remained stable. Overall, the share of pharmaceutical imports in the period 1998-2004 had risen most substantially relative to exports<sup>41</sup>. The Czech Republic and Hungary recorded the biggest increase of exports over the entire period.

**Table 10: Trade in Pharmaceuticals (per cent, 1992-2004)**

year	share of regional trade				share exports				share imports				share of export earnings				share of import earnings			
	Cz	Hu	Pl	Sk	Cz	Hu	Pl	Sk	Cz	Hu	Pl	Sk	Cz	Hu	Pl	Sk	Cz	Hu	Pl	Sk
92	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	na	2.5	1.2	n.a.	n.a.	2.7	3.4	n.a.
93	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	1.0	3.3	1.7	n.a.	2.6	2.8	3.7	n.a.
94	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	1.2	2.8	1.4	n.a.	3.2	3.3	3.6	n.a.
95	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	1.1	2.5	1.2	n.a.	3.2	3.1	3.3	n.a.
96	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	1.1	2.7	1.2	n.a.	2.7	3.1	3.1	n.a.
97	23.4	23.1	41.4	12.2	5.8	10.3	8.1	3.6	17.5	12.8	33.3	8.6	1.1	2.3	1.3	1.6	2.7	2.5	3.3	3.1
98	23.5	22.9	42.6	10.9	5.6	9.0	5.3	2.9	17.9	14.0	37.2	8.1	0.9	1.7	0.8	1.2	2.5	2.3	3.4	2.7
99	24.5	23.1	41.4	11.1	5.6	8.4	4.1	2.7	18.9	14.7	37.3	8.4	0.9	1.4	0.6	1.1	2.8	2.2	3.4	3.2
0	23.5	23.8	42.3	10.5	5.7	9.9	4.0	2.3	17.8	13.9	38.3	8.2	0.9	1.6	0.6	0.9	2.4	1.9	3.4	2.9
1	23.5	23.6	42.7	10.2	5.7	10.3	4.1	2.3	17.8	13.4	38.6	7.9	0.9	1.7	0.6	0.9	2.5	2.1	4.0	2.8
2	23.7	24.1	41.6	10.6	5.1	9.9	4.2	2.3	18.6	14.2	37.4	8.3	0.8	1.7	0.6	0.9	2.7	2.3	4.0	3.0
3	24.6	28.0	37.5	9.9	5.1	11.7	3.8	2.0	19.6	16.2	33.8	7.9	0.8	2.1	0.5	0.7	2.9	2.6	3.8	2.7
4	25.0	29.0	35.6	10.4	5.5	12.7	4.6	1.9	19.5	16.3	31.1	8.5	0.8	2.3	0.6	0.7	2.8	2.7	3.5	2.9
<b>Av.</b>	24.0	24.7	40.6	10.7	5.5	10.3	4.8	2.5	18.5	14.4	35.9	8.2	0.9	2.2	0.9	1.0	2.8	2.6	3.5	2.9

Note: Cz=Czech Republic, Hu=Hungary, Pl=Poland, Sk=Slovakia, Av.=average

Source: Own calculations on the basis of OECD, Bilateral Trade Statistics, 1994-2004

<sup>40</sup> Own calculations from OECD, Stan Bilateral Trade Database (1992-2004).

<sup>41</sup> Considering the export/import ratio (exports as a percentage of imports for an industry) the V-4 record substantial trade deficits from 1993 onwards (Cz=38.2, Hungary=92, Poland=28.4) which increase over the entire period to 2002 (Cz=27.7, Hungary=69.9, Poland=11.3, Slovakia=27). See OECD STAN Indicators Database, (1990-2002).

Demand for more advanced and predominantly foreign produced pharmaceutical products in Central Europe contributed to a steady growth of imports. The EU accounted for more than 60 per cent of total imports.

The Polish and Czech pharmaceutical markets grew most respectively<sup>42</sup>. In per capita terms the Czech Republic's consumption rose from around US\$ 96 in 1998 to US\$ 144 in 2003. The other more wealthy market in the region was Hungary growing from an estimated US\$ 88 in 1998 to 112 US\$ per capita in 2003. Slovakia and Poland were the poorer markets with Slovakia consuming around US\$ 85 in 1998 and 2003. Poland went from US\$ 78 (1998) to US\$ 93 per capita (2003).

The Polish and Hungarian markets 2001-2002 were dominated by local pharmaceutical producers claiming between 50 and 70 per cent of the market by volume. Slovakia imported more than 75 per cent of its consumption by volume, mostly from the Czech Republic. The share of domestically produced medicines in the Czech Market declined from 30 per cent (1999) covering around 20 per cent of domestic consumption in value terms in 2002<sup>43</sup>.

### **Eastern Exports**

Export of pharmaceuticals before 1990 was almost exclusively oriented towards the CEECs and COMECON markets. The pharmaceutical industry in Central Europe produced mainly generic drugs<sup>44</sup>. These exports were a source of high profits in the 1980s. They fell dramatically in the 1990s due to the production crunch in the early 1990s and breakdown of former export markets in the S.U.

By the mid 1990s exports to these countries had redeveloped. In 1995 Russia cancelled import licences for pharmaceuticals. Local producers picked up generic exports to the CEECs and S.U. where they had left them in the early 1990s. However, as Figure 12 indicates only Hungary

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<sup>42</sup> Espicom Business Intelligence, *World Pharmaceuticals Market*, West Sussex, August 2003, pp. 42.

<sup>43</sup> In value, Slovakia has one tenth coverage of drug consumption by domestic producers. It is the lowest among the surrounding countries, with Hungary and Poland both covering about one third of their requirements. The Czech Republic covers one fifth, in: J. BIEHUNEK, *The Expected Effects of the EU Accession on the Pharmaceutical Industry in the Slovak Republic*, Budapest: International Center of Economic Growth (Europe Center), May 2003., p 11.

<sup>44</sup> Czech Ministry of Trade and Industry (Chemical and Pharmaceutical Industry Department), *The Czech Pharmaceutical Industry*, Prague, June 2000, pp. 12.

survived the temporary loss of its pre-1990s export market. Between 1992 and 2004 it was the only V-4 that continuously maintained a trade surplus with non-EU countries.

The Russian financial crisis in 1998 was a second blow for the regions already volatile pharmaceutical export markets. It contributed to a re-orientation of trade towards the EU. For the Czech Republic, Poland and Slovakia the trade deficit in pharmaceuticals with non-EU 15 countries stabilised or grew<sup>45</sup>.

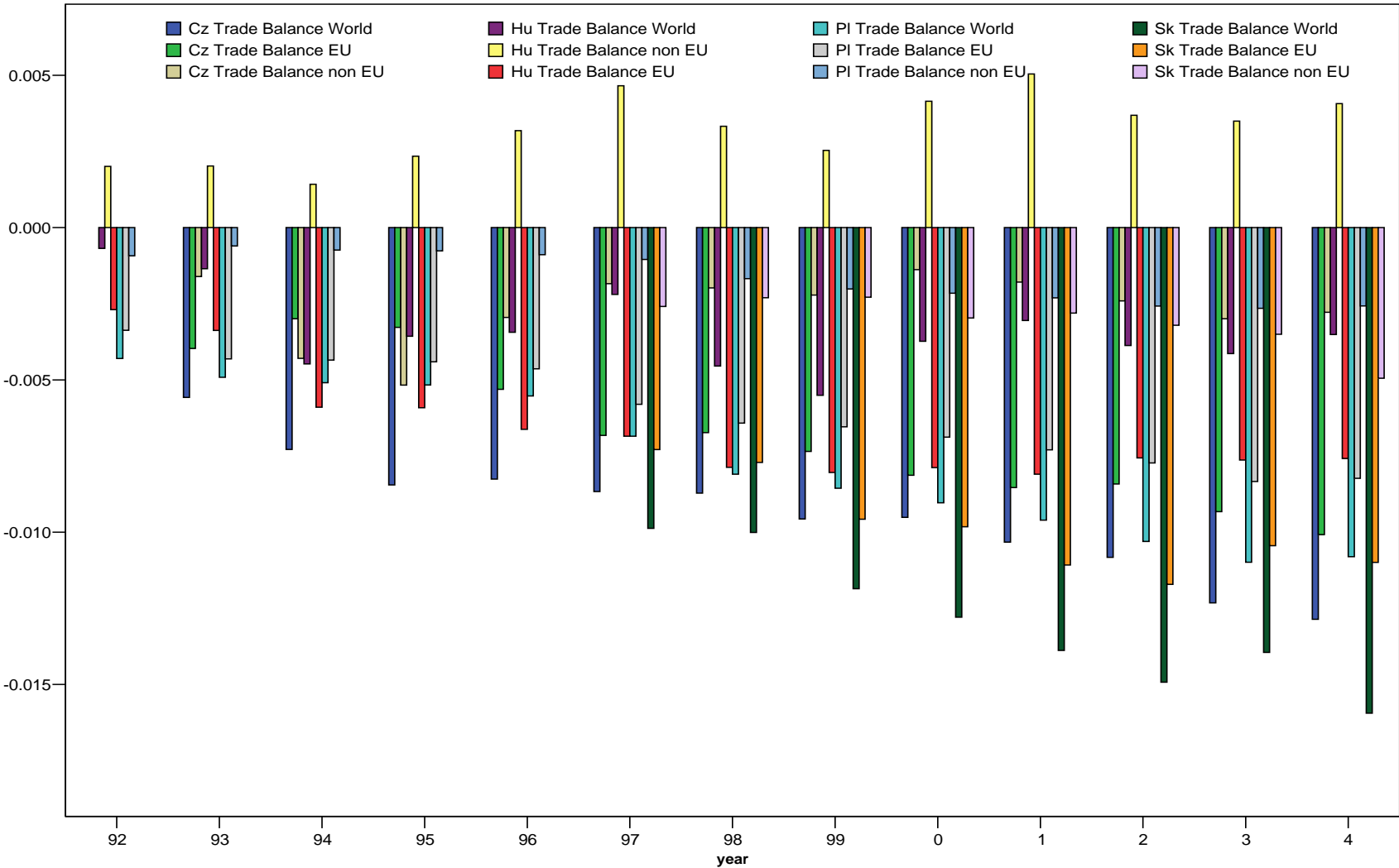
The Hungarian pharmaceutical industry had been by far the largest exporter. In 1997 it accounted for 37.2 per cent of total V-4 exports followed by Poland (29 per cent), Czech Republic (21 per cent) and Slovakia (12.8 per cent). At the end of 2004 the Hungarian pharmaceutical industry had expanded its export markets by a remarkable 14.3 per cent accounting for just over half of total regional exports in the sector. Polish and Slovak exports shrunk over the same period from 29 and 12.8 per cent to 18.6 and 7.6 per cent respectively. Merely the Czech pharmaceutical producers had been able to follow Hungary's lead, however, only by 1.33 per cent. Considering export earnings, Hungarian exports of pharmaceuticals account on average for 2.2 per cent of total export earnings between 1992 and 2004 while all other V-4 countries are exporting below 1 per cent of total exports. The Hungarian industry is the only one to consistently show a growing positive trade balance<sup>46</sup> (see Figure 12).

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<sup>45</sup> Export specialisation shows a country's exports for an industry relative to total industries' exports. A value of 100 in certain country implies that the country tends to specialise in exports in that given industry. The index of revealed comparative advantage for the V-4 indicates that only Hungary specialised in pharmaceutical exports in 1993 (Cz&Sk=49, Hu=158.5, Pl=83.7, EU-14=119). Hungary's specialisation in pharmaceuticals progressively deteriorates by 2002 (Cz=19.1, Hu=41.4, Pl=14.8, Sk=22.2 with the EU-14=127.3). See OECD STAN Indicator database, (1990-2002).

<sup>46</sup> The contribution to trade balance (CMTB) indicator makes it possible to identify an economy's structural strength via the composition of international trade flows. It takes into account not only exports, but also imports, and compares an industry's trade balance with the overall trade balance. It indicates whether an industry performs relatively better than the manufacturing total regardless of an overall trade surplus or deficit. While negative, Hungary's CMTB scores over the period 1997-2002 are better than its neighbours at -0.2 (1997) to -0.3 (2002) with Poland and Slovakia moving from -1.1 (1997) to -1.9 and -1.3 (2002) respectively followed by the Czech Republic at -1 (1997) to -1.1 (2002). The EU-14 was 0.2 in 1993 and 0.3 in 2002. See OECD STAN Indicator database, (1990-2002).

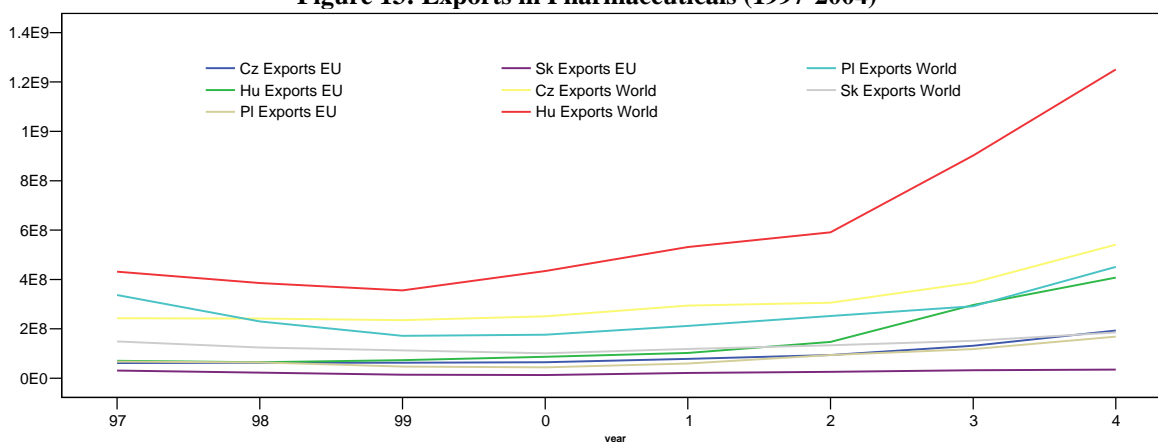
Figure 12: Trade Balance in Pharmaceuticals (1992-2004)



Note: Cz=Czech Republic, Hu=Hungary, PI=Poland, Sk=Slovakia  
 Source: Own calculations on the basis of OECD, Stan Bilateral Trade Database (US\$ normalised by GDP), 1992-2004, Data 1992-1996 for Sk not available.

By the mid 1990s the regional pharmaceutical producers started to consider EU markets as export destinations (see Figure 13). Exports to the EU had been flat or declining for most of the 1990s. They rose annually from 1999 onwards with particularly the Hungarian industry seeing its exports soar from 2000 onwards. Also the Czech Republic and Poland expanded their market share in the EU. Trade by value remains small compared to non EU markets and particularly compared to EU imports (see Figure 12)<sup>47</sup>.

**Figure 13: Exports in Pharmaceuticals (1997-2004)**



Note: Cz=Czech Republic, Hu=Hungary, Pl=Poland, Sk=Slovakia

Source: Own calculations on the basis of OECD, Bilateral Trade Statistics, US\$, 1997-2004

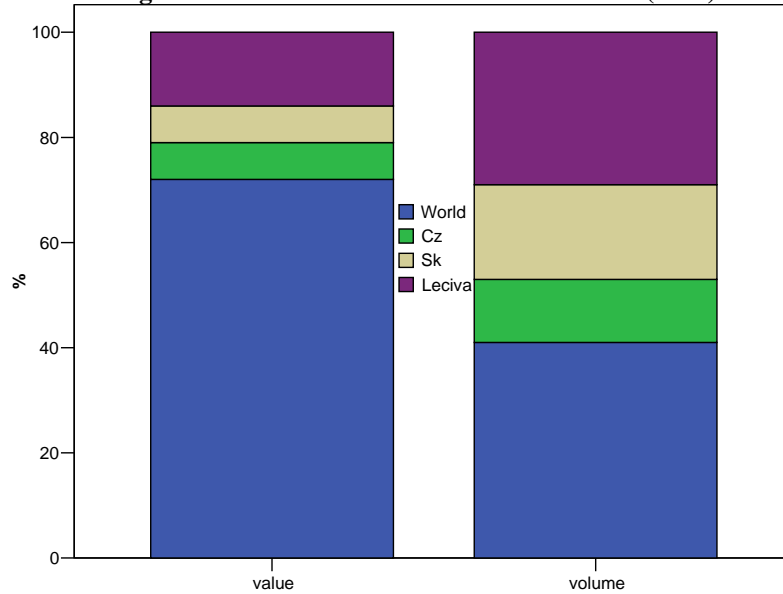
### Western Imports

At the outset of the 1990s the V-4 opened up their markets for finished pharmaceutical products from the EU. Its citizens had developed a taste for more modern medicine coming from abroad. The pharmaceutical trade deficit that emerged in the years 1991-1992 grew substantially towards the end of the decade and early 2000s resulted in an overall pharmaceutical trade deficit for all V-4 countries (see Figure 12)<sup>48</sup>.

<sup>47</sup> For instance, 75 per cent of Hungarian pharmaceutical imports come from the EU, in: S. DILOVA and L. MALYCHEVA, *Corporate Finance; Emerging Markets Special Report: Pharmaceuticals in Central and Eastern Europe*, FitchRatings, September 2002., p. 10.

<sup>48</sup> Export shares of production indicate that the Czech Republic increasingly exports its domestic produce. In 1993 33.1 per cent of its domestic production is destined for export markets reaching 67.3 per cent by 2002. Also Hungary raises the share of its exports relative to domestic production (38.6 in 1998 to 48.3 in 2001). Poland share of exports relative to domestic production declines from 29.2 in 1997 to 15.5 in 2001. Available import penetration ratios confirm these findings as the Czech Republic exports 63.5 per cent of its domestic production rising to 86.5 by 2000. Hungary's import penetration ratio is stable around 50 per cent with Poland's hovering between 54 and 65 over the same period. The EU-14 import penetration ratio stood at 40.3 in 1995 rising to 53.7 by the turn of the century. Data for Slovakia are absent. See OECD, STAN Indicator database, (1992-2002).

**Figure 14: The Czech Pharmaceutical Market (1999)**



Note: Cz=Czech Republic, Sk=Slovak Republic, Leciva=Czech pharmaceutical company

Source: Episcom Business Intelligence, *World Pharmaceutical Markets: Czech Republic*, West Sussex, March 2001, p 25

The Czech pharmaceutical market relied mainly on pharmaceutical imports by value (see Figure 14). Liberalisation brought a loosening of the pharmaceutical market resulting in an enormous rise of foreign medicines on the Czech market. In 1999 world imports in value terms totalled 72 per cent while domestic production, i.e. Czech produced medicines and those produced by the Czech market leader, Leciva, accounted for 20 per cent of the market followed by Slovak originated medicines with 7 per cent. In volume terms, however, world imports accounted for 41 per cent while Leciva, Czech and Slovak produced medicines took a combined 59 per cent of the market<sup>49</sup>.

Imported drugs dominated the pharmaceutical market by value and volume in Slovakia<sup>50</sup>. Slovak producers covered 15.1 per cent of the market by value in 1995 declining to 10.9 per cent in 2001, the lowest of all V-4 with Hungary and Poland covering about one third of their requirements and the Czech Republic just one fifth<sup>51</sup>. Competition in the V-4 for domestic producers came above all from large multinational companies producing original drugs.

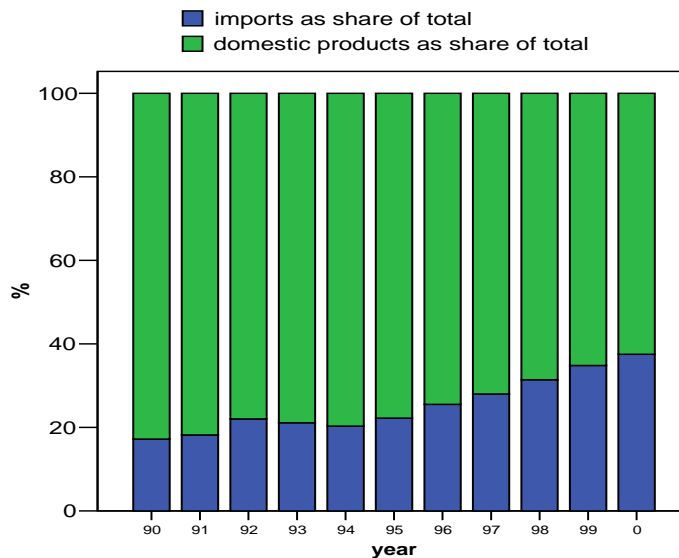
<sup>49</sup> Episcom Business Intelligence, *World Pharmaceutical Markets: Czech Republic*, West Sussex, March 2001, pp. 46.

<sup>50</sup> Episcom Business Intelligence, *World Pharmaceutical Markets: Slovakia*, West Sussex, April 2003, pp. 42., p. 27.

<sup>51</sup> In 1995 it was 24.1 per cent declining to 17.9 per cent in 2001, in: J. BIEHUNEK, *The Expected Effects of the EU Accession on the Pharmaceutical Industry in the Slovak Republic*, Budapest: International Center of Economic Growth (Europe Center), May 2003., p. 45-46.

In Hungary (see Figure 15) imports account for around 47 per cent of the market by value. Despite the increasing reliance on imported drugs, domestic manufacturers continue to dominate with locally-produced drugs accounting for the lion's share of the market equal to 62.5 per cent of the total in 2000. Like in Poland, this volume share is falling from 74.5 per cent in 1996 and above 80 per cent in 1990<sup>52</sup>.

**Figure 15: The Hungarian Pharmaceutical Market (1990-2000)**



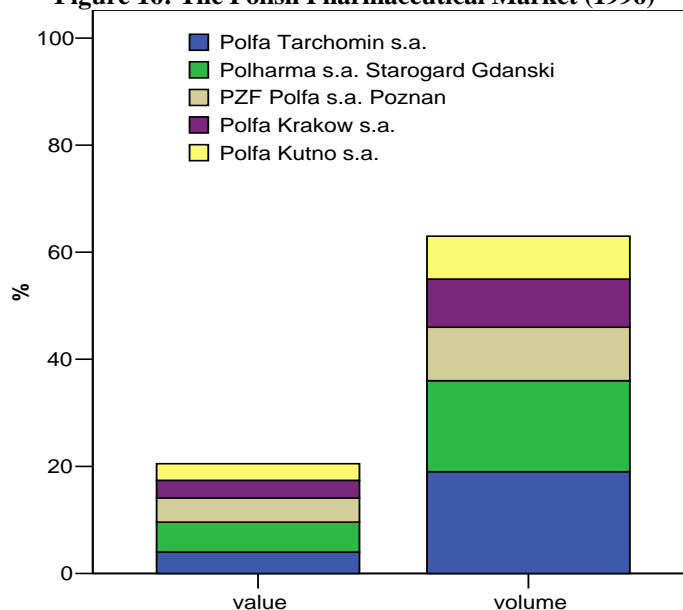
Source: Episcom Business Intelligence, *World Pharmaceutical Markets: Hungary*, September 2003, p. 24.

In Poland the five leading domestic producers had a share of the Polish market by value of approximately 20 per cent (see Figure 16). However, in volume terms the five leading polish producers accounted for more than 50 per cent of total consumption in 1996.

<sup>52</sup> Episcom Business Intelligence, *World Pharmaceutical Markets: Hungary*, West Sussex, September 2003, pp. 50., p. 24.



**Figure 16: The Polish Pharmaceutical Market (1996)**



Source: Episcom Business Intelligence, World Pharmaceutical Markets: Poland, April 2000, p. 30

The local industry produced for about 90 per cent generic medicines and supplied 2/3<sup>rd</sup> of the market volume but only approximately 40 per cent in value terms.

There are a number of reasons for the high-volume-low-value exports; and high-value-low-volume imports and domestic consumption in the V-4 countries. First, locally produced pharmaceuticals have lower prices compared to imported products due to government controlled prices of domestically produced pharmaceuticals<sup>53</sup>. Second, low reimbursement rates of drugs made generics more affordable for local consumers compared to imported drugs.

Selective evidence suggests that imports relative to domestic production rose steadily in the region. Under threat of international competition revenues are likely to decline. Under these conditions the pharmaceutical industry faced higher adjustment costs leading to an overall

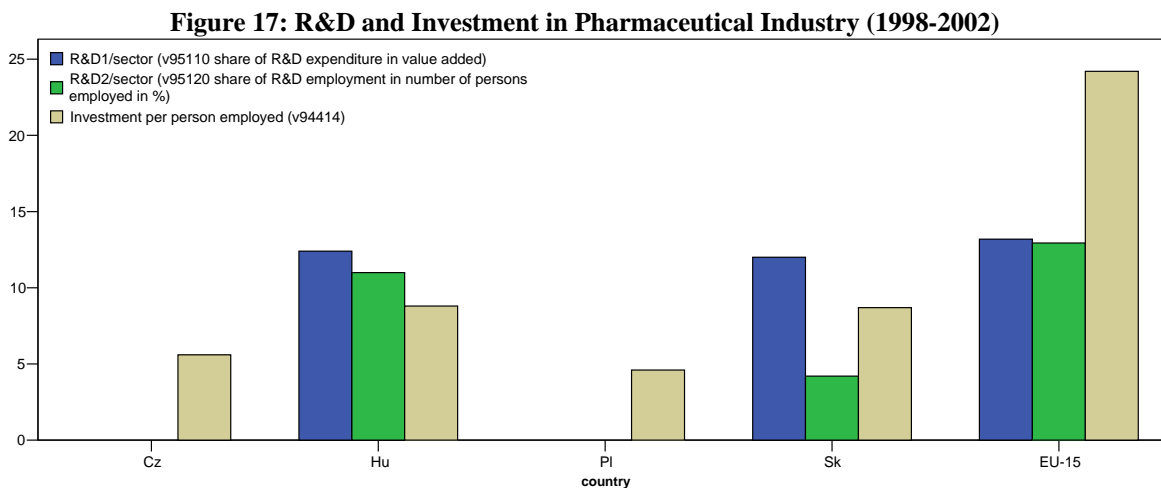
<sup>53</sup> According to 2001 figures from Polfarmed, the Polish Pharmaceutical Industry Association, the average price of Polish medicines in pharmacies was Zl 4.70 compared to imported medicines costing on average Zl 17.61. An estimated bn 1.2 bn packages with an average price of Zl 7.10 were sold on the Polish market in 2001. Domestically produced drugs took a share of the market volume at around 70 per cent of packages sold, in: Episcom Business Intelligence, *World Pharmaceutical Markets: Poland*, West Sussex, July 2003, pp. 56., p. 28.

decline in income. The pharmaceutical industry, having specific assets, had great incentives to expend more resources to avert this economic loss.

### 3.3.2. Asset Specificity: A High Technology Manufacturing Industry?

How factor and asset specific is the pharmaceutical industry in Central Europe? And is there a variation of specificity within the pharmaceutical Industry in the region?

According to the OECD Classification of manufacturing industries based on technology the pharmaceutical industry is regarded as a high-technology manufacturing industry<sup>54</sup>. The pharmaceutical sector has assets that are tied specifically to inventing, producing and distributing medicines. The degree to which these assets are present can be measured with industry data from R&D expenditures.



Note: Cz=Czech Republic, Hu=Hungary, Pl=Poland, Sk=Slovak Republic,  
Source: Own calculations based on Eurostat, Annual Detailed Enterprise Statistics (averages, 1998-2002); no R&D data available for the Czech Republic and Poland

The Hungarian pharmaceutical industry invested most followed closely by the Slovak, the Czech and the Polish industry (see Figure 17). Overall, the level of investment per person is around three times as small as the EU-15 average. Taking into account the other R&D measures the Hungarian producers lead the V-4. Its R&D expenditure comes close to the average for the EU-15. Slovakia trails Hungary by a narrow margin but not as much when observing the number of R&D persons employed.

<sup>54</sup> OECD, *Science, Technology and Industry Scoreboard, Classification of manufacturing industries based on technology*, Paris, 2003. The scoreboard is based on the OECD, ANBERD and STAN databases.

The numbers indicate that the pharmaceutical industry in Central Europe is high on factor specificity but less so than in the EU-15. Within the region Hungary appears most asset specific followed by Slovakia, Czech Republic and Poland. Much of the difference between the industry in Central Europe and the EU-15 can be explained by the product range. The pharmaceutical industry in Central Europe manufactures products with low value added. The share of high value added is insufficient to close the gap with the EU-15<sup>55</sup>.

Figures on the number of annually granted patents and R&D personnel largely confirm these findings (see Table 11). In relative terms both measures are at least five times smaller in Central Europe compared to the EU-15. Despite a favourable turn in the late 1990s and early 2010s the level of investment in the pharmaceutical industry in Central Europe remains relatively low – roughly at one third of the level in the EU-15. Investment in Central Europe from major global drugs firms is predominantly geared towards the distribution and manufacture of off-patent drugs, which requires lower levels of R&D and investment.<sup>56</sup>

**Table 11: Specificity of the Pharmaceuticals Sector (1998-2002)**

<b>country</b>	<b>patent 1</b>	<b>patent 2</b>	<b>skill</b>	<b>R&amp;D3</b>	<b>R&amp;D4</b>
Czech Republic	16	0.2	4	n.a.	n.a.
Hungary	34	0.24	4	1572	0.11
Poland	27	0.1	4	n.a.	n.a.
Slovakia	12	0.3	4	179	0.04
EU-15	5282	1.07	4	806	0.2

Note: patent 1= number of patents related pharmaceuticals  
patent 2= number of patents per 100 persons employed in pharmaceuticals  
skill= ISCO-88 skill level  
R&D3= number of R&D personnel employed  
R&D4= number of R&D personnel employed over total sectoral employment

Source: European Patent Office (EPO) and Eurostat (Annual Detailed Enterprise Statistics, averages 1998- 2002)

While the share of generics has declined with the rising availability of sophisticated imports and the tightening of patent laws, generic pharmaceutical products typify the industry in the V-4 (see Table 12).

<sup>55</sup> Eurostat, *Industry Trade and Services, Statistics in focus: the Pharmaceutical Industry in the European Union*, Luxembourg, 2005, pp. 8.

<sup>56</sup> Ministry of Industry and Trade (Department of Chemistry and Pharmaceuticals) Czech Republic, *Perspectives of the Czech Pharmaceutical Industry*, Prague, 16 September 2002

In the Czech Republic all the major generic medicine producers hold stakes in the country such as ICN, IVAX and Pliva. The share of high value added domestic products based on original molecules remains insufficient. Multinational production is limited. Most original and modern branded produce at the high end of the market are imported in retail form. As a result, the R&D base remains underdeveloped and little room for innovation exists<sup>57</sup>.

Likewise, in Hungary the domestic market has been traditionally supplied by locally-produced generic products, which often were copies of western originals legal under Hungarian law. Generic drugs account for around 55 per cent of drugs registered in Hungary with around 10 per cent being copies of patented products. When considering domestic production a majority produces generic medicines with R&D expenditures that are considerably smaller compared to those producing original medicines<sup>58</sup>. Nonetheless, the Hungary industry remained the most innovative and advanced in the region (see table 11).

Over 90 per cent of Polish produced medications out of the 10,000 pharmaceuticals registered at the end of the 1990s can be categorised as inexpensive generic drugs. In Slovakia the number is estimated at 55 per cent. In both countries multinationals producing original medicines have limited manufacturing presence with the exception of Hoechst-Aventis in Slovakia. The largest R&D spenders in Slovakia are Slovakofarma and its subsidiary *VULM* (the Drug Research Institute in Modra), where research is carried out for Slovakofarma. Hoechst Biotika under the control of pharmaceutical giant Aventis has focused exclusively on production, keeping R&D activities in the West<sup>59</sup>.

### **3.3.4. Sectoral Cohesion: A Split Political Organisation**

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<sup>57</sup> Association of the Czech Pharmaceutical Industry (ACPI), *The Czech Pharmaceuticals Industry*, Prague, November 1999, pp. 6, Foreign Commercial Service and U.S. Department of State, *International Market Insight: Pharmaceutical Industry, Czech Republic, Profile of Leading Firms*, September 2001, pp. 6, Espicom Business Intelligence, *World Pharmaceutical Markets: Czech Republic*, West Sussex, March 2001, pp. 46, Espicom Business Intelligence, *World Pharmaceutical Markets: Czech Republic*, West Sussex, April 2002, pp. 48, Czech Ministry of Trade and Industry (Chemical and Pharmaceutical Industry Department), *The Czech Pharmaceutical Industry*, Prague, June 2000, pp. 12.

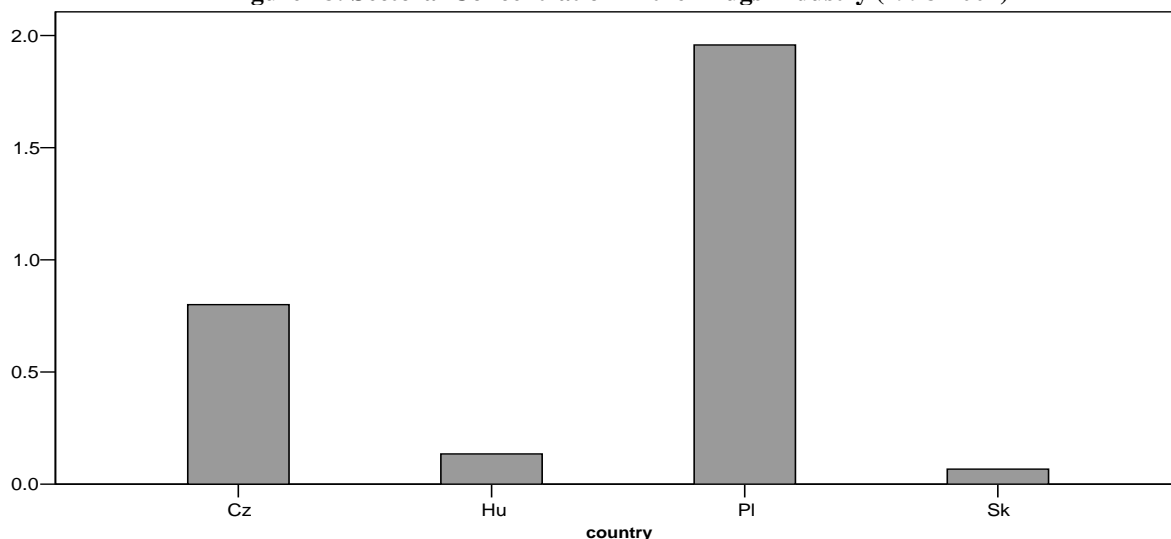
<sup>58</sup> Ministry of Economy and Transportation, *The Pharmaceutical Industry in Hungary*, Budapest, October 2000, pp. 15, Espicom Business Intelligence, *World Pharmaceutical Market: Hungary*, West Sussex, May 2002, pp. 50, Espicom Business Intelligence, *World Pharmaceutical Market: Hungary*, West Sussex, February 2001, pp. 46, Espicom Business Intelligence, *World Pharmaceutical Markets: Hungary*, West Sussex, September 2003, pp. 50.

<sup>59</sup> J. BIEHUNEK, *The Expected Effects of the EU Accession on the Pharmaceutical Industry in the Slovak Republic*, Budapest: International Center of Economic Growth (Europe Center), May 2003., p. 6.

Sectors that encounter fewer collective action problems have the greatest incentive to lobby for industry-specific policies. They are likely to exert more political pressure on policy makers and tend to be more successful. It is possible to test this conjecture using the number of firms per sector combined with the number of employees per firm and calculating a sectoral concentration ratio for the years 1998-2002. A small number of firms with a high number of employees per firm produce a small concentration ratio. Ergo, the smaller the ratio, the higher the concentration.

Slovakia and Hungary have highly concentrated pharmaceutical sectors followed by the Czech Republic and Poland (see Figure 18). The sectoral concentration ratio for Slovakia and Hungary is close to zero followed by the Czech Republic. Poland on the contrary is characterised by a large number of smaller firms.

**Figure 18: Sectoral Concentration in the Drugs Industry (1998-2002)**



Note: Cz=Czech Republic, Sk=Slovak Republic, Leciva=Czech pharmaceutical company

Source: Own calculations based on Eurostat, Detailed Enterprise Statistics (averages 1998-2002) ratio of number of firms over number of employees per firm (indicators v92100 and v16130)

Taking into account the four firm concentration ratio, around 50 per cent of the Czech pharmaceutical market (see Table 12) by value is dominated by just 13 companies. When considering market share by volume and employment the number of firms declines to just four, i.e. Leciva (Zentiva), Slovakofarma, Pliva-Lachema and ICN Czech Republic (VUAB). In Hungary ten firms control more than 50 per cent of the total market by value. Taking into account

volumes and employment the so-called big six, i.e. Egis, Gideon Richter, ICN, Chinoin, Biogal and Human account for a large majority of sales and number of persons employed. From all the Central European countries Hungary has the highest number of large firms in the sector.

By comparison, the Polish pharmaceutical market is fragmented with many firms and a smaller number of employees per firm. While their share has declined sharply over the 1990s the 14 major domestic players, which were all part of the former United Pharmaceutical Works Polfa, dominate the market<sup>60</sup>. According to the Polish Chamber of the Pharmaceutical Industry 350 companies are allowed to produce medicine in Poland. Most of them are small private enterprises that produce plant based medicines. Only 20 per cent or around 70 companies employ more than 49 people.

The Slovak pharmaceutical industry output was generated by four companies, Slovakopharma, Biotika, Hoechst-Biotika and Imuma. Hlohovec-based Slovakopharma dominates Slovak output accounting for 75 per cent of sales in 2001. The remaining industry capacity consists of smaller local companies whose influence in the sector is insignificant.

#### **3.3.4.1. National Associations**

National and international associations are the most common political assets of the industry. They are the political extensions of the economic interests that sometimes might function as a go-between in the economy-state relationship. Associations influence the heavily regulated environment in which the industry operates. They seek policy partnership with the authorities.

The authorities regulating the industry are by far its largest customer. Funding health care is a major component of national budgets and more so in the V-4 than other OECD countries. Governments have a powerful vested interest in securing the cheapest possible drugs and hence partnership with the market operators to attain these goals<sup>61</sup>. Therefore, the authorities have a

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<sup>60</sup> S. DILOVA and L. MALYCHEVA, *Corporate Finance; Emerging Markets Special Report: Pharmaceuticals in Central and Eastern Europe*, FitchRatings, September 2002., p. 11.

<sup>61</sup> See S. BERGER, *Organizing interests in Western Europe: pluralism, corporatism, and the transformation of politics*, Cambridge UK; New York: Cambridge University Press, 1981.

preference for consultation and co-operation with the industry to achieve mutually beneficial agreements over unitary decision-making processes<sup>62</sup>.

However, empirical analysis of political assets of the regional pharmaceutical industry suggests that associations and authorities do not always operate in tandem because of opposing economic interests. National associations in the pharma sector are by and large split along the lines of domestic producers and multinational subsidiaries; and/or generic drugs producers and innovative research based companies. The split mirrors the European and international division among pharmaceutical producers.

Generic drugs manufacturers tend to be associated in a national generic pharmaceutical association which in turn are member of the European generics federation. Likewise, original drug producers are associated in research based associations and federated in the European research based sectoral representation (**see table x and World Pharma Markets**). The latter are professional lobby agents while the former are industrial representatives.

#### **Czech Republic: CAFF and MAFS**

There are two leading manufacturers' associations in the Czech Republic. The *Czech Association of Pharmaceutical Companies (CAFF)* represents local companies and predominantly generic manufacturers<sup>63</sup>. The *International Association of Pharmaceutical Companies (MAFS)* represents the global research-based companies<sup>64</sup>.

CAFF was created in 2001 out of the Association of Producers of Healing Substances (SVLP) and the Association of the Czech Pharmaceutical Industry (SCFP). The association had a market share of 55 and 32 per cent by volume and value respectively. It had a dominant position in the drug market reimbursed by the Czech health care<sup>65</sup>. CAFF associates 30 companies. It had three membership levels. At the highest level each company had one vote. They counted more heavily in the decision-making. Among its members nine were domestic producers and 18 were importers of generic medicine. Four companies had disproportionate sway in the association's

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<sup>62</sup> J. GREENWOOD and K. RONIT, Pharmaceutical Regulation in Denmark and the UK: Reformulating interest representation to the transitional level, in: *European Journal of Political Research*, 1991, 19(3), pp. 327-59, p. 329.

<sup>63</sup> See website: <http://caff.tradecentrum.cz/>

<sup>64</sup> See website: <http://www.mafs.cz/cz/index.php>

<sup>65</sup> Interview by Author with Representative of the Czech Association of Pharmaceutical Companies, Prague, 02/05/2004.

decision making with Zentiva as the market leader taking a special place<sup>66</sup>. The bigger companies also contributed more to the budget of the association. With the exception of Pliva-Lachema the presidency, vice presidency and members of the board come predominantly from Zentiva, Teva Pharmaceuticals CR, IVAX Pharmaceuticals and VUAB, all major generic medicine producers (see Table 12).

CAFF is a member of the Association of the European Self-Medication Industry (AESGP)<sup>67</sup>. It did not join the *European Generic Medicine Association* (EGA) because amongst its members were also original producers of medicines. Some of its bigger member companies are directly member of EGA<sup>68</sup>. Because of the representation of domestic pharmaceutical producers the authorities regard CAFF as an insider. It has well trodden communication channels with the Czech MoTI and the MoH.

From 1998 onwards its members felt the effects of EU enlargement regulations impinging upon the market environment: ‘Application of EU legislation ahead of EU enlargement started to have a substantial impact on our member’s profits. There was a dominant feeling among the members that we were left out in the cold’<sup>69</sup>.

CAFF’s members mobilised politically: ‘The Czech pharma producers did not want to pay royalties on some of the medicines they were producing. They wanted to continue producing generic medicines. They were very active to protect their interests and contacted the ministry. Their goal was to export to the East and keep these markets. They opposed retroactive patent protection for medicines in production and asked for a transition period’<sup>70</sup>.

‘Foreign producers including those that did not have a production base in the country were also politically active. They lobbied for the strict application of the *acquis*. Particularly German firms pressured the ministries and the [chief negotiator] team for strict application of EU pharma

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<sup>66</sup> Ibid.

<sup>67</sup> The AESGP is the representative body of the non-prescription pharmaceutical industry in Europe. Its membership consists of national associations of manufacturers and distributors of medicines, which are available without prescription, with or without a prior medical diagnosis. Sectoral organisations from Central and Eastern European countries are associate members. The organisation was not lobbying in regard to EU enlargement.

<sup>68</sup> See <http://www.egagenerics.com/>

<sup>69</sup> Interview by Author with Representative of the Czech Association of Pharmaceutical Companies, Prague, 02/05/2004.

<sup>70</sup> Interview by Author with Representative 3 of the Negotiation Team of the Czech Republic, Prague, 19/03/2004 and 22/03/2004.



legislation in the Czech Republic<sup>71</sup>. The latter were represented by the International Association of Pharmaceutical Companies (MAFS).

According to its spokesperson MAFS is comparable to an ‘import representation’<sup>72</sup>. It was founded in 1993 and associated 32 out of a total of 35 representatives of the largest global innovative and research based pharmaceutical companies present in the Czech Republic. Its membership changed slightly because of M&As and the entry of new players in the market. In 1989 its member companies had zero market share: ‘Modern drugs were only available to Czech elites’. By 2001 these 32 firms had just over 50 and 30 per cent of the Czech pharmaceutical market by value and volume respectively<sup>73</sup>. MAFS is well funded and runs a small secretariat of internationally schooled personnel in Prague.

The mission of MAFS is to represent importing pharmaceutical companies on a national and international level. It co-ordinated joint efforts and helped its members in obtaining new market authorisations and represent their companies in annual drug pricing negotiations with the MoH. MAFS encouraged absolute transparency, monitored the market for correct observance of intellectual property rights protection and ‘attempts to ensure that national legislation does not damage its members’.

Being an import representative of the global research based pharmaceutical companies they encouraged the application of intellectual property rights and EU patent legislation. MAFS supported EU enlargement and welcomed the transposition of the *acquis*: ‘We are used to international regulations and the *acquis*. The Czech market has accepted EU harmonisation and adjusted. It increased drug quality standards [safety and efficacy of drugs] and encouraged steady growth for our members over the last five or six years at 1-digit level [5 or 6 per cent]’<sup>74</sup>.

MAFS chief concern was drug pricing differences between the candidate countries and the EU-15, which they feared would lead to parallel trade after EU accession. With the applicant countries having lower price levels particularly because of the presence of a strong generic

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<sup>71</sup> Ibid.

<sup>72</sup> *Interview by Author with Representative of the Czech Research Based Pharmaceutical Industry Prague, 25/03/2004.*

<sup>73</sup> Ibid.

<sup>74</sup> Ibid.

industry the risk of parallel trade after EU membership was real. Strict application of EU legislation would preclude parallel trade<sup>75</sup>. Unlike its domestic counterpart MAFS was not regarded an insider. It became a member of EFPIA in 2001 and the International Federation of pharmaceutical manufacturers and associations (IFPMA) based in Geneva in 1995.

### **Hungary: MAGYOSZ and AIPM**

The majority of domestic pharmaceuticals producers by volume in Hungary are associated in the *Hungarian Pharmaceutical Manufacturers Association (MAGYOSZ)*. The representatives of foreign pharmaceutical producers that predominantly import finished pharmaceutical products are allied in the *Association of Pharmaceutical Manufacturing (AIPM)*. The former predominantly speaks for generic producing manufacturers while the latter acts for the original and research based manufacturers. Only a minority of the innovative industry joined MAGYOSZ.

MAGYOSZ was established in 1990 to help its members cope with a changing economic situation. Up to 1995 MAGYOSZ incorporated all actors in the Hungarian pharmaceutical sector, i.e. producers of innovative, generic and over-the-counter (OTC) products, retailers, research firms and institutes<sup>76</sup>. It represented 50 firms in 2000<sup>77</sup>. Of those the seven largest have a majority (approximately 80 per cent) of the domestic market by volume and sectoral employment (see Table 12). Large firms with more than 1,000 employees are the driving forces behind the organisation<sup>78</sup>. They nominate the president, the vice-president and the majority of the seven members of the presidential council<sup>79</sup>. The concentration of influence in the top six firms ensures that the organisation functions well. Gideon Richter and EGIS take on a special role within the organisation as they are correspondingly the largest and third largest pharmaceutical producers in Hungary.

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<sup>75</sup> Ibid.

<sup>76</sup> In the second half of the 1990s retailers set up their own association. In 1992 four member companies launched a generic producers association. They later rejoined MAGYOSZ. Also OTC producers attempted an independent organisation but re-joined in 1997.

<sup>77</sup> For a more detailed overview see P. CZAGA, Chapter 3: Case study on the pharmaceutical sector, in: *Interest Groups and the Eastern Enlargement of the EU*, 2001, *Ph.D dissertation (University of Sussex, European Institute)*.

<sup>78</sup> Out of the remaining 43, 18 companies have between 50 and 500 employees, while 25 of them belong to the smallest category, with between 1 and 50 employees. These latter ones are mostly small R&D institutes.

<sup>79</sup> P. CZAGA, Chapter 3: Case study on the pharmaceutical sector, in: *Interest Groups and the Eastern Enlargement of the EU*, 2001, *Ph.D dissertation (University of Sussex, European Institute)*.

MAGYOSZ is a well-funded and well-resourced interest group as its members are affluent firms. It is represented by multilingual administrators that are domestically well connected. MAGYOSZ is regarded an insider for the authorities. It is consulted on draft legislation and public policy through a partially formalised structure such as the annual roundtable discussions with the MoH and MoFi over price levels and the reimbursement system for medicines.

This insider status is partly explained by its shared interests with the government in the use of cheaper domestically produced generic medicines in the state owned health care system. General budgetary constraints in the social insurance system encourage the use of domestic generic medicines as opposed to more expensive imported innovative products<sup>80</sup>. According to one official the influence of international ownership such as for Gideon Richter gave them additional sway on an international level to push for lenient application of EU legislation<sup>81</sup>.

MAGYOSZ mobilised early on EU enlargement and the application of the *acquis*. In 1998 it set up a lobbying campaign to convince the Hungarian authorities about a TPR delaying patent protection legislation. The strategy was based on ‘gaining the health authorities as an ally’. The leaders of MAGYOSZ used their close working relations with the MoH, social security funds and the medicine agency. MAGYOSZ aimed at raising awareness and convincing health officials that it was also in their interest to keep a large number Hungarian produced generic products available for Hungarian patients. The industry chose to present the problem as not only an industrial protection issue, but as a general economic, political and health issue.

At a conference on EU accession, *Gyorgy Thaler*, CEO of Gideon Richter affirmed that ‘putting in force any kind of regulation that would result in the disappearance of these generics from the Hungarian market is not only a business question, but a social, and therefore a political one as well. It would cause social and political tension. We believe that all regulation should consider the interest of the domestic general industries and should use a stepwise approach’<sup>82</sup>.

MAGYOSZ put forward two TPRs to the government:

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<sup>80</sup> Ibid.

<sup>81</sup> Interview by Author with Representative of the Slovak State Institute for Drug Control, Bratislava, 12/03/2004.

<sup>82</sup> P. CZAGA, Chapter 3: Case study on the pharmaceutical sector, in: *Interest Groups and the Eastern Enlargement of the EU*, 2001, *Ph.D dissertation (University of Sussex, European Institute)*., p. 78-79.

- A TA of five years for the application of Council Regulation (EEC) No 1768/92 of 18 June 1992 concerning the creation of supplementary protection certificate (SPC). The Hungarian rules guaranteed a shorter patent protection period than those in the EU, i.e. 15 years instead of 20. MAGYOSZ requested a five years TA delaying the introduction of the SPC<sup>83</sup>;
- A second TA request concerned the exclusivity of clinical and test trial data. According to EU regulations pharmacological and toxicological tests and the results of the clinical trials generated by a producer of an innovative drug enjoy protection for six years that can be extended to ten. Under Hungarian law the special protection of the results for a period of six to ten years did not exist. It enabled companies to manufacture and to place generic pharmaceutical products on the market without having to wait for six or ten years<sup>84</sup>.

Both TPRs were intensely opposed by the AIMP. The association was created in 1992 as a result of the potential adverse effects on its members by the health care and reimbursement system. They argued that the system discriminated against their members and favoured those of MAGYOSZ<sup>85</sup>. AIMP's membership stood at 37 member companies in 2000 and predominantly comprised importing global drug firms. Therefore, AIMP was a professional lobbying agent for its clients rather than an industrial representative. By value the AIMP represented a majority of the Hungarian pharmaceutical market. It ran a small secretariat that consisted of employees professionally trained in lobbying<sup>86</sup>. The authorities relationship with the AIMP remained at arms length. AIMP is mostly excluded from consultations even when expressing their interest to participate. AIMP's interests ran opposed to those of the MoH and MoFi on drug pricing and market presence of generics.

### **Poland: Polfarmed, PZPPF and SPFF**

Three associations represented the more fragmented pharmaceutical market in Poland. Local companies and foreign generic producers are represented by the Polish Chamber of Pharmaceutical Industry and Medical Products (Polfarmed) and Polish Association of Employers

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<sup>83</sup> Interview by Author with Representative of the Hungarian Pharmaceutical Manufacturers Association, Budapest, 06/02/2004.

<sup>84</sup> Ibid.

<sup>85</sup> P. CZAGA, Chapter 3: Case study on the pharmaceutical sector, in: *Interest Groups and the Eastern Enlargement of the EU*, 2001, Ph.D dissertation (University of Sussex, European Institute).

<sup>86</sup> Ibid.

in the Pharmaceutical Industry (PZPPF)<sup>87</sup>. The Association of Innovative Pharmaceutical Companies' Representatives (SPFF, formerly known as SPFFwP) represent predominantly foreign subsidiaries<sup>88</sup>.

Polfarmed commenced its activities in 1994. It had a sectorally dispersed membership and was active in the market of pharmaceuticals, basic chemicals and medical devices. Within the pharmaceutical industry it associated 94 companies (2002) mainly producing generic products with a market share of circa 30 per cent by value. The majority of its members were smaller firms. Four former large Polfa companies including the largest (*Grodziskie Zakłady Farmaceutyczne Polfa*) had a disproportionate influence within the association. The Vice President of Polfarmed, *Wojciech Kuzmierkiewicz*, was also Vice President of *Grodziskie Zakłady Farmaceutyczne Polfa*.

Because of the membership of former Polfa companies Polfarmed was an insider. Polfarmed cooperated with state authorities and corresponding parliamentary commissions on pharmaceutical legislation. From 1995 the pressure from legislative changes became increasingly costly for its members. Since 1998 Polfarmed learned more about accession and the impact on the industry. Legislation was in constant upgrade and Parliament was unaware about the EU's legislation on pharmaceuticals. The government consulted the association, however, it was not until the new Polish administration came to power (2001) that they were thoroughly informed about the effects of EU integration: 'We were not properly consulted but informed. We had several meetings with the Hungarian representatives. They were faster and their solution was extended to us'<sup>89</sup>. The association was re-active rather than proactive in the process.

At the end of 2001 Polfarmed set up a lobby campaign to preserve the country's patent laws allowing its members to launch generics<sup>90</sup>. The association also requested the preservation of process patent legislation. Process patent legislation allows companies to conduct research on drugs still under patent to get a head-start once the patent has expired.

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<sup>87</sup> See <http://www.polfarmed.pl/> and <http://www.producencilekow.pl/index.php>

<sup>88</sup> See <http://www.spff.pl/>

<sup>89</sup> Interview by Author with Representative of Polfarmed, Warsaw, 26/04/2004.

<sup>90</sup> N. SPIRO, Bitter Pill, in: *Economist Intelligence Unit*, 18/12/2001.

Polfarmed representatives wanted long TAs. Their campaign on a national level focussed on the budgetary cost and price hikes for citizens: ‘Polish products, which are now three to four times cheaper than EU products, would quickly become more expensive if Poland had to adopt EU rules all at once’, said Kuymierkiewicz<sup>91</sup>. On an international level Polfarmed invoked the principle of equality referring to a 17 years TA East Germany received upon entering the EU.

As a member association of EGA since 1999 it made its position clear in Brussels<sup>92</sup>. Kuymierkiewicz stressed the dangers for the industry: ‘If there were no transition periods, the consequences for the Polish pharmaceuticals industry would be catastrophic’<sup>93</sup>. Circa 9,000 medicines in Poland were registered but few had full documentation that met all the EU requirements as opposed to those registered by large innovation companies. The registration of the documents of nearly all medicines had yet to be supplemented<sup>94</sup>. Supplementing registration documentation requires time and money for additional research. Therefore, Polfarmed lobbied heavily for a TPR extending the period to provide additional documentation<sup>95</sup>.

The PZPPF assisted Polfarmed in its campaign. The association founded in 1991 represented 22 international generic producers present in the Polish market. They imported or produced generics locally. It is a member of EGA and the Polish Confederation of Private Employers. The PZPPF asked the government directly to postpone the market exclusivity arrangements and used its membership of the Polish Confederation of Private Employers to achieve that objective. Despite the membership of *GlaxoSmithKline Pharmaceuticals* the Confederation lobbied the government on behalf of the PZPPF because as they said ‘the PZPPF represented Polish companies’<sup>96</sup>.

Simultaneously, *Zdzislaw Sabillo*, President of the SPFF which represented the interests of foreign pharmaceuticals firms, had been pressing the government to bring its patent laws in line with those of the EU prior to accession. His association wanted to ensure that price controls did not discriminate against western suppliers<sup>97</sup>. The SPFF (then as the Association of the

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<sup>91</sup> J. SPARSHOTT, Poland to reopen EU chapter for drugs industry, in: *ISI Emerging Markets*, 11/02/2001

<sup>92</sup> *Interview by Author with Representative of Polfarmed*, Warsaw, 26/04/2004.

<sup>93</sup> J. SPARSHOTT, Poland to reopen EU chapter for drugs industry, in: *ISI Emerging Markets*, 11/02/2001

<sup>94</sup> *Pharmaceuticals: A Cure is Needed* in: *Warsaw Voice*, Warsaw: 28 August 2003.

<sup>95</sup> *Ibid.* in:

<sup>96</sup> *Interview by Author with Representative of the Polish Confederation of Private Employers*, Warsaw, 15/04/2005.

<sup>97</sup> N. SPIRO, Bitter Pill, in: *Economist Intelligence Unit*, 18/12/2001.

Pharmaceutical Companies Representatives in Poland – SPFFwp) was established in 1993. It associated 42 manufacturers of modern pharmaceuticals (2002). In September 1994, the association became a member of the Polish Chamber of Commerce and in May 2004 a full member of EFPIA. SPFF is also a member of IFPMA in Geneva.

Mr Sabillo's group advised the MoH in 1999-2000 to bring pharmaceutical legislation in line with the EU. Polfarmed actions directly opposed his association's work: 'Polfarmed now wants the draft altered to ensure that only local drugs are reimbursed. This contravenes EU guidelines and would eliminate foreign competition [...] Foreign firms in Poland suffer from one of the worst sales volume/market share ratios in the region'<sup>98</sup>.

### **Slovakia: ZCHFP and SAFS**

In Slovakia domestic producers are represented by the Association of Chemical and Pharmaceutical Industry of the Slovak Republic (ZCHFP)<sup>99</sup>. Its counterpart is the Slovak Association of Research Based Pharmaceutical Companies (SAFS)<sup>100</sup>.

The ZCHFP was founded in November 1991. Its membership was dispersed and included 41 manufacturers, trading companies and research and development institutions. Activities of the association concentrated on environmental issues, safety in operations, health protection of employees, certification activities, and transportation of hazardous chemical substances and removal of trade barriers. Because of its diffuse membership and the wide variety of its members the association failed to mobilise. It did not request any TPRs or other measures of interest. In fact, 'the government closed the relevant chapters of the *acquis* without paying attention to any concern of the domestic industry'<sup>101</sup>. The government owned the largest domestic producer, Slovakopharma, which counted for 75 per cent of domestic output. One member of the governing board of Slovakopharma solicited a delay for the application of the legislation on data exclusivity. The government refused: 'They could do that since the state retained a 34 per cent veto [34 per cent of the shares] in Slovakopharma'<sup>102</sup>.

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<sup>98</sup> Ibid.in:

<sup>99</sup> See <http://www.zchfp.sk/>

<sup>100</sup> See <http://www.safs.sk/>

<sup>101</sup> *Interview by Author with Representative of the Slovak State Institute for Drug Control, Bratislava, 12/03/2004.*

<sup>102</sup> Ibid.

The decision was rather odd given that Slovakopharma produced 250 generic medicines. It had one or two original molecules of its own: ‘As long as the state kept its golden share the association and the company did not request anything. Only when the company was privatised [2001-2002] did the new owners put forward a TPR. All the same, the new owners woke up too late and the government subsequently refused to re-open the chapter. It was closed they said’<sup>103</sup>.

EU legislation particularly affected the Slovak market. Most Slovak production is destined for domestic consumption and the Czech Republic: ‘A loss of export markets is not expected. Slovak producers did not have a massive export capacity. If parallel trade is to happen it would happen between the applicant countries. The generic prices in Poland are lower than in Hungary’<sup>104</sup>.

The association representing foreign firms, SAFS, was established in 1997 and represented 22 multinationals with a presence in Slovakia claiming to represent 50 per cent of the total market<sup>105</sup>. To become a member of SAFS the proportion of generic products unprotected by patents owned by the SAFS member company must not exceed 30 per cent. Most of the U.S. and third country suppliers were members of SAFS, which in turn was a member of EFPIA.

SAFS set up an ethical committee that supervised and monitored adherence to ethical principles of advertising and marketing practices by pharmaceutical companies. This Committee reviewed whether production and trade activities of pharmaceutical companies in introducing new products were in line with international legislation. SAFS members have repeatedly pointed at non-transparency in drug pricing policy in Slovakia and the respective payments.

Foreign companies with a representation in the Slovak Republic did try to influence Parliament (National Council) to have a strict application of the *acquis*: ‘Banning generics would increase their profits’<sup>106</sup>. The joint venture Aventis-Hoechst-Biotika is the only company producing

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<sup>103</sup> Ibid.

<sup>104</sup> Ibid.

<sup>105</sup> Epsicom Business Intelligence, *World Pharmaceutical Markets: Slovakia*, West Sussex, April 2003, pp. 42., p. 22.

<sup>106</sup> Interview by Author with Representative of the Slovak State Institute for Drug Control, Bratislava, 12/03/2004.



originals under licence in the country<sup>107</sup>. EU legislation prevents their original products from appearing in other forms on the Slovak market.

### 3.3.4.2. European Federations

There are three major European level pharmaceutical associations all representing different segments of the industry. The *European Federation of Pharmaceutical Industries and Associations* (EFPIA) is primarily the association of the innovative drug producers<sup>108</sup>. The Association of the European Self-Medication Industry (AESGP) is the representative of the non-prescription pharmaceutical industry<sup>109</sup>. The European Generic Association (EGA), is the group that represents the European generics industry<sup>110</sup>. It is the first and the last that concern this chapter. The AESGP members were largely unaffected in the EU enlargement process.

#### EFPIA

EFPIA is the most significant, influential and the oldest of the two organisations. Through its membership, the association represents the shared views and interests of over 3,350 pharmaceutical companies undertaking R&D and manufacturing of medicinal products for human use in Europe. It is an organisation of predominantly innovative producers and counts among its members the 100 largest global pharmaceuticals companies that are highly factor and asset specific. Its members represent a high value added industry with large R&D expenditures. They have large profits and accounts for 40 per cent of the world pharmaceutical output<sup>111</sup>.

It is a well-resourced and well-staffed organisation. It has a secretariat of 30 people, a relatively large size institutions compared to other European sectoral federations<sup>112</sup>. National pharmaceutical associations provide the largest financial contributions and enjoy the highest influence in decision-making. EFPIA acts with a high degree of delegated authority. According to *Justin Greenwood* these two institutional arrangements add to EFPIAs effectiveness<sup>113</sup>.

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<sup>107</sup> J. BIEHUNEK, *The Expected Effects of the EU Accession on the Pharmaceutical Industry in the Slovak Republic*, Budapest: International Center of Economic Growth (Europe Center), May 2003.

<sup>108</sup> See <http://www.efpia.org/>

<sup>109</sup> See <http://www.aesgp.be/>

<sup>110</sup> See <http://www.egagenerics.com/>

<sup>111</sup> EFPIA, *The Pharmaceutical Industry in Figures*, Brussels, 2002., p. 15.

<sup>112</sup> See [www.efpia.org](http://www.efpia.org) The General Assembly consist of full members and convenes annually. The executive board comprises 11 association representatives and 11 member companies that are complete members. General Management is concerned with implementation.

<sup>113</sup> J. GREENWOOD, *Pharma and Biotech: Virtues and Trends in EU lobbying*, in: R. H. PEDLER and M. P. C. M. V. SCHENDELEN, *Lobbying the European Union : companies, trade associations and issue groups*, Aldershot, England; Brookfield, Vt., USA: Dartmouth, 1994, pp. pp. 183-98.p. 187.

The association provides a link between the research-driven pharmaceutical industry and policy-makers at European and international level. It maintains close contacts with EU institutions, regulatory authorities, health care professionals and patient and consumer associations. EFPIA is a highly successful sectoral lobby organisation. Evidence suggests that it had direct impact upon national arrangements between its members and national governments. It has achieved more than the individual national associations would have<sup>114</sup>.

Some argue this is related to the nature of the industry. Pharmaceutical firms operate in an essentially similar regulatory environment confronted by comparable challenges in different markets. International concerted action is therefore likely to be more successful<sup>115</sup>. Highly developed national interest representation in the drug producing industry and prominent government involvement with a sizeable impact on national budgets and profits of drug firms helped the association overcome collective action problems on a European level. It has made the industry a strategic concern for states and the EU. The international outlook and the vertically integrated nature of the industry (R&D, production and distribution) provided the backbone to overcome international collective action problems<sup>116</sup>.

As a Brussels' insider EFPIA used its privileged status to inform the EC of its opinion and gain information about issues affecting the single market and the industries in the applicant states: 'There were no specialised channels or forums to discuss enlargement related matters, but being in a very tight policy community with the Commission, EFPIA knows about everything that happens concerning the sector'<sup>117</sup>. EFPIA pushed for full implementation of the *acquis* ahead of EU enlargement and initiated a special campaign in 1997.

It proposed upon accession 'an appropriate transition period providing for safeguard measures [...] until distortions are eliminated in the CEEC economies and operating environments reach

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<sup>114</sup> J. GREENWOOD and K. RONIT, *Established and Emergent Sectors: Organised Interests at the European Level in the Pharmaceutical Industry and the New Biotechnologies*, in: J. GREENWOOD, J. R. GROTE and K. RONIT, *Organized interests and the European community*, London; Newbury Park: SAGE, 1992, pp. 69-98., pp. 77-83.

<sup>115</sup> *Ibid.*, pp. 71.

<sup>116</sup> EFPIA, *The Pharmaceutical Industry in Figures* (Brussels, 2002), 24.

<sup>117</sup> P. CZAGA, Chapter 3: Case study on the pharmaceutical sector, in: *Interest Groups and the Eastern Enlargement of the EU*, 2001, *Ph.D dissertation (University of Sussex, European Institute)*.

EU standards and norms<sup>118</sup>. It set up a priority action team conducting its own screening exercise in the applicant states to verify how well the CEECs were adopting the *acquis*. Through its network of national associations and global companies present in the candidate countries (see Table 12) it was well informed and equipped.

### **EGA**

EGA, is the representative body for the European generic pharmaceutical industry. It was formed in 1992 and is the youngest of the pharmaceutical interest groups. It represented over 400 companies either directly or through national associations throughout the EU<sup>119</sup>. EGA was regularly involved in the development of pharmaceutical legislation and guidelines and maintained a constant dialogue with the EU institutions and various international, European and national agencies<sup>120</sup>. The association was only 6 years old when the accession process commenced. Many of its members were operating in the former Communist bloc. EGA's first position papers on EU enlargement date from the period 2002-2003 when accession negotiations were over. Interviews carried out in the V-4 indicated that during the accession negotiations (1998-2002). It was not as active compared to EFPIA.

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<sup>118</sup> EFPIA, *The Accession of Central and Eastern European Countries (CEECs) to the European Union (EU)*, Brussels, July 1997, pp. 15.

<sup>119</sup> See <http://www.egagenerics.com>

<sup>120</sup> *Ibid.*

**Table 12: Economic and Political Market Structure**

country	firm	rank	market share value	market share volume	employment	employment share	ownership	privatization	orientation	national membership	international membership	production
Cz	LECIVA (Zentiva)	1	14	29	1164	17.75	Cz	1997	domestic	CAFF(2)	AESGP(12)/EGA(13) (EGA observer)	generic
Cz	SLOVAKOFARMA	2	7	19	n.a.	n.a.	Cz		import	CAFF	AESGP/EGA (EGA observer)	generic
Cz	AVENTIS	3	4.5	n.a.	n.a.	n.a.	FR		import	MAFS(3)	EFPIA(14)/IFPMA(15)	original
Cz	NOVARTIS	4	3.8	n.a.	n.a.	n.a.	CH		import	MAFS	EFPIA/IFPMA	original
Cz	GlaxoSmithKline	5	3.3	n.a.	n.a.	n.a.	UK		import	MAFS	EFPIA/IFPMA	original
Cz	BRISTOL-MEYERS	6	3.1	n.a.	n.a.	n.a.	UK		import	MAFS	EFPIA/IFPMA	original
Cz	SANOI/Aventis	7	2.9	n.a.	n.a.	n.a.	FR		import	MAFS	EFPIA/IFPMA	original
Cz	MERCK and Co	8	2.7	n.a.	80	1.22	D		import	MAFS	EFPIA/IFPMA	original
Cz	KNOLL/ABBOTT	9	2.5	n.a.	111	1.69	D		import	MAFS	EFPIA/IFPMA	original
Cz	PFIZER	10	2.1	n.a.	120	1.83	US		import	MAFS	EFPIA/IFPMA	original
Cz	SCHERING PLOUGH	11	2	n.a.	n.a.	n.a.	D		import	MAFS	EFPIA/IFPMA	original
Cz	GALENA (IVAX CR)	12	1.9	n.a.	872	13.3	US	1994	export	CAFF	AESGP/EGA (EGA observer)	generic
Cz	Janssens-Cilag	13	1.5	n.a.	75	1.14	BE		import	MAFS	EFPIA/IFPMA	original
Cz	Lachema						Cr	1999				generic
Cz	VUAB						US	1998				generic
<b>total</b>		<b>13</b>	<b>51.3</b>	<b>48</b>	<b>2422</b>	<b>36.93</b>						
Hu	EGIS	1	8.46	n.a.	2579	18	Hu		export	MAGYOSZ(4)	EGA/IFPMA/AESGP	generic
Hu	GIDEON RICHTER	1	9.57	n.a.	4730	33.02	Hu	state	export	MAGYOSZ	EGA/IFPMA/AESGP	generic
Hu	NOVARTIS	2	6.76	n.a.	n.a.	n.a.	CH		import	AIPM	EFPIA	original
Hu	CHINOIN SAN. WINTHR	3	5.92	n.a.	2645	18.46	FR	1993	export	MAGYOSZ	IFPMA/AESGP	generic
Hu	BIOGAL (TEVA Magyarország Rt.)	4	5.25	n.a.	n.a.	n.a.	IS	1996	export	MAGYOSZ	IFPMA/AESGP	generic
Hu	PFIZER	5	3.69	n.a.	n.a.	n.a.	US		import	AIPM (5)	EFPIA	original
Hu	MERKSHARP DOHME	6	3.61	n.a.	n.a.	n.a.	US		import	AIPM	EFPIA	original
Hu	ROCHE HUNGARY	7	3.56	n.a.	n.a.	n.a.	CH		import	AIPM	EFPIA	original
Hu	ELI LILLY	8	3.55	n.a.	n.a.	n.a.	US		import	AIPM	EFPAI	original
Hu	GLAXO WELLCOME	9	2.8	n.a.	n.a.	n.a.	UK		import	AIPM	EFPIA	original
Hu	BRISTOL MEYERS SQUIBB	10	2.79	n.a.	n.a.	n.a.	US		import	AIPM	EFPIA	original
Hu	SCHERING PLOUGH	11	2.79	n.a.	n.a.	n.a.	D		import	AIPM	EFPIA	original
Hu	PHARMACIA UPJOHN	12	2.65	n.a.	n.a.	n.a.	US		import	AIPM	EFPIA	original
Hu	JOHNSON & JOHNSON	13	2.08	n.a.	n.a.	n.a.	US		import	AIPM	EFPIA	original
Hu	ASTRA	14	2.05	n.a.	n.a.	n.a.	SW		import	AIPM	EFPIA	original
Hu	AVENTIS PHARMA	15	2.02	n.a.	n.a.	n.a.	FR		import	AIPM	EFPIA	original
Hu	SMITHKLINE BEECHAM	16	1.99	n.a.	n.a.	n.a.	UK		import	AIPM	EFPIA	original
Hu	HUMAN	17	1.79	n.a.	n.a.	n.a.	IS	1993	export			original
Hu	ICN Magyarország Rt. (Alkaloida)	18	1.71	n.a.	n.a.	n.a.	US		export	MAGYOSZ	IFPMA/AESGP	generic
Hu	ZENECA	19	1.67	n.a.	n.a.	n.a.	UK		import	AIPM	EFPIA	original
Hu	NOVO NORDISK	20	1.56	n.a.	n.a.	n.a.	CH		import	AIPM	EFPIA	original
Hu	Alkaloida						US	1995				
<b>total</b>		<b>20</b>	<b>76.27</b>	<b>n.a.</b>	<b>9954</b>	<b>69.48</b>						

Notes: (2) Pharmaceutical Association of the Czech Republic (12) Association of the European Self-Medication Industry  
(3) Czech International Association of Pharmaceutical Companies (13) European Generic Medicines Association  
(4) Hungarian Pharmaceutical Manufacturers Association (14) European Federation of Pharmaceutical Industries and Associations  
(5) Association of Innovative Pharmaceutical Manufacturers (15) International Federation of Pharmaceutical Manufacturers & Associations

Source: Own compilation – period 1998-2002

country	firm	rank	market share value	market share volume	employment	employment share	ownership	privatization	orientation	national membership	international membership	production
PI	POLPHARMA SA STAROGARD GDANSKI	1	5.4	17	2800	10.85	PI	1999	domestic	PZPPF (6)	EGA	generic
PI	SERVIER	2	5.7	n.a.	n.a.	n.a.	FR		import	SPFFwP(7)/SPFF(8)	EFPIA/IFPMA	original
PI	GLAXOSMITHKLINE SA (1)	2	7	15	1400	5.42	UK	1998	domestic	SPFFwP/SPFF	EFPIA	generic
PI	TERPOL (Polfa Lublin)	3	n.a.	n.a.	n.a.	n.a.	PI		domestic	PZPPF	EGA	generic
PI	ICN PHARMACEUTICALS (Polfa Rzeszow)	3	5	n.a.	n.a.	n.a.	US	1998	export	PZPPF	EGA	generic
PI	NOVARTIS	4	4.9	n.a.	n.a.	n.a.	CH		import	SPFFwP/SPFF	EFPIA/IFPMA	original
PI	POLFA WARZSAWA	4	n.a.	6	1200	4.65	PI	state	domestic	PZPPF	EGA	generic
PI	PLIVA KRAKOW (Polfa Krakow sa)	5	2.4	5	1100	4.26	CR	1998	domestic	PZPPF	EGA	generic
PI	POLFA PABIANICKIE	5	4	n.a.	1200	4.65	PI	state	domestic	PZPPF	EGA	generic
PI	POLFA KUTNO SA	6	1.9	5	n.a.	n.a.	PI	1998	export	PZPPF	EGA	generic
PI	US PHARMACIA	6	3.5	n.a.	n.a.	n.a.	US		import			original
PI	JELFA SA	7	n.a.	5	n.a.	n.a.	PI	1998	domestic	POLFARMED(9)/PZPPF	EGA	generic
PI	POLFA SA TARCHOMIN	7	3	7	2400	9.3	PI	state	export	PZPPF	EGA	generic
PI	NOVO NORDISK	8	2.9	n.a.	n.a.	n.a.	CH		import	SPFF	EFPIA	original
PI	MERCK and Co	9	2.9	n.a.	n.a.	n.a.	D		import	SPFFwP/SPFF	EFPIA/IFPMA	original
PI	ELI LILLY	10	2.9	n.a.	n.a.	n.a.	US		domestic	SPFFwP/SPFF	EFPIA/IFPMA	original
PI	JOHNSON & JOHNSON	11	2.8	n.a.	n.a.	n.a.	US		import			original
PI	ROCHE	12	2.7	n.a.	n.a.	n.a.	CH		import	SPFF	EFPIA	original
PI	SANOFI-SYNTHELABO	13	2.7	6	n.a.	n.a.	FR		import	SPFFwP/SPFF	EFPIA/IFPMA	original
PI	PFIZER	14	2.4	n.a.	n.a.	n.a.	US		import	SPFF	EFPIA	original
PI	AVENTIS	15	2.1	n.a.	n.a.	n.a.	FR		import		EFPIA	original
PI	BRISTOL MEYERS SQUIBB	16	2.1	n.a.	n.a.	n.a.	US		import	SPFF	EFPIA	original
PI	ABBOTT LABARATORIES POLAND	17	2	n.a.	n.a.	n.a.	US		import	SPFF	EFPIA	original
PI	LEK POLSKA (Zakłady Farmaceutyczne Argon)	18	2	n.a.	100	0.39	SL		export	PZPPF	EGA	generic
PI	GIDEON RICHTER (Polfa Grodzisk Mazowiecki)	19	1.8	n.a.	1000	3.87	Hu		domestic	PZPPF	EGA	generic
PI	KRKA POLSKA Sp.	20	1.7	4	n.a.	n.a.	SL		domestic	PZPPF		generic
PI	Astrazeneca	21	1.6	n.a.	n.a.	n.a.	UK		import	SPFF	EFPIA	original
<b>total</b>		<b>21</b>	<b>75.4</b>	<b>70</b>	<b>11200</b>	<b>43.39</b>						
Sk	SLOVAKOFARMA	1	n.a.	75	2168	40.85	Sk	2001/2	domestic/export	ZCHF		generic
Sk	BIOTIKA Lupca	2	n.a.	n.a.	1077	20.2	Sk	1992	export	ZCHF		
Sk	LECIVA (Zentiva)	3	10	n.a.	n.a.	n.a.	Cz	1996	export	ZCHF	EGA	generic
Sk	Aventis Pharma, s.r.o.	3	n.a.	n.a.	n.a.	n.a.	FR		import	SAFS	IFPMA/EFPIA	original
Sk	HOECHST BIOTIKA (Aventis)	3	n.a.	n.a.	310	5.84	GR		domestic/export	SAFS		original
Sk	IMUMA	4	n.a.	n.a.	600	11.3	Sk	2002	export	ZCHF		
Sk	Solvay Pharma s.r.o.	n.a.	n.a.	n.a.	n.a.	n.a.	BE		import	SAFS (10)	IFPMA/EFPIA	original
Sk	Novartis s.r.o.	n.a.	n.a.	n.a.	n.a.	n.a.	CH		import	SAFS	IFPMA/EFPIA	original
Sk	Roche Slovensko, s. r. o.	n.a.	n.a.	n.a.	n.a.	n.a.	CH		import	SAFS	IFPMA/EFPIA	original
Sk	Boehringer Ingelheim Pharma	n.a.	n.a.	n.a.	n.a.	n.a.	D	1994	import	SAFS	IFPMA/EFPIA	original
Sk	MERCK and Co	n.a.	n.a.	n.a.	n.a.	n.a.	D		import	SAFS	IFPMA/EFPIA	original
Sk	SCHERING PLOUGH	n.a.	n.a.	n.a.	n.a.	n.a.	D		import	SAFS	IFPMA/EFPIA	original
Sk	Fournier Slovakia, s.r.o.	n.a.	n.a.	n.a.	n.a.	n.a.	FR		import	SAFS	IFPMA/EFPIA	original
Sk	Sanofi-Synthelabo Slovakia s.r.o.	n.a.	n.a.	n.a.	n.a.	n.a.	FR		import	SAFS	IFPMA/EFPIA	original
Sk	Lundbeck Slovensko s.r.o.	n.a.	n.a.	n.a.	n.a.	n.a.	Sk		domestic	SAFS	IFPMA/EFPIA	original
Sk	MEDIKA	n.a.	n.a.	n.a.	750	14.13	Sk		domestic			generic
Sk	MEVAK	n.a.	n.a.	n.a.	n.a.	n.a.	Sk		export	ZCHF (11)		generic
<b>total</b>		<b>6</b>	<b>10</b>	<b>75</b>	<b>4905</b>	<b>92.32</b>						

Notes: (1) Poznanskie Zakłady Farmaceutyczne Polfa (6) Polski Związek Pracodawców Przemysłu Farmaceutycznego  
(7) Association of Innovative Pharmaceutical Companies' Representatives  
(9) Polish Chamber of Pharmaceutical Industry and Medical Devices

(11) Association of Chemical and Pharmaceutical Industry of the Slovak Republic  
(8) Association of Innovative Pharmaceutical Companies' Representatives  
(10) Slovak Association of Research Based Pharmaceuticals Companies

Source: own compilation – period 1998-2002

### 3.3.4.3. A Special Insider: Economic and Political Strength

Economic strength is based upon relative economic measures. We assume that if a sector has a higher share of national GDP, total regional and national export earnings it has more economic strength and is more likely to be successful at influencing decision making. Furthermore, the sector with a higher share of total national and regional employment, particularly when it is regionally concentrated, is likely have more political strength by the sheer numbers of its employees.

**Table 13: Economic and Political Strength**

country	share value added	share national export earnings	share regional exports	share national employment
Cz	0.003167	0.852	25.358	0.1375
Hu	0.011437	1.622	43.402	0.3753
Pl	0.003903	0.644	19.882	0.1777
Sk	0.00244	1.002	11.358	0.2016
Av.	0.00523675	1.03	25	0.223025

Note: Cz=Czech Republic, Hu=Hungary, Pl=Poland, Sk=Slovakia  
share of value added (at factor costs)= share value added pharmaceuticals normalised by gross value added at factor costs  
Source: Eurostat, averages 1998-2002

Following Table 13 the Hungarian pharmaceutical industry scores highest on all economic and political measures of the V-4. It is followed by Slovakia, the Czech Republic and Poland.

A much more powerful reason for the industry to be a state insider is related to its potential common interest concerning the widest possible use of domestically produced and cheaper generic medicines. All V-4 were confronted with rising healthcare budgets over the 1990s and early 2010s. They are among the OECD countries spending the highest share of national GDP on state sponsored healthcare. Expenditure on pharmaceuticals increasingly ate away a large portion of national healthcare budgets.

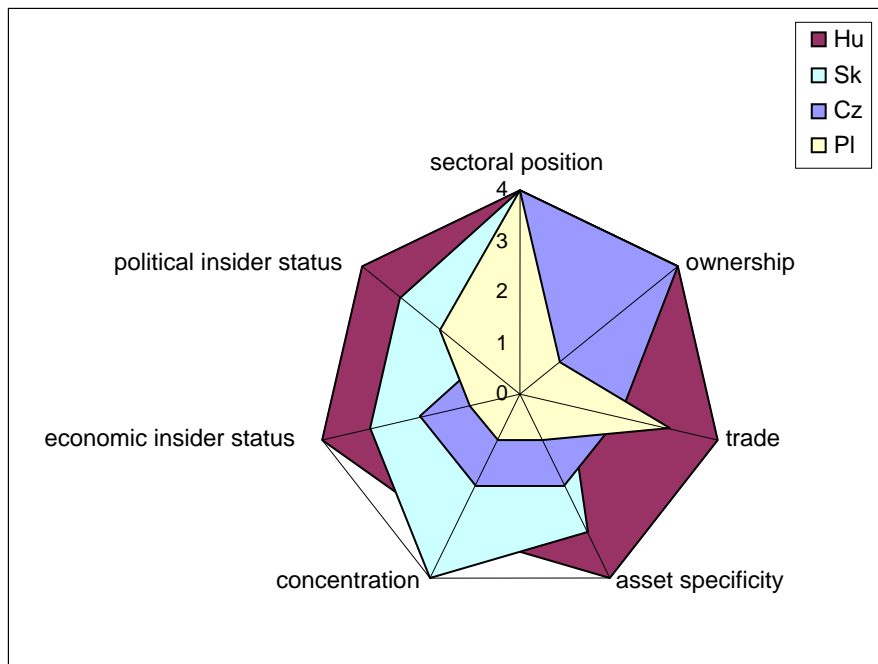
## 3.4. Conclusion

Chapter three assessed four hypotheses on the economic and political behaviour of the pharmaceutical industry in the EU enlargement process. It recognized that NTBs and behind the border issues had different effects on the industry in the V-4 countries. They divided the sector between domestic producers and importing firms and their respective industrial representation and lobby agents. The former predominantly produced generic drugs. The latter manufactured original products.

Upon EU entry V-4 generic producing firms stood to lose market share and their export markets. Strict application of the *acquis* threatened their business throughout the region. They mobilised politically in all countries with different intensity. National pharmaceutical sectors still undergoing transition at the turn of the century failed to mobilise as effectively.

Polish and Slovak industries compared to the Czech and Hungarian sectors failed to consolidate ahead of EU membership. While all V-4 drug industries lost domestic market share and export markets, Slovak and Polish drug producers lost out more. The Hungarian industry, by far the largest generic producing sector, consolidated first and built up substantial export markets in the former S.U. It invested most in R&D and carried most patents between 1998 and 2002. It was the most highly asset specific industry in the region and stood to lose most. Hence, it held the strongest preferences about EU enlargement.

**Figure 19: Sectoral Comparison of the V-4 Pharmaceutical Industry**



Note: Cz=Czech Republic, Hu=Hungary, Pl=Poland, Sk=Slovakia  
 Source: Own compilation, based on Table 23 (see Conclusion Part II)

The Hungarian pharmaceutical producers' political assets were well developed. Its early privatisation had given it an international outlook, with a small number of large firms. Only the

small Slovak sector had a higher market concentration. The Czech industry was more fragmented, although, not to the extent of the particularised Polish market.

It meant that the Hungarian drug makers could more easily overcome collective action problems. Their single highly effective association mobilised first and proactively. They set up a campaign targeting the authorities and formulated two TPRs. The Hungarian pharmaceutical industry comes close to the ideal type of a sector with strong preference formation, subsequent political mobilisation and a high likelihood of success.

In neighbouring Slovakia the state owned industry and its association failed to mobilise in time. When the new private owners exerted political pressure the government did not reply. State ownership was counterproductive for political mobilisation. The Czech industry mobilised politically, however, it failed to have its agenda realised. The Czech authorities did not see the benefit of their demands.

In Poland the domestic industry was represented by two associations with a diverse membership across sectors. Both pursued different routes and were re-active rather than pro-active. In fact, the government already had closed the negotiations. However, unlike in Bratislava, Warsaw lawmakers re-opened the chapters of the *acquis* under pressure from the Polish industry helped by their Hungarian colleagues.

Global pharmaceutical companies and their lobby agents in the V-4 opposed and countered the interests of the regional generic producing industry. They were highly asset specific and stood to lose from EU enlargement. They ran the risk that their counterparts gradually copied research based drugs and undercut the market in the enlarged EU through parallel trade. They held strong preferences on the enlargement process.

Foreign firms had been highly successful in Central Europe. Their market share rose from nothing in 1989 to more than 50 per cent by value in 2002. They set up a well organised and resourced interest representations in each of the V-4 countries and commenced a campaign to protect their interests as early as 1998. The EC and one of the most successful European



Federations, EFPIA, supported their efforts for strict application of the pharma acquis. EFPIA made sure that provided its national associations were unsuccessful it could request a limitation of free movement of pharmaceuticals in the enlarged EU.

Nevertheless, the research based industry could not prevent the domestic Hungarian industry from achieving its objectives. Initially the global industry was successful in Poland. Only at the last minute did its domestic counterparts thwart its efforts. The Czech and Slovak Republics ignored the local producers in favour of the importing industries.



## CHAPTER 4: THE BASIC IRON AND STEEL INDUSTRY

This chapter considers the economic issues affecting the basic iron and steel sector in the V-4 in the run up to EU membership. It describes the industry's concerns in the context of EU enlargement. It provides a brief historical overview of the regional and national iron and steel industries in Central Europe. The chapter then applies the theory on factor and asset specificity assessing four hypotheses. It specifies the industries' trade in basic iron and steel, its factor and asset specificity, national cohesion and concentration as well as its insider status in the policy process.

The focus is on the period 1992-2004 treating the period of the enlargement negotiations (1998-2002) in more detail. The chapter demonstrates that the industry in Central Europe was confronted by similar issues, however, the national sectoral characteristics differed including policy resulting in different intensity of preference over policy and political mobilisation around EU enlargement.

### 4.1. The Industry's Concerns: Restructuring and Market Access

#### 4.1.1. The Sector in the EU

Restructuring, capacity reduction and state aid restrictions are concepts well known to the EU basic iron and steel producers. Throughout the 1980s until the mid 1990s the sector went through a painful steel crisis. In the 1980s the industry dismantled circa mn 32 tonnes of hot rolled steel in exchange for around €40 bn of state aid. Producers closed an additional 19 tonnes of hot rolled capacity by the mid 1990s laying off approximately 100,000 workers. In exchange governments and the EU granted an additional €17 bn in subsidies<sup>1</sup>.

When the Berlin Wall fell in 1989 these producers were alarmed at the potential of competition from Eastern European large integrated steel works producing steel at lower costs propped up with national subsidies<sup>2</sup>. EU steelmakers wanted to make sure that basic iron and steel from the region would not disrupt the EU market, undercut production and sales. They lobbied hard at

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<sup>1</sup> At the time reduction of overcapacity was only achieved after the so-called State Aid Code made capacity reduction a precondition for state aid. The principles were embodied in the person of the former EC industry Commissioner, *Etienne Davignon*, who set up the so-called *Davignon Plan*, in: European Commission, Directorate General Competition (Unit H-1), *State Aid for Restructuring the Steel Industry in the New Member States* Brussels, pp. 9., p. 94.

<sup>2</sup> The Steel Industry: Enlargement creates opportunities for EU mills, in: *Deutsche Bank Research, EU-Monitor No 11*, January 2004. 24, pp. 11-18.

national and European level to make basic iron and steel trade subject to a different set of rules and prevailed. Production in the V-4 and trade in basic iron and steel with the EU became subject to a different regime under the EAs. From the early 1990s trade in basic iron and steel products between the V-4 and the EU was subject to a special trade regime first stipulated in the so-called Trade and Co-operation Agreements (1988-1989) and subsequently in the EAs (1991-2004).

A historic belief in the region that basic iron and steel manufacturing is a ‘sensitive industry’ in need of a special set of market rules helped them along to achieve their objective. Until 2002 the sector was governed by the European Coal and Steel Community (ECSC, 1951-2002) which lay at the foundations of the EU. The ECSC Treaty expired in 2002. Regulations for the EU steel industry were normalised mirroring those applicable to manufacturing and the European single market. It made the conditions of EU entry of the V-4 steelmakers all the more pressing.

The enlargement negotiations over the integration of the Central European basic iron and steel industry centred on these ECSC rules and their application in the V-4 throughout the 1990s up to the end of the accession negotiations (2002) and eventual EU membership (2004). Over the entire period the EUs executive attempted to ensure that its basic iron and steel laws were not circumvented in Central Europe<sup>3</sup>.

Overloaded global steel markets, a cyclical downturn exemplified by over-capacity in Europe and a re-orientation of Central European steel trade towards the EU contributed to the tough stance of EU steel producers. They wanted trade protection<sup>4</sup>. The EU and individual V-4 regularly imposed restrictions on basic iron and steel trade through the use of contingent protectionist measures. EU steel producers considered competition from CEECs producers as unfair as their steel exports were distorting the market due to predatory pricing, i.e. lower than

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<sup>3</sup> European Commission, Directorate General Competition (Unit H-1), *State Aid for Restructuring the Steel Industry in the New Member States* Brussels, pp. 9., p. 95.

<sup>4</sup> For instance the 1991 announced quota of 3 mn tons of iron ore were almost filled by the end of the first half of 1992, in: Z. WANG and L.A. WINTERS, *EC imports from Eastern Europe: iron and steel*, London: EBRD, October 1993., p. 21.

cost. They argued that low price exports were the result of state ownership of integrated steel works that often were subsidised heavily<sup>5</sup>.

#### **4.1.2. The Sector in the Applicant States**

Many policy makers in the applicant states considered the basic iron and steel industry a sunset industry – an inheritance from the Communist era. It was hit hard by regime change and characterised by overcapacity, outdated technology, low productivity and rising regionally concentrated unemployment. EU integration compounded these problems. It made the modalities of restructuring conditional on trade and eventually on EU membership. Compared to the restructuring of the industry in the EU over the 1980s and 1990s restructuring in the CEECs was planned over a short time frame (1991-2004). In other words, EU enlargement became thoroughly intertwined with the clean-up of an industry in decline.

The process of enlargement was identified by policy makers as an outside anchor for reform. It also would provide continuous access for the steel industry to a huge export market. Simultaneously, the process was viewed with scepticism because it seriously limited the options for the industry. Restructuring and contingent state aid required approval from the EU institutions and hence EU member states. The danger that the EU could restrict trade and intervene in restructuring had a profound impact on the privatisation of the industry.

The EAs formed the starting point of the European integration of the V-4 basic iron and steel industry. They are the legal basis for the relationship between the applicant countries from Central Europe and the EU. They were more or less similar for all the V-4<sup>6</sup>. The rules for trade liberalisation did not need ratification by national parliaments and came into force immediately<sup>7</sup>. The EAs aimed to generate free trade at the turn of the century and provided for tariff reductions, customs duties and limitations of quantitative restrictions. They contained delays and exclusions for the basic iron and steel industry stipulated in protocol 2.

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<sup>5</sup> Steel is responsible for a disproportionately large share of total trade disputes in the World Trade Organization (WTO). Nearly all major steel producing countries in the world take recourse to trade restrictions in the form of quotas, tariffs, anti-dumping or countervailing duties to protect their domestic markets.

<sup>6</sup> They are based on Article 238 of the Treaty of Rome. The predecessor agreements were the so-called interim Association and Co-operation agreements. They were given a more permanent basis under the Association Agreements(AAs).

<sup>7</sup> They attracted much criticism because they excluded so-called sensitive sectors in which Central Europe was considered most competitive, such as basic iron and steel, from trade liberalisation. At the time of the EA negotiations the CEEC had little choice but to accept the terms of the EU and even less of the expertise needed to come up with an agreement weighted more in their favour. For an extensive overview see: J.I. TORREBLANCA PAYA, *The European Community and Central Eastern Europe (1989-1993): foreign policy and decision-making*, Madrid: Centro de Estudios Avanzados en Ciencias Sociales, 1997.

Steel was one of the most sensitive industries that the EAs dealt with because of their significance to the economy. Protocol 2 regulated the industry through reductions in tariffs and quota's and behind the border regulations with the most important features being capacity reductions, restructuring and contingent state aid. Trade and output was bound by EU rules on competition policy and subsidies including effective deadlines for their application and expiration.

Strict compliance with the EUs steel aid code was required. The basic iron and steel industry had to present restructuring plans for approval to the EU. The overall aim of the requirement to produce a national restructuring programme in a pre-accession context was to obtain transparency in the sector. The EC and the Council of the EU had to ensure that there were no competitive distortions in form and substance. They also wanted that Central European basic iron and steel producers progressively respected environmental and labour legislation<sup>8</sup>. Under Article 8(4) of protocol 2 an applicant country could exceptionally grant state aid for restructuring purposes in the first five years after entry into force of the agreement under four conditions:

- restructuring leading to the viability of the benefiting firms under normal market conditions at the end of the future restructuring period;
- the amount and intensity of restructuring aid strictly limited to what is absolutely necessary in order to restore viability and that the aid is progressively reduced;
- restructuring linked to a global rationalization and reduction of overall production capacity<sup>9</sup>;
- transparency in the area of public aid through a full and continuous exchange of information including amount, intensity and purpose of the aid and a detailed restructuring plan.

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<sup>8</sup> And they did, see: EC, *Regular Report from the European Commission on the Czech Republic's, Hungary's, Poland's and the Slovak Republic's Progress towards Accession*, Brussels, 1998-2002.

<sup>9</sup> Commission Decision No 2496/96/ECSC, OJ L 338, 28/12/1996, p42. Rules on capacity reductions were the result of lessons learned from the steel crisis in the EU (1980-1995), in: European Commission, Directorate General Competition (Unit H-1), *State Aid for Restructuring the Steel Industry in the New Member States* Brussels, pp. 9., p. 94.

Execution of the restructuring plans in the first half of the 1990s was piecemeal and patchy. In the second half of the 1990s protocol 2 formed the basis for restructuring in the sector. The individual V-4 ordered audits and restructuring plans from large international consultancy firms. When the plans were nationally sanctioned they were submitted for approval to the EC and the Council of Ministers of the EU. The EC gave an opinion to the Council. The Council could turn the plans down if it judged that they comprised too little reduction of production capacity, too much state aid for the industry; or that the risk for imports at low prices was too high.

With the survival of the industry in Central Europe at stake compulsory EU approval of restructuring plans proved difficult. Compliance with the EAs and protocol 2 was one of the preconditions for starting accession negotiations. It forced the countries to reduce capacity, restructure the industry under the EU's regulatory framework and open up their markets to steel imports.

In the run up to EU membership the EU increasingly reminded individual applicant countries of their obligations under protocol 2. As a result, Central European producers were forced into a regulatory framework that increasingly resembled a dilemma. On the one hand, restructuring and privatisation combined with state aid were essential for the industry's survival. On the other hand, investors were deterred because of the EU's required approval of restructuring plans, levels of production capacity, output and state aid as well as the terms of the privatisation of the industry.

The threat of limited access to the European single market compounded the problem. Provided protocol 2 conditions were not met the EA signatories were allowed to take appropriate measures following 30 days of consultation and the General Agreement on Tariffs and Trade (GATT) – the equivalent of contingent protection for output and trade in basic iron and steel. As a result, one would expect that EU membership without any TA a significant repositioning of the basic iron and steel industry on the Central European market would ensue.

## **4.2. Historical Overview**

### **4.2.1. 1945-1989**

Following 1945 the Communist regimes in Central Europe nationalised, centralised, expanded and upgraded the basic iron and steel industry. In those countries where the steel industry played a minor role in the national economy, i.e. Hungary and the Slovak lands of the Czechoslovak Federation, the Communist regime would build one. The national importance of the industry under Communism in the region's economy was greater than the arithmetic of employment and production figures suggest. Iron and steel formed the basis of the modernisation programme of the Soviet bloc and provided the raw material base for metallurgy, which was perhaps the leading link in Communist planning, sharing the top priority for equipment, materials and manpower with machine building and the armaments industry<sup>10</sup>.

Steel production was increased annually meeting rising output targets. Fuel and energy demand were high. After initial modernisation labour productivity declined and was lower than in the EU. Iron ore was progressively imported from further east while the prime energy sources such as coal and electricity were produced locally. Finished products were destined for the domestic market and exported throughout the COMECON<sup>11</sup>.

In Czechoslovakia the basic iron and steel industry had a long history and was of major importance to its manufacturing base. The production strategy divided steel manufacturing between the Czech and Slovak lands. The Czech steel producers specialised in long products while the Slovak steel producers concentrated on the production of flat products. The country had eight steel plants. *Nova Hut*, *Zelezarny Vitkovice*, *Trinecke Zelezarny*, *Poldi Kladno United Steel Works* and *Vychodne Slovenske Zeleziarne (VSZ)* were the main steel producers. Nova Hut, Trinecke Zelezarny, Vitkovice Steel, and VSZ accounted for a combined capacity of approximately 85 per cent of total national steel output<sup>12</sup>.

The Steel industry in Hungary formed only a small part of total Hungarian manufacturing. Three large firms, i.e. *Ozdi Kohaszati Uzemek*, *Lenin Kohaszati Muvek* and *Dunai Vasmu*

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<sup>10</sup> J.M. MONTIAS, The Polish Iron and Steel Industry, in: *American Slavic and East European Review*, 1957, 16(3), pp. 301-22.

<sup>11</sup> The Vienna Institute for International Economic Studies (WIIW), *Developments and Prospects of the Basic Metals and Fabricated Metal Products Sector in the Central and Eastern European Countries*, Vienna, February 2002, pp. 65., p. ii.

<sup>12</sup> W.G. STEBLEZ, The Mineral Industry of The Czech Republic, in: *International Minerals Statistics and Information*, 1999, pp. 6., p. 11.2.



dominated the industry. Dunai Vasmu, the integrated steel works, was built shortly after 1945. It was the centrepiece of a grand investment programme that would provide Hungary with basic iron and steel. By 1965 the completely new metallurgical cycle was finished. A new and modern steel town, *Dunaujvaros*, provided for the steel workers. In 1983 the name of the company changed to *Dunaferr*. As early as 1983 the Hungarian basic iron and steel industry fell prey to an economic crisis. Rising energy prices combined with unfavourable industrial location led to high operating costs and lower productivity than in neighbouring countries<sup>13</sup>.

Before 1945 Poland's industrial base was concentrated in the iron and steel sector. The country operated as many as 20 steel mills. The Communists built another six mills of which three had the largest capacity in the country<sup>14</sup>. The largest steel works were *Huta Sendzimir*, *Huta Warszawa*, *Huta Czestochowa* and *Huta Katowice* with more than 70 per cent of total production capacity and employing the lion's share of steel workers. The steel producing Katowice-Krakov region became Poland's industrial power house. Demand for basic iron and steel products and investment and output in the 1980s declined. The industry failed to restructure. By the end of the 1980s much of the basic iron and steel industry was old and outdated characterised by a high cost base, inefficient use of energy, raw materials and low labour productivity. The industry exemplified overcapacity, surplus-employment and the production of generally low price, low value added produce<sup>15</sup>.

#### **4.2.2. Transition and Consolidation (1989-2004)**

After the Berlin Wall came down in 1989 Czechoslovakia, Hungary and Poland embarked upon a transition towards democracy and a market economy. The basic iron and steel industry underwent significant changes. The most serious challenges of the transition process were the need to overcome the supply side effects, to reverse the loss of the COMECON market after the break up of the S.U. (1991) and to manage restructuring and privatisation processes.

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<sup>13</sup> K. FARKAS, A Sunset Industry in Eastern Europe. The Iron and Steel Industry in Hungary (A case of sluggish adjustment), in: *WIIW Research Reports (Vienna Institute for International Economic Studies)*, 1988, No 149.

<sup>14</sup> Metallurgical Chamber of Industry and Commerce in Poland (HIPH), *Polish Steel industry*, Katowice, 1996-2004.

<sup>15</sup> The Vienna Institute for International Economic Studies (WIIW), *Developments and Prospects of the Basic Metals and Fabricated Metal Products Sector in the Central and Eastern European Countries*, Vienna, February 2002, pp. 65.,p. 43.

The basic iron and steel industry was hit more severely than virtually any other industry. Domestic demand for steel collapsed and there was shift away from steel-intensive sectors. By 1992 the industry's output had dropped to an all time low. Markets in the CEECs and particularly the biggest export market, the former S.U., disappeared. Between 1990 and 1993 the output of crude steel more than halved in Czechoslovakia. In Poland it dropped from over mn 16 tonnes to less than mn 10 tonnes. The production in Hungary shrunk between 30 to 40 per cent of its 1989 level<sup>16</sup>.

Central European basic iron and steel producers re-oriented themselves from East to West in difficult times. Global steel market recorded low world prices. The US increased its tariffs as a consequence of overcapacity. The interim trade agreement with the EU and its attendant EAs forced the industry to adapt to a new environment in a short time span. The restrictive steel trade regime under the EAs resulted in disputes over steel quotas and anti-dumping actions throughout the 1990s<sup>17</sup>. Despite these adverse conditions most V-4 producers succeeded in carving out a significant role in world and EU export markets, particularly in semi-finished steel products.

Simultaneously, the industry underwent dramatic changes in structure and ownership. All steel firms in the region needed to restructure, shed overcapacity and reduce costs. Most accumulated huge debt overhangs in doing so. With the exception of US Moravia Steel (1995) and US Steel (2000) the V-4 did not succeed in finding suitable private partners for their largest steel firms before the accession negotiations were finished (2002). No major producer based in the EU-15 had entered the Central European steel sector (see Table 16). As a result, the EU-15 steel industry had large steel producing outsiders on its doorstep in Central Europe<sup>18</sup>. Only by 2004-2005 was the privatisation process complete and could the consolidation of the industry in Central Europe begin.

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<sup>16</sup> Steel statistic archive (1989-1993), International Iron and Steel Institute (IISI) Homepage: [www.worldsteel.org](http://www.worldsteel.org).

<sup>17</sup> The EC curbed Czechoslovak steel exports on 18 October 1992 and on 25 February 1992 followed by retaliations on 11 April 1992 by the V-3; After signing the EAs the EC initiated several anti dumping measures against Eastern steel producers, in: J.I. TORREBLANCA PAYA, *The European Community and Central Eastern Europe (1989-1993): foreign policy and decision-making*, Madrid: Centro de Estudios Avanzados en Ciencias Sociales, 1997., pp. 541-548. See also R. BALDWIN, P. HAAPARANTA and J. KIANDER eds, *Expanding membership of the European Union, Factor market barriers are trade barriers, gains from trade in 1992*, Cambridge; New York: Cambridge University Press; NBER, 1995.

<sup>18</sup> Interview by Author with Representative of Steel Federation of the Czech and Slovak Republics, Prague, 22/03/2004a.; Interview by Author with Representative of the Iron and Steel Institute, Budapest, 04/02/2004.

It had taken almost 15 years for the industry to consolidate. In the late 1980s between 385,000 and 320,000 workers were employed in the Czech, Polish, Hungarian and Slovak steel industry *sensu stricto*. Many more worked in dependent industries such as the metallurgy, the defence industry and the primary resources producing sectors such as coal and iron ore. Most were employed in only a few geographic concentrated areas, in so called steel towns. By 1998, barely a decade later, their number had almost halved bottoming out at between 120,000 and 145,000. Somewhere between 150,000 and 200,000 workers had lost their job in the sector. At the end of the 1980s steel producers in the V-4 produced circa mn 30 tonnes of crude steel annually. The industry reduced its output to tonnes mn 17.2 tonnes in 1998. Over the entire period the total number of companies producing steel declined substantially either through bankruptcies or mergers<sup>19</sup>.

#### **4.2.2.1. Czechoslovak Basic Iron and Steel (Czech and Slovak Republics)**

The Czech lands accounted for approximately 75 per cent of total national basic iron and steel output in Czechoslovak Federation. Following the break up of the country in 1993 the Czech Republic took over the bulk of the industry as it was concentrated in North Moravia (Moravia-Silesia region). The industry delivered the iron and steel for the nationally and regionally important tool making, machine building and construction industry. It accounted for over 70 per cent of the country's metal sector output. Eight large steel plants were present in the Czech Republic importing all their raw materials and producing all types of steel. Nova Hut, Zelezarny Vitkovice, Trinecke Zelezarny and Poldi Kladno United Steel Works accounted for approximately 85 per cent of total output.

Restructuring and privatisation of the largest steel plants essentially failed during the 1990s<sup>20</sup>. The industry was largely excluded from the first wave of voucher privatisation in 1992<sup>21</sup>. Nova Hut, the Czech largest steel plant, was the key in the overall restructuring of the Czech steel industry. Its modernisation with outside help failed<sup>22</sup>. Employment declined and debt accumulated. The company faced bankruptcy in 2001. In June 2002 the authorities agreed to

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<sup>19</sup> Own calculations based on national employment and output levels (1988-1989 and 1998-1999).

<sup>20</sup> *Interview by Author with Representative of Steel Federation of the Czech and Slovak Republics*, Prague, 22/03/2004a.

<sup>21</sup> Economic policy: Gov't forced to take action over steel firm, in: *Economist Intelligence Unit*, 08/04/1996

<sup>22</sup> Nova Hut subsidiaries were: Vysoke Pece Ostrava, Nova Hut Hungaria, Valcovny Plechu and Jakl Karvina.

sell Nova Hut to *LNH Holdings* headed by *Lakshmi Mittal* for US\$ 270 mn including a guarantee to keep 8,860 out of the total of 13,000 employees at work until at least 2005<sup>23</sup>.

The second largest steel plant, Ostrava-Vitkovice, made the highest loss of all steel companies in the country. At the beginning of 2000 it teetered on the verge of bankruptcy. The Czech state stepped in and provided a capital life line for another two years. The sale of Nova Hut and Vitkovice involved considerable state aid, mainly in the form of debt write-offs. Nevertheless under the privatisation plans the Czech steel industry stood to receive €453 mn while it was required to close down tonnes 0.59 mn of finished steel producing capacity.

Trinecke Zelezarny, the third largest Czech integrated steel producer, was the only company that enjoyed a relatively successful privatisation. At the end of 1991 it was a fully privatized company under the name Moravia Steel<sup>24</sup>. The privatisation was a mixed blessing because once private it no longer received state aid compared to the other Czech producers<sup>25</sup>.

Between 1993 and 2002 employment in the Czech steel industry declined from 94,129 workers to just 30,494 workers *sensu stricto*. Industry indebtedness rose and output declined from tonnes 10.7 mn of crude steel (1989) to tonnes 6.5 mn (2002) with 1993 as the turning point for a continuous drop<sup>26</sup>.

After the break up of Czechoslovakia (1993) Vychodoslovenske Zeleziarne (VSZ) or the East Slovakian Steel Works became the single largest steel maker in the Slovak Republic. It was the driving force behind the Kosice economy, the second largest Slovak city, with a total workforce of around 25,000 workers<sup>27</sup>. The steel company specialised in flat products and was regarded as technically advanced. It supplied the emerging car producers in the region including some located in the EU. In 1991 it had turned into a fully state-owned joint-stock company and was privatised under the first Czechoslovak voucher privatisation programme (1992). The

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<sup>23</sup> Mining and Metals: Czech Republic, in: *Economist Intelligence Unit*, 03/06/2002.

<sup>24</sup> See [www.trz.cz](http://www.trz.cz)

<sup>25</sup> Interview by Author with Czech and Slovak Steel Consultant and Regional Advisor Prague, 18/03/2004.

<sup>26</sup> Hutnictvi zeleza, *Steel Federation of the Czech and Slovak Republics: the Czech Steel Industry in the Economy (output, economy, trade, environment and situation 1998-2002)* Prague, 2002b, pp. CD-rom.

<sup>27</sup> VSZ is also the largest single integrated industrial firm in Slovakia. It had 128 subsidiaries including the production of machinery, ceramics, engineering, sports goods, information and hotel services, banking and insurance as well as a football club, in: Metalworking & Processing Slovakia, in: *Economist Intelligence Unit*, 22/02/1999.

management of VSZ accumulated most of the shares and effectively owned the company. By 1997 it accounted for 10 per cent of Slovakia's GDP and 20 per cent of export earnings.

By the end of 1998 the company made a loss and defaulted on a US\$ 35 mn syndicated loan. *US Steel*, the American steel maker, set up a joint venture in 1998 with VSZ taking 50 per cent of the corporation<sup>28</sup>. By April 2000 VSZ was sold to US steel, which took over all its debt. The company retained 15,482 employees. Early in the 21<sup>st</sup> century VSZ had become the most technologically advanced flat steel producing company in the region<sup>29</sup>.

The privatisation of VSZ to US Steel became a bone of contention between the EU and Slovakia in the context of the EU enlargement process<sup>30</sup>. As part of the privatisation contract US Steel was allowed a 10 year income tax holiday. In return the company agreed to keep employment levels stable and invest in the modernisation of the plant. The deal was beneficial for the Kosice region where unemployment stood at 24.4 per cent in 2000 with a higher jobless rate amongst those below 25 years of age. Slovak legislation did not forbid tax exemptions<sup>31</sup>.

The EC considered the tax holiday as state aid and not in accordance with protocol 2 of the EAs and EC competition regulation. The EC also considered US steel to benefit from state aid in the form of deferrals and write offs of tax debt in 1999 and 2000<sup>32</sup>. The terms of the privatisation deal were only acceptable to the EU provided US Steel reduced output capacity. Slovakia tried to keep the issue outside the EU enlargement process and failed.

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<sup>28</sup> Business news: VSZ announces a joint venture with US Steel, in: *Economist Intelligence Unit*, 27/02/1998.

<sup>29</sup> Development of Metallurgical Industry Slovakia, *IGM Conference*. Berlin, 5 and 6 February 2004.

<sup>30</sup> VSZ accumulated debt in 2000 reached US\$325 mn which US Steel took over. US Steel also pledged to invest US\$ 700 mn over a period of 10 years while the government forgave past tax arrears, in: Deal of the Week: Heavy Metal, in: *Economist Intelligence Unit*, 03/04/2000.

<sup>31</sup> Under a tax investment incentive programme agreed between US Steel Kosice and the Slovak government the steel maker received a US\$ 500 mn tax credit from 2000 through 2009. The agreement placed limits on total production and sales allowing for modest growth during the period covered by the investment incentive, in: United States Steel: Slovakian Competition Policy for Entry Into European Union Expected to Have No Significant Impact on U. S. Steel Kosice, in: *PRNewswire-FirstCall*, Pittsburgh: 25/10/2000.

<sup>32</sup> Interview by Author with Representative of Slovak State Aid Office, Bratislava, 26/02/2004.; Slovak State Aid Office, *Key Issues for Closing Chapter 6*, Bratislava, April 2002, pp. 6., p. 5. Another company where tax holidays played an important role was Volkswagen Slovakia.

Between 1989 the total number of workers in the Slovak steel industry declined from 30,000 to 15,500 in 2001<sup>33</sup>. Over that period Slovak output measured in crude steel declined from tonnes 4.5 mn to circa tonnes 2.9 mn in 1999.

#### **4.2.2.2. Hungarian Basic Iron and Steel**

The Hungary basic iron and steel industry was already in crisis in 1989. Due to the economic change over and the collapse of the COMECON market production dropped by 54 per cent between 1989 and 1992. Uneconomic capacity was dismantled between 1992 and 1996 and production stabilised at circa tonnes 2 mn<sup>34</sup>. By then the industry was regarded a sunset industry associated with the Communist plan economy.

The country's single steel producer, Dunaferr Steel Works, failed to privatise<sup>35</sup>. The industry lacked capital and investment to restructure and modernise. In contrast to neighbouring countries the Hungarian government decided to limit state aid to the industry. After 1998 the industry no longer received state aid.

At the turn of the century the company made a loss. Dunaferr was being kept alive by banks<sup>36</sup>. Employment had fallen to 9,000 workers<sup>37</sup>. A new management team was appointed in February 2001<sup>38</sup>. By then the production of the country's other steel companies had dropped to a negligible level. Hungarian steel producers reported combined losses of HUF 8.8 bn at the end of 2001.

EU restrictions added to the difficulties of the sector. The threat of import restrictions made EU importers halt orders from Hungary for the third quarter of 2001. Traditional costumers of the Hungarian steel producers relied rather on other EU steel producers to fill their demand<sup>39</sup>. In

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<sup>33</sup> This does not include metal working or the substantial Slovak armaments industry where the number is far larger.

<sup>34</sup> VAS-ES, *State of the Hungarian Steel Industry*, Budapest, 2004.

<sup>35</sup> *Interview by Author with Representative of the Iron and Steel Institute*, Budapest, 04/02/2004.

<sup>36</sup> Newswire: Lifeline for Domestic Steel Industry, in: *EUI Businessnews*, 02/04/2003.

<sup>37</sup> Between 1989 the number of employees in the Hungarian steel industry declined from 44,000 to less than 10,000.

<sup>38</sup> Dunaferr anticipates HUF 3.3bn in losses this year, in: *MTI-Econews*, 13/04/2001.

<sup>39</sup> Temporary steel tariffs no cause for backlash, in: *MTI-Econews*, 21/05/2002.

2003 the company continued to be in state hands<sup>40</sup>. At the end of 2004 the Ukrainian Steel company *Donbass* bought *Dunaferr*<sup>41</sup>.

#### 4.2.2.3. Polish Basic Iron and Steel Sector

After 1989 The Polish steel industry badly needed revamping. The sector was largely seen as a sunset industry in need of a long and costly restructuring, lay offs, plant closure and upgrading of product lines<sup>42</sup>. The transition process revealed the steel industry's poor competitiveness. Over the 1990s and early 2000s the industry became a tricky matter for successive government's privatisation efforts. Fears of boosting unemployment and alienating trade unions made privatisation an even more loaded issue than usual. Only one major steel works, Huta Warszawa, was privatised and sold to the *Italian Lucchini* concern in the 1990s.

Throughout the 1990s around mn 8.3 tonnes of steel-making capacity was put out of operation and as many as 47 open-hearth furnaces were closed in addition to seven outdated electric furnaces. Indecision over how to package the sector's assets allowed the industry's debts to grow, reaching US\$ 2.4 bn by the end of 2000 and severely hampering subsequent sell-off attempts. Poland's steel mills were still in state hands by the end of 2001. The EC was critical of different restructuring plans. EU member states refused to give their assent to restructuring plans as happened in 1998<sup>43</sup>.

Huta Katowice became a government owned joint stock company in 1991. The company employed 25,000 workers in 1989 and predominantly produced low value added steel. The number of workers fell to 5,570 in 2001<sup>44</sup>. Huta Katowice had accumulated huge debts and the state stepped in to prevent the company filing for bankruptcy in November 2000<sup>45</sup>. Huta Tadeusza Sendzimira (HTS) or the Lenin Steel Works in Krakow was the largest steel works in Poland. In 1989 it employed approximately 40,000 people declining to 9,955 in 2000. A first

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<sup>40</sup> Interview by Author with Representative of the Iron and Steel Institute, Budapest, 04/02/2004.

<sup>41</sup> See: [www.dunaferr.hu](http://www.dunaferr.hu)

<sup>42</sup> The Vienna Institute for International Economic Studies (WIIW), *Developments and Prospects of the Basic Metals and Fabricated Metal Products Sector in the Central and Eastern European Countries*, Vienna, February 2002, pp. 65., p. i.

<sup>43</sup> Poland: Economic Policy: New differences with EU emerge over steel restructuring, in: *Economist Intelligence Unit*, 15/11/1998.

<sup>44</sup> Metalworking & processing in Poland, in: *Economist Intelligence Unit*, 22/09/1997.

<sup>45</sup> Poland: Steel privatisation runs into difficulty, in: *Economist Intelligence Unit*, 09/03/2001.

attempt at privatising the company failed in 1998<sup>46</sup>. In 1999 HTS made a loss of US\$ 24 mn contributing to the staggering net loss of US\$ 300 mn of the entire state owned steel industry that year<sup>47</sup>.

Industry debt accumulated impacting on the general government budget. The government was pressed to submit another restructuring plan to the EC for approval on 30 June 1998. The plan envisaged a full restructuring of the entire steel industry by 2001 keeping steel production capacity at mn 13.4 tonnes while reducing total employment in the sector from 87,000 to 40,000 by 2010. Privatisation of a total of 12 steel plants would be completed with the two largest mills, Huta Katowice and Huta Sendzimira, privatised in the short run<sup>48</sup>.

The EC expressed three concerns. First, the government would take on too much debt. Second, the state subsidies exceeded the total sum proposed by the government. Finally, the EC argued that the Polish market would absorb less steel than the plan suggested and feared that excess capacity would end up on EU markets. In September 1998 several EU member states objected to the optimistic growth and demand projections. They were worried that Poland would offload its excess steel production on the EU market<sup>49</sup>. The plan was rejected.

In February 2001 the government made another attempt by merging together the four largest steel mills, which accounted for over 70 per cent of local steel output. The new company was called the *Polish Steel Group (Polski Huty Stali - PHS)*. It combined Huta T. Sendzimira, Huta Katowice, Huta Florian and Huta Cedler. The plan involved a general restructuring programme for the entire industry including government subsidies until 2006 of which a majority would be spend on PHS. It also involved a reduction of labour from 23,000 to 16,000 and a capacity reduction of almost mn 1 tonnes out of a total of mn 10 tonnes by the end of 2006<sup>50</sup>.

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<sup>46</sup> A consortium of Voest Alpine Stahl (Austria) and Hoogovens (Netherlands) suspended negotiations on the purchase of Huta Sendzimira, the country's second-largest steel mill in January 1999 because it wanted the consolidation of the two largest mills, Huta Katowice and Sendzimira, in: Metalworking & processing in Poland, in: *Economist Intelligence Unit*, 16/03/1998. ; Poland: Metal Working & Processing in Poland, in: *Economist Intelligence Unit*, 04/01/1999.

<sup>47</sup> Metalworking & processing in Poland, in: *Economist Intelligence Unit*, 13/03/2000.

<sup>48</sup> Announcement of the Metallurgical Chamber of Commerce, in: Economic Policy in: *Economist Intelligence Unit*, 01/09/1998.

<sup>49</sup> Poland: Economic Policy: New differences with EU emerge over steel restructuring, in: *Economist Intelligence Unit*, 15/11/1998.

<sup>50</sup> Poland: Long Divisions, in: *Economist Intelligence Unit*, 12/02/2001.



The stakes were high as bankruptcy of PHS would have had knock on effects for local energy producers, coal mining and the metals sector. To support the privatisation the government introduced temporary import tariffs on selected steel products from July 2002 for the duration of 200 days with a range of 11 to 36 per cent<sup>51</sup>. Both subsidies and capacity exceeded what was legally allowed under EU legislation. In effect the plan entailed a TPR of at least 2 years. The plan cleared the fences and the EC gave its approval. In August 2003 the UK-based LNM Group struck a deal to buy PHS. Under the privatisation plan the Polish steel industry stood to receive €12 mn of aid until 2006 mainly for financial restructuring. It would shut down inefficient facilities amounting to an additional tonnes 1,35 mn of finished steel products.

On the whole, the Polish state owned basic and iron steel industry in the late 1980s produced circa tonnes 16 mn of crude steel with as much as 140,000 to 145,000 steel workers. These figures declined to tonnes 7.3 mn by 1999 with 55,000-60,000 workers while the industry accumulated a substantial debt<sup>52</sup>. By 2003-2004 the industry was privatised. Consolidation could begin.

### **4.3. Characteristics and Preferences: A Sunset Industry**

In the next section I will consider trade patterns (1992-2004), factor and asset specificity, sectoral cohesion and insider status for the sector across the region and for each of the V-4 countries. The EU integration of the industry was problematic and complicated by government subsidies, anti-dumping measures, which had an influence on production and trade patterns, and industry specificity. Social pressures arising from plant closures had strong influence on sectoral preference formation and political mobilisation.

#### **4.3.1. Trade**

Trade in basic iron and steel between the EU and Central Europe has been characterised by (a) excess production capacity in Europe and declining world prices for basic iron and steel; (b) the special trade regime under the expiring ECSC Treaty (2002) and EAs (1996-2004); (c) World and EU trade surpluses for all V-4 up to 1995 with the exception of Hungary followed by progressive trade deficits towards the end of the 1990s with the notable exception of the Slovak

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<sup>51</sup> Mining and Metals: Poland, in: *Economist Intelligence Unit*, 29/07/2002.

<sup>52</sup> Metallurgical Chamber of Industry and Commerce in Poland (HIPH), *Polish Steel industry*, Katowice, 1996-2004.

steel makers; and (d) exports of predominantly low value-added steel products with the exception of the Slovak producers.

#### **4.3.1.1. World Steel Markets (1992-2004)**

Between 1992 and 2002 world steel markets registered significant disparities between crude steel production capacity and production. The output gap put downward pressure on world steel prices<sup>53</sup>. In 2000 excess capacity was some tonnes 300 mn, the equivalent of almost one-third of total world crude steel production capacity at tonnes 1.1 bn. The world average capacity utilisation rate was a mere 71 per cent in 1999 with 76 per cent in the EU.

Increased production in non-OECD countries put further downward pressure on steel prices. Several Asian countries had more than doubled their steel production capacity since the mid-1980s. Imports of relatively cheap steel from these countries to the EU increased. Steel producers in the CEECs, having lost their formerly huge market in the region with the collapse of the S.U., also diverted some of their exports to the EU and other foreign markets.

Excess capacity and tougher competition encouraged steel makers to downsize production. In 2001 the OECD initiated a multilateral effort to cut steel production capacity. A total of 43 countries agreed that oversupply was at the root of the world's steel market problems. They agreed to explore ways to facilitate the closure of inefficient excess capacity in their respective countries and strengthen competition by reigning in subsidies and related support measures. However, to maintain their profit margins in the face of falling prices many steel producers continued high volume production.

A massive consolidation in the steel industry, particularly in the EU and US, ensued. Pursuing economies of scale five major groups, Arbed (Luxembourg), Usinor (France), Corus (British Steel, United Kingdom; Hoogovens, Netherlands), ThyssenKrupp (Germany) and Riva (Italy) formed in the EU. Together with the world's largest steel producers in Asia and others such as LNM (Ispat International) they produced one-fifth of the world's steel in 1999<sup>54</sup>.

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<sup>53</sup> OECD, *Iron and Steel Industry in 2000* Paris, 2002a, pp. pp. 1 - 49 , p. 42.

<sup>54</sup> OECD, *New Patterns of Industrial Globalisation Cross-border Mergers and Acquisitions and Strategic Alliances*, Paris, 2001 pp. pp. 1 - 175., pp. 87-91.

Over the same period world steel trade by volume rose faster than world production. An increasing share of total steel production crossed international boundaries. The EU's net surplus in steel trade became small. It increasingly imported steel and moved from being a major steel exporter at the beginning of the 1990s to a position of near balance in steel trade in volume terms. It remained a net exporter in value terms.

#### **4.3.1.2. The EUs Steel Trade Regime (ECSC and EAs)**

The first-generation trade agreements between the EU and the V-4, i.e. the Trade and Cooperation Agreements (1988-1989) followed by the EAs (1991-2004) envisaged free trade with the exception of sensitive products such as basic iron and steel<sup>55</sup>.

Under the iron and steel protocol of these agreements (so-called protocol 2 or the ECSC Treaty) the EC eliminated its quantitative restrictions on imports of ECSC products from the V-4 countries. Tariffs were completely abolished in 1996<sup>56</sup>. By that time tariffs and quotas were of lesser importance than price monitoring. EC price monitoring prevented low cost producers' exports to the EU<sup>57</sup>. EU-15 iron and steel producers started to prepare wholesale anti-dumping cases in preparation of the liberalization. Central European producers anticipated such market behaviour and felt obliged to manage their exports to the EU resulting in cartel behaviour<sup>58</sup>. In other words, steel trade was far from free under the EAs<sup>59</sup>.

Protocol 2 gave ample scope to resort to temporary protectionism if the signatories deemed their domestic industries greatly at risk because of import competition<sup>60</sup>. The main problem was so-called contingent protection on both sides. An increase in imports that caused or threatened to cause serious injury to domestic producers could limit or halt imports. In addition, there were

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<sup>55</sup> Z. WANG and L.A. WINTERS, *EC imports from Eastern Europe: iron and steel*, London: EBRD, October 1993., pp. 18-21.

<sup>56</sup> The V-4 negotiated longer periods with Poland seven years and Hungary and Czechoslovakia nine years, in: A. MAYHEW, *Recreating Europe: the European Union's policy towards Central and Eastern Europe*, Cambridge; New York: Cambridge University Press, 1998., p. 63.

<sup>57</sup> L.A. WINTERS, *Import surveillance as a strategic trade policy*, London: Centre for Economic Policy Research, 1990., p. 22.

<sup>58</sup> J. ROLLO and A. SMITH, The Political Economy of Eastern European Trade with the European Community: Why So Sensitive?, in: *Economic Policy*, April 1993, 16, pp. 139-81., p. 173.

<sup>59</sup> Ibid.

<sup>60</sup> A. MAYHEW, *Recreating Europe: the European Union's policy towards Central and Eastern Europe*, Cambridge; New York: Cambridge University Press, 1998., p. 63.

a number of specific safeguards, most importantly the anti-dumping clause<sup>61</sup>. Another provision allowed each side to take measures unilaterally to counter 'perceived breaches of the agreement after 60 days at the latest' giving considerable room to use these clauses for protectionist purposes.

The EU proved ready to use commercial policy to shield domestic producers against low-cost competition from the CEECs. The main damage for the Central European industry did not stem directly from the occasional reintroduction of duties and quotas but from the lingering threat that hung over their EU exports<sup>62</sup>.

Between 1990 and 1994 a total of 15 anti-dumping cases were launched against Central European firms. Between 1996 and 2002, 11 measures were still in force against the Czech basic iron and steel industry<sup>63</sup>. Generally, Czech steel exports to the EU were held in check by the threat of other safeguard measures<sup>64</sup>. According to a representative of the Czech steel industry: 'Each time they initiate an anti-dumping action, we lose our position in the market and our market share for the duration of the procedure. Then we have to start all over again'<sup>65</sup>.

Hungary cut its steel production capacity by half in compliance with the EAs and had no extra steel making capacity at the end of the 1990s. Seven anti-dumping measures were still in force at the end of the accession negotiations (2002) accusing the Hungarian basic iron and steel industry of either dumping or unfair trade<sup>66</sup>.

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<sup>61</sup> During one interview by this author the interviewee asked his staff to provide a list of EU anti-dumping cases initiated against the Czech basic iron and steel industry and came up with a list of 25 pages of anti-dumping cases (threats, initiations, investigations and decisions). He argued that in the EU a concerted effort existed to push the Central Europeans out of the market, in: *Interview by Author with Representative of the Czech Trade Union of the Steel Industry*, Prague, 22/03/2004b.

<sup>62</sup> Trade economists have shown conclusively that the mere threat of safeguard measures such as anti-dumping is a major drag on trade flows. The knowledge that undercutting EU producers can lead to penalties may have deterred many CEE producers from exploiting their price advantages. Also, foreign investors may have been reluctant to put money into CEE industries that might then not be allowed to export to the EU market.

<sup>63</sup> European Commission (Directorate-General for Trade), *Anti-Dumping and Anti-Subsidies Measures List*, Brussels, 07/05/2003.; On 18 January 1996 the EC announced anti-dumping measures, in: *Foreign trade & payments: EU drops one anti-dumping action but imposes another* in: *Economist Intelligence Unit*, 08/04/1996.

<sup>64</sup> Another EU action was approved on 17 November 1998 involving the imposition of special duties ranging from 5% to 47%. Czech producers were shown to be selling at prices between 21 per cent and 43 per cent below those charged by EU producers, but there was no evidence of selling exports at below prices, in: *Foreign trade & payments: EU restricts Czech steel imports*, in: *Economist Intelligence Unit*, 28/01/1998.

<sup>65</sup> *Interview by Author with Representative of the Czech Trade Union of the Steel Industry*, Prague, 22/03/2004b.

<sup>66</sup> European Commission (Directorate-General for Trade), *Anti-Dumping and Anti-Subsidies Measures List*, Brussels, 07/05/2003.

As many as 19 protectionist measures were initiated against Polish producers between the entry into force of the EAs (1996) and the end of the accession negotiations (2002). Over the same period five cases affected the Slovak basic iron and steel industry under the banner of dumping or unfair trade<sup>67</sup>.

Despite the contingent protectionism of the EAs they had a dampening effect on resurgent protectionism in the CEECs. Protectionist hurdles for non-EU exporters were higher than those coming from the EU<sup>68</sup>. The CEECs took up protectionist measures sometimes in reaction to calls from local producers and sometimes in retaliation against the EU. At the end of 2002, the Czech Republic, Hungary, Poland and Slovakia had six safeguard measures in force (three by the Czech Republic, one provisional by Hungary, one provisional by Poland and one by Slovakia)<sup>69</sup>. In the light of these protectionist measures full EU membership became all the more important as it would eliminate the uncertainty of protectionism once and for all.

#### **4.3.1.3. From Trade Surplus to Deficit**

Regional trade in basic iron and steel in 1998, the year the accession negotiations started, was worth between US\$ 8.2 and 8.3 bn<sup>70</sup>. When the V-4 joined the EU, regional trade in basic iron and steel had more than doubled reaching a total of US\$ 18.6 bn. In 1998 exports of basic iron and steel accounted for 51.2 per cent of total regional trade while imports took 48.8 per cent. At the end of 2004 imports as a share of regional trade had largely remained stable at 51.7 per cent; exports had fallen slightly to 48.3 per cent (see Table 14).

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<sup>67</sup> Ibid.

<sup>68</sup> Is the EU protectionist in its relations with the applicant Central and East European countries (CEEC)? , in: *Economist Intelligence Unit*, 11/05/1999.

<sup>69</sup> European Commission (Directorate-General for Trade), *Report for the 133 Committee: Overview of third country trade defence actions (anti-dumping, countervailing and safeguard cases) against the Community*, Brussels, 09/04/2003 , pp. 22-26.

<sup>70</sup> Output or production data on basic iron and steel are not readily available in equal measurement unit. Trade data in € or US\$ is available in Eurostat Comext and the OECD trade databases respectively. Eurostat prodcom annual and monthly steel trade data record production of steel products for the V-4 from 2001-2002 onwards. The OECD provides data on steel production in million tonnes product equivalent (Mtpe) while the IISI provides crude steel production data in mn metric tonnes (mmt) – both are not comparable in value.

**Table 14: Trade in Basic Iron and Steel (per cent, 1992-2004)**

year	share of regional trade				share exports				share imports				share of export earnings				share of import earnings				share of regional production			
	Cz	Hu	Pl	Sk	Cz	Hu	Pl	Sk	Cz	Hu	Pl	Sk	Cz	Hu	Pl	Sk	Cz	Hu	Pl	Sk	Cz	Hu	Pl	Sk
92	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	3.2	7.3	n.a.	n.a.	2.7	2.1	n.a.	31.9	6.9	44.3	17.0
93	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	10.2	3.5	6.7	n.a.	3.5	2.3	2.3	n.a.	30.2	7.8	44.3	17.7
94	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	9.2	3.4	6.6	n.a.	3.8	2.7	2.6	n.a.	28.7	8.0	46.5	16.8
95	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	9.4	3.3	5.6	n.a.	4.6	3.1	3.2	n.a.	28.9	7.5	47.7	16.0
96	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	7.0	2.8	4.9	n.a.	4.0	2.7	2.8	n.a.	29.0	8.4	46.6	16.1
97	33.5	12.0	32.5	22.0	18.7	4.7	17.5	16.9	14.8	7.3	15.0	5.2	6.2	1.9	5.1	13.2	4.1	2.6	2.7	3.3	28.3	7.1	48.6	16.1
98	35.9	12.8	31.3	20.0	18.3	4.5	13.6	14.8	17.6	8.3	17.7	5.2	5.4	1.6	4.0	11.4	4.8	2.7	3.1	3.3	30.0	8.4	45.8	15.8
99	35.0	14.2	32.6	18.1	17.6	4.9	13.5	13.7	17.5	9.3	19.1	4.5	4.3	1.3	3.2	8.9	4.0	2.2	2.7	2.6	26.6	9.4	45.5	18.5
0	34.2	13.8	33.2	18.8	16.2	4.7	14.4	14.4	18.0	9.1	18.8	4.4	4.2	1.3	3.5	9.3	4.3	2.2	2.9	2.6	24.6	8.7	49.2	17.5
1	35.0	13.0	33.0	19.0	17.3	4.3	13.2	13.8	17.7	8.7	19.8	5.2	4.2	1.2	3.0	8.9	4.0	2.1	3.2	2.8	26.6	9.7	43.8	19.8
2	35.2	13.4	32.0	19.4	17.4	4.5	12.3	13.9	17.9	8.9	19.7	5.5	3.9	1.1	2.6	8.3	3.8	2.0	3.1	2.9	29.2	9.9	40.3	20.6
3	33.7	12.7	32.7	21.0	16.7	4.1	11.9	15.4	17.0	8.5	20.8	5.5	3.9	1.1	2.6	8.1	3.8	2.1	3.5	2.8	30.2	8.8	40.6	20.4
4	34.2	11.5	35.0	19.4	16.6	3.8	14.4	13.4	17.5	7.7	20.6	5.9	4.6	1.3	3.6	9.1	4.8	2.4	4.3	3.8	29.4	8.2	44.3	18.2
Av.	34.6	12.9	32.8	19.7	17.3	4.4	13.9	14.5	17.2	8.5	18.9	5.2	6.0	2.1	4.5	9.6	4.1	2.4	3.0	3.0	28.7	8.3	45.2	17.7

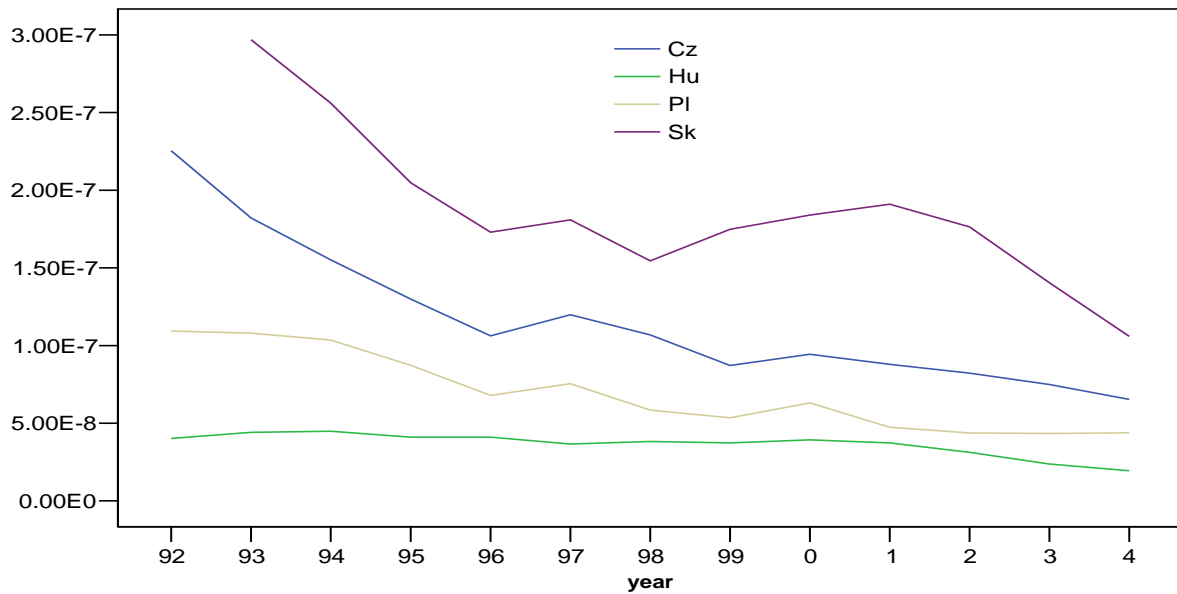
Note: Cz=Czech Republic, Hu=Hungary, Pl=Poland, Sk=Slovakia, Av.=average

Source: Own calculations based on OECD, Bilateral Trade Statistics, 1994-2004, own calculations; Crude steel production data from: International Iron and Steel Institute, (1992-2004, million metric tons - mmt).

In 1998 the Czech Republic was the leading regional basic iron and steel trader (35.91 per cent) followed by the Poland (31.32 per cent), Slovakia (19.96 per cent) and Hungary (12.82 per cent). The relative shares of regional trade in basic iron and steel largely remained stable between 1998 and 2004 with exports declining overall. Imports had risen only substantially for Poland from 17.7 to 20.6 per cent. Overall, the share of steel imports in the period 1998-2004 rose somewhat relative to exports with Poland accounting for the biggest rise in imports.

When observing the shares of regional crude steel production the capacity of the domestic industry accounts for most of the relative variation in trade. The importance of production of crude steel declined over the period (Figure 20) with Poland being the regions largest producer with 44 per cent (Table 14). The Czech Republic accounts for one third of total production followed by Slovakia with 16 per cent and Hungary with just under 9 per cent.

**Figure 20: Output crude steel over GDP (mmt, 1992-2004)**



Note: Cz=Czech Republic, Hu=Hungary, Pl=Poland, Sk=Slovakia, mmt=million metric tonnes normalised by GDP  
 Source: International Iron and Steel Institute, 1992-2004

It is striking that relative trade and production figures do not vary all that much over the period. The V-4's shares of regional trade, exports and regional production are relatively stable. Global excess production capacity and most importantly the EAs restrictive trade regime are the key explanatory factors. The biggest changes occurred in rising imports for Poland and the Czech Republic relative to production; and the rising importance of the Slovak steel industry by value towards the end of the decade. When considering trade balances for the V-4 only Slovakia stands out with a positive trade balance throughout the decade (see figure 21)<sup>71</sup>.

<sup>71</sup> Considering the export/import ratio (exports as a percentage of imports for an industry) only Slovakia maintains a figure above 250 per cent from 1997 onwards. The Czech Republic, Poland and Hungary all move from surpluses (291.4, 110, 221.5 in 1993 respectively) into deficits for all three with 97.4; 50.3 and 62.5 respectively in 2002. See OECD, STAN Indicators Database, (1990-2002).

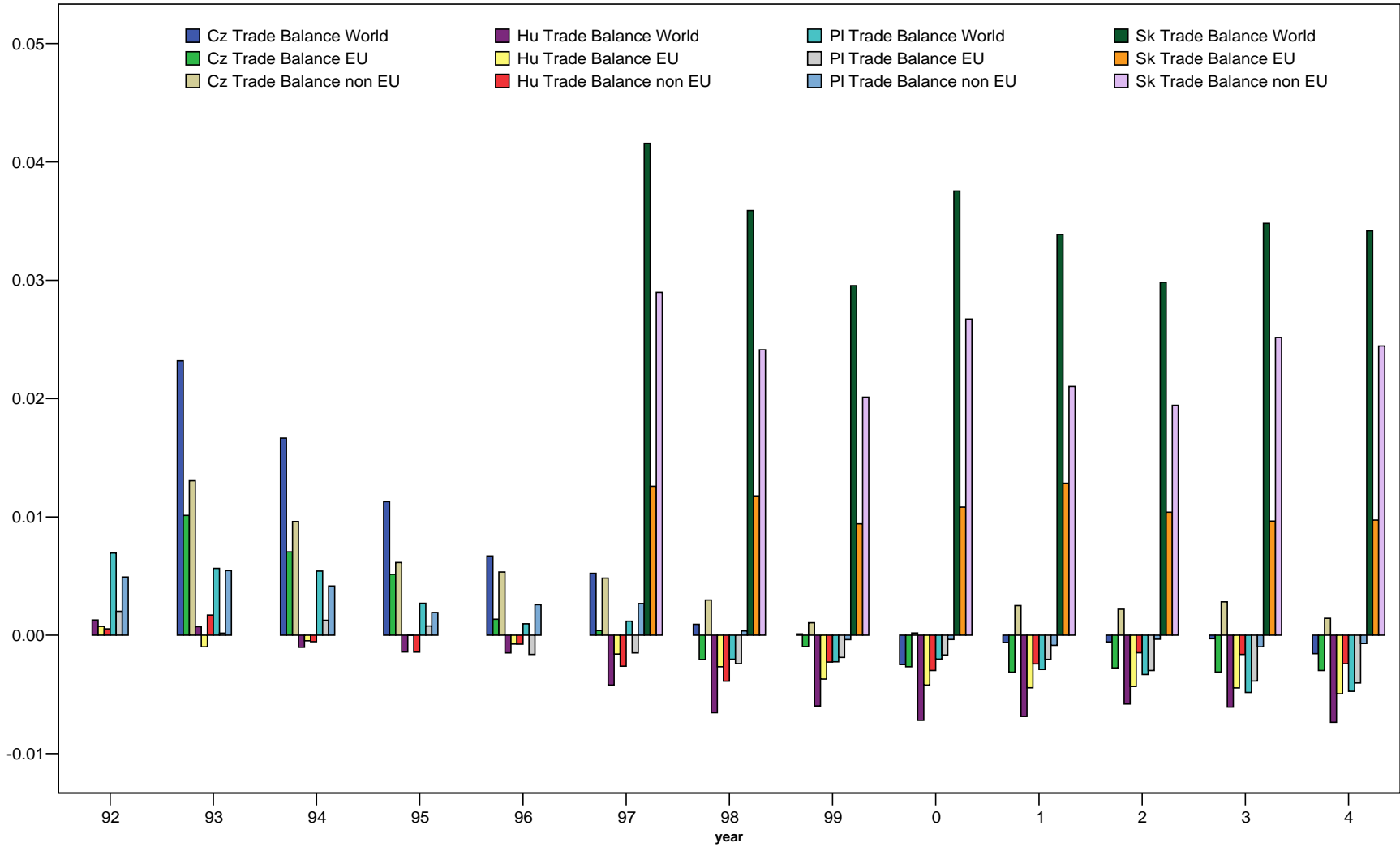
Slovakia recorded trade surpluses both with the EU and the world over the entire period. These are accounted for in higher value added flat steel produce or steel sheet predominantly used in the regional automobile industry. The revealed comparative advantage confirms this finding with the Slovak steel industry performing remarkably better relative to manufacturing, including in comparison to other V-4 countries<sup>72</sup>.

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<sup>72</sup> The contribution to trade balance (CMTB) indicator makes it possible to identify an economy's structural strength via the composition of international trade flows. It takes into account exports and imports and compares an industry's trade balance with the overall trade balance. It indicates whether an industry performs relatively better than the manufacturing total regardless of an overall trade surplus or deficit. Slovakia's CMTB scores over the period 1997-2002 are remarkably higher at 4.7 (1997) to 2.6 (2002) with Poland moving from 1.2 (1997) to -0.4 (2002) followed by the Czech Republic 0.9 (1997) to -0.1 (2002). The EU-14 was 0.3 in 1993 and 0 in 2002. See OECD STAN Indicator database, (1990-2002).



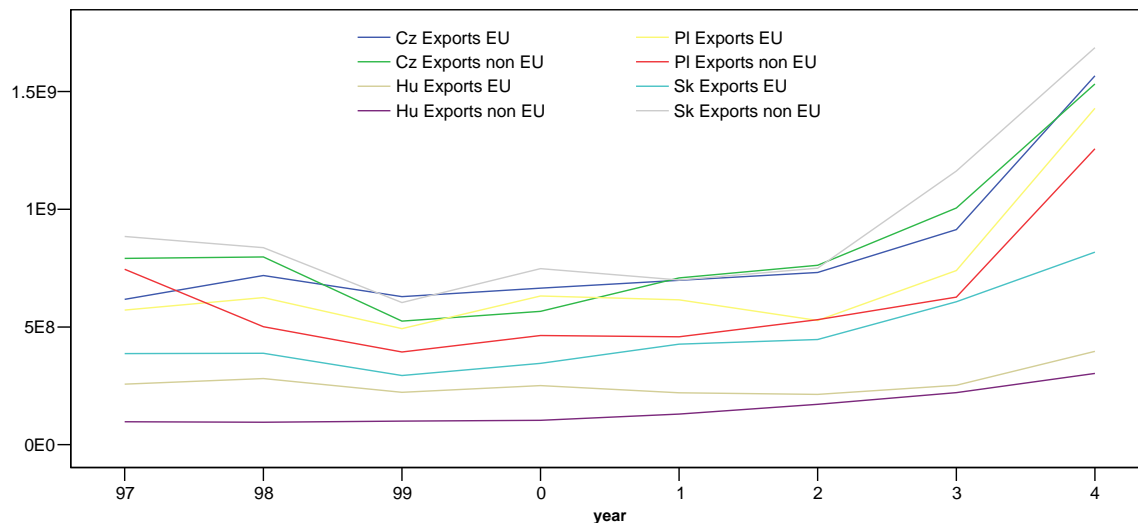
**Figure 21: Trade Balance in Basic Iron and Steel (1992-2004)**



Note: Cz=Czech Republic, Hu=Hungary, Pl=Poland, Sk=Slovakia  
 Source: OECD Stan Bilateral Trade Database (US\$ normalised by GDP), 1992-2004: Data Sk 1992-1996 not available

Furthermore, Slovakia progressively specialised in the 1990s and early 2010s in the exports of basic iron and steel relative to the other V-4 and the EU<sup>73</sup>.

**Figure 22: Exports World and EU (1997-2004)**



Note: Cz=Czech Republic, Hu=Hungary, Pl=Poland, Sk=Slovakia  
 Source: OECD, Bilateral Trade Statistics, US\$, 1997-2004

As Figure 22 shows basic iron and steel producers in Central Europe, having lost the formerly huge COMECON market with the collapse of the S.U., diverted their exports to the West, particularly the EU. Czech and Polish exports to the EU even temporarily overtook their exports to the rest of the world, most of which went to the CEECs and former S.U., after the Russian financial crisis in 1998.

#### 4.3.2. Asset Specificity: Medium Low Technology Industry

How specific is the basic iron and steel industry in Central Europe? And is there variation of specificity within the basic iron and steel industry in Central Europe.

Generally, the industry is capital, energy and labour intensive and highly site specific as its factors are immobile and their value depends on geographic location. Basic iron and steel producing firms maximise value through minimising transport costs. Integrated steel works were founded in the vicinity of coal mines and iron ore deposits. This was particularly the

<sup>73</sup> Export specialisation shows a country's exports for an industry relative to total industries' exports. A value of 100 in certain country implies that the country tends to specialise in exports in that given industry. The index of revealed comparative advantage for the V-4 indicates that all V-4 specialised in basic iron and steel exports in 1993 (Cz&Sk=356, Hu=123.5, Pl=254.5, EU-14=114). With exception of Hungary the V-4 are all specialised in the export of basic iron and steel and Slovakia progressively more relative to neighbouring Czech Republic and Poland by 2002 (Cz=173.5, Hu=50.2, 115.5=Pl, Sk=369.7 with the EU-14=112.9). See OECD, STAN Indicator database, (1990-2002).

case in the Moravia-Silesia region in the Czech Republic and Poland where the largest integrated steel works are located within a 100 km radius of each other<sup>74</sup>. The steel mills in Hungary and Slovakia, constructed by the Communists, were primarily built in locations with easy access to transport. The Slovak mills in the eastern city of Kosice are sited next to a broad-gauge railway line along which raw materials are imported from Russia and the Ukraine. Railway tracks in the western direction serve as transport routes for finished products. The Dunaferri Iron Works in Hungary were set up near the Danube basin with little regard for the presence of raw materials.

When measuring the industry's specificity by innovation the industry is categorised at the bottom of the table of the medium-low-technology manufacturing industry<sup>75</sup>. Data indicate that the basic iron and steel industry in Central Europe is low on asset and factor specificity compared to the EU. The Slovak industry exemplifies the highest investment including in R&D. Figure 23 shows that the Slovak industry invested most, which was part of the privatisation contract with the government. As in neighbouring countries the workforce declined significantly and was only to a certain extent involved in the privatisation process<sup>76</sup>.

Hungarian producers are the only ones that kept pace with Slovakia, however, at a level less than half of its smaller neighbour. In Hungary the Iron and Steel Research Institute was liquidated in 1993 and R&D expenditure was at an all time low. R&D expenditure per tonne of crude steel declined from US\$ 1.2 in 1996 to 0.7 in 2000<sup>77</sup>. Czech and Polish producers were at the bottom of the table investing roughly 1/7<sup>th</sup> of Slovakia's steel industry: 'Generally, investment and expenditure in R&D was a phenomenon of the past. The Czech industry simply lacked money for such tasks. In the metallurgy faculty of Ostrava Technical University (Banska) the number of students declined dramatically because nobody wanted to study the craft. Generally people thought it [the industry] would disappear. Only the big

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<sup>74</sup> The biggest Czech steel plants are located close to Ostrava (Northern Moravia). Poland's largest steel plant is sited approximately 80 km North across the Czech-Polish border in Katowice. The Czestochowa steel plant is located about 60 km North West of Katowice. The giant steel mill built near Krakow is barely 60 km east of Katowice.

<sup>75</sup> According to the OECD Classification of manufacturing industries based on technology, in: OECD, *Science, Technology and Industry Scoreboard, Classification of manufacturing industries based on technology*, Paris, 2003. The scoreboard is based on the OECD ANBERD and STAN databases.

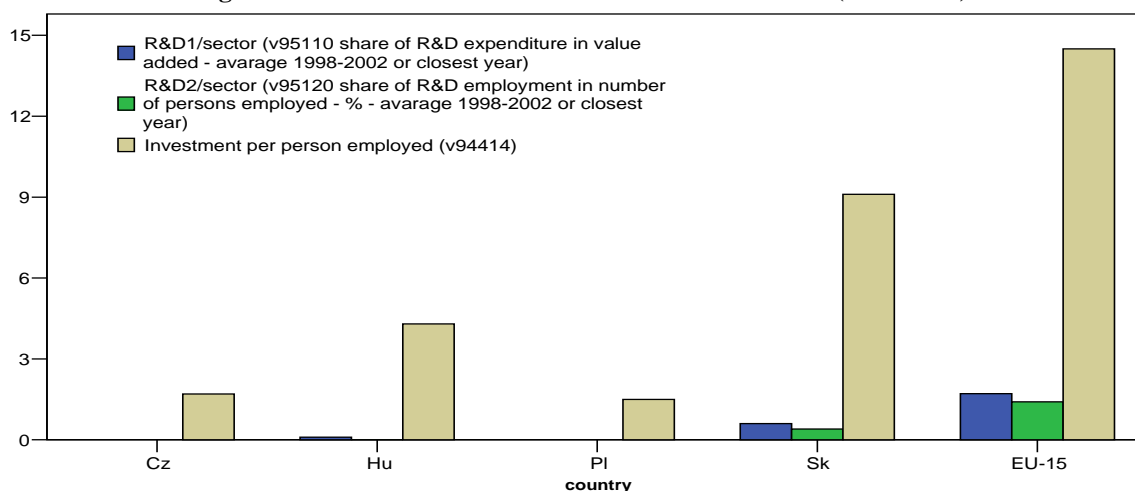
<sup>76</sup> Interview by Author with Representative of Os Koz, Bratislava, 27/02/2004.

<sup>77</sup> Interview by Author with Representative of the Iron and Steel Institute, Budapest, 04/02/2004.

firms have their proper research centre and also their R&D expenditure has been low and irregular<sup>78</sup>.

The average level of investment per person remains much lower compared to the EU average over the same period. Other R&D measures such as R&D employment and share of R&D expenditure in value added, confirm the Slovak basic iron and steel industry's lead, however, at less than 1/3<sup>rd</sup> of similar average expenditures in the EU.

**Figure 23: R&D and Investment in Basic Iron and Steel (1999-2002)**



Source: Eurostat, Annual Detailed Enterprise Statistics (averages 1998-2002); no R&D data available for the Czech Republic and Poland

Note: Cz=Czech Republic, Hungary=Hu, Pl=Poland, Sk=Slovakia

Within the region Slovak steel makers invested most by a wide margin. When controlling for total sectoral employment the Slovak steel industry appears to employ more R&D personnel than the EU-15 on average combined (see Table 15). Much of the investment levels appear to be related to the type of steel produced. The Slovak steel sector produces flat products which are predominantly of higher quality compared to the raw steel long products that Polish and the Czech Steel Works were producing<sup>79</sup>.

<sup>78</sup> Interview by Author with Representative of Steel Federation of the Czech and Slovak Republics, Prague, 22/03/2004a.

<sup>79</sup> Slovakia and Hungary produce for 100 and 85 per cent flat product respectively. The Czech Republic and Poland produce for around 35 per cent flat products of total. Flat products are used for instance in the car and tin industry which require increasingly more sophisticated steel products, in: European Commission, *Country Steel Profiles: Czech Republic, Hungary, Poland and Slovakia 2004* (reference year).

**Table 15: Selected Asset Specificity Indicators (1998-2002)**

country	skill	R&D3	R&D4
Czech Republic	2	n.a.	n.a.
Hungary	2	0	0
Poland	2	n.a.	n.a.
Slovakia	2	171	0.4
EU-15	2	451	0.02

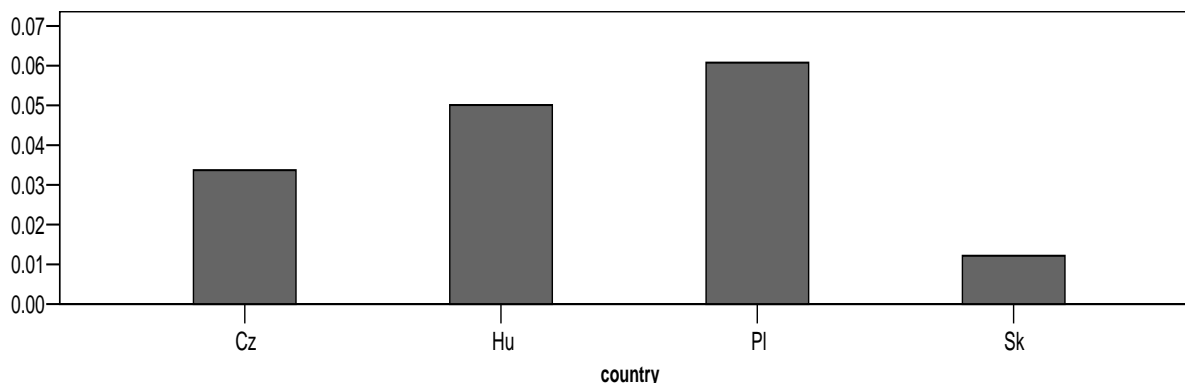
Note: skill= ISCO-88 skill level  
R&D3= number of R&D personnel employed  
R&D4= number of R&D personnel employed over total sectoral employment  
Source: Eurostat (Annual Detailed Enterprise Statistics – average 1998-2002)

#### 4.3.3. Sectoral Cohesion: A Highly Concentrated Industry

Sectors with fewer firm and higher number of employees per firm are more likely to be able to bring pressure on politicians compared to sectors where the number of firms is higher and their size smaller. The former also tend to have a higher likelihood of success from lobbying and are inclined to pursue the lobbying route more often.

The basic iron and steel industry is highly concentrated (Figure 24) in all V-4. Hungary's and Slovakia's basic iron and steel industry is dominated by one large firm producing between 85 and 100 per cent of the production respectively. The Slovak industry accounts for the lion share of sectoral employment. The complete domination of US Steel in the Slovak Republic results in a concentration ratio of close to zero. The Czech and Polish basic iron and steel industries are similar in that a number of very large firms dominate the industry with the Czech Republic having the largest firms by number of persons employed. Only in Hungary is the steel sector in part characterised by a higher number of smaller firms.

**Figure 24: Sectoral Concentration in the Basic Iron and Steel Industry (1998-2002)**



Note: Cz=Czech Republic, Hungary=Hu, Pl=Poland, Sk=Slovakia  
Source: Eurostat, Annual Detailed Enterprise Statistics, Averages 1998-2002, own calculation of ratio between number of firms and average number of employees per firm and sector

#### **4.3.3.1. National Associations**

National and international associations are the common political assets of the industry. They are the political extensions of the economic interests that sometimes might function as a go-between in the economy-state relationship. According to the dominant view in the lobbying literature associations influence the regulated environment in which the industry operates. They seek policy partnership with the authorities. The state attaches high importance to policy input from market operators.

The Central European national associations represent the industry in policy partnership with national authorities. The primary reason for their existence is the importance of data gathering in relation to trade issues. The national associations inform and co-operate with the government and individual ministries to fend off or launch safe guard measures and protect the interests of the industry. In all individual V-4 countries one national association represents the basic iron and steel manufacturing industry. The Slovak industry is associated in both the Czech and Slovak political organisations.

#### **Steel Federation of the Czech and Slovak Republics (HZ)**

Hutnictví železa a.s. (HZ) or the Steel Federation of the Czech and Slovak Republics is the one leading association for the basic iron and steel industry in the Czech Republic and Slovakia<sup>80</sup>. Founded in November 1992 in Prague and launched in January 1993 the HZ had 18 members and represented all major steel producers in the Czech Republic and Slovakia. The largest steel companies, Nova Hut, Vitkovice Steel, Trinecke Zelezarny and US Steel Slovakia dominated the association. HZ covered 100 per cent of total basic iron and steel production capacity and had a regional powerbase in North Moravia in the Czech Republic and Kosice in South East Slovakia.

The Federation provided information, co-ordinated lobbying activities and lobbied state administration bodies for its members. HZ had a contact function when negotiating particular procedures for completing the EAs and discussed tariff and non-tariff trade terms with the MoIT, the MoFA and the government. Its links with the government were reinforced as a majority of the Czech steel industry were still owned by the NPF. The

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<sup>80</sup> See website <http://www.hz.cz/>.

association was politically very active ahead of EU enlargement: ‘We mobilised on several occasions [1992, 1996, 1997, 1999, 2001 and 2002] including on EU enlargement and contacted the Czech MoIT, which was in charge of the basic iron and steel industry. But their influence was limited as the industry had to fulfil the criteria of viability under protocol 2’<sup>81</sup>.

The association also represented Slovak steel producers. VSZ surpassed the other Slovak members in size and political sway. The company functioned as a regional power base for the former authoritarian Prime Minister, *Vladimir Meciar*. Under Meciar’s rule the importance of VSZ’s CEO exceeded those of individual government ministers. He dealt with important political issues directly. He had a habit of publicly commenting on the steel industries’ problems in the context of EU enlargement. That tradition did not change when US Steel took over under the new CEO *John Goodish*. The latter considered Eurofer’s and the EC’s anti-dumping as ‘attempts of European producers to protect the domestic market during the economic depression’<sup>82</sup>.

HZ joined Eurofer on 21 November 1996 in the wake of the associated membership of its largest Czech and Slovak members. The companies and the federation hoped that their membership would make it easier to counter accusations of dumping made by Eurofer against the Czech steel industry in July 1995<sup>83</sup>. Alas, its associated membership did not prevent Eurofer and the EC from acting against the interests of the Czech and Slovak basic iron and steel industry. New EC initiated anti dumping and safeguards were launched following complaints by Eurofer.

#### **Association of Metallurgy, Mining Industry and Geology of the Slovak Republic (ZHTPG)**

US Steel was also represented through the Association of Metallurgy, Mining Industry and Geology of the Slovak Republic (ZHTPG) in Slovakia. The association represented 40 institutions. These included firms, research institutes, business companies and three Slovak basic iron and steel producing enterprises with an employment of 30,000 workers. Around 15,000 were employed by US Steel Kosice. ZHTPG covered 100 per cent of total basic iron

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<sup>81</sup> Interview by Author with Representative of Steel Federation of the Czech and Slovak Republics, Prague, 22/03/2004a.

<sup>82</sup> Slovak steel maker rejects accusation of price dumping in: *Intellinews*, 23/11/2001

<sup>83</sup> Steel Producers Join Eurofer, in: *Economist Intelligence Unit*, 31/01/1996.

and steel production capacity. US Steel took a prominent position in the association. The President of the association was simultaneously Vice President of US Steel Kosice.

The association argued that EU enlargement was positive overall, although: 'on sectoral level the process did not necessarily bring positive results for the industry. US Steel Kosice lost out as the EU imposed quota and a strict regulatory environment, which it [the EC] wanted to apply ahead of EU accession'<sup>84</sup>.

'US Steel associated membership of Eurofer in 1996 had basically no effect on issues that emerged during the [enlargement] negotiations apart from relations, personal contacts and information'<sup>85</sup>. Good relations with the MoE and direct access to the government, the Minister of European Integration (MoEI) and the chief negotiator were helpful: 'You must not forget that the city of Kosice stands and falls with the steel industry. US Steel Kosice is very important to the city and for Slovakia. We were involved in the EU enlargement process from the beginning. The government and MoE consulted the association and US Steel during the screening process. We asked the government that the privatisation contract would be respected and were prepared to comply with the environmental chapter of the acquis. In return we asked for indirect subsidies to deal with the environmental problems'<sup>86</sup>.

#### **Association of the Hungarian Steel Industry (MVAE)**

The Magyar Vas-es Acelipari Egyesules (MVAE) or Association of the Hungarian Steel Industry represented all 19 basic iron and steel producers (2001), including the largest steel producer by volume and employment, Dunafer. It covered 100 per cent of total basic iron and steel production capacity<sup>87</sup>.

It was the prime contact for the government, the MoET and MoFA in preparing draft measures to protect Hungary's steel market<sup>88</sup>. Its regular line of communication was with the MoET. When EU related issues were on the agenda the MoFA assisted. In co-operation the

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<sup>84</sup> Interview by Author with Representative of Association of Metallurgy, Mining Industry and Geology of the Slovak Republic, Bratislava, 25/02/2004.

<sup>85</sup> Ibid.

<sup>86</sup> Ibid.

<sup>87</sup> See website <http://www.mvae.hu/>.

<sup>88</sup> Hungarian steel interests preparing protection measures in: *MTI-ECONEWS*, 26/03/2002.



three institutions it set up a steel imports monitoring system and prepared measures to restrict steel imports in 1998 and again in 2002<sup>89</sup>.

The association was consulted regularly on EU enlargement. MVAE highlighted its concerns on a number of occasions to the government. It had two possible routes for political mobilisation: 'One was the government and the individual ministries. The prime route was the MoET and sometimes the MoEN. In relation to EU accession the MoFA took the lead. The association had the impression that good relations with the EU took priority over the interest of the Hungarian steel industry. EU enlargement issues were also raised in the Federation of Hungarian Industrialists of which MVAE was member. All industry related legislation was introduced to the Federation. They would distribute information and opinions to the sectoral associations which would in turn put them forward to steel producing companies. After having received feedback from their members the Federation would make one single opinion and present it to the government and ministries'<sup>90</sup>.

The second route to exert political pressure was Eurofer. The association was an associated member of Eurofer: 'We had the impression our association did not have total access. We asked Eurofer to speak on our behalf. But, Eurofer only goes to the EC when a certain per cent of its members agree. It is a zero sum game'<sup>91</sup>.

Dunaferr, the country's largest producer, also would enter into direct contact with Hungarian state institutions. The company had a director of EU and integration issues. *Laszlo Toth*, chief executive of Dunaferr until 2001 was also President of the Association of the Hungarian Iron and Steel Industry. Mr. Toth had direct access to policy makers such as *Peter Balas*, Deputy State Secretary of the MoFA and *Marianna Csakvari*, Deputy State Secretary of the MoET<sup>92</sup>. Dunaferr's management, appointed in February 2001, had stronger links to the ministries. The new CEO, *Csaba Farago*, was president-CEO of state privatisation agency (APV) and accountable to the Hungarian parliament and government<sup>93</sup>.

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<sup>89</sup> Newswire: Economic ministry to set up steel imports monitoring system, in: *Economist Intelligence Unit*, 31/05/2002

<sup>90</sup> *Interview by Author with Representative of the Iron and Steel Institute*, Budapest, 04/02/2004.

<sup>91</sup> *Ibid.*

<sup>92</sup> Possible measures are considered to protect steel industry, in: *MTI-Econews*, 16/04/2001.

<sup>93</sup> Dunaferr anticipates HUF 3.3bn in losses this year, in: *MTI-Econews*, 13/04/2001.

Representatives of the association found EU enlargement a mixed blessing. On the one hand it would provide Hungarian basic iron and steel producers with permanent access to the European single market. On the other hand the steel industry in neighbouring countries (Czech Republic, Slovakia and Poland) was much stronger supported by a continuous flow of state aid. The Hungarian association asked for state aid and special quotas. The special quotas were meant as protection against steel imports from the CIS after EU membership. The Hungarian steel industry feared that after the national protection system would be disbanded its geographic proximity to the Ukraine and Russia would give rise to the full absorption of EU-CIS quota to the detriment of its domestic steel industry: 'The MoFA did not formally request a TA and Brussels said no in advance. The EC never contacted the association directly asking about the fate of the industry. The refusal was not directed against Hungary, it was a general rule. In Hungary the capacity and contribution to the economy was too low and the government and MoET were not really concerned'<sup>94</sup>.

#### **Metallurgical Chamber of Industry and Commerce (HIPH)**

The Metallurgical Chamber of Industry and Commerce (HIPH) in Poland, set up in 1991, associated 56 enterprises of which 30 manufacture basic iron and steel including steel processing. The other 26 members were suppliers or active in iron and steel commerce<sup>95</sup>. The chamber was the only organised representative of the steel sector in Poland. It represented the country's three largest steel mills, Huta Sendzimir, Huta Katowice and Huta Czesochowa covering over 80 per cent of total basic iron and steel production capacity.

The association prime contacts were with the MoE which would initiate safeguard measures following requests from the association. The HIPH had a direct channel to the government and individual ministers including at deputy level. The MoE held consultations with EU representatives in turn to represent the position of the country<sup>96</sup>. The MoE also held consultations directly with large individual companies<sup>97</sup>. Sometimes Polish companies would enter in direct negotiations with the EC on price settlements of certain steel products to fend off EU safeguard measures<sup>98</sup>.

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<sup>94</sup> Interview by Author with Representative of the Iron and Steel Institute, Budapest, 04/02/2004.

<sup>95</sup> See website: [www.hiph.com.pl/index\\_en.htm](http://www.hiph.com.pl/index_en.htm).

<sup>96</sup> EU to Impose Penal Duty on Polish Pipes?, in: *Gazeta Wyborcza* No. 253, p. 25, 29/10/1997.

<sup>97</sup> Ministry Takes Measures Against Sheet Metal Imports, in: *Prawo i Gospodarka* No. 142, p. 2, 07/07/1999.

<sup>98</sup> EU Imposes Duties on Polish Steel Cable Exporters, in: *Rzeczpospolita*, No. 193, p. B3, 19/08/1999

Like in neighbouring countries HIPH joined Eurofer following the associated membership of its three biggest steel producers in 1996 in part to help deflect dumping complaints from EU countries<sup>99</sup>. And like in neighbouring countries Eurofer's membership did not prevent EU initiating trade disputes.

#### **4.3.3.2. European Federation: Eurofer**

The most important European association representing national iron and steel federations and companies is the European Confederation of Iron and Steel Industries (Eurofer). It was founded in 1976 and located in Brussels. In 2000, mn 155 tonnes of crude steel were produced by its member companies representing 95 per cent of the total production in the EU-15. Eurofer dealt with all matters related to the basic iron and steel industry. It represented the common interests of its member's vis-à-vis third parties, notably the European institutions and other international organisations<sup>100</sup>.

When the EAs between the individual V-4 and the EU were concluded Eurofer extended its membership to the Central European steel industries. The Czech, Hungarian, Polish and Slovak largest steel producers became associate members in 1996. According to Eurofer the objective was to facilitate their adaptation to the conditions of a free market economy and to the competition rules of the EU steel market.

The objective was reinforced in the light of the accession of the V-4 to the EU. Eurofer acted primarily in the interests of EU-15 producers as a series of continuing complaints against some of its associated members from Central Europe demonstrates. These complaints usually resulted in trade restrictive measures. Eurofer also invited the Czech producers to agree to a minimum price arrangements. Other east European negotiators reported that representatives of Eurofer were 'in the room next door' throughout the crucial stages of the negotiations on east-west steel trade<sup>101</sup>.

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<sup>99</sup> Iron & Steel: Poland, in: *Economist Intelligence Unit*, 01/04/1996.

<sup>100</sup> See website <http://www.eurofer.org/home.htm>.

<sup>101</sup> Z. WANG and L.A. WINTERS, *EC imports from Eastern Europe: iron and steel*, London: EBRD, October 1993.p. 22; see also J. ROLLO and A. SMITH, *The Political Economy of Eastern European Trade with the European Community: Why So Sensitive?*, in: *Economic Policy*, April 1993, 16, pp. 139-81., p. 173-174.

The anti dumping measures in 2001 against Hungarian steel producers are a case in point. The EC started dumping procedures against Hungarian steel, i.e. steel from Dunaferr, as a result of a complaint submitted by Eurofer concerning hot-rolled coil steel. Hungarian steel maker Dunaferr along with the Hungarian Steel and Iron Industry Association expressed surprise that as associate members of Eurofer they were not officially informed of Eurofer's intention to initiate an anti-dumping case against Dunaferr. Another example concerned Eurofer filing complaints with the EC regarding hot-rolled coil from Slovakia without prior notice to its Slovak associated members<sup>102</sup>. This was also the case for Poland. In 1999, the Polish government agreed to impose a licence requirement on its steel exports to EU in order to avoid an imposition of anti-dumping duties on Polish steel exports. In consenting to have its steel exports licensed Poland bowed to the demand of Eurofer, which complained that Polish steel is exported to EU at dumping prices<sup>103</sup>.

In 2001 Eurofer clearly stated that ‘the restructuring of the steel industry in the candidate countries is an important element in their preparation for accession. The companies have to carry out the necessary adaptation to be able to withstand the competitive pressure of the internal market. Restructuring of the CEEC steel industry before accession is, therefore, vital. The accession of these countries to the EU with industries which have capacities unadapted to the market, with unresolved social, technical and environmental problems, with companies which are unviable and therefore reliant on state aid would have major consequences for the EU and risks seriously destabilising the steel market’<sup>104</sup>.

Eurofer also complained that, with the exception of Slovenia ‘no other candidate country has presented a plan which is acceptable, notably in terms of capacity reductions and the viability of companies. Of the six CEEC (Poland, Hungary, Czechia, Slovakia, Romania, Bulgaria) only three [Poland, Czechia and Hungary] have presented plans. All three are considered as unacceptable by the Commission since they will not lead to the viability of the

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<sup>102</sup> Eurofer complaint unjustified, Hungarian steel industry says, in: *MTI-Econews*, 23/11/2001.

<sup>103</sup> Poland-EU: Licences for Polish Steel Exports, in: *Gazeta Wyborcza* No. 30, p. 26; *Rzeczpospolita* No. 30, p. 11, 05/02/1999.

<sup>104</sup> Eurofer, *Enlargement of the European Union: Objectives as regards Steel Industry*, Brussels, March 2001.

industries'. It argued that 'two of the plans presented [Poland and Hungary] actually led to capacity increase'<sup>105</sup>.

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<sup>105</sup> Ibid.

**Table 16: Economic and Political Market Structure (1998-2002)**

country	firm	rank	pro- duction volume	emp- loy- ment	employ- ment share	ow- ner- ship	pri- vati- sation	production	orien- ta- tion	national mem- bership	international membership
Cz	NOVA HUT	1	90(1)	12549	35.03	LNM Holdings/ISPAT	2003	integrated (2)	export	HZ (3)	Eurofer (7)
Cz	VITKOVICE STEEL AS	2	90(1)	10000	27.91	state	state	integrated (2)	export	HZ (3)	Eurofer (7)
Cz	TRINECKE ZELEZARNY AS	3	90(1)	9451	26.38	US Moravia Steel	1995	integrated (2)	export	HZ (3)	Eurofer (7)
Cz	JAKL KARVINA	1	n.a.	n.a.	n.a.	ISPAT	2004		n.a.	HZ (3)	Eurofer
Cz	VALCOVNA ZA STUDENA	1	n.a.	n.a.	n.a.	ISPAT	2004		n.a.	HZ (3)	Eurofer
Cz	VALCOVNY PLECHU FRYDEK MISTEK	1	n.a.	n.a.	n.a.	ISPAT	2004		n.a.	HZ (3)	Eurofer
total		7	90	32000	89.32			integrated (2)	export		
Hu	DUNAFERR	1	85	9300	93	IUF/DUFERCO	2004	flat products	export	MVAE (4)	Eurofer (7)
total		1	85	9300	93			flat products	export		
Pl	HUTA KATOWICE (Dabrowa Gornicza) - PHS (2002)	1	70(1)	14500	36.08	LNM Holdings/ISPAT	2003	integrated (2)	dom/exp	HIPH (5)	Eurofer (7)
Pl	Huta SENDZIMIRA (Krakow) - PHS (2002)	2	70(1)	16000	39.81	LNM Holdings/ISPAT	2003	flat products	dom/exp	HIPH (5)	Eurofer (7)
Pl	HUTA FLORIAN - PHS (2002)	4	70(1)	n.a.	n.a.	LNM Holdings/ISPAT	2003	integrated (2)	dom/exp	HIPH (5)	Eurofer
Pl	Huta CEDLERA - PHS (2002)	3	70(1)	n.a.	n.a.	LNM Holdings/ISPAT	2003	integrated (2)	dom/exp	HIPH (5)	Eurofer
Pl	HUTA CZESTOCHWA	5	10	2509	6.24	IUF/DUFERCO	2004		n.a.	HIPH (5)	Eurofer (7)
Pl	HUTA ZAWIERCE	8	10	1248	3.11	CMC (US-Swiss)	2003		n.a.		
Pl	HUTA OSTROWIEC	6	5	3024	7.52	GRUPO CELSA	2003		n.a.	HIPH (5)	
Pl	HUTA WARSAWA	7	5-10	1744	4.34				n.a.		
total		9	100	39025	97.11			integrated	export		
Sk	VSZ INTEGRATED STEELWORKS KOSICE	1	92	20000	76.94	US Steel Corp	2000	flat products	export	HZ (3)/ZHTPG (6)	Eurofer (7)
total		1	92	20000	76.94			flat products	export		

Notes: Cz=Czech Republic, Hungary=Hu, Pl=Poland, Sk=Slovakia

(1) combined national production by volume

(2) majority of long products at 65-70 per cent of total production

(3) Magyar Vas- és Acélipari Egyesülés (MVAE) or Association of the Hungarian Steel Industry

(4) Hutnictví zezeza, a.s. or Steel Federation of the Czech and Slovak Republics

(5) Metallurgical Chamber of Industry and Commerce in Poland

(6) Association of Metallurgy, Mining Industry and Geology of the Slovak Republic

(7) associate member in 1996

Source: Own compilation

#### 4.3.4. Insider Status: Economic and political Strength

Economic strength is based upon relative economic measures throughout the region. A sector with a higher share of national GDP and total regional and national export earnings has more economic strength and is likely to be more successful at influencing decision making. Furthermore, the sector that has a higher share of total national and regional employment, particularly when it is regionally concentrated, is likely to have more political strength by sheer numbers of its employees.

**Table 17: Economic and Political Strength**

Country	share of value added	share of national export earnings	share of regional exports	share of national employment
Cz	0.0087590	6.043	35.09	0.7509
Hu	0.0023450	2.071	9.26	0.2088
Pl	0.0057440	4.511	27.10	0.2078
Sk	0.0015830	9.643	28.56	1.4000
Av.	0.0046078	5.567	25.00	0.6419

Note: Cz=Czech Republic, Hu=Hungary, Pl=Poland, Sk=Slovakia  
share of value added (at factor costs)= share value added basic iron and steel normalised by gross value added at factor costs  
Source: Eurostat (value added and employment), OECD (exports) averages 1998-2002

Table 17 shows that the Slovak Republic followed by the Czech Republic score highest on all economic and political measures. In absolute terms Poland has the largest industry, but comes third in relative terms. Hungary closes the table for the V-4.

A much more powerful reason for the industry to be a state insider is related to its state ownership. With exception of VSZ in Slovakia the industry was still in state hands (see Table 16). The steel industry in the Czech Republic, Hungary and Poland was making huge losses at the turn of the century, which were covered by the state budget. To that extent the authorities had an interest in finding a solution to the industry's problems. In the Czech Republic, Poland and Hungary public owners were worried about the impact of the industry on the budget. Only in Hungary were state authorities prepared to take the risk of cutting the industry's subsidies.

#### 4.4. Conclusion

This chapter evaluated four hypotheses on the economic and political behaviour of the basic iron and steel industry in the Czech Republic, Hungary, Poland and Slovakia in the EU enlargement process. It recognised that quota's and tariffs as well as NTBs and behind the border issues had similar effects on the industry in the V-4. However, it elicited different company behaviour.

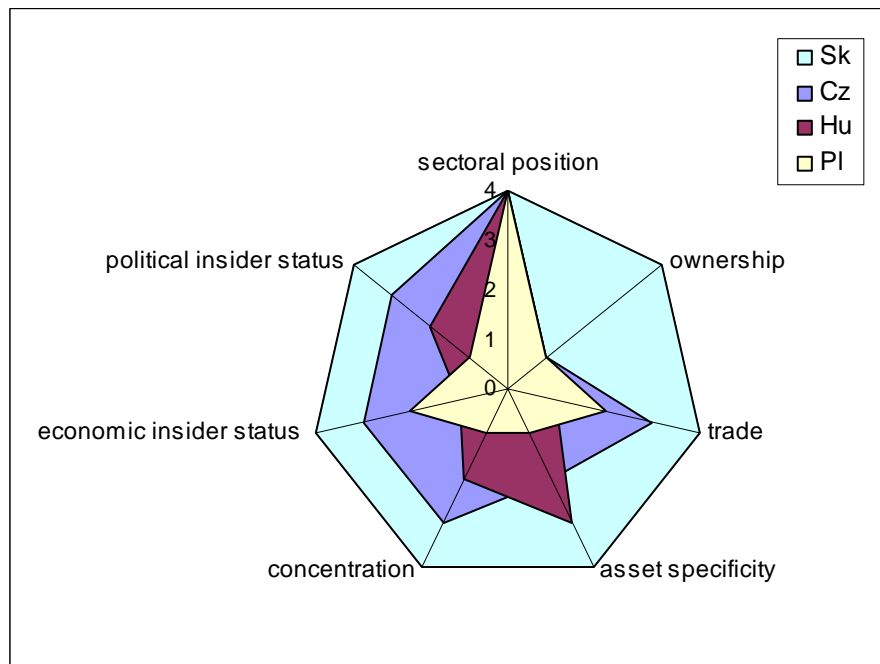
Ahead and upon EU entry V-4 steel producers were forced to restructure, reduce capacity and limit state aid in return for EU market access and eventual EU integration. Restructuring of the industry and trade was conditioned by the EAs. Restructuring was subject to EU approval. The combination of contingent protection and EU approval of restructuring plans was a catch-22 for the V-4 industries. It put off investors throughout the 1990s.

The difficult situation of the industry resulted in a clear cut case of preference formation and subsequent political mobilisation at the firm, associative and federative level with different intensity. Those industries still undergoing the transition process at the turn of the century (the Czech, Hungarian and Polish steel producers) carried less strong preferences about EU enlargement than those that were privatised (the Slovak industry). Czech, Hungarian and Polish steel producers lost valuable export markets. EU enlargement forced them into a regulatory framework for trade, restructuring and eventual privatisation.

On the whole, the industry stood to lose from EU enlargement because of regulatory limitations on restructuring plans, capacity and output, trade and state aid. The Slovak industry was the most highly asset specific in the sector. Hence it stood to lose most. It held the strongest preferences about EU enlargement.



**Figure 25: Sectoral Comparison of the V-4 Basic Iron and Steel Industry**



Note: Cz=Czech Republic, Hu=Hungary, Pl=Poland, Sk=Slovakia  
 Source: Own compilation, based on table 23 (see Conclusion Part II)

The Slovak steel maker, VSZ, was the first to privatise. It maintained or increased its exports markets of higher value added produce. It was the only company in the region investing in new products and sustaining R&D activity. Privatisation had given it an international outlook. In the privatisation process its new owner, US Steel, secured a tax holiday for ten years. It subsequently overshot its EU agreed quota ahead of EU entry. In the run up to EU enlargement the EC and EU member states questioned the privatisation deal and the export quota the industry was maintaining. US steel Kosice was instructed to give up its tax holiday, pay back tax arrears retroactively and apply the EU's steel quota ahead of EU membership. US Steel Kosice refused.

Political assets were well developed in the industry and allowed for regular political mobilisation. The presence of national tariffs, anti-dumping measures and quotas throughout the 1990s and early 2010s in all V-4 countries demonstrate the political mobilisation of the industry. The sector was highly concentrated in each country with only a number of firms accounting for the bulk of production. One national association represented each national sector with the exception of the Slovak industry, which was associated both in the Czech and Slovak Republics. The associations functioned as information providers for the ministries. They lobbied regularly on behalf of their

members achieving effective policy changes. It meant that all steel companies could easily overcome collective action problems. The data indicate that this was easier in Slovakia and Hungary relative to the Czech Republic and Poland.

All national associations became member of their European counterparts, Eurofer, in the wake of the associative membership of the largest of their member companies. Nevertheless, membership of Eurofer did not bring substantial benefits as the association continued to file complaints against V-4 countries producers including its associated member companies.

In fact, Eurofer had made clear as early as 1991 that it would take a tough stance on the application of EU legislation for Central European steel makers. It continued to influence EU steel policy including for EU enlargement. The shadow of the Eurofer's lobbyists can be seen behind some of the EU's strict interpretations of the *acquis*. All applicant countries received a sharp reminder that their negotiating position on competition should include details of its steel restructuring plan, which was supposed to be completed and agreed by tight deadlines. Many EU ministers were under heavy pressure from their own national steel industries, which had already undergone painful restructuring, to make sure the V-4 stopped supporting their large, ailing and cheaper steel sectors.

This did not stop the Polish and Czech Steel makers from mobilising politically and putting pressure on their respective authorities to request grace periods. The TPRs were designed to allow additional state aid at least until 2006. They also included exemptions from the environmental *acquis*. Equally, the Hungarian Steel industry requested intra-EU protection against cheaper steel imports from further East because of its geographic proximity. The more specific and already consolidated Slovak industry requested a 10 year grace period on taxation. It argued against the EU output and quota limitations.

## **CHAPTER 5: INTERNATIONAL ROAD FREIGHT INDUSTRY**

This chapter considers the economic issues affecting the international road freight industry in the V-4 when integrating with the EU. It describes the concerns and opportunities of road haulers in the context of EU enlargement with a brief historical overview of the regional and national road transport sector in Central Europe. The chapter then moves on applying the theory on factor and asset specificity assessing four hypotheses specifying the industries' trade in international transport services, its factor and asset specificity, national cohesion and concentration as well as its insider status in the policy process. The focus is on the period 1992-2004 treating the period of the enlargement negotiations (1998-2002) in greatest detail.

Because of limited data availability before 2002 the chapter attempts to indicate a trend of the sector's evolution<sup>1</sup>. The chapter demonstrates that the industry in Central Europe was confronted by similar economic issues, however, national sectoral characteristics differed – with Czech, Polish and Slovak truckers at one end and the Hungarian road freighters at the other extreme – including policy which resulted in a variation of political mobilisation.

### **5.1. The Industry's Concern: Competitiveness and Market Access**

#### **5.1.1. The Sector in the EU**

Between 1992 and 1998 the EU decided to progressively liberalise its international road transport market. Liberalisation contributed to the rising dominance of road transport within the EU's inland freight transport sector as well as between member states. Between 1990 and 1998 the volume of international road goods transport in the EU increased by nearly 40 per cent while international rail goods and inland waterways transport rose by just 17 and 12 per cent respectively<sup>2</sup>.

Cabotage – road transport within one EU member state carried out by a non-residential haulier – was fully liberalised from mid-1998. While cabotage represented 0.67 per cent (2000) of the total EU-15 freight transport it grew more rapidly at an annual rate of 15 to 16 per cent. Together with

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<sup>1</sup> Data availability for the road haulage sector before 2002 is limited particularly for Poland, Hungary and Slovakia with the notable exception of the Czech Republic.

<sup>2</sup> Eurostat, Theme 7 Transport, *Highlights of the Panorama of transport 1970-1999*, Luxembourg, 2002., p. 3-4.

cross trade – third country road transport between two EU member states – representing just under 3 per cent of total EU-15 freight transport (2000) cabotage became of considerable importance to road haulage companies, particularly in some smaller EU member states<sup>3</sup>. The liberalisation of international road haulage dramatically encouraged competition between EU-15 international haulers and profit margins were progressively under pressure<sup>4</sup>.

To ensure a level playing field for EU-wide competition, including access to the profession, social, safety and environmental standards, a series of legislative initiatives had accompanied the liberalisation of international trade in road transport. While the liberalisation was preceded by a long and protracted negotiation rounds in the 1980s and 1990s the industry revealed divergent patterns among EU road haulage operators. A report published by the *International Road Transport Union* (IRU) recorded substantial divergence in the cost base of EU operators and the implementation of legislation within the EU-15<sup>5</sup>. The highly international character of the industry contributed to the fast transmission of these market diversity effects.

In the EU enlargement process the international road freight transport industry was identified as a risk sector. It was expected to endure painful competition<sup>6</sup>. EU-15 operators were concerned that by 2004 the EU's international road transport market would see 155,867 enterprises employing just under 400,000 drivers added to the existing fleet. EU road freight operators were afraid of the level of competitiveness and comparative advantage from their Central European colleagues. Operational costs of road goods transport by operators from most candidate countries were significantly below the EU average. According to the IRU wages of road hauliers in the EU were five times the average of the Central European truckers. The existing cost differentials were anticipated as damaging and disruptive in the case of a sudden opening of national markets, particularly for cabotage<sup>7</sup>.

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<sup>3</sup> Eurostat, *Statistics in Focus: Road Freight Cabotage (1999-2001)*, Luxembourg, 2003., p. 2.

<sup>4</sup> International Road Transport Union (IRU), *Road Transport and EU Enlargement: Main Problem Areas in the Pre-Accession Period and Progress Made (Progress Report Nr. 3)* Spring 2002, pp. 116., p. 8; The ECMT, *Social Dumping in the ECMT Area: The Road Freight Haulage Case*, Bucharest, 22/04/2002, pp. 13.

<sup>5</sup> International Road Transport Union (IRU), *Road Transport and EU Enlargement: Main Problem Areas in the Pre-Accession Period and Progress Made (Progress Report Nr. 3)* Spring 2002, pp. 116., p. 14.

<sup>6</sup> Ministry of Transport and Communications Finland, *Differences in taxation on heavy goods vehicles in Europe*, Helsinki, 2004, pp. 113., p. 16.

<sup>7</sup> Enlargement: Commission proposes to delay access to national markets of Member States in the road Haulage sector after accession, in: *Euractiv*, Brussels: 08/11/2001.

EU operators wanted strict application of EU legislation in the area of international road transport to ensure a level playing field for competition in the enlarged EU. EU Legislation was believed to contribute to convergence of the cost base of the V-4 and EU-15 road haulage operators. It would alleviate the most pressing competitive concerns of the industry<sup>8</sup>. EU-15 road haulers also proposed restrictive market access for the V-4 operators in the field of cabotage. They argued that liberalising cabotage would change the business environment of the road haulage sector. Competition would become unsustainable for many EU-15 international and domestic road freight operators<sup>9</sup>.

Limiting the market access for Central European haulers after EU enlargement through the request for TPRs would prevent the big bang effect of opening the cabotage market. Finally, EU-15 road haulers were proponents of a proper market monitoring mechanism with a view to supplying both the industry and the policy decision-makers with relevant economic information. The mechanism would prevent market crises after EU enlargement.

The demand for TPRs in international road haulage was driven in particular by German and Austrian road lobbies. They feared to be the first to bear the brunt of liberalised competition in road haulage because of past trends, their geographic proximity and the effect it would have on the industry in the border regions<sup>10</sup>. Operators from smaller EU member states were concerned about the effect of liberalised cabotage on their domestic and neighbouring markets and shared the reservations of their Austrian and German colleagues. Also the EC *White Paper on the Common Transport Policy* stated that price competition in the road haulage sector could be

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<sup>8</sup> Deutsche Bank Research, *Effects of the EU's eastern enlargement on the European transport market*, Frankfurt am Main, January 2003, pp. 19-24., p. 23-24.

<sup>9</sup> Ministry of Transport and Communications Finland, *Differences in taxation on heavy goods vehicles in Europe*, Helsinki, 2004, pp. 113., p. 19; For instance figures from Germany indicated that the bankruptcy rate in the road transport sector and road transport-related sectors was several times higher than in the economy as a whole, see: BAG, *Marktbeobachtung Guterverkehr*, Cologne, Herbst 2001, pp. 36.

<sup>10</sup> The cost advantages of Polish operators were estimated at around 15 to 20 per cent. German operators expected an enhanced market presence of their Polish colleagues after Poland's entry to the EU, in: Bundesamt Fur Guterverkehr *Marktbeobachtung Guterverkehr: Sonderbericht zum deutsch-polnischen Guterverkehr*, Cologne, 2001c.; The Austrian Federal Chamber of Labour (AK), a trade union organisation, laid out its conditions for accession countries in the field of transport: (a) Full application of social provisions in accession countries was a prerequisite for market access and freedom to provide services; (b) cabotage could not be applied automatically and requested quota with every accession country over a period of four years to be increased by 30 per cent each year; After a final check (c) road haulage operators could only be admitted after at least three years after accession and fulfilment of the criteria for admission to the occupation was to be ensured; (d) a new transit agreement based on a combination of charging of and quantitative restrictions for heavy goods vehicles to reduce environmental pollution, in: Austrian Federal Chamber releases position paper on transport and enlargement, in: *EurActiv*, London: 12/03/2002. ; See also EC, *Regular Report from the European Commission on the Czech Republic's, Hungary's, Poland's and the Slovak Republic's Progress towards Accession*, Brussels, 1998-2002.

further exacerbated as a result of the entry of the candidate countries. The paper contended that EU operators might suffer a loss of market share to operators from candidate countries. These trends would be strengthened provided the road haulage market was fully opened to candidate countries<sup>11</sup>.

### **5.1.2. The Sector in the Applicant States**

In contrast, road transport enterprises in the V-4 were generally positive about EU membership. They had built up a strong market position in east-west trade from the mid 1990s onwards. This was due to their strong competitive position and comparative advantage related to lower operating costs and a high entry of new firms. By 1998 Central European hauliers had captured more than 80 percent of the total east-west road haulage volume.

EU enlargement represented an opportunity. It would do away with the secretive bilateral license agreements and multilateral quotas that had limited the sectors international expansion since the early 1990s. It would provide Central European hauliers with full access to the EU's liberalised road transport market. As far as Czech, Polish and Slovak drivers were concerned EU enlargement symbolised a substantial gain. Despite additional cost related to the harmonisation of V-4 legislation to EU standards they expected to maintain or improve their competitive position and comparative advantage in east-west trade after EU membership<sup>12</sup>.

Ahead of EU enlargement many competition issues in the east-west road freight transport sector arose in an international context because of severe limitations on market access in EU countries. V-4 hauliers were conscience that limited access to the enlarged single European market in road transport would limit their expansion. The only possibility outside the enlargement framework to safeguard and improve their position was to increase the number of permits for international road transport operations from individual EU member states; as well as increased bilateral quotas for cabotage<sup>13</sup>. Therefore, EU accession of the V-4 hauliers offered the prospect for substantial change in their road transport market provided they were granted similar legal opportunities as

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<sup>11</sup> European Commission, *White Paper: European transport policy for 2010: time to decide*, Brussels, November 2001, pp. 124., pp 93-94.

<sup>12</sup> *Interview by Author with Representative of CESMAD BOHEMIA Association of Road Enterprises & Passenger Transport*, Prague, 03/05/2004.

<sup>13</sup> CZ in bilateral road transport talks with D to unlock enlargement negotiations, in: *Uniting Europe* 18/02/2002a.

the EU-15. V-4 haulers clearly stood to win from the process. Any limitation imposed on V-4 road haulers for access to the EU market would have adverse consequences on anticipated gains for the entire road freight sector<sup>14</sup>.

CEECs operators were concerned with the opening of their market of international services to the fleets of neighbouring applicant states. The cost base among the candidate countries differed markedly. Czech, Slovak, Polish and Hungarian haulers would enter each others markets after EU membership with similar or even better competitive characteristics and comparative advantages. Their market concerns were remarkably similar to those of their EU-15 counterparts and directed to other candidate countries. This was particularly the case for Hungary which would see its market of international trucking services fully opened to the fleets of 24 countries practically overnight. Hungarian haulers feared the full market entry of neighbouring haulers from the Czech Republic, Poland and Slovakia with better competitive characteristics and comparative advantages compared to their own operators<sup>15</sup>.

Under the prospect of EU membership the competitive Central European road haulers would have full access to the EUs liberalised road transport market. They expected to increase their market share. In contrast EU-15 haulers would face competition from Central European countries which already dominated east-west road transport traffic. Under full sectoral EU membership without any TA a significant repositioning of industrial players in the EU-15 transport market would be likely to take place.

## **5.2. Historical Overview**

### **5.2.1. 1945-1989**

Under Communism transport by rail dominated over road transport. The expansion and safeguarding of the railways, which were largely oriented towards the east, remained a primary transport policy objective under Communist state planning. Within road transport, road freight enterprises were publicly owned and dominated both domestic and international transport. Foreign firms were prohibited from operating. International road transport was further regulated

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<sup>14</sup> D. PARKER, The Road Freight Sector in the Czech Republic in: OECD, *Background Report on Regulatory Reform in Electricity, Gas, Road and Rail Freight*, Paris: OECD, 2001, pp. 68, pp. 40-52., p. 41.

<sup>15</sup> *Interview by Author with Representative of the Hungarian Ministry of Economy and Transport*, Budapest, 10/02/2004.; *Interview by Author with Representative of Slovak Ministry of Transport*, Bratislava, 02/03/2004.

by restrictive bilateral and multilateral agreements. Nevertheless, in all Central European Communist countries road freight transport increased its share in the total volume of goods transported between 1945 and 1989.

The road transport industry was nationalised following the Communist takeover in the Czechoslovak Federation. 11 large state enterprises or *public road transports (CSADs)* controlled road transport. The so called *works road transport* entities formed the second tier of road transport provision. They were road transport units part of larger enterprises for which they provided necessary transport services. They carried out approximately 80 to 85 per cent of Czechoslovak road transport. So-called *minor socialist enterprises or co-operatives* formed the third and smallest category of road transport provision and accounted for 5 to 10 per cent of the national fleet<sup>16</sup>. Between 1970 and 1989 works road transport tripled their volume from tonnes 297 mn to 929 mn with the tonnage rising particularly fast after 1984 when a first liberalisation had been approved. By the end of the 1980s an estimated 80 per cent of the total volume of Czechoslovak transport was carried by road.

From the late 1960s onwards two large state owned road transport companies, i.e. *Hungarocamion* and the *Volan companies*, shared the Hungarian road haulage market. The international road haulage monopoly was reserved for *Hungarocamion*. It had an operating fleet of about 1,500 trucks and international representation with subsidiaries throughout Europe<sup>17</sup>. The *Volan companies* focussed on the domestic market<sup>18</sup>. After the first transport liberalisation in the early 1980s, the *Volan companies* entered the international market on routes with limited competition for *Hungarocamion*. In 1988 the Hungarian international road transport market was liberalised ending the duopolistic road freight market<sup>19</sup>. Several more Hungarian companies entered the haulage market<sup>20</sup>. New regulations allowed unlimited entry and the number of road

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<sup>16</sup> J. OPLETAL and RYBA, *Privatisation and Regulation of Road Freight Transport: 1st Part: Privatisation and Deregulation of Road Freight Transport: Lessons Learnt, Mistakes Made: Case Study: Czech Republic, ECMT Seminar*. Paris, 1996., p. 2-3.

<sup>17</sup> É. MOLNAR, *Privatisation and Regulation of Road Freight Transport: 1st Part: Privatisation and Deregulation of Road Freight Transport: Lessons Learnt, Mistakes Made: Case Study: Hungary, Ibid.*, 15.

<sup>18</sup> Prior to 1988, road haulage was regulated mainly by the Civil Code of 1956 and by government decrees of 1981. International road transport was initially regulated only by international agreements. The UN multilateral agreements (for example CMR, ADR, and ATP) were enacted in Hungarian legislation.

<sup>19</sup> Parliamentary Law No. 1. of 1988 and its enactment as the 89/1988 (XII.20) government decree.

<sup>20</sup> É. MOLNAR, *Privatisation and Regulation of Road Freight Transport: 1st Part: Privatisation and Deregulation of Road Freight Transport: Lessons Learnt, Mistakes Made: Case Study: Hungary, ECMT Seminar*. Paris, 1996., p. 3.



transport companies rapidly increased. Their limit for international expansion was the shortage in international bilateral, transit and third country permits.

In Poland road transport was restricted to short distances of less than 100 km and parcels traffic. Large state owned firms dominated the road transport market. PKS (*Panstwowa Komunikacja Samochodowa* or *National Road Transport*) as the largest state-owned road transport enterprise dominated the sector. After 1981 PKS fragmented under the influence of a growing number of smaller companies in the road sector<sup>21</sup>. Road haulage co-operatives set up to transport agricultural produce formed a second category in the sector. A third category of road freight transport was the sector-based transport service companies. Road haulage was gradually liberalised between 1970 and 1988 with an increase in private sector participation. Road transport grew rapidly. The number of private firms rose from an estimated 911 private owners and 6,261 employees in 1970 to 62,262 firms in 1990. The public road transport sector accounted for 97 per cent of total employment in the sector in 1970. This figure declined to 87.1 per cent in 1988 with the biggest change in favour of the private road transport occurring from 1984 onwards<sup>22</sup>.

### **5.2.2. Transition and Consolidation (1989-2004)**

Between 1989 and 1995 the transition process in the road transport sector broke down the state-monopolies and ‘oligopolistic’ structures. It enhanced competition, lowered prices and increased the variety of services boosting the total share of road transport in the total transport volume. However, it resulted in an excessively fragmented sector with a record number of transportation firms with lower average employment level.

At the outset of the transition process total freight carried by all land modes fell about 40 per cent<sup>23</sup>. As the economy recovered road haulage increased its relative share of total land transport, particularly at the expense of the railway sector<sup>24</sup>. Liberalisation and privatisation in the road transport sector in the V-4 followed different routes. Generally, the sector was among the first in the economy to disintegrate, privatise and adapt to the new market forces. Spontaneous

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<sup>21</sup> J. BURNEWICZ, *Privatisation and Regulation of Road Freight Transport: 1st Part: Privatisation and Deregulation of Road Freight Transport: Lessons Learnt, Mistakes Made: Case Study: Poland* Ibid., pp 10-11.

<sup>22</sup> Ibid., p. 5.

<sup>23</sup> D. PARKER, *The Road Freight Sector in the Czech Republic in: OECD, Background Report on Regulatory Reform in Electricity, Gas, Road and Rail Freight*, Paris: OECD, 2001, pp. 68, pp. 40-52., nr. 120.

<sup>24</sup> Ibid.in, pp., 42.

privatisation played a substantial part in the changeover ahead of or simultaneous with official privatisation programmes.

Simultaneously the sector fully deregulated. Barriers preventing access to the profession were eliminated. New private actors entered the sector en masse<sup>25</sup>. It resulted in the creation of 41,779 goods enterprises with as many as 350,121 employees by the end of 1993 when the worst years for the road freight transport sector were over.

The industry became dominated by small firms with on average less than five vehicles. The sector continued to grow and the number of enterprises selling road freight transport services tripled over the next decade reaching 155,867 enterprises with almost 400,000 employees. Competition increased and profits tapered. The spontaneous nature of the process accompanied by the deregulation of the sector led to overcapacity<sup>26</sup>. By the mid 1990s, 80 per cent of the road freight transport industry was in private hands with little or almost no foreign investment. From 1995 onwards the sector consolidated and road transport activity picked up dramatically.

#### **5.2.2.1. Czech and Slovak Trucking services**

After 1989 the state owned public road transport (CSADs) and the works transport units rapidly disintegrated under pressure of spontaneous privatisation rubber stamped by legislative changes.

In 1991 during the so called first round of privatisation the sector began its most profound changeover. As many as 70 out of the total of 80 CSADs had transferred into private hands. The change for the works transport was even more far-reaching. Some units disappeared entirely together with the transformation of their parent companies. After just five years government participation was residual. By 1995 more than 90 per cent of the sector had been passed on to private owners and a new privatised sector had emerged. Simultaneously the government liberalised price controls<sup>27</sup>. Road transport was organised and regulated by the Ministry of Transport and Communications (MoTC). The MoTC set no numerical limits on the number of

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<sup>25</sup> W. RYDZKOWSKI, Privatisation and Regulation of Road Freight Transport: Conclusion, *ECMT Seminar*. Paris, 1996., p. 5.

<sup>26</sup> *Ibid.*, p. 5.

<sup>27</sup> Act no. 455/1991 Coll or Zivnostensky zakon. An enterprise is regarded as having Czech origin and thus has access to the Czech market if it is registered in the Czech Republic. No checks on the level of shares owned by foreigners existed, in: D. PARKER, The Road Freight Sector in the Czech Republic in: OECD, *Background Report on Regulatory Reform in Electricity, Gas, Road and Rail Freight*, Paris: OECD, 2001, pp. 68, pp. 40-52., p. 44.

licences issued in total or to any individual carrier. Neither did the authorities attempt to match demand and supply in the industry by the use of licensing. Much of the excess capacity moved into international road haulage.

Soon the sector was awash with small road transport firms. Approximately 61 per cent of the road freight enterprises had only one vehicle. Circa 30.5 per cent had between 2-5 vehicles. There were just 110 firms (0.3 per cent of the total fleet) with more than 50 trucks<sup>28</sup>. Previous drivers for the CSADs and works transport bought vehicles and set up small private road freight transport companies on the basis of bank loans. Only about 20 companies out of a total of 32,715 received foreign investment and predominantly engaged in international transport<sup>29</sup>. The entry into the road transport sector of so many new firms gave way to increased competition with prices falling significantly. The Czech international road transport industry supplied as much as 53 per cent of total road transport in the country compared to an EU average of 19 per cent<sup>30</sup>.

In contrast to domestic transport international road freight transport remained highly restrictive. Entry was regulated by a web of bilateral and multilateral agreements. This restricted quantity and capacity in various ways. Under these agreements, domestic haulage markets of most neighbouring countries including those of the EU-15 remained protected. Cabotage was forbidden. In total the MoTC exchanged more than 60 different kinds of permits with European and Asian states. By the end of the 1990s the MoTC had about 375,000 single permits for international transport which it distributed to international road operators.

Authorities described the industry as being in a state of crisis at the end of the 1990s. An economic downturn (1997-1998) compounded by severe restraints on international business limited the opportunities for the industry to adjust by shifting supply to export markets. The Czech MoTC and the industry's association, *CESMAD*, expected that Czech road haulage overcapacity would cause difficulties in the EU accession negotiations. They anticipated the EU

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<sup>28</sup> Good transport data is only available from 1994 onwards due to the break up of Czechoslovakia and a change of methodology in 1994.

<sup>29</sup> J. OPLETAL and RYBA, *Privatisation and Regulation of Road Freight Transport: 1st Part: Privatisation and Deregulation of Road Freight Transport: Lessons Learnt, Mistakes Made: Case Study: Czech Republic, ECMT Seminar*. Paris, 1996., p. 6-12.

<sup>30</sup> D. PARKER, *The Road Freight Sector in the Czech Republic in: OECD, Background Report on Regulatory Reform in Electricity, Gas, Road and Rail Freight*, Paris: OECD, 2001, pp. 68, pp. 40-52., p 44.

to reduce the degree or slow the pace of full entry of Czech trucks into European single market<sup>31</sup>. In anticipation Czech authorities tightened the requirement to demonstrate financial competence and approximated its law with the *acquis*.

Of all V-4 the Czech Republic had the most advanced road freight transport market by 1993s. It had over 32,769 total number of road transport firms that employed as much as 110,297 people. By 2003 this number had almost doubled to 55,475 enterprises while the number of workers in the sector had increased by half to 144,107 employees.

The evolution of the Slovak Road haulage market was similar to that of the Czech Republic after 1993. The domestic market was completely liberalised resulting in large-scale entry of new operators and vehicles. Transport capacity of Slovak haulers exceeded demand of transport services. As a result Slovak road transport operators were seeking to offer services on the international market. This possibility was restricted because of the qualitative limitations on international transport permits<sup>32</sup>. In 1995 Slovakia had 405 road transport firms employing 19,594 people rising to 9,861 enterprises employing 21,418 people in 2003.

#### **5.2.2.2. Hungarian Trucking Services**

In Hungary the liberalisation and deregulation of the sector had already begun in the 1980s. A 1988 landmark regulation introduced effective competition. Between 1990 and 1994 the number of road freight companies in Hungary increased by 130 per cent with about 80 to 90 per cent of the total consisted of small firms. Medium sized firms grew slowly. The number of big transport companies decreased. The structural changes lead to an overall decrease in employment. In 1994 approximately 2555 road transport firms were operating in the sector employing 38,142 people<sup>33</sup>.

The number of international road transport companies rapidly increased. The shortage of bilateral and multilateral, transit and third country permits was the only limit preventing further expansion. In 1995 the government introduced qualitative conditions for market access in the domestic road freight market. Hungary was the first to introduce the obligation for an operating

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<sup>31</sup> *Interview by Author with Representative of CESMAD BOHEMIA Association of Road Enterprises & Passenger Transport, Prague, 03/05/2004.*

<sup>32</sup> International Road Transport Union, *Slovak Republic: Road Transport Fact File*, Geneva, March 2003b, pp. 7.

<sup>33</sup> É. MOLNAR, *Privatisation and Regulation of Road Freight Transport: 1st Part: Privatisation and Deregulation of Road Freight Transport: Lessons Learnt, Mistakes Made: Case Study: Hungary, ECMT Seminar*. Paris, 1996., p. 4, p. 27; see also annex 1 pp. 36-42.

license in the domestic market. A new government decree also changed the principles for granting an operation license for international road haulage. The market share between Hungarian and foreign firms between 1991 and 1994 changed in favour of foreign trucks from 36 per cent of total rising to 43 per cent. Hungarian haulers faced growing competition in the Hungarian market from foreign haulers.

As the private road haulage sector boomed the state owned transport companies, the Volan Companies and Hungarocamion, were in decline. Volan Companies' fleet was outdated and its road haulage activities unprofitable. In 1993, Volan enterprises, then called *Volan Tefu*, took part in the first privatisation programme. The company failed to find a suitable buyer on a number of occasions. The company had Ft 1.5 bn in debt and generated losses of Ft 500 mn annually. Under pressure from changing market conditions and a deteriorating performance the enterprise was privatised in 1994.

By 1997 just 44 road transport enterprises remained in state hands including the market leader Hungarocamion<sup>34</sup>. Hungarocamion's remained one of the largest Hungarian trucking companies. Its business was in rapid decline. A number of attempts to privatise the firm failed. In 1998 the company was still in state hands. Prolonged underinvestment left its vehicle fleet in danger of becoming obsolete. Obtaining international transport licences became increasingly difficult. With a commitment to modernise and restructure the business a capital group, *DBG* and *BA Capital Partners*, secured 88 per cent of the equity in 1998 through a management buy-in. In 2002 the enterprise was sold to Volan Tefu, Hungary's second largest road haulage operator<sup>35</sup>. The scale and market power resulting from the merger made it the largest Hungarian international transport operator in the country and Central Europe.

Since 1989 the Hungarian transport market had witnessed drastic changes. In 1989, 290 Hungarian road transport firms were operating employing as many as 99,464 people. The number of firms rose steadily to 1395 firms in 1993 with 64,153 employees. By 2003 the total number of firms reached 5,566 enterprises while employment had declined halved to 31,243 drivers.

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<sup>34</sup> 86 per cent of the industry was private by the end of 1997.

<sup>35</sup> European Private Equity and Venture Capital Association, *Central and Eastern Europe Success stories: MBI creates Central and Eastern European transportation market leader*, Luxembourg, October 2004, pp. 76., pp. 44-46.

### 5.2.2.3. Polish Trucking Services

In Poland the act on economic activity of 1989 was a major break-through in the deregulation of the transport market. For domestic transport a mere registration with a public administration office sufficed to start a private transport business. Operators were free to provide any type of freight service. Operating licences were only required for international transport services.

The road transport sector became one of the most advanced sectors in the process of privatisation in Poland. By 1994, 84.4 per cent of the total volume was carried by private operators<sup>36</sup>. De-monopolisation of the market, free access and the development of new companies cleared the way for free competition. The number of companies operating in international transport rose from circa 8,500 in the early 1980s to 82,342 private undertakings with a total workforce of circa 83,400. The number of lorries rose from 617,800 to 964,900 between 1980 and 1994 with a 43 per cent increase from 1990 onwards<sup>37</sup>.

The restructuring and privatisation of existing transport enterprises was difficult due to the poor financial state of most large firms, worker opposition, lack of capital, and resistance to privatisation. The most significant obstacle to privatisation, however, was the lack of domestic investment. Uncertainties surrounding the sector combined with low profit margins made the sector unattractive to foreign capital<sup>38</sup>.

The largest state-owned road transport company, PKS, was split into 234 smaller firms of which 142 provided both passenger and freight services, 25 operated exclusively passenger services and 67 operated freight, ancillary and forwarding services. The first two groups of firms reported to the MoT while third resided under the authority of the regions (województwo). Restructuring involved selling off vehicles, liquidation of unnecessary subsidiaries and divisions and the leasing of assets to private operators. On the whole only a few state owned transport firms were privatised before 1994.

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<sup>36</sup> J. BURNEWICZ, *Privatisation and Regulation of Road Freight Transport: 1st Part: Privatisation and Deregulation of Road Freight Transport: Lessons Learnt, Mistakes Made: Case Study: Poland ECMT Seminar*. Paris, 1996., p. 32.

<sup>37</sup> *Ibid.*, p. 22-23, p. 27.

<sup>38</sup> W. RYDZKOWSKI, *Privatisation and Regulation of Road Freight Transport: Conclusion*, *Ibid.*, p. 5.

By 1994 a new transport policy encouraged the creation of small enterprises believing that greater competition was required. For the large PKS road transport enterprises the policy was geared towards privatisation on a case-by-case basis. As a result, the road sector became highly dispersed in the second half of the 1990s. Competition became fierce and average profitability declined<sup>39</sup>.

While the domestic market was fully liberalised the international market remained partially closed. Annual quotas were fixed in bilateral negotiations on reciprocal terms. To stem the flow of domestic road haulers into the international market, Parliament re-introduced licenses for international road carriages and laid down conditions for foreign carriers entering Poland in 1991.

Since 1989 the Polish transport market had witnessed drastic changes. Poland counted 268 road transport enterprises in 1989 employing as many as 266,400 people. The number of firms increased rapidly to 1,574 firms and while employment declined to 138,992 people in 1993. From 1993 onwards the number of firms would rise dramatically to 84,965 enterprises employing just under 200,000 labourers in 2003.

### **5.3. Characteristics and Preferences: A Sunrise Industry**

#### **5.3.1. Trade**

##### **5.3.1.1. European Trade in Trucking Services (1992-2004)**

The volume of freight transport in European countries doubled after 1975 with a tripling of road haulage which accounted for close to 90 per cent of total freight transport in Europe at the end of the 1990s. Despite these trends, trade in trucking services between 1992 and 2004 in Europe was far from free. It was heavily regulated on a national and international level including for the Czech, Hungarian, Polish and Slovak road haulers.

Regulatory intervention in the road haulage industry has been inspired by the need to limit the competitive threat of road haulage to state run railways, the negative externalities of the sector, such as on the environment, and fear of market instability induced by strong competition. Market intervention limited entry, restricted quantity and type of services that could be provided. The

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<sup>39</sup> *Interview by Author with Representative of the Association of the International Road Transport Operators Poland (ZMPD), Warsaw, 23/04/2004.*

predominant impediment to international competition was the presence of a restrictive patchwork of multilateral and bilateral agreements which usually discriminated against foreign hauliers<sup>40</sup>.

The first step towards liberalisation for international transport was achieved in 1974. Under the auspices of the OECD, the *European Conference of Ministers of Transport* (ECMT) set up a system of multilateral licences for non-cabotage haulage between its 40 member states. A quota system allocated licences between countries according to their relative importance in terms of GDP and road freight traffic. The ECMT distributed around 10,000 permits annually among member Transport Ministers<sup>41</sup>. In 1998 this figure had risen only slightly to 10,970 licences<sup>42</sup>.

All former Communist countries of the V-4 were member of the ECMT receiving an annual multilateral quota (see Table 18) with Poland being assigned the highest category followed by the Czech Republic, Hungary and Slovakia respectively. ECMT data show that the Czech road haulage industry was by far the largest relative to the size of its economy and population. It was also the only country of the V-4 in which domestic haulers had more international than domestic business<sup>43</sup>.

**Table 18: ECMT Multilateral Licence Indicators (1998)**

country	goods traffic in bn tonnes- of km	ECMT rank by bn tonnes- of km	ECMT rank by number of licenses
Czech Republic	22.66	14	7
Hungary	13.01	19	7
Poland	45.36	9	5
Slovakia	5.87	29	9

Source: ECMT, Road Transport Multilateral Quota, Copenhagen, 1998.

<sup>40</sup> O. BOYLAUD and G. NICOLETTI, Regulatory Reform in Road Freight, in: *OECD Economic Studies*, 2001, 32(I), pp. 229-51., p. 234-235.

<sup>41</sup> See ECMT website: [www.cemt.org](http://www.cemt.org)

<sup>42</sup> See ECMT agreements on trucking (Box 7), in: D. PARKER, The Road Freight Sector in the Czech Republic in: OECD, *Background Report on Regulatory Reform in Electricity, Gas, Road and Rail Freight*, Paris: OECD, 2001, pp. 68, pp. 40-52.

<sup>43</sup> O. BOYLAUD and G. NICOLETTI, Regulatory Reform in Road Freight, in: *OECD Economic Studies*, 2001, 32(I), pp. 229-51., p. 233.



The ECMT multilateral authorisations applied to only a small fraction of international trade in road freight transport services. The multilateral system applied only to certain vehicles and certain countries. Other restrictions included environmental and safety standards<sup>44</sup>.

The majority of international trade in trucking services was regulated by bilateral deals which were on most occasions secretly negotiated between countries. The bilateral agreements were not uniform. In 1997 the ECMT recommended a standard in an attempt to harmonise bilateral agreements and reduce fragmentation of the road freight markets. The bilateral agreements and limited scope of the ECMT licence system meant that the freight markets among the CEEC and EU were fragmented. Regulatory arrangements prohibited cabotage and in the absence of multiple licences third country haulage was restricted.

Similarly, international trade before 1998 in trucking services between the Czech Republic, Hungary, Poland and the Slovak Republic was regulated by bilateral agreements. The bilateral trade regime in trucking services between Czech and Slovak republics was free permitting open access of firms from either country to international trade<sup>45</sup>. The Hungarian market was the most restrictive of the V-4 followed by the Czech Republic and Slovakia with Poland having the most liberal regime in 1998<sup>46</sup>. The Czech Republic was regarded the least discriminatory towards foreign firms. In the Czech Republic, Hungary and Poland the regulator had the power to limit sector capacity. The obligation to use domestic haulers for government contracts existed in Poland and Hungary<sup>47</sup>.

### **5.3.1.2. EU Trade Regime in Trucking Services (1992-2004)**

International road transport has been subject to the application of EU competition rules since 1968. However, many quantitative and qualitative trade barriers remained in place<sup>48</sup>. After a series of protracted negotiations rounds in the 1980s and 1990s EU obstacles to international

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<sup>44</sup> D. BIGGAR, Competition Issues in Road Transport, in: *OECD Journal of Competition Law and Policy*, 2003, 4(4), pp. 39-139., pp. 54-56; pp113-114.

<sup>45</sup> D. PARKER, The Road Freight Sector in the Czech Republic in: OECD, *Background Report on Regulatory Reform in Electricity, Gas, Road and Rail Freight*, Paris: OECD, 2001, pp. 68, pp. 40-52., nr. 132.

<sup>46</sup> O. BOYLAUD and G. NICOLETTI, Regulatory Reform in Road Freight, in: *OECD Economic Studies*, 2001, 32(I), pp. 229-51., pp. 239-240.

<sup>47</sup> *Ibid.*, pp. 9-10.

<sup>48</sup> See Council Regulation 1017. By definition, international transport is border-crossing transport between an origin in one country and a destination in another country. International transport can be divided into international bilateral transport (for example transport between origin D and destination A carried by a French or Italian haulier) and cross trade (for example the transport between origin D and destination A carried by a Dutch haulier).

trade in road haulage were progressively removed. The 1992 landmark legislation on intra EU road transport fully liberalised trade in trucking services and only a few substantial restrictive effects for competition remained on the books<sup>49</sup>. Restrictions on the basis of nationality or company residence were abolished. Limitations for domestic road transport and cabotage remained in place.

To encourage transport efficiency and reduce the number of empty journeys the liberalisation of cabotage transport was gradually introduced from 1992 onwards<sup>50</sup>. First, the Benelux countries decided to liberalise cabotage in 1992. A second step was the introduction of national quotas in the period between 1 January 1994 and 30 June 1998 through a system of authorizations. The quota rose annually although remained largely underused. The cabotage regime was extended to the EFTA countries on 1 July 1994 with the exception of Austria, which joined on 1 January 1997, and Switzerland<sup>51</sup>.

Finally, cabotage for road freight within the EU was fully liberalised on 1 July 1998<sup>52</sup>. Any non-resident carrier who was a holder of an EU road transport authorisation was entitled to operate, albeit on a temporary basis, without quantitative restrictions national road haulage in another EU member state without having a registered office or other establishment in that state<sup>53</sup>. Otherwise, restrictions for the domestic transport markets of the EU member states largely survived the EU's liberalisation drive of road transport<sup>54</sup>.

The liberalisation of the EU road freight market went hand in hand with the reinforcement of operating standards with the objective of creating an EU wide level playing field for road haulers. Since January 1993 binding criteria found their way into directives enforcing common standards

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<sup>49</sup> Council Regulation 881/92 of 26 March 1992 applies to the international transport of goods by road for hire or reward for journeys carried out within the territory of the Community.

<sup>50</sup> Road cabotage transport is governed by Council Regulation No 3118/93 which lays down the conditions under which non-resident carriers may operate national road haulage. Road transport within one EU member state carried out by a non-residential haulier is cabotage transport services within an EU member state.

<sup>51</sup> See EC report on the application of this scheme (COM/98/0047).

<sup>52</sup> In accordance with article 12 of Council Regulation No 3118/93 of 25 October 1993, most cabotage restrictions have been lifted since 1 July 1998 in the 15 Member States of the EU.

<sup>53</sup> See Regulation No 3118/93 on freight transport cabotage. The regulations on cabotage did allow countries to fall back on more restrictive provisions in the event of a negative outcome or market disruption.

<sup>54</sup> In domestic or national transport a flow of goods between an origin A and destination B remains within the same country. See Article 1 of Council Regulation 3118/93.

including social legislation<sup>55</sup>. Competition in the road transport market resulted in rising violations of certain regulations, particularly those concerning driving and resting times<sup>56</sup>. In July 2000 the EU strengthened the criteria for market entry by increasing the level of financial capacity.

### 5.3.1.3. The Figures

The road freight transport industry in the former Communist countries went through the transition process between 1989 and 1995<sup>57</sup>. By the mid 1990s private enterprises dominated the sector and contributed to a rising share of road transport in the mode of international transport with the EU. Road transport surpassed rail transport during the 1990s (see table x).

**Table 19: Mode of International Transport V-4-EU-15 (2002)**

share of mode of transport in total volume of trade in goods V-4-EU (%)																
year	Cz				Hu				Pl				Sk			
	road	rail	sea	air	road	rail	sea	air	road	rail	sea	air	road	rail	sea	air
2002	62.1	37.6	0	0.3	51.1	48.7	0	0.2	36.9	27.8	35.2	0.1	48.5	51.5	0	0

Note: Cz=Czech Republic, Hu=Hungary, Pl=Poland, Sk=Slovakia, Av.=average  
Source: Eurostat, Road Transport Statistics, 2002-2004, own calculations

It took the largest share in total volume of trade in goods with the EU for the Czech Republic and Hungary. Just under half of the total volume of trade in goods between Slovakia and the EU was provided by international trucking services. In Poland – the only country of the V-4 that is not landlocked – road freight transport came just before sea transport (see Table 19).

The share of the EU-15 east-west transport market for all ten candidate countries remained small, i.e. roughly ten percent by volume and 3 per cent by value. This market grew more rapidly<sup>58</sup>. The average value per tonne of goods carried by road from the EU to the CEECs is more than twice

<sup>55</sup> Council Regulation 3820/85 of December 1985 deals with common rules on the minimum age of drivers, driving times, breaks and rest periods for drivers, prohibition of certain payments, control procedures and penalties.

<sup>56</sup> See Council Regulation 3820/85. Infringements present a road safety hazard and are unacceptable in terms of unfair competition; Council Regulation 3821/85 of December 1985 and a subsequent amendment Council Regulation 2135/98 of September 1998 lay down common rules on construction, installation, use and testing of recording equipment in road transport.

<sup>57</sup> Note on data sources and data reliability: Quantitative data concerning road cabotage transport comes predominantly from Eurostat's transport statistics such as road transport statistics (theme 7) and statistics in focus on road freight cabotage (1999-2001, 1991-2001), trends in road freight transport (1990-2003).

<sup>58</sup> International Road Transport Union (IRU), *Competition in East-West Road Transport Markets: Providing Opportunities for All*, Geneva, 2001a, pp. 11., p. 6.; Eurostat, *Statistics in Focus: Trade in goods with Candidate Countries by mode of transport*, Luxembourg, 2004, pp. 8., p. 1.

that in the opposite direction. The volume carried from the EU to the CEECs is slightly more than half than that going in the opposite direction<sup>59</sup>.

**Table 20: Road Transport V-4-EU-15 (2002 and 2004)**

year	volume of road transport V4-EU-15 ('000 tonnes)				share of volume of road transport V-4-EU-15 (%)				share of national hauliers (%)					bilateral share of national hauliers (%)				
	Cz	Hu	Pl	Sk	Cz	Hu	Pl	Sk	Cz	Hu	Pl	Sk	EU	Other	Cz	Hu	Pl	Sk
2002	22241	10563	24076	5832	35.5	16.8	38.4	9.3	27.6	8.4	31.3	6.0	13.7	13.0	77.8	49.9	81.4	64.1
2004	23883	9872	23440	9498	35.2	14.7	35.7	14.4	27.5	5.9	29.5	9.6	8.4	19.1	78.1	40.1	82.6	66.7
Av.	23062	10218	23758	7665	35.3	15.8	37.1	11.8	27.5	7.2	30.4	7.8	11.1	16.1	78.0	45.0	82.0	65.4

Note: Cz=Czech Republic, Hu=Hungary, Pl=Poland, Sk=Slovakia, Av.=average  
Source: Own calculations, Eurostat, Road Transport Statistics (theme 7), 2002-2004.

Considering Table 20 Poland accounts for 37 per cent of total V-4-EU-15 trade in freight trucking services followed by the Czech Republic, Hungary and Slovakia. The latter experienced a particular strong growth rate (5 per cent) between 2002 and 2004. Within the V-4-EU-15 market Czech and Polish hauliers take the lion share with around 30 per cent each followed by Slovakia and Hungary with circa 7 per cent each<sup>60</sup>.

V-4 hauliers captured more than 70 per cent of the total east-west road haulage volume in just over one decade<sup>61</sup>. With the exception of Hungarian truckers Czech, Polish and Slovak road hauliers dominate their national-EU-15 road haulage market (see Table 19 and Table 20). EU hauliers have failed to make inroads in the V-4-EU-15 market carrying even less goods by volume than non EU and V-4 truckers.

The trend becomes even more pronounced when considering bilateral trade among the V-4 countries for the period 1999-2004. Table 21 demonstrates the strength of the Slovak, Czech and Polish road hauliers respectively. Hungarian truckers penetrate the market by total volume at just under four per cent. Slovak and Czech hauliers appear to be able to capture a majority of total freight transport by road with both Hungary and Poland.

<sup>59</sup> International Road Transport Union (IRU), *Competition in East-West Road Transport Markets: Providing Opportunities for All*, Geneva, 2001a, pp. 11., p. 6.

<sup>60</sup> The data confirm the 1997 trends when the Czech Republic (32 per cent) and Poland (30 per cent) followed Hungary and Slovakia ranked highest in the region on international goods traffic by road, in: Eurostat, *Road freight transport in PHARE countries in 1997 (theme 7)*, Luxembourg, 1999, pp. 7.

<sup>61</sup> International Road Transport Union (IRU), *Competition in East-West Road Transport Markets: Providing Opportunities for All*, Geneva, 2001a, pp. 11., p. 6.

**Table 21: Bilateral Transport in the V-4 (1999-2004)**

country	share of national hauliers of V-4 volume (%)				volume of road transport V4 ('000 tonnes)						bilateral share of national hauliers V-4-V-4(%)					
	Cz	Hu	Pl	Sk	Cz-Hu	Cz-Pl	Cz-Sk	Hu-Pl	Hu-Sk	Pl-Sk	Cz-Hu	Cz-Pl	Cz-Sk	Hu-Pl	Hu-Sk	Pl-Sk
Cz	36				988	1688	3161				92	48	53			
Hu		4			91			232	298		8			17	11	
Pl			22			1819		1116		640		52		83		45
Sk				37			2826		2402	771			47		89	55
total	36	4	22	37	1079	3507	5987	1348	2700	1411	100	100	100	100	100	100

Note: Cz=Czech Republic, Hu=Hungary, Pl=Poland, Sk=Slovakia  
 Source: Eurostat, Road Transport Statistics, 1999-2004, averages, own calculations

Much of the variation of market share can be explained by efficiency and competitiveness, i.e. the cost structure of the Czech, Hungarian, Polish and Slovak hauliers. In road haulage the cost difference is decisive in the shipper's choice. The cost of a V-4 hauler is on average some 60 per cent of those of an EU hauler. To a large extent, the gap can be attributed to labour costs (remuneration) differences. On average, wages in the EU were five times the V-4 average. This explains the sheer domination of V-4 hauliers in their trade with the EU-15<sup>62</sup>. The wage cost differential between the V-4 and the EU-15 in some cases can rise to 1:10. Transport companies in Germany and Austria were particularly hard-hit by the wage cost differential<sup>63</sup>. As a result, EU lorries played a decreasing role in cross-border traffic with the V-4 over the last decade.

Despite the quotas in place on the number of international trips in the V-4 the cost level and competition from the V-4 hauliers intensified because of diverging regulatory standards affecting the cost base such as traffic related taxes, levies, fees and subsidies, working hours, occupational safety and health, environmental regulations, occupational standards and market entry, and through side stepping EU and international regulations on international road haulage. The industry also increasingly reported the employment of V-4 drivers in the EU-15 regardless of EU working permits and social standards<sup>64</sup>. No market indicators, detailed overviews or data are available to evaluate the intensity of competition at both EU level and from the V-4. Selective

<sup>62</sup> While calculations show considerable differences between countries the order does not change over time. Total costs per vehicle have constantly increased for all operators ahead of EU enlargement mainly due to the increases in fuel prices. The differences in total costs between competitors is almost entirely explained by personnel costs and fixed costs rather than variable costs and infrastructure charges, in: International Road Transport Union (IRU), *Road Transport and EU Enlargement: Main Problem Areas in the Pre-Accession Period and Progress Made (Progress Report Nr. 3)* Spring 2002, pp. 116., Annex 2.

<sup>63</sup> Deutsche Bank Research, *Effects of the EU's eastern enlargement on the European transport market*, Frankfurt am Main, January 2003, pp. 19-24., p. 22-23.

<sup>64</sup> The BGL cites the example of a police road block conducted on a route in Germany. 48 EU-registered lorries carrying cross-border freight and driven by persons from third countries were inspected. Not one driver was in possession of a German work permit. Two had permits issued by the corresponding EU country. 37 drivers only had a visitor's visa, and nine drivers had neither a work permit nor a visa, in: *Ibid.*, p. 23. See also literature on this topic in: The ECMT, *Social Dumping in the ECMT Area: The Road Freight Haulage Case*, Bucharest, 22/04/2002, pp. 13.

evidence from Germany indicated that the bankruptcy rate in the road transport and road transport-related sectors was several times higher than in the economy as a whole.

Cross trade road transport – international road transport between two countries performed by a hauler registered in a third country – also grew significantly in the late 1990s and early 2010s with an on average rise of 4.4 per cent. In 1997 the Czech Republic, Poland and Slovakia accounted for the bulk of cross trade among all the CEECs<sup>65</sup>. The trend continued and in 2003 Czech and Slovak haulers cross traded at tonne-kilometres 3,147 and 2,654 mn. nearing the top of the league among EU cross traders such as Belgium, the Netherlands and Austria. It reflected the cost effectiveness of their industry and the potential for growth after EU accession. In contrast, Hungarian haulers relative higher cost structure reflects their low share in cross trade in 1997 and in 2003 at tonne-kilometres 395 mn<sup>66</sup>.

In 2000 cabotage transport represented a share of 0.67 per cent of the total road freight transport in the EU-14. It was one of the fastest growing market segments in road transport reaching 0.76 per cent and tonne-kilometres 10 bn of total road freight transport in the EU-14 (Greek data is not available) in 2002. By 2004 it had grown steadily to tonne-kilometres 13.8 bn at an annual rate of 5.4 per cent<sup>67</sup>. The national share of cabotage is unevenly distributed among the EU member states. Geographically small countries have more incentives to undertake cabotage because their own national market is small and other national transport markets geographically close. Those countries that are centrally located and feature a national road transport market of considerable size such as Germany are preferred territories for foreign cabotage carriers<sup>68</sup>.

All the data on the developments in road freight transport in the V-4 and international markets including cabotage and cross-trade point to high growth rates in the sector and the competitive potential for the Czech, Polish and Slovak road haulers after EU accession. Prognosis in the industry projected growth rates of up to 70 per cent for road freight in the V-4 and up to 40 per cent in road transport among the V-4 between 1998-2015. The growth rate of cross-border

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<sup>65</sup> Eurostat, *Road freight transport in PHARE countries in 1997 (theme 7)*, Luxembourg, 1999, pp. 7., p 3-4.

<sup>66</sup> No data is available for Poland, in: Eurostat, *Statistics in Focus: Trends in Road Freight Transport up to 2003* Luxembourg, 2005., p. 2.

<sup>67</sup> Eurostat, *Trends in road freight transport up to 2003*, Luxembourg, 2005, pp. 7., p. 1.

<sup>68</sup> Eurostat, *Statistics in Focus: Road Freight Cabotage (1999-2001)*, Luxembourg, 2003.

transport between the V-4 and the EU-15 was projected to be more pronounced than regional growth. Estimates for the period 1997-2015 expected growth of up to 200 per cent. Countries bordering the V-4 that are more intensely affected by international trade in trucking services are expected to grow faster than domestic trucking services<sup>69</sup>.

### **5.3.3. Asset Specificity: Low Entry Barriers**

How factor and asset specific is the road freight industry in Central Europe? And is there variation of specificity within the industry in the region?

Only limited data is available to gauge asset and factor specificity for the road freight transport sector. The sector does not carry out R&D. Innovation in the sector is related to modernization of vehicles and transport infrastructure or alternatively those related to the introduction of new regulations. Much R&D and innovation is therefore accounted for by other sectors in manufacturing.

The sole indicators available to gauge asset and factor specificity, which ultimately have an influence on the mobility of both labour and capital between sectors, is related to the level of skills and market entry barriers for the industry. As section 5.2.2. laid out the sectoral entry barriers were absent or low (capital, labour, cost, regulations, skills). In the first half of the 1990s this resulted in a massive inflow of labour. Thousands of companies over a period of less than five years were set up. Investments based on the prospect of continuing sales to a particular customer were small enough that on balance a calculation of significant excess capacity did not exist. Foreign direct investment was largely absent from the sector<sup>70</sup>.

By the start of the accession negotiations (1998) supply of trade in trucking services in those countries with the lowest barriers to entry, i.e. the Czech Republic, Poland and Slovakia, surpassed demand. This was reflected by strong competition and declining prices. EU membership was largely seen as an outlet for excess capacity.

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<sup>69</sup> Deutsche Bank Research, *Effects of the EU's eastern enlargement on the European transport market*, Frankfurt am Main, January 2003, pp. 19-24., pp. 21-22.

<sup>70</sup> International Road Transport Union (IRU), *Czech Republic: Road Transport Fact File*, Geneva, March 2003a, pp. 6.

Entry barriers for labour in the sector were low. All that was required to enter the sector were a few months of training. The skills were easily transferable. The easy with which labour entered the sector and the relatively low requirements to enter the sector indicate the low factor and asset specificity of the industry.

#### **5.3.4. Sectoral Cohesion: A Highly Fragmented Sector**

Sectors with fewer firms and higher numbers of employees per firm on average are more likely to bring pressure on politicians compared to sectors where the number of firms is higher and their size smaller. The former also tend to have a higher likelihood of success and are more inclined to engage in lobbying. The smaller the number of employees on average per firm the more dispersed the sector. It is possible to test this conjecture using the number of employees per firm for the years 1998-2002<sup>71</sup>.

The number of firms operating in the sector rose drastically immediately after 1989 and continued to rise throughout the 1990s and early 2010s for all former Communist countries in Central Europe. According to Eurostat the road transport sector in the V-4 was dominated by micro-enterprises with more than 90 per cent of the companies having less than 10 employees. The number of employees and firms in the road haulier service sector were characterised by a near ratio of 1:1 with only the Hungarian, Czech and Slovak industry having few large companies operating (see Figure 26 and 27).

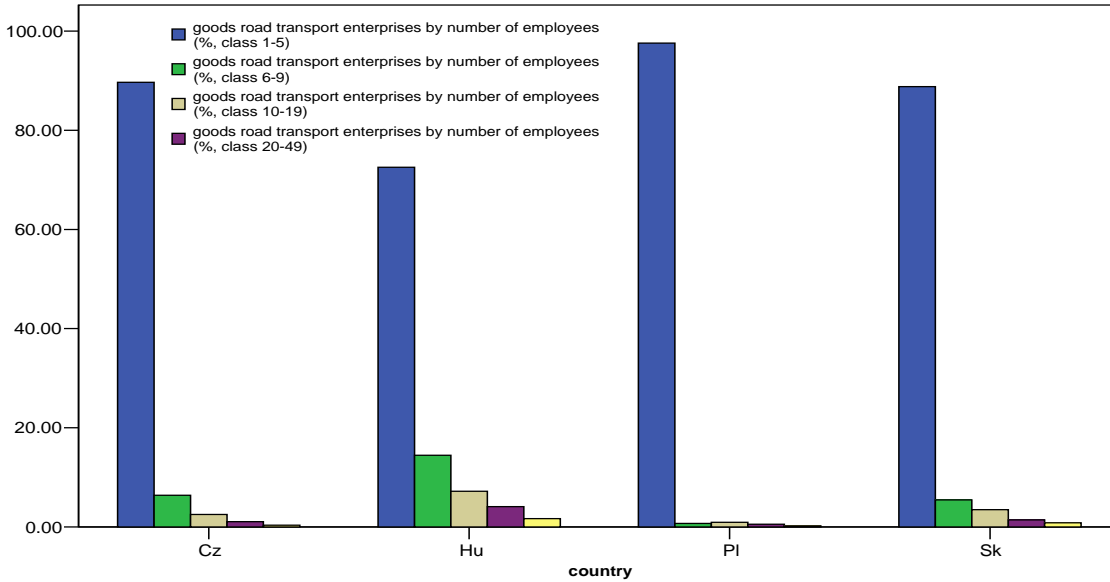
In all V-4 countries more than 70 per cent of all good transported is carried by enterprises with less than six employees with the Czech Republic, Poland and Slovakia having more than 85 per cent micro-enterprises. Only in Hungary are just over 15 per cent of total goods transported by road shipped by firms having on average between five and 10 employees; with a further five per cent in the class of 10 to 20 employees and nearly 3 per cent in those above 20 (see Figure 26).

**Figure 26: Sectoral Cohesion of the Road Transport Industry in the V-4 (1998-2002)**

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<sup>71</sup> See Eurostat, Annual Detailed Enterprise Statistics, 1998-2002, averages for indicators v92100 and v16130.

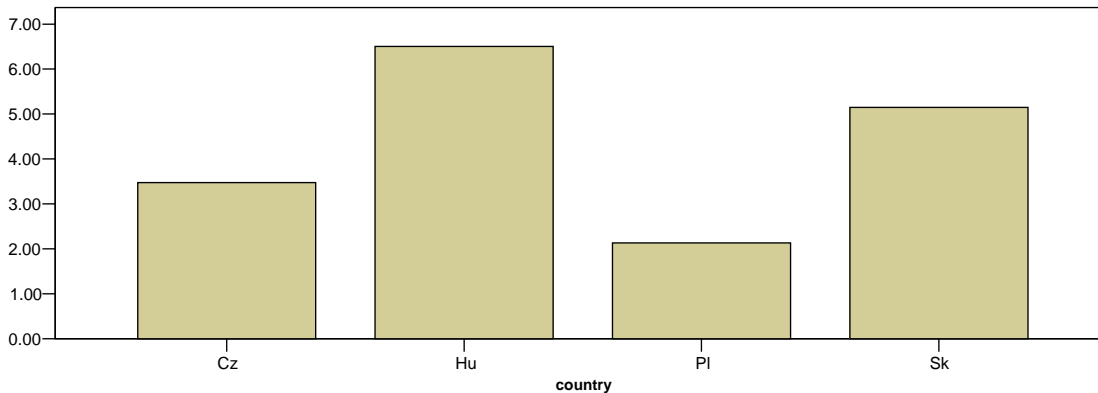




Note: Cz=Czech Republic, Hu=Hungary, Pl=Poland, Sk=Slovakia  
 Source: Eurostat, Transport Statistics; Road Transport (Enterprises, Economic Performance and Employment and Cabotage Transport), Averages 1998-2002.

When surveying the number of employees per enterprise (see Figure 26) the sector is most dispersed in Poland followed by the Czech Republic, Slovakia and Hungary. Therefore, Polish and Czech road haulers would have more difficulties in overcoming collective action problems relative to their Slovak and particularly Hungarian counterparts.

**Figure 27: Sectoral Cohesion of the Road Transport Industry in the V-4 (1998-2002)**



Note: Cz=Czech Republic, Hu=Hungary, Pl=Poland, Sk=Slovakia  
 Source: Own calculations and averages 1998-2002, Eurostat, Transport Statistics; Road Transport (Enterprises, Economic Performance, Employment and Cabotage Transport)

Much of the dispersion of the sector is related to political passivity exhibited by the state authorities. For a variety of reasons, large road transportation enterprises were not included in initial privatisation programmes. The authorities in the region shared the conviction that such enterprises performed a strategic role. The assumption was that it was better for the state to retain control. Consequently, their position in the market and appeal to investors gradually diminished as newly established private businesses took over<sup>72</sup>.

#### **5.3.4.1. National Associations**

The role of industry bodies in shaping and implementing the regulations applicable to the sector can be interpreted as part of a consultative effort by authorities to involve the stakeholders in the decision-making process. It is also a way of protecting firms already in the market. The involvement of industry bodies in regulatory decisions varies widely among the V-4. In Hungary and Czech Republic they were involved regulating fares and market access. In Poland they were involved in defining the market entry conditions<sup>73</sup>.

#### **Association of Road Enterprises & Passenger Transport (CESMAD BOHEMIA)**

On 21 February 1966 the Czechoslovak road haulers established the *Interest Group of Enterprises of Czechoslovak Automotive Transport (CESMAD)*. It immediately joined the *International Road Transport Union (IRU)* in Geneva. CESMAD chose Prague for its headquarters and built seven regional offices. In 1992 the association split between the Czech and Slovak Republics with *CESMAD Bohemia* becoming the largest trade association of road transport operators in the Czech Republic. CESMAD Bohemia represented a majority of Czech operators. The organisation associated more than 100 other association members and almost 2,000 enterprises. It provided services to both domestic and international freight as well passenger transport operators.

Circa 15 per cent of all operators are not associated or represented by smaller regional associations. One of the largest operators in the country with between 1,500 and 2,000 vehicles

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<sup>72</sup> W. RYDZKOWSKI, *Privatisation and Regulation of Road Freight Transport: Conclusion, ECMT Seminar*. Paris, 1996., p. 4.

<sup>73</sup> O. BOYLAUD and G. NICOLETTI, *Regulatory Reform in Road Freight*, in: *OECD Economic Studies*, 2001, 32(I), pp. 229-51.

left CESMAD Bohemia in 2002<sup>74</sup>. In addition to CESMAD the Czech Republic has three specialised branch associations.

CESMAD Bohemia's main activities were focused on the representation and defence of members' interests, services to members such as legal assistance, training and administration and the provision of daily information. Most importantly, CESMAD Bohemia secured and distributed bilateral permits for freight transport and provided customs documents or so-called TIR carnets<sup>75</sup>. The association had an impact on legislation and maintained direct contacts with the MoTC, which consulted the association on legislation to ensure smooth implementation<sup>76</sup>.

Through its membership of IRU, CESMAD Bohemia was well informed about the EU enlargement process. The MoTC, the Parliament and the IRU representation in Brussels consulted and involved the association on the legal approximation of Czech legislation with the EU. During the negotiations CESMAD Bohemia '[...] had direct contact with the Prime Minister and the Chief negotiator. The MoTC was passive in the negotiation process [...]'<sup>77</sup>.

EU membership was welcome: 'For our members EU membership is positive [...] We did not ask for TPRs. It was not necessary. We are competitive and had the impression that our colleagues in the EU feared the level of competitiveness in eastern markets, particularly in the border regions with Germany and Austria. Generally the sector in the EU and in the Czech Republic is in trouble. The margins are too low and there is a sense of overcapacity. Therefore, we tried to avoid the cabotage limitations the EU imposed but that was impossible. In the end it turned out to be an attempt by our chief negotiator to trade between chapters. It was a game, a bargain based on the principle of fair play. *Telicka* failed because other applicant countries accepted the deal'<sup>78</sup>.

### **Association des Transporteurs Routiers Hongrois (ATRH)**

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<sup>74</sup> *Interview by Author with Representative of CESMAD BOHEMIA Association of Road Enterprises & Passenger Transport, Prague, 03/05/2004.*

<sup>75</sup> The TIR carnet is a Customs transit document used for an international transit operation of goods.

<sup>76</sup> *Interview by Author with Representative of CESMAD BOHEMIA Association of Road Enterprises & Passenger Transport, Prague, 03/05/2004.*

<sup>77</sup> *Ibid.*

<sup>78</sup> *Ibid.*

The ATRH was established in 1965 representing all companies in road freight and passenger transport. The association was entirely regulated by the state. It provides interest representation for its members. By the turn of the century the association had nearly 2000 member enterprises representing a majority of those employed in the sector including road hauliers carrying passengers and goods, own-account hauliers, forwarders and freight organisers. It was the largest domestic association in the field of international road transport in the country.

The most important activity of the ATRH was the safeguarding of the hauliers interests. It concentrated on the regulations and taxation affecting the road transportation and the activities of the foreign haulier in Hungary.

The ATRH had a stake in the regulatory process and participated in decisions concerning entry and pricing<sup>79</sup>. It controlled market entry and protected incumbent operators against outsiders through distribution of Hungarian and foreign road permits. In addition, the association provided information, customs documents, legal and financial consulting, and professional training for operators. Its partners were the MoI, MoEF, MoEn, MoFi and various other transport bodies. The ATRH was a longstanding member of IRU.

‘In Hungary we had several rounds of consultations on EU membership and the sectoral implications. All the sectoral partners were involved from the moment of the screening up to the first reactions to the initial regular reports. We consulted the partners on TPRs, whether a status quo was possible and on how to present TPRs. Hungary’s TPRs in the transport position paper are based on the opinion of the sectoral business associations. We asked ourselves what their opinion would be on the introduction of the *acquis* before accession or upon accession. Initially they put forward TPRs of 14-15 years. These were reduced by half in consultation with the EC’<sup>80</sup>. According to the Hungarian Chief negotiator ‘Hungarian hauliers preferred to protect their domestic market rather than seek early freedom to penetrate the EU market themselves’<sup>81</sup>.

In the end the Hungarian government asked for seven transition periods in the transport sector. In the area of road freight transport the TPR’s objective was not to raise the EU level of taxes paid

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<sup>79</sup> See website <http://www.mkfe.hu/>

<sup>80</sup> *Interview by Author with Representative of the Hungarian Ministry of Economy and Transport, Budapest, 10/02/2004.*

<sup>81</sup> Enlargement negotiations on the transport chapter: what has been achieved so far in the field of marketing opening, in: *Uniting Europe and IRU Journal on Transport and EU enlargement*, Geneva: 18/02/2002b.

by heavy duty vehicles with a total weight of over 25 tons. It would allow Hungarian truck owners to continue paying a much lower tax than those in the EU-15. As these trucks were used mostly for international transport, such TPR violated the principles of the European single market. Hungary also put forward a TPR for cabotage in road freight transport until the end of 2006. It also wanted to maintain minimum tax rates for vehicles until end of 2005 and special user charges on some heavy lorries.

### **Association of International Road Transport Operators (ZMPD)**

The ZMPD, founded in 1957, was Poland's largest national road transport association. Since 1989 it has seen its membership rise by 500 per cent. In 2000 it had approximately 3,800 members or just over half of the total registered businesses involved in international road transport activities including all the larger companies<sup>82</sup>. It indirectly represented 200,000 workers in the road transport sector. Less than 50 per cent of the businesses in the country were associated with either the regional associations or the Polish Chamber of Road Transport.

The ZMPD was involved in regulatory decisions. It participated in decisions concerning entry and pricing. Only the ZMPD was authorised by the Polish government to issue authorisations for international road transport including bilateral, EU and ECMT permits and customs documents. The ZMPD had its own vocational training centre. It provided assistance and information and represented members' interests in relations with authorities and international organisations. On a national level it had well trodden institutional communication channels with the MoT. The ZMPD was an active and longstanding member of the IRU<sup>83</sup>.

The association was upbeat about EU enlargement. EU membership would abolish a good number of bilateral limitations and make multilateral permits obsolete on a substantial number of routes. The ZMPD anticipated tremendous advantages for its members. It took an active part in working out and modifying legislation according to EU requirements.

The ZMPD, the Polish Chamber of Road Transport and the Polish Employers in Road Transport were consulted by the MoT on the adaptation of national regulations to the *acquis*. The ZMPD

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<sup>82</sup> International Road Transport Union (IRU), *Poland: Road Transport Fact File*, Geneva, October 2003, pp. 5., p. 4.

<sup>83</sup> See website <http://www.zmpd.pl/>

took 'part in the transportation adaptation programme while the IRU helped the ZMPD prepare for EU membership and approximation of EU transport law'<sup>84</sup>.

'We did not mobilise ahead of EU enlargement. We regarded the process as positive. Our members are competitive. We did not ask for a TPRs on road freight transport. The issue of TAs came up on the EU's side. Poland's chief negotiator asked the association's opinion. We expressed our opposition against the EU measure on cabotage. We did not set up a campaign. From a different perspective the measure might benefit our smaller operators on domestic routes as they might have competition from neighbouring countries. Lithuania is the most competitive of our neighbours'<sup>85</sup>.

#### **Associations des Transporteurs Internationaux Slovaques (CESMAD Slovakia)**

In 1992 CESMAD Slovakia was founded in Bratislava. The membership of CESMAD Slovakia Association grew substantially and the association made an effort to be included in international structures. It joined the IRU in 1993 as a fully-fledged member.

In 1994 the association became responsible for the issuance of domestic and international road transport permits<sup>86</sup>. Based on an authorisation from the MoT and Posts and Telecommunications CESMAD Slovakia handed over international transport permissions for international road-, passenger- and freight transport. It provided information on tax issues and professional training for operators. The association also became involved in regulatory decisions and participated in decisions concerning entry and pricing of the sector.

CESMAD Slovakia was not consulted ahead of the EU enlargement negotiations because of the speed at which the process progressed in Slovakia: 'We did not request anything in the area of transport. Neither did our associations. We did not have the time to consult the association and they did not ask. They were asked at the end to comment on the position papers and they did not object to our position. The TPRs of neighbouring countries [Hungary] and the EU originated out

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<sup>84</sup> *Interview by Author with Representative of the Association of the International Road Transport Operators Poland (ZMPD), Warsaw, 23/04/2004.*

<sup>85</sup> *Ibid.*

<sup>86</sup> See website: [www.cesmad.sk/](http://www.cesmad.sk/)

of fear of the competitiveness of the Czech and Slovak Republics. Our road transport sector had nothing to fear<sup>87</sup>.

In fact the association was observing what was happening in the Czech Republic because of market similarities: 'If the Czech Republic was not asking anything why would we? The Slovak association in way followed what was going in the Czech Republic. If they did not ask it was a signal that we would do the same. We also assumed that if employers were not asking then it should be OK'. Moreover, we were told there was no time<sup>88</sup>.

#### **5.3.4.2. European Federation: International Road Transport Union (IRU)**

The largest Czech, Hungarian, Polish and Hungarian road haulage associations were full members of the IRU. The IRU is a world-wide organisation founded in 1948. It has its registered office in Geneva with an established EU representation in Brussels. By 2000 it united more than 100 national associations including all the most important V-4 associations. The IRU monitors the correct implementation of the provisions stipulated in the Customs Convention on the International Transport of Goods – a multilateral agreement of the UN Economic Commission. The IRU is recognised by EU institutions and national governments for its expertise in issues related to enlargement. Its activities included a series of major east-west road transport conferences, expert workshops on specific issues, technical support to new member associations in candidate countries, economic studies and publications on road transport regulations<sup>89</sup>.

The IRU was very active on the international and European integration of the CEECs road haulers. It was involved in deregulation and liberalisation of road transport throughout the 1990s. Together with the ECMT it was the most important source of research and information on road haulage in the CEECs. It created the IRU Academy as an instrument for harmonising and raising training standards across the EU and beyond. It provided an internationally recognised qualification for road transport professionals<sup>90</sup>.

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<sup>87</sup> Interview by Author with Representative of Slovak Ministry of Transport, Bratislava, 02/03/2004.

<sup>88</sup> Interview by Author with Representative of the Slovak International Transport Trade Union, Bratislava, 26/02/2003.

<sup>89</sup> See IRU's website at: [www.iru.org](http://www.iru.org)

<sup>90</sup> Press Release: Enlargement: great, but where's the catch, in: *IRU Journal on Transport and EU enlargement*, Geneva: 9/10/2002.

As early as 1997 it set out its views on EU enlargement towards the CEECs. It objected against a big bang approach to road transport enlargement which could be followed by a damaging economic free-for-all.

In its position papers the IRU argued that ‘without specific accompanying measures, the road transport sector in the enlarged single market risks severe disruption, to the detriment of the EU’s overall economic performance’. The IRU believed that the potential for disruption stemmed from big variations in many different areas, including wage levels, social regulations, technical standards, infrastructure, financial resources, and managerial competence.

In its 2001 position paper the IRU advocated a ‘step-by-step’ approach to EU enlargement. It stood for an annual increase of community quota, multilateral authorisations for international road transport similar to the ECMT quotas and for bilateral and third country transport with the exception of cabotage. It also stressed full application of the *acquis* for road transport and emphasised the freedom of establishment for EU registered road haulers in the applicant states<sup>91</sup>.

In its third *Progress Report on Pre-Accession Problems in Road Transport* the IRU highlighted its key measures to dampen the economic shock of a big bang enlargement. These included:

- a market monitoring system which would provide early warning of potentially harmful developments in the marketplace;
- stricter criteria governing admission to the occupation of road transport operator to minimise unsustainable competitive practices;
- uniform interpretation and enforcement of existing social regulations; and
- harmonisation of taxation regimes.

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<sup>91</sup> IRU, *IRU Strategy for the Enlargement of the European Union*, Geneva, 2001b, pp. 7.; International Road Transport Union (IRU), *Road Transport and EU Enlargement: Main Problem Areas in the Pre-Accession Period and Progress Made (Progress Report Nr. 3)* Spring 2002, pp. 116.



In other words, ‘the IRU enlargement strategy foresees the possibility for a transitional period for cabotage in the case of persisting discrepancies in the social, market and economic fields between the newly admitted member state and the current EU member states’<sup>92</sup>. It was supported by the Secretary General of the European Transport Federation (ETF)<sup>93</sup>.

### 5.3.5. Insider Status: Economic and Political Strength

Economic strength is based upon relative economic measures throughout the region. We assume that the sector that has a higher share of national GDP, total regional and national export earnings has more economic strength and is more likely to be successful at influencing decision making. Furthermore, a sector that has a higher share of total employment, particularly when it is regionally concentrated, will have more political strength by the sheer numbers of its employees.

**Table 22: Economic and Political Strength**

country	share value added	share V-4 road haulage	share V-4-EU-15 road haulage	share national employment
Cz	0.0107600	36.4	35.32	3.0000
Hu	0.0173800	3.9	15.78	0.6900
Pl	n.a.	22.3	37.07	1.3000
Sk	0.0085200	37.4	11.83	1.0400
Av.	0.0122200	25.0	25.00	1.5075

Note: Cz=Czech Republic, Hu=Hungary, Pl=Poland, Sk=Slovakia, Av.=Average  
share of value added (at factor costs)= share value added road transport normalised by gross value added at factor costs  
Source: Eurostat, transport statistics, averages 1998-2004

Following Table 22 the Czech road freight transport sector scores highest on all economic and political measures of the V-4 with exception of value added. It is followed Poland with 1.3 per cent of total employment and Slovakia with 1.04 per cent. While having the smallest market share among the V-4 as well as in trade with the EU and employing the least number of people in the sector the Hungarian road freight industry records the highest productivity measured by value added. Table x provides one powerful reason for the industry to be a state insider, i.e. the share of total national employment, however, in road transport it did not matter as much to state authorities as the data indicate (see part III).

## 5.4. Conclusion

This chapter considered four hypotheses on the economic and political behaviour of the international road transport industry in the EU enlargement process. It recognized that NTBs and

<sup>92</sup> Verheugen almost certain about transition period for cabotage after accession, in: *IRU Journal on Transport and EU enlargement*, 01/10/2001.

<sup>93</sup> European Trade Unions Want Social Enlargement, in: *EurActiv*, London: 07/12/2001.

behind the border issues had a different effect on the industry across the V-4 countries. They divided the industry with the Czech, Polish and Slovak truckers at the one end and the Hungarian road freighters at the other side.

The Czech, Polish and Slovak industry regarded the process as an opportunity. Upon EU entry they stood to raise their market share in the regional and EU market. Despite multilateral and bilateral restrictions they had captured more than 80 per cent of the total east-west road freight market. They also had made substantial inroads in the Hungarian road transport market by dominating bilateral trade in trucking services.

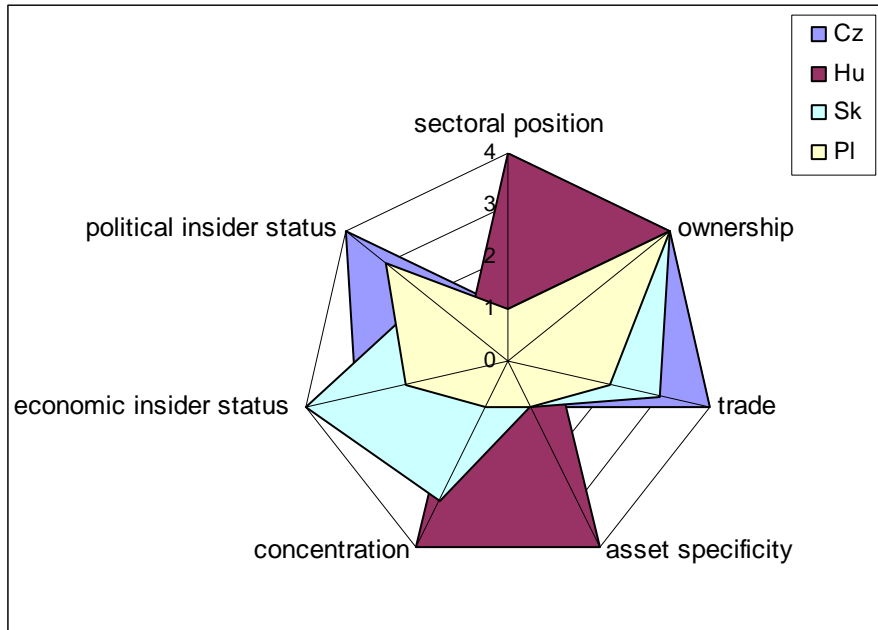
EU enlargement was seen as a welcome safety valve for the overcapacity of supply in trucking services in domestic markets for the Czech Republic, Poland and Slovakia. Strict application of the *acquis* upon accession did not threaten the sector even if it raised the service related costs. The Czech, Polish and Slovak international road haulers competitive and comparative advantage resided in the wage differential and the abundance of trucking services. Hence, Czech, Polish and Slovak haulers did not hold strong preferences on EU accession (see Figure 28).

When the EU announced it would limit market access for truckers from the V-4 in the area of cabotage, political mobilisation was absent in the sector. Initiating an immediate lobbying campaign opposing the EU's limitation on cabotage was too difficult for the dispersed sector in the Czech Republic, Poland and Slovakia. The Czech sectoral lobby made its preference known about access to the EU's fast growing cabotage market. However, it exerted limited pressure. The Czech chief negotiator used it as a bargaining chip to obtain concessions in other fields during the negotiations. Despite the EU's restrictions on cabotage in the enlarged EU the Czech, Polish and Slovak truckers failed to mobilise.

In contrast, Hungarian road haulers found the European single market in trucking services threatening. In the run up and during the accession negotiations they had lost regional market share to Slovak, Czech and Polish drivers. They only were able to capture circa 50 per cent of the Hungarian east-west market. EU enlargement would eliminate the restrictions that protected the Hungarian industry. The process would give the haulers from the neighbouring former

Communist countries full access to the Hungarian market. Thus, it stood to lose and held the strongest preferences about EU enlargement of the entire regional industry.

**Figure 28: Sectoral Comparison of the V-4 International Road Freight Industry**



Note: Cz=Czech Republic, Hu=Hungary, Pl=Poland, Sk=Slovakia  
 Source: Own compilation, based on table 23 (see Conclusion Part II)

The strong preferences about EU membership were transmitted at firm and associative level. The Hungarian industry was also the most concentrated industry in the region. One market player dominated the sector, i.e. Volan Tefu. It was the largest international road transport company in the region and going through a privatisation. Together with the association's members it benefited from protection in the Hungarian market. Despite a high fragmentation of the sector Hungarian haulers' political assets were well developed. In contrast to neighbouring countries, the Hungarian national association was allowed to provide its opinions ahead of the EU accession negotiations. Political pressure through the association resulted in three TPRs in the Hungarian transport position papers for road haulage.

The relatively lower intensity of preferences held by Czech, Polish and Slovak haulers combined with a highly fragmented sector was not conducive to a well organised political campaign. Regardless of the high political and economic insider status in the Czech and Slovak Republics political assets were less developed for the Czech, Slovak and Polish haulers and used reactively

rather than pro-actively. With the exception of Hungary the relatively underdeveloped privatisation of large-sized state companies had provided an obstacle to the concentration of the industry. The larger firm's position in the market gradually diminished and their attractiveness to potential investors declined. Unlike in the pharmaceutical industry and the steel industry FDI did not flow into the sector. Highly fragmented ownership contributed to the fragmentation of the industry.

## CROSS SECTIONAL COMPARISON

In this section comparison shifts from an intra-sectoral to an inter-sectoral analysis. The focus swings from a sector effect – how does the sector compare across all countries – to a country effect – how does the sector compare within each country.

**Table 23: Cross Sectional/Country Comparison**

Analysis			Czech Republic			Hungary			Poland			Slovakia					
stage	indicator	level	pharma	steel	haulage	pharma	steel	haulage	pharma	steel	haulage	pharma	steel	haulage			
preference formation	sectoral position	N	3	3	1	3	3	3	3	3	1	3	3	1			
		R	4	4	1	4	4	4	4	4	1	4	4	1			
	ownership	N	3	1	2	3	1	2	2	1	2	3	2	2			
		R	4	1	4	4	1	4	1	1	4	4	4	4			
	trade	N	1	2	3	3	1	1	1	1	3	1	3	3			
		R	2	3	4	4	1	1	3	2	2	1	4	3			
asset specificity	N	3	2	1	3	2	1	3	2	1	2	3	1				
	R	2	2	1	4	3	4	1	1	1	3	4	1				
political mobilisation	concentration	N	2	3	1	2	3	1	2	3	1	2	3	1			
		R	3	3	2	2	2	4	1	1	1	4	4	3			
	insider status	E	1	3	2	2	3	1	2	3	1	1	3	2			
		R	2	3	3	4	1	1	1	2	2	3	4	4			
	insider status	P	1	2	3	2	1	3	1	2	3	1	2	3			
		R	1	3	4	4	2	1	2	1	3	3	4	2			
<b>total</b>			32	35	32	0	44	28	31	0	27	27	26	0	35	47	31
results	expected mobilisation		1	1	1	1	1	1	1	1	0	1	1	1			
	mobilisation		1	1	0	1	1	1	0/1	1	0	0	1	0			
	position paper		0	1	0	1	0	1	0/1	1	0	0	1	0			
	expected outcome		0	1	0	1	0	2	1	1	2	0	1	1			
outcome/TA	EU		1	1	1	1	0	2	1	1	2	1	1	1			

Note: N=national, R=regional, E=economic, P=political; the sectoral coding is relative and the scaling is ordinal for both intra-sectoral (R, chapter 3,4,5) and inter-sectoral (N) comparison with the exception of the indicators expected mobilisation, mobilisation, position paper and expected outcome, which are nominal. The indicator outcome/TA is nominal and reflects the number of sectoral TAs.

Source: Own compilation based on data from chapter 2, 3, 4 and 5

Table 23 is based on an ordinal scoring system providing an indication of strengths and weaknesses for each economic sector reflecting (a) the intensity of the preferences it held over the EU enlargement policy; (b) the likelihood and intensity of its political mobilisation; and (c) the likelihood of success to obtain a grace period for not applying EU legislation upon EU entry.

The radar charts (Figures 29, 30, 31 and 32) summarise the results of the four hypotheses that test seven concepts on the basis 15 indicators followed throughout chapters 3, 4 and 5. Each sector assumes a relative ordinal position for each concept subsequently plotted along six axes. The axes represent the sector's position, ownership, trade, asset specificity, market concentration and economic and political insider status. Variations in the scores are shown by the distance from the centre of the chart. The conclusions of chapters 3, 4 and 5 include the radar charts on a regional basis. The charts below represent the sectors on a national level.

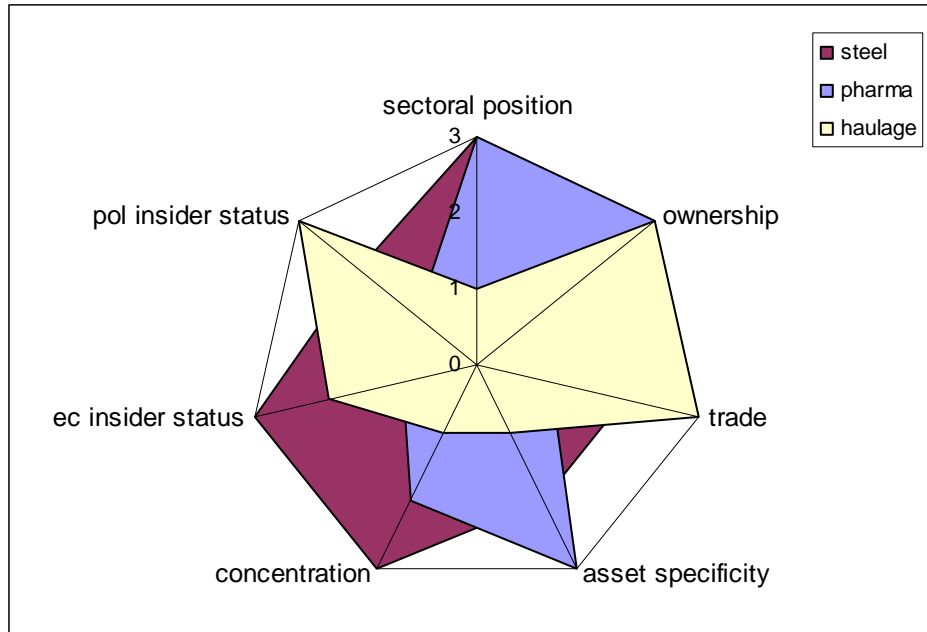
## **Czech Republic**

The Czech steel and pharmaceutical industry stood to lose from the enlargement process. Since the mid 1990s they experienced rising imports. They became comparative disadvantage sectors. The pharmaceutical industry was privatised to foreign interests by the time the accession negotiations had started. No new companies had entered the sector and few picked up R&D activity reflecting its asset specificity.

The steel industry, in contrast, remained mired in legal uncertainty in regard to its trade regime, restructuring and state aid. Since 1989 it had experienced a declining output (above 30 per cent) and a drastic exit of capital and labour (60 per cent). A distinct majority of Czech steelmakers failed to find a strategic investor. The industry's performance declined and debt accumulated fast by the turn of the century.

Due to a combination of these factors the basic iron and steel and the pharmaceutical sectors formed strong preferences over enlargement policy. Only the steel industry was sufficiently concentrated with the economic and political strength to push its political agenda. The Czech authorities took into account the steel maker's plight and ignored demands for protection of the pharmaceutical industry. Czech pharmaceutical producers did not have sufficient market power. The heavy presence of foreign subsidiaries opposed local producer's interests which added to the weakness of their political assets.

### **Figure 29: Cross Sectional Comparison Czech Republic**



The road transport sector would gain from EU entry. It did not hold strong preferences about EU enlargement policy. The competitive road haulage sector dominated Czech international road transport. In less than a decade it had experienced a dramatic inflow of labour (50 per cent) and the number of enterprises had almost doubled. It was looking forward to strengthen its position in the enlarged EU. As the EU proposed a limitation for Czech road haulers in the fast growing cabotage market of the enlarged EU the latter failed to rapidly set up a lobby campaign. While its political assets were well developed, setting up a lobby campaign for its vast membership spread across the country would have posed organisational difficulties. By the end of the accession negotiations the Czech chief negotiator, Pavel Telicka, attempted to use international road haulage to extract concessions in other areas during the negotiations (see chapter 6 and 7).

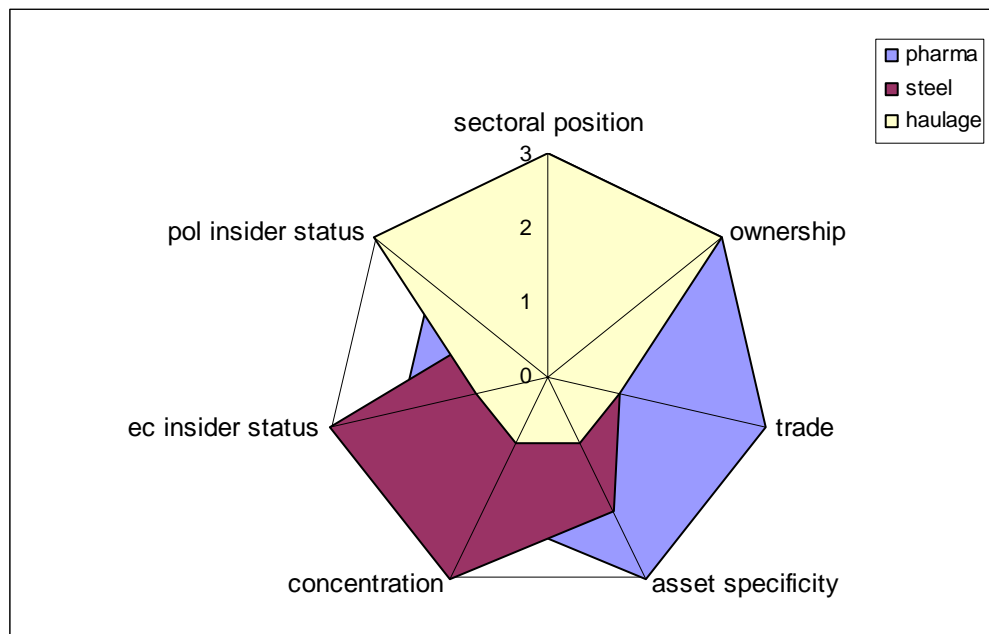
## Hungary

The Hungarian pharmaceutical, basic iron and steel and international road haulage sectors assumed they would lose income as a result of EU entry. The steel sector and road freight haulage were comparative disadvantage sectors. Over the 1990s they progressively lost market share and recorded a negative trade balance.

While Hungarian drug companies anticipated losing out from the process they had built up large export markets in the former S.U. and enjoyed rising exports. They were dominated by private

ownership. Substantial FDI inflows, including in R&D, reflected its asset specificity relative to the other two sectors. It had an insider status as apposed to foreign lobby agents. The Hungarian pharmaceutical industry comes close to the ideal type of a sector with strong preference formation, subsequent political mobilisation and a high likelihood of success. The combination of private ownership, anticipated loss of income while having a strong presence in export markets resulted in intense preference formation. It provided the strongest incentive to set up an effective lobby campaign and exert intense political pressure at marginal costs because of well organised political assets. They succeeded in putting two TPRs in the Hungarian position papers for the EU accession negotiations.

**Figure 30: Cross Sectional Comparison Hungary**



The plight of the steel industry was the worst. It remained mired in legal uncertainty surrounding the EU trade regime, restructuring and state aid. Since 1989 it had experienced declining output and a drastic exit of labour (75 per cent). It was looking desperately for a strategic investor. The industry's performance declined and debt accumulated becoming a serious burden for the Hungarian authorities. The industry politically mobilised on EU enlargement at marginal costs because of high market concentration and its economic insider status in the area of anti-dumping and trade. Nonetheless, it failed to extract TPRs from the authorities, which cut subsidies and placed the industry under administration.



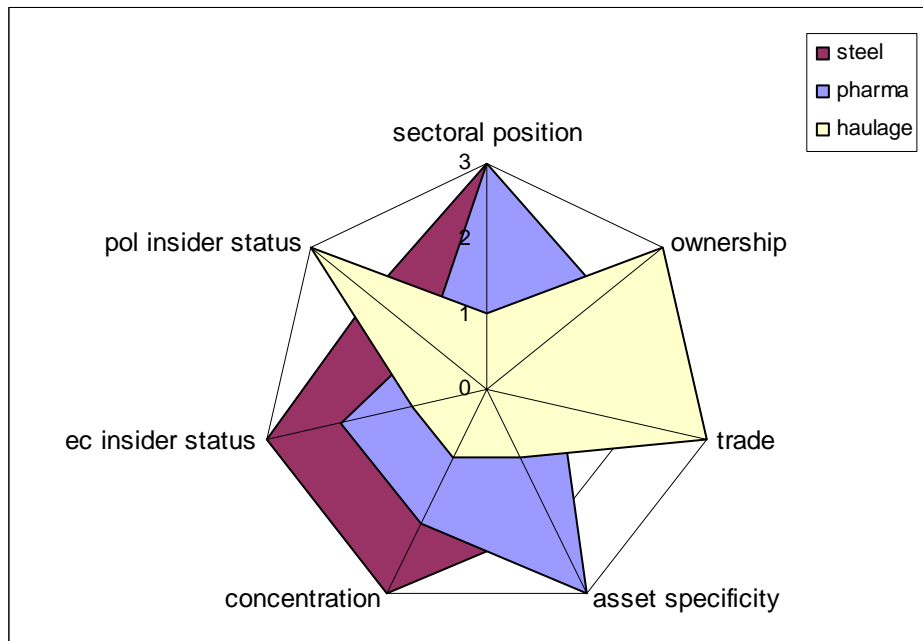
Hungarian road haulers held intense preferences. Their association was a political insider because of its large workforce and the concentration at the top in one private national and regional market leader with longstanding contacts to the authorities. Well organised concerted action ahead of EU enlargement made the Hungarian authorities list two TPRs in the position papers at no cost for the Hungarian state. The TPRs were devised to shield the Hungarian market from competition from neighbouring applicant countries rather than the EU.

## **Poland**

Because of EU enlargement the income of Polish steel and pharmaceutical sectors was under threat. They anticipated losing from EU membership. Since the mid 1990s they had experienced rising imports and became comparative disadvantage sectors. Privatisation in both sectors was difficult. The steel industry failed several privatisation attempts because amongst other factors the failed to support the plans. The steel industry remained mired in legal uncertainty in regard to its trade regime, restructuring and state aid. Since 1989 it had experienced a declining output (50 per cent) and a drastic exit of capital and labour (60 per cent). The Polish basic iron and steel industry formed strong preferences over enlargement policy. It was sufficiently concentrated and had the economic and political strength to push a TPR on the government position paper in the EU entry negotiations.

Hesitation on the part of the authorities slowed the privatisation in the pharmaceutical industry. It failed to consolidate with the state retaining a substantial part of the industry. While being the most asset specific industry of all three it predominantly provided the domestic market with low value added products. Initially the industry appeared unaware of the implications of EU enlargement. Its geographic and sectoral dispersion, its diverse sectoral representation and its lesser political and economic insider status were less conducive to political mobilisation. As a result, the government did not take up a TPR in its position paper. It closed the relevant chapter in the EU accession negotiations. The well organised foreign lobby agents and subsidiaries meanwhile contributed to new drug legislation that was put on the books in Poland. It was only late in the process that domestic producers upon advice of their Hungarian and Slovenian counterparts mobilised and successfully pressured the government.

**Figure 31: Cross Sectional Comparison Poland**



In contrast to steel and pharmaceuticals, road transport would gain from EU entry. It did not hold strong preferences about the process. The competitive road haulage sector dominated the Polish international road transport market. It had doubled the number of road freight enterprises and more than doubled its labour force in less than one decade. It was looking forward to strengthening its position in the enlarged EU. As the EU proposed a limitation for Polish road haulers in the fast growing cabotage market of the enlarged EU the latter failed to set up a lobby campaign. While its political assets were well developed, setting up a lobby campaign for its vast membership spread across the country would have posed organisational difficulties.

### **Slovakia**

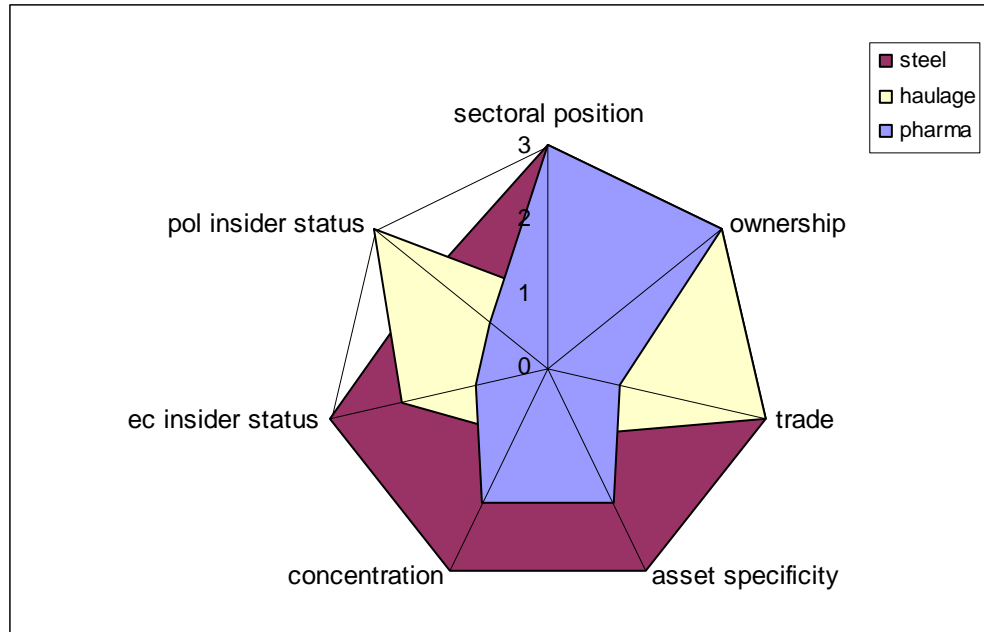
The Slovak steel and pharmaceutical industry anticipated income losses from the enlargement process with only the road hauliers anticipating gains. The Slovak steel makers and road hauliers had built up a strong foreign presence in export markets. The pharmaceutical industry experienced rising imports in the sector and had become a substantial comparative disadvantage sector. Preferences opposing EU entry without TAs was strong in the domestic pharmaceutical industry. The Slovak steel industry, represented by US Steel Kosice, opposed the process outright refusing to abide by EU legislation ahead of EU entry. The anticipated income losses would hurt private owners in both sectors.

The Slovak pharmaceutical industry had consolidated, invested in R&D and was rather concentrated in one company, Slovakopharma. It dominated domestic production for the Slovak and Czech market. The state, which had kept a golden share in the company had opposed the TPR put forward by the board members. The authorities had closed the EU negotiations without bargaining. Foreign lobby agents and production facilities, with a market share in value of above 90 per cent, had lobbied intensely for a strict application of the *acquis*.

The steel industry was the first to privatise in the region. It consolidated and invested in product upgrading and R&D. In contrast to the pharmaceutical industry US Steel Kosice mobilised all its resources and exerted intense political pressure through its membership of both the Czech and Slovak steel associations. It wanted to maintain its tax benefits that contravened EU legislation. Its economic insider status and geographic and sectoral concentration facilitated matters for its CEO who negotiated directly with the government and the EU. Its TPR was inserted in the Slovak position paper.

The Slovak steel industry comes close to the ideal type of a sector with strong preference formation, subsequent political mobilisation and a high likelihood of success. The combination of private ownership, anticipated loss of income while having a strong presence in export markets resulted in intense preference formation. It provided the strongest incentive to set up a lobby campaign and exert intense political pressure at marginal costs because of well organised political assets.

### **Figure 32: Cross Sectional Comparison Slovakia**



Slovak road haulers did not hold strong preferences. They were somewhat astonished about the position of their Hungarian counterparts. The competitive road haulage sector dominated Slovak international road transport as well as that of the entire region. It had experienced a 30 per cent increase in employment. The number of enterprises had risen more than 14 times in less than a decade. It was looking forward to strengthen its position in the enlarged EU. As the EU proposed a limitation for Slovak road haulers in the fast growing cabotage market of the enlarged EU the latter failed to set up a lobby campaign. As I will show in chapter 6 and 7, the association and authorities looked at the neighbouring Czech Republic. Since Prague had not requested a TPR the Slovak representatives thought it wise to take a similar position in the EU accession negotiations.

## CONCLUSION PART II

Why do sectoral conditions for joining the EU (the presence of transitional arrangements) vary for the individual applicant states? And, what do transitional arrangements reveal about sectoral interests' ability to influence the enlargement process?

The strategy to address both questions has been to:

- analyse what was at stake for economic sectors and the effect of EU integration on sectoral incomes and the intensity of sectoral preference formation over EU enlargement;
- analyse the sectoral political assets and elicit their propensity to exert political pressure.

Sectoral conflicts that occur because of the income redistribution induced by market integration have strong effects on preference formation. In the sample preference formation occurred along sectoral lines with only the Polish pharmaceutical industry partially exerting political pressure through a national peak association.

All but one sector (the Slovak pharmaceutical industry) that expected losses from EU integration formed strong preferences and exerted political pressure in one form or another. Within this group seven sectors were characterised by a progressive comparative disadvantage. They opposed strict application of the *acquis* and the redistributive effect it would have on their income.

Anticipated loss of income provokes stronger preferences over EU enlargement policy than anticipated gains. In the sample those sectors (the Czech, Polish and Slovak international road freight industry) which anticipated benefits the EU curbed during the entry talks, did not form strong preferences. They subsequently failed to mobilise.

EU integration would reposition the remaining two sectors in the sample (the Hungarian pharmaceutical and the Slovak basic iron and steel industry) in their domestic and growing export markets. This they vehemently opposed. The combination of loss of income and comparative advantage induced the strongest preference formation. Sectors positioned in export markets were

better informed about the process. They held stronger preferences over EU enlargement than those exclusively focussed on the domestic market.

Sectoral socio-economic assets condition the distribution of demand for protection that result from changes in economic actors' preferences. They contribute to the ability of actors sharing common interest to overcome collective action problems critical to the effects of political capacity.

Political capacity was highest for the basic iron and steel industry as it could mobilise at the lowest marginal cost to overcome collective action problems. The continuous steel trade disputes throughout the 1990s and early 2010s are a case in point. Concentration for the pharmaceutical industry was lower and the marginal costs to overcome collective action problems were higher. Within the pharmaceutical industry collective action problems were compounded by the sectoral division between local producers and foreign subsidiaries. The dispersed road hauliers industry had a lowest sectoral concentration. Road haulers had difficulty in mobilising their vast and geographically spread membership at short notice, which EU accession negotiations required. The sectoral cohesion of Hungarian road haulers, the highest in the regional sector, resulted in additional political weight opposing the full application of EU legislation.

Cross-sectorally, the Hungarian pharmaceutical and Slovak basic iron and steel sector held the highest national and regional score for asset specificity. They had invested heavily in anticipation of continuing sales. They would not stray from expanding their markets because of EU entry and mobilised sectorally. With the exception of the Slovak pharmaceutical industry all other comparable asset specific industries exerted political pressure. Czech, Polish and Slovak road haulers whose asset specificity was the lowest failed to mobilise. Their Hungarian counterparts put pressure on the authorities and might have been helped by the regionally and nationally dominating road freight enterprise, Volan Tefu.

Nevertheless, empirical evidence about sectoral associations from the sample appears to contradict the assumption that factor specific sectors are more likely to hold better organised political assets. Despite the variation in asset specificity, all three sectors had equally well

organised sectoral associations. For instance, during the interviews the author was surprised by the well funded, equipped, staffed and informed road haulage associations in the V-4 countries. Their political assets expressed in terms of the information they provided and the political contacts they maintained, matched at least those of the pharmaceutical and steel industry. The empirical research also established that membership of European or international associations did not contribute to the weight of political assets of the V-4 industries. European or international association protected the interests of their respective insiders; and opposed those of its new Central European associative members. Therefore on the basis of the sample, this research concludes that the nature of preference formation is decisive for political mobilisation and its intensity rather than political capacity.

I complemented the research with the notion of insider status expressed through ownership structures and political and economic strength assuming that ownership structures indicate access to policy makers. A state owned firm is likely to have a higher insider status compared to a private firm. The former would be more successful in protecting its interests. A firm owned by a foreign subsidiary is assumed to be an outsider. Both assumptions did not hold for the sample. Therefore, in **table x** I ranked the cases inversely to the assumed causal effect.

The state's conviction in Central Europe that enterprises performed a strategic role and thus should remain state-controlled, was an obstacle for their privatisation. Consequently, their position in the market gradually diminished, as did their attractiveness to investors. In addition, while state ownership provided direct access to policy makers in the enlargement process, it did not result necessarily in a better protection of the firm's interests.

Empirical evidence from our sample suggests that private owners were less inclined to compromise on the preference they held than publicly owned enterprises and sectors (a point which I will pursue further in chapter 6). For instance, the state's golden share in Slovafarma prevented the drugs company from requesting a grace period. The Polish authorities, part owner of the pharmaceutical industry, closed the relevant chapter of the EU negotiations only to re-open it again when the Hungarian industry had negotiated TAs. The Hungarian authorities refused the state owned steel industry a TPR. Lastly, compared to the exemption of Slovakia's private owned

steel industry the state owned Czech and Polish steel works might have agreed to less beneficial terms.

Relative economic and political strength on a national and regional level is a good indicator for the supply of protection when mobilisation occurred. The exception is the Hungarian steel industry. The effect appears less outspoken for Poland than for the other three countries. When controlling for economic size and population the effect of a large industry in a small country continues to be overriding because mobilisation in the V-4 predominantly occurred in the national context. Only those with a strong and rising presence in international markets were able to mobilise internationally. However, also they chose the national lobbying route. Examples are the steel industry in Slovakia and the drug industry in Hungary.

Enlargement policy played a sectoral redistributive role that resulted in preference formation and political mobilisation along sectoral lines. It confirms the underlying argument that the presence and variations in sectoral conditions (TAs) for EU entry is due to sectoral interests and their ability to influence EU enlargement policy. Chapters 3, 4 and 5 demonstrate that sectoral preference formation and political mobilisation are necessary conditions for the presence of TAs or grace periods in the EU's enlargement process.

On the basis of chapters 3, 4 and 5 and Table 23 one can conclude that the hypotheses based on an asset specific theory combined with assumptions about asymmetric lobbying hold up surprisingly well. The exceptions are the assumptions about insider status and ownership structures whereby causality travels in the opposite direction.

Following *Frieden*, *Rogowski* and *Gilligan* an asset and factor specific theory usually picks up changes in sectoral economic positions and in ensuing socio-economic institutions over *la longue durée*. Given the short period this research studies (1989-2004 and more specifically 1998-2002) the theory performs remarkably well. The theory, which is essentially based on the idea of sectoral mobility of factors, continues to pick up the EU enlargement effect in transition economies where everything is on the move – from trade-flow reorientation, price adjustments to



market mechanisms, extreme work force movements between sectors, to privatisation and FDI inflows.

Those sectors that are more asset specific hold stronger preferences. When considering preference formation and the likelihood of political mobilisation, the framework explains up to 83 per cent of the cases, or ten out of 12 cases. Interpreting events *sensu stricto* the exceptions are the Slovak and the Polish pharmaceutical industry.

Those that stand to lose income mobilise rather than those that would gain income. This binds in with claims stressing the uncertain nature of gains relative to losses. Economic actors only know that some markets will open up, not whether they will be able to capitalise on this opportunity in the face of international competition. Moreover, actors tend to react more strongly to losses than gains, again favouring losers in the mobilisation dynamic. As chapter 3, 4, and 5 point out very few actually lobby for opportunities in the enlargement process.

Yet, exporters with a comparative advantage that would lose because of changing policies hold the strongest preferences. They tend to mobilise most intensely. Because of their international exposure they know precisely what they will be losing as a result of EU integration, enhancing their incentives politically mobilise.

Private owners are likely to hold stronger preferences and exert more political pressure than public owners do. This is true within and across sectors and contradicts the original assumptions about insider status and ownership structures.

Social inference on the basis of an asset and factor specific theory is less clear cut (66 per cent or in eight out of 12 cases) when taking into account the supply for protection or the position papers of the applicant states. An additional two industries held strong preferences and exerted intense pressure (the Czech pharmaceutical industry and the Hungarian steel makers). It subsequently did not materialise in the respective position paper ahead of the negotiations. In other words, their respective state institutions decided to ignore sectoral political preferences.

The discrepancies between preference formation, political mobilisation and national position papers rise to almost one in two in the sample when taking into account the eventual outcomes. TAs appear for sectors that did not hold strong preferences or mobilise, and for states that did not ask for grace periods. Sectors characterised by these occurrences are indicated in grey in Table 23. These discrepancies may be stochastic. Alternatively they may well reflect a pattern (see chapter 7).

The implicit political model of economic pluralism in modern political economy has its strengths. It performs well in anticipating political mobilisation of economic sectors. The presence and the degree of political pressure is a function of political conflict shaped by actor's preference formation, weighted by their political and economic insider status and socio-economic organisational capacity. It performs less well in its assumptions that the effects of market integration on sector's preference formation and mobilisation will automatically feed into policy outcomes and institutional arrangements. Policy outcomes are not automatically a result of sectoral preference formation and political mobilisation as 'demand side' international modern political economic theory predicts. One does not always find the respective policy outcomes on a national and international level after economic sectors carried strong preferences and mobilised politically.

Nevertheless, on a regional level sectoral preference formation and political mobilisation appear necessary conditions for the presence of TPRs and TAs in the enlargement process. Part III conclusively confirms this result. It elicits the discrepancies between sectoral policy demands and national and international policy outcomes. It deals with institutions in the EU enlargement process which aggregate interests in the public arena. It clarifies the government and international institutions' responsiveness to sectoral preferences – the supply side of TPRs and TAs.

**PART III: STATES AND STRATEGIES**  
**SUPPLY FOR PROTECTION**



## Introduction

Where Part II explores the effect of EU enlargement on sectoral preferences formation and ensuing sectoral political mobilisation (a preference driven approach) Part III explores how institutions aggregate and influence sectoral preferences in the public arena (an institutional driven approach)<sup>1</sup>. It concentrates on the mediating role national and EU institutions play between sectoral interests and outcomes in the EU enlargement negotiations. In other words, what are the interactive effects between sectoral preferences and their political mobilisation; and national and EU institutions in the enlargement process? Part III discerns these interactive institutional effects through a structured comparison of the Czech, Hungarian, Polish, Slovak and EU institutions' response to changes in sectoral preferences catalysed or induced by EU enlargement.

Chapter 6 and 7 systematically seek to examine whether, how and why institutions at the time of EU enlargement mediated the relationship between sectoral interests and political outcomes. Chapter 6 and 7 are concerned with why national and EU institutions responded as expected to the sectoral political pressure in seven out of the 12 cases thoroughly analysed in chapter 3, 4 and 5; and why national and EU institutions did not behave in ways anticipated for the remaining five sectors (see conclusion part II).

In answering these questions Part III argues that *state and EU institutions and the strategies of actors occupying these institutions mediate sectoral interests along the logic of destructive and constructive interference in the enlargement negotiations*. Institutions affect both which societal preferences have priority in the public arena and how receptive the political system is to sectoral interests that exerted political pressure. National and EU institutions act as constraints upon societal preferences when their interests are not aligned. I call this phenomenon destructive interference. Conversely, when societal and institutional preferences are aligned states and strategies sustain or amplify sectoral interests. I call this phenomenon constructive interference. In other words, sectoral conditions under which the EU enlarges, the presence of TAs, is due to

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<sup>1</sup> P.A. GOUREVITCH, Squaring the Circle: The Domestic Sources of International Cooperation, in: *International Organization*, 1996, 50(2), pp. 349-73., p. 6.

the domestic cost and benefit calculation, i.e. constructive and destructive interference and sufficient impact of the influence of sectoral interests on that calculation.

## **Assumptions**

### **Two Levels of Analysis**

Part III makes an analytical distinction between national and EU institutions and the interaction between them. On a national level it is concerned with the conditions under which authorities were responsive to sectoral interests' preferences in the EU enlargement process. On an EU level it concentrates on the conditions under which the EU was willing to accept temporary departures from the *acquis* when negotiating EU membership with the CEECs. The analysis provides the narrative of the action revolving around the national and EU bargaining tables which perilously were intertwined during the enlargement negotiations. I use the two-level game metaphor to analyse the interaction effects between the national and EU institutions. A two-level game allows to test theory and hypothesis geared towards second-image (domestic causes of international effects in chapter 7) while not excluding those geared towards second-image-reversed (international causes of domestic effects in chapter 6)<sup>2</sup>.

### **An Open Polity**

Part III departs from the assumption that states are unitary actors because the main argument rests on the opposite supposition that domestic politics in the applicant states bear heavily on the prospects of countries joining the EU, the related TPRs and the ensuing TAs. It assumes that the state is an open polity composed of central decision makers, legislatures, and domestic groups<sup>3</sup>. These actors have varying preferences and share formal decision-making authority according to their national constitutions. Formal political institutions distribute power among these actors in

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<sup>2</sup> The term second image was coined by Kenneth Waltz, in: K.N. WALTZ, *Man, the state and war: a theoretical analysis*, New York; London: Columbia University Press, 1959, P. GOUREVITCH, *The Second Image Reversed: The International Sources of Domestic Politics*, in: *International Organization*, 1978, 32(4), pp. 881-912.; J.A. CAPORASO, *Across the Great Divide: Integrating Comparative and International Politics*, in: *International Studies Quarterly*, 1997, 41(4), pp. 563-91.; According to Putnam, 'the politics of many international negotiations can be usefully conceived as a two-level game. At a national level, interest groups pursue their interests by pressuring the government to adopt favourable politics. At an international level, governments seek to maximize their own ability to satisfy domestic pressures, while minimizing the adverse consequences of foreign developments. Neither of the two games can be ignored by central decision-makers, so long as their countries remain interdependent, yet sovereign', in: R.D. PUTNAM, *Diplomacy and Domestic Politics: The Logic of Two-Level Games*, in: *International Organization*, 1988, 42(3), pp. 427-60. , p. 434.

<sup>3</sup> G. GARRETT and P. LANGE, *Internationalization, Institutions, and Political Change*, in: *International Organization*, 1995, 49(4), pp. 627-55., p. 627.

the policy making process and contribute to policy formation. The structure of domestic policy preferences refers to the relative positions of the preferences of important domestic actors on EU enlargement policy.

Differences among states in the selection of political institutions dealing with EU accession and the preferences of the actors that inhabit these institutions are assumed to have important effects on domestic and international politics. According to *Tsebelis'* theory on political institutions the distribution of decision-making power among these actors and the extent to which their preferences diverge defines the number of veto players in a country and the likelihood of policy change<sup>4</sup>. For *Milner* the corollary of this argument on an international level is that 'differences among states in their internal preferences and political institutions have important effects on international politics'<sup>5</sup>.

Of all the political actors that fill a state's political system I focus on three important categories in chapter 6, i.e. the executive, the legislature and sectoral interests groups. The government and the bureaucracy make up the executive with the bureaucracy comprising the various working groups, committees, departments and ministries dealing with EU accession. The legislature encompasses parliament comprising political parties which, depending on the issue, oppose or support the executive's policy on EU accession. The third set of actors is composed of sectoral interest groups that exert political pressure such as the socio-economic institutions of the pharmaceutical, steel and road transport sectors analysed in chapter 3, 4 and 5.

Central to the assumption of an open polity model is that domestic politics cannot be treated as a unitary actor when the preferences of these three sets of actors differ over policy on which they share decision making power. Conversely, when these three actors have similar preferences state interests or national interest are present and a unitary actor assumption is justifiable. According to *Lange* and *Garrett* such scenario appears most likely in extreme situations where 'the inhabitant preferences are more likely to coincide'. Similarly, an open polity model is irrelevant when

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<sup>4</sup> G. TSEBELIS, *Veto players: how political institutions work*, New York: Princeton, N.J.: Russell Sage Foundation; Princeton University Press, 2002.; E.D. MANSFIELD, H.V. MILNER and J.C. PEVEHOUSE, *Vetoing Co-operation: The impact of Veto Players on International Trade Agreements*, s.l., 26 January 2005, 46., p. 3.

<sup>5</sup> H.V. MILNER, *Interests, institutions, and information: domestic politics and international relations*, Princeton, N.J.: Princeton University Press, 1997., p. 10.

political actors have different preferences but with only one single actor controlling decision making<sup>6</sup>.

In short, domestic policy outcomes under the open polity model are the result of prevailing national institutions ingrained in a body of law or constitution and the manner in which they distribute power among political actors, and the amalgam of the actor's preferences that inhabit those institutions.

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<sup>6</sup> G. GARRETT, Internationalization, Institutions and Political Change, in: G. GARRETT, P. LANGE, R. O. KEOHANE and H. V. MILNER, *Internationalization and domestic politics*, New York: Cambridge University Press, 1996, pp. 48-75., pp 11-12.



## CHAPTER 6: STATES

Why is it that when economic sectors carry strong preferences and mobilise politically one does not always find the respective policy outcomes as ‘demand side’ international political economic theory predicts (see Part II)? More precisely, why did sectoral political mobilisation in the applicant countries not always result in corresponding national negotiation positions? In concentrating on the role of national institutions in an open polity model chapter 6 demonstrates that states composed of formal and partisan political institutions mediate sectoral interests along what I call *the logic of destructive and constructive interference*.

Chapter 6 appraises this conjecture by scrutinising the responsiveness of the Czech, Hungarian, Polish and Slovak political institutions to sectoral interests discussed in Part II. It engages with the national institutions dealing with EU accession policy according to their ability to amplify or constraint sectoral demands for maintaining the status quo. This ability is assumed to be related to: (a) the formally mandated number of veto players according to their ability to set the agenda, amend or ratify policy and organise ratification constraints; and (b) the insulation of the policy process which draws the attention to the executive. Variation in either is likely to affect the room for manoeuvre of governmental negotiators in the international arena (see chapter 7).

Throughout chapter 6 the analysis centres on the dynamic of three specific empirical factors for the period 1998-2003: the distribution of decision making power for enlargement policy, the articulation of sectoral preferences within the national institutions and the formulation of national negotiation positions on EU enlargement.

### 6.1. Institutional Processes

In order to change the legislative status quo a certain number of individual or collective actors have to agree on a proposed change. *Tsebelis* assigned such actors veto player status. Veto players are institutional or partisan actors whose consent is needed to alter policies. Institutional and partisan veto players are specified by a country’s constitution and political process. A constitution can assign the status of a veto player to a different individual or collective actor identified as an institutional veto player. In parallel, partisan veto players emerge from the

political game<sup>1</sup>. Concurringly, a crucial factor in explaining policy making is to realise how the game is rooted in a country's constitution and how it is played between domestic actors. The domestic game depends on two variables: (a) the number of veto players; (b) the nature of the veto players; and (c) the insulation of the institutional processes from sectoral preferences. The variables reflect the formal avenues of access to the policymaking process available to sectoral interests. I concentrate on the constitutional powers and the institutional responsiveness to demands for policy change. The spotlight is on the consequences of the variations in the number of institutional actors whose support is required to generate a policy change<sup>2</sup>.

### **6.1.1. Constitutionally Mandated Number of Veto players**

Each state in Central Europe has a set of rules for the distribution of authority in the field of foreign policy. These rules are strengthened when negotiating membership to international organisations particularly when it involves the transfer of national sovereignty. The constitutions of the V-4 have built in provisions that create ample opportunities for maintaining the policy status quo, i.e. not joining the EU.

#### **6.1.1.1. Czech Republic**

In the Czech Republic the responsibility for foreign affairs lies with the president and the government. The president negotiates and ratifies international treaties. Presidential power is largely delegated to the government. On EU accession President *Vaclav Havel* delegated his authority to the government while retaining symbolic power in the field of EU foreign policy.

The government embodies the highest executive power in the Czech Republic with responsibility to the Lower House. The Czech constitution requires the bi-cameral Parliament to ratify international agreements unless Parliament decides to hold a referendum. Parliamentary ratification of international agreements requires approval of both the Lower House and the Senate with a three-fifths majority of all MPs and Senators in attendance. For EU enlargement Parliament decided to hold a referendum. It necessitated approval by a majority of the country's citizens who took part. Efforts of the centre-right opposition party, the Civic Democrats (ODS),

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<sup>1</sup> G. TSEBELIS, *Veto players: how political institutions work*, Princeton: Princeton University Press, 2002., p. 2-19.

<sup>2</sup> Note that the relationship between the number and preferences of veto players and reform is not necessarily static and/or linear. The number of formal veto players might only have an indirect relationship on the likelihood of reform, in: A. HÉRITIER and C. KNILL, Differential Responses to European Policies, in: *Gemeinschaftsgüter: Recht, Politik und Ökonomie (Max-Planck-Projektgruppe Recht der Gemeinschaftsgüter, Bonn)*, 2000, 7, pp. 32., p. 2.

to insert a minimum turnout requirement failed<sup>3</sup>. The pronouncement of the referendum's result superseded parliamentary ratification<sup>4</sup>. In other words, constitutionally the Czech Republic had three formal veto players present with the third veto player having a low threshold.

#### **6.1.1.2. Hungary**

The president participates in the development of Hungarian foreign policy. He concludes international treaties in the name of the government. In practice the president delegates his authority to government.

The government is the highest body of the state administration and is responsible for foreign policy and concluding international agreements. The Hungarian constitution assigns the power to conclude international agreements of outstanding importance such as EU membership to the single chamber Parliament. Prior parliamentary ratification under a quorum with a simple majority is necessary for conclusion of an international treaty. Parliament may set a national referendum upon the initiative by the president, the government, one-third of MPs or by 100,000 voting citizens. It must ultimately be called by Parliament<sup>5</sup>. The legislature decides whether the referendum is binding or consultative, although, any poll backed by over 200,000 signatures is automatically binding. According to the 1997 reform the ratification by referendum necessitates an approval of '25+1' per cent of the electorate regardless of the turnout<sup>6</sup>.

Constitutionally Hungary had three formal veto players present. Admittedly, the third veto player, a ratification constraint by referendum, had a particularly low threshold.

#### **6.1.1.3. Poland**

The Polish president is the state's representative in foreign affairs. He ratifies or renounces international agreements and notifies the House of Representatives (Sejm) and the Senate (Senat). The president has limited executive prerogatives. The government is the primary executive body.

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<sup>3</sup> A constitutional act providing for a referendum on EU accession was passed in October 2002 with near unanimity. The act stated that Parliament's normal powers of decision and treaty ratification on accession were to be replaced by a referendum. Accession would be approved by a simple majority of all those voting, in: S. HANLEY, *Referendum Briefing No. 6: The Czech EU accession referendum (13-14 June 2003)*, School of International Studies, Brunel University, 2003.

<sup>4</sup> *Constitution of the Czech Republic (Constitutional Act No. 1/1993 Coll. of the Czech National Council of 16th December 1992 as amended by Acts No. 347/1997 Coll., 300/2000 Coll., 448/2001 Coll., 395/2001 Coll. and 515/2002 Coll.)*, Prague, 16 December 1992. Articles 62 (1), 10a, 39 and 49. Article 49 of the Constitution stipulates that all records on human rights and fundamental freedoms, political and economic agreements and agreements which requires a law to be passed before implementation, need to be given consent by the Parliament before their ratification by the president of the Republic.

<sup>5</sup> *Constitution of the Republic of Hungary*, Budapest, 23 October 1989., articles 19, 30, 35 and 28.

<sup>6</sup> B. FOWLER, *Referendum Briefing No. 4: The Hungarian EU accession referendum (12 April 2003)*, Birmingham: Centre for Russian and East European Studies, European Research Institute, University of Birmingham, 2003.

It conducts foreign policy and concludes international agreements, which requires presidential ratification.

In the beginning of the 1990s the constitutional powers in EU-related decision-making were delegated to the government plenipotentiary for European integration and foreign assistance in the rank of an Undersecretary of State. The possibility for accession to the EU was laid down in the Polish constitution of April 1997. It provided a framework for integration with international organisations. EU related decision-making powers were delegated to the Committee of European Integration.

The Sejm can initiate a referendum. To be binding it requires a simple majority under a quorum. Alternatively, the president with the consent of the Senate under a simple majority and a quorum can decide<sup>7</sup>. The Sejm decided in favour of a nationwide referendum on EU accession with a 50 per cent turnout requirement. In other words, Poland had three formal veto players present<sup>8</sup>.

#### **6.1.1.4. Slovakia**

The president represents the Slovak Republic in international relations. He negotiates and ratifies international agreements. He can delegate the power to the government to negotiate international agreements without consent of the single chamber Parliament (the National Council). The National Council gives consent, prior to ratification, on international political treaties provided the execution requires legislation or the adoption of a constitutional law.

The government is the supreme executive body. It decides collectively on the Slovak entry into international treaties. A referendum can be called by the president upon request of a petition signed by at least 350,000 citizens, the National Council or the government. The results of the referendum are valid under a quorum provided the decision was endorsed by more than 50 percent of the participants<sup>9</sup>. In other words, constitutionally Slovakia had three formal veto players present.

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<sup>7</sup> *Constitution of the Republic of Poland as adopted by National Assembly on 2 April 1997 and Confirmed by Referendum in Oct 1997*, Warsaw, 2 April 1997, articles 125, 146 and 133.

<sup>8</sup> A. SZCZERBIAK, *Referendum Briefing No 5: The Polish EU accession Referendum (7-8 June 2003)*, Sussex: Sussex European Institute, University of Sussex, 2003.

<sup>9</sup> *The Constitution of the Slovak Republic from (including the Amendments from July 14th, 1998 and January 14th, 1999)*, Bratislava, 3 September 1992., articles 86, 102(1), 108, 119 and 95-98; K. HENDERSON, *Referendum Briefing No 7: The Slovak EU accession Referendum (16-17 May 2003)*, Leicester: Department of Politics, University of Leicester, 2003.

## **6.1.2. Policy Processes and Delegation**

Negotiating EU membership required the preparation and adjustment of national legislation to the body of EU legislation. Approximately 80,000 pages of EU legislation, the largest part pertaining on the functioning of the European single market, needed to be transposed in the countries aspiring EU membership. EU legislation affected nearly all policies and sectors in the applicant countries. The transposition took on a breathtaking pace. To accomplish this gargantuan legislative overhaul the applicants could not fall back upon an administrative EU blueprint. Partially under influence of the EU's screening exercise each country set up its idiosyncratic institutional framework and specific procedures for dealing with EU accession. Within those structures the executive created mechanisms that allowed for sectoral consultation and the formulation of TPRs.

### **6.1.2.1. Czech Republic**

Czech preparations for EU integration started before its EU membership application on 17 January 1996. The Czech government established seven institutional bodies responsible for defining and co-ordinating European policy. The MoFA co-ordinated the accession negotiations with the EU. It gained responsibility after an organisational reform in April 2000. Within the MoFA the Prague authorities set up several EU policy bodies to reinforce its administrative capacity (see Figure 33)<sup>10</sup>.

#### **Line Ministries**

The line ministries were the workhorses and the main mechanism for harmonisation of Czech legislation with the *acquis*. The EU departments, experts and officials in the line ministries formed the first line in the administration confronted with transposing the *acquis*. During the preparations for the EU accession negotiations and in response to the EC's questionnaires the line ministries set up 32(1998) to 35 (2002) working groups. Among these 23 took the lead on the most important chapters of the *acquis*<sup>11</sup>. The working groups comprised the line ministries' experts, academics and interest group representatives. Experts and members of the working

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<sup>10</sup> A. PODRAZA, *Central Europe in the Process of European Integration. A comparative Study of Strategies of the Czech Republic, Hungary, Poland and Slovakia; Towards Deepening and Widening of the European Union*, Research Support Scheme, Open Society Support Foundation, 2000., p. 6.

<sup>11</sup> Except in the Ministry of Defence, in: P. PAVLIK, *Europeanisation and Transformation of Public administration: The Case of the Czech Republic*, Prague: Institut für Europäische Politik Berlin, Jean-Monnet-Lehrstuhl für Politikwissenschaft Universität zu Köln, Centre for European Analysis, Institute of international Relations, November 2002., p. 32.

groups were invited to Brussels to share their experience with colleagues from the EC and other applicant countries.

The working groups' task commenced during the screening process of national legislation (April 1998-June 1999)<sup>12</sup>. The representatives of the working groups collected relevant information which they converted into instructions. These were passed on downstream to the respective line ministries<sup>13</sup>. Upstream, the working groups formulated non binding negotiation positions to the working committee and the working team for European integration.

The meetings at expert level set the stage for the negotiation positions. They had the most important agenda setting power in the EU related institutional process. The experts were vertically embedded in the line ministries, had knowledge of the national regulations, had built up contacts with the sector representatives over the years and were in contact with the EC. Their influence on the position papers proved substantial and based upon expertise<sup>14</sup>. At this level most TPRs emerged. Experts tended to represent the corresponding sectors of the ministries.

When a chapter of the *acquis* touched upon the authority of several ministries conflicts of interests emerged. To resolve these conflicts the responsibility for the individual chapters of the *acquis* veered towards inter-ministerial consultations among the line ministries. The MoTI, MoFI and the MoFA (OKEU) took the lead in these horizontal meetings<sup>15</sup>. From November 2000 the MoTI intensified these inter-ministerial meetings. It concentrated overall responsibility to avoid conflicts between the line ministries and remedy the high turnover of personnel<sup>16</sup>.

### **Working Committee for European Integration**

The working groups' proposals went to the working committee for European integration. It counted 30 members including the Deputy Ministers and heads of the government's central agencies. Many of its members were part of the negotiation team. The Czech Republic's chief

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<sup>12</sup> The screening is a multilateral review of national legislation and its compatibility with EU law. It is carried out by the EC and individual directorates general.

<sup>13</sup> *Interview by Author with Representative 3 of the Negotiation Team of the Czech Republic*, Prague, 19/03/2004 and 22/03/2004.

<sup>14</sup> *Interview by Author with Representative of the Confederation of the Czech Industry*, Prague, 03/05/2004.

<sup>15</sup> P. PAVLIK, *Europeanisation and Transformation of Public administration: The Case of the Czech Republic*, Prague: Institut für Europäische Politik Berlin, Jean-Monnet-Lehrstuhl für Politikwissenschaft Universität zu Köln, Centre for European Analysis, Institute of international Relations, November 2002., p 38.

<sup>16</sup> European Commission, *Pre Accession Report Czech Republic*, November 2000.

negotiator chaired the meetings. The body reported to the government committee for EU integration from which it received its powers. The working committee for European integration was a principal co-ordinating body approving the line ministries' proposals and dealing with the implementation of EU legislation. It would submit the line ministries proposals to the government committee for European Integration when it reached an accord. Otherwise the proposals would be sent back to the line ministry for clarification<sup>17</sup>.

### **Working Team for European Integration**

The working team for European integration was part of the Council of Social and Economic Agreement chaired by the PM. Its members were economic and social partners. They were represented according to a tri-partite structure (seven representatives of the employers, trade unions and the government). The chief negotiator convened and chaired the meetings. The tripartite body met for the first time in 1998 and from then onwards every six weeks. It discussed issues which had a socioeconomic impact. It was a forum where the government needed to explain its negotiation position. Its members had the legal power to influence the negotiation position. Employers and trade unions had the opportunity to use the forum to put forward TPRs and express their grievances. Nevertheless, its role was weak and remained informative and consultative<sup>18</sup>. According to a representative of the MoFA the social partners never used the forum<sup>19</sup>. When questioned about TPRs chief negotiator explained that requesting too many exemptions from the *acquis* was not in the country's interests<sup>20</sup>. Large firms would approach the government directly when their interests were at stake.

### **Negotiation Team and Chief Negotiator**

The negotiation team was formed in 1998. It initially comprised 18 members of which some also seated on the working committee for European integration. It was headed by the three double-hatted chief negotiator who was also a Deputy Minister of Foreign Affairs, State Secretary for European Affairs in the MoFA and methodically supervising the Office of European Integration (OEI) in the Prime Minister's Office of the Government (PMO). His position and that of the members of his team was established and appointed by the government. The team's members –

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<sup>17</sup> A. PODRAZA, *Central Europe in the Process of European Integration. A comparative Study of Strategies of the Czech Republic, Hungary, Poland and Slovakia; Towards Deepening and Widening of the European Union*, Research Support Scheme, Open Society Support Foundation, 2000., p. 7.

<sup>18</sup> Interview by Author with Representative of the Czech Trade Union of the Steel Industry, Prague, 22/03/2004a.

<sup>19</sup> Interview by Author with Representative of the Ministry of Finance of the Czech Republic, Prague, 24/03/2004b.

<sup>20</sup> Interview by Author with Representative of the Czech Confederation of Trade Unions (CMKOS), Prague, 23/03/2004b.

later reduced to 11 and subsequently to 8 by the end of the negotiations<sup>21</sup>– comprised three diplomats, high-level civil servants from the MoFI, MoTI, MoJ, MoI, MoA, Centre for Environmental Issues at Charles University and the Czech National Bank (CNB). They met formally every two to three months at the MoFA<sup>22</sup>. They did not represent the line ministries and their tasks concerned horizontal issues. Its members were individually responsible for designated chapters of the acquis. Frictions arose between the negotiation team and the expert groups in the line ministries.

The team was very much plugged into the EC community in Brussels. Particularly towards the end of the negotiations members of the team often worked out negotiation positions without consulting the line ministries. These amended positions were then presented as a *fait accompli* to the ministry for a signature<sup>23</sup>. For the position paper to be approved the responsible line ministry and the MoFA always needed to co-sign<sup>24</sup>. The chief negotiator, however, did not have the capacity to change commodity specific positions papers set at the level of the line ministry and co-signed by the MoFA. He could change the general Czech negotiation position<sup>25</sup>. All the interviewees argued that the contribution of negotiation team was limited. The centre of gravity in the negotiations moved to the MoFA. As negotiations progressed the MoFA would directly contact the experts in the various institutions bypassing several institutions<sup>26</sup>.

### **Ministry of Foreign Affairs**

The MoFA co-ordinated the accession negotiations with the EU. It gained in responsibility after an organisational reform in April 2000. The MoFA steered the Czech mission to the EU. The mission had direct links with the line ministries with more than half of its 40 staff coming from the line ministries. The remaining personnel consisted of diplomats. The mission offered expertise and liaised with EU institutions and EU member states. It could not set EU policy. It supported the chief negotiator during the accession negotiations with the provision of relevant information from the EU.

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<sup>21</sup> Interview by Author with Representative 3 of the Negotiation Team of the Czech Republic, Prague, 19/03/2004 and 22/03/2004.

<sup>22</sup> Interview by Author with Representative 2 of the Negotiation Team of the Czech Republic, Prague, 25/03/2004.

<sup>23</sup> Interview by Author with Representative 1 of the Negotiation Team of the Czech Republic, Prague, 23/03/2004a.

<sup>24</sup> Interview by Author with Representative of the Ministry of Finance of the Czech Republic, Prague, 24/03/2004b.

<sup>25</sup> Ibid.

<sup>26</sup> P. PAVLIK, *Europeanisation and Transformation of Public administration: The Case of the Czech Republic*, Prague: Institut für Europäische Politik Berlin, Jean-Monnet-Lehrstuhl für Politikwissenschaft Universität zu Köln, Centre for European Analysis, Institute of international Relations, November 2002., p. 32.



The MoFA was very much engaged in the international accession game and wanted to compete with the other applicant states over EU membership. Of all domestic institutions it bought in to the EC's naming and shaming during the annual progress reports. Representatives of the MoFI complained that the MoFA disregarded the quality of EU membership in favour of swift EU accession<sup>27</sup>.

### **Prime Minister's Office (PMO)**

The government had a final say over EU enlargement policy through the creation of the government committee for European integration with an advisory role<sup>28</sup>. Initially, the Committee counted 12 members<sup>29</sup>. In February 2000 the cabinet decided to change the statute of the Committee in an effort to streamline the procedures and speed up the alignment of Czech legislation. The government willing to accelerate the negotiations reduced its size at the advantage of the MoFA<sup>30</sup>. The Committee's standing membership, the board or presidency, was restricted to five and comprised the Minister of Foreign Affairs (chair), the Ministers of Labour and Social Affairs, and Finance, the Chairman of the Legislative Board of the Government and the chief negotiator (secretary). Non standing members did not have vote in the Committee and comprised executives of other central administration bodies such as the Governor of the CNB, the head of the mission to the EU and the president's representative. Its members would meet at least every two months. The meetings were closed and held at the PMO and called by the Minister of Foreign Affairs.

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<sup>27</sup> For instance, the MoFI was prohibited to co-operate on specific issues with other countries because it was argued that this could negatively influence the Czech Republic's relative position in the EU accession process, in: *Interview by Author with Representative of the Ministry of Finance of the Czech Republic*, Prague, 24/03/2004b.

<sup>28</sup> *Interview by Author with Representative 3 of the Negotiation Team of the Czech Republic*, Prague, 19/03/2004 and 22/03/2004.

<sup>29</sup> P. PAVLIK, *Europeanisation and Transformation of Public Administration: The Case of the Czech Republic*, Prague: Institut für Europäische Politik Berlin, Jean-Monnet-Lehrstuhl für Politikwissenschaft Universität zu Köln, Centre for European Analysis, Institute of International Relations, November 2002., p. 33.

<sup>30</sup> European Commission, *Pre Accession Report Czech Republic*, February 2000.; Government of the Czech Republic, *Resolution of the Government of the Czech Republic concerning the proposal to change the resolution of the Government No. 1333 from 13th December 1999, on the proposal to make changes in the institutional facilitation of the integration of the Czech Republic to the European Union*, Prague, 14th January 2001. As a rule (2000) decisions were taken unanimously with the Minister of Foreign Affairs having a deciding vote, in: M. BRUSIS and J.A. EMMANOUILIDIS, *Negotiating EU Accession: Policy Approaches of Advanced Candidate Countries from Central and Eastern Europe*, Bertelsmann Foundation, Bertelsmann Group for Policy Research, Centre for Applied Research, July 2000., p. 2.

The Committee was an expert, advisory, co-ordination and initiating organ of the government. It defined and co-ordinated EU enlargement policy<sup>31</sup>. The members co-ordinated the Czech preparation for EU membership, laid out priorities defined during the EU negotiation talks, supervised the process of legal harmonisation and co-ordinated activities of various ministerial departments in their relations with institutions of the EU<sup>32</sup>. It handled inter-ministerial disputes and could change individual negotiation positions<sup>33</sup>. The committee also dealt with the government's communication strategy on the state of preparation for EU membership. Decisions were adopted under a quorum with at least half of the members present. The Committee presented decisions to the government in the form of resolutions for approval. It co-operated with the Chamber of Deputies and the Senate and their respective Committees for European Integration.

Because the committee had too large a number of senior executives some ministries preferred to contact the EU directly. The Committee turned out to be an access point for large companies present in export markets<sup>34</sup>.

### **Parliament**

In addition to its Foreign Affairs Committee the Czech Lower House set up a Committee for European integration in July 1998. The former was responsible for foreign policy issues including the expression of its consent on international agreements. The latter was responsible for monitoring all aspects of the Czech Republic's integration into the EU. The Committee for European Integration co-ordinated its activities with the sub-committee on European Affairs in the Senate founded in December 1998<sup>35</sup>. It had a right to propose and veto legislation sent by the Lower House when it considered an item incompatible with Czech legislation.

Parliament's power was substantial. Nevertheless, its influence and that of parliamentary committees was dependent on the actual political composition of both chambers. Their decisions

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<sup>31</sup> A. PODRAZA, *Central Europe in the Process of European Integration. A comparative Study of Strategies of the Czech Republic, Hungary, Poland and Slovakia; Towards Deepening and Widening of the European Union*, Research Support Scheme, Open Society Support Foundation, 2000., p. 7.

<sup>32</sup> *Ibid.*, p. 7.

<sup>33</sup> *Interview by Author with Representative of the Ministry of Finance of the Czech Republic*, Prague, 24/03/2004b.

<sup>34</sup> *Interview by Author with Representative of the Confederation of the Czech Industry*, Prague, 03/05/2004.

<sup>35</sup> A. PODRAZA, *Central Europe in the Process of European Integration. A comparative Study of Strategies of the Czech Republic, Hungary, Poland and Slovakia; Towards Deepening and Widening of the European Union*, Research Support Scheme, Open Society Support Foundation, 2000., pp. 7-8;

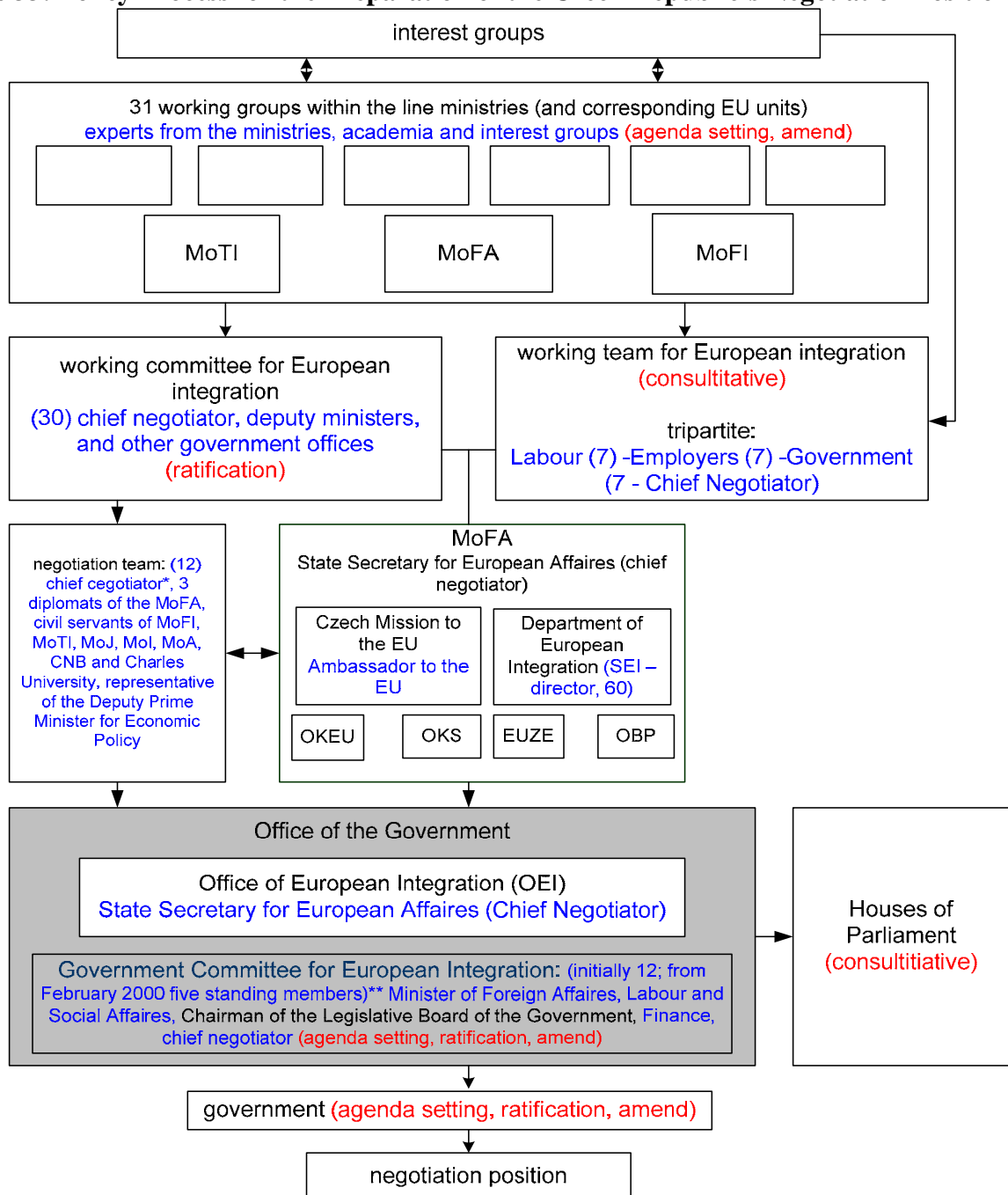
depended on the political will of the major political parties<sup>36</sup>. In 1999 the government attempted to adopt a constitutional law, which would have allowed EU related legislative to pass by decree. In January 2000 the government succeeded in reducing parliamentary procedures that required three readings for EU-legislation to pass<sup>37</sup>. Not one MP in his respective legal personality was represented in the executive institutional structure handling EU membership. While the parliament was necessitated to pass all EU related legislation over a relatively short period of time the accession process was overwhelmingly managed by the Czech executive and insulated from political or partisan pressures.

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<sup>36</sup> P. PAVLIK, *Europeanisation and Transformation of Public administration: The Case of the Czech Republic*, Prague: Institut für Europäische Politik Berlin, Jean-Monnet-Lehrstuhl für Politikwissenschaft Universität zu Köln, Centre for European Analysis, Institute of international Relations, November 2002., pp 34-35.

<sup>37</sup> M. BRUSIS and J.A. EMMANOUILIDIS, *Negotiating EU Accession: Policy Approaches of Advanced Candidate Countries from Central and Eastern Europe*, Bertelsmann Foundation, Bertelsmann Group for Policy Research, Centre for Applied Research, July 2000., p. 4.

**Figure 33: Policy Process for the Preparation of the Czech Republic's Negotiation Position**



Note: (\*) chief Negotiator = State Secretary of European Affairs (PMO) = First Deputy Foreign Minister (MoFA)  
 (\*\*) initially including Ministers of Interior, Justice, Industry and Trade, Regional Development and Agriculture. Decisions were taken by consensus. In case of disagreement the Minister of Foreign Affairs decided. From 2000 onwards decisions were taken by a quorum and a simple majority.  
 blue=membership; red=decision-making rule; grey = primary decision making body

Source: Own compilation based on interviews with ministerial and government representatives, and Europeanisation literature: A. PODRAZA, *Central Europe in the Process of European Integration. A comparative Study of Strategies of the Czech Republic, Hungary, Poland and Slovakia Towards Deepening and Widening of the European Union*. Research Support Scheme. Open Society Support Foundation, 2000; P. PAVLIK, *Europeanisation and Transformation of Public administration: The Case of the Czech Republic*. Prague: Institut für Europäische Politik Berlin, Jean-Monnet-Lehrstuhl für Politikwissenschaft Universität zu Köln, Centre for European Analysis, Institute of international Relations, November 2002.

### Negotiation Positions

Regardless of the seven bodies dealing with EU accession the formulation of a negotiation position involved only four active administrative levels, i.e. the line ministries, the negotiation team, the PMO and the government<sup>38</sup>. The contours of a negotiation position were reached at expert level in the line ministries<sup>39</sup>. The first drafts of the Czech position documents were prepared during the screening process.

The respective line ministry was the responsible co-ordination entity for each national position document. Once it approved a position paper in co-operation with the working committee and working team the MoFA would co-sign the position paper. Sensitive issues required submission for approval to the government committee for European integration and the government. The Parliament did not have any decision-making capacity. Some symbolic and controversial issues were discussed in both chambers. The government always kept a final say. The government attempted to reduce Parliament's influence on a number of occasions<sup>40</sup>. After the adoption of the position paper the positions were presented to the parliamentary committees and the general public.

Most TPRs in the position papers originated on a firm or sectoral level. They were transmitted at the level of the line ministries. During the meetings held with EC experts TPRs would often be eliminated or reduced in length and scope. According to the Czech Confederation of Industry consultations also took place at the level of the working team and the government committee for European integration. Larger companies argued that Czech business associations and authorities were not effective<sup>41</sup>. Czech companies that concentrated on the domestic market were less informed about the impact of EU legislation. Companies operating in export markets had experience in dealing with the EU and were much better informed<sup>42</sup>.

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<sup>38</sup> Interview by Author with Representative of the Office of the Government of the Czech Republic, Prague, 04/05/2004d.

<sup>39</sup> The screening occurred between April 1998 and June 1999. From 2000 onwards screening updates were carried out for newly adopted legislation.

<sup>40</sup> P. PAVLIK, *Europeanisation and Transformation of Public administration: The Case of the Czech Republic*, Prague: Institut für Europäische Politik Berlin, Jean-Monnet-Lehrstuhl für Politikwissenschaft Universität zu Köln, Centre for European Analysis, Institute of International Relations, November 2002, pp 37-38.

<sup>41</sup> Interview by Author with Representative of the Ministry of Foreign Affairs of the Czech Republic, Prague, 04/05/2004b.

<sup>42</sup> Interview by Author with Representative of the Confederation of the Czech Industry, Prague, 03/05/2004.

Seldom would the government or the negotiation team initiate TPRs. Usually government involvement would result in the reduction of TPRs. Generally TRPS were not based on impact studies of the acquis on the Czech Republic. Only a limited number of studies existed<sup>43</sup>. According to several interviewees impact studies were notoriously difficult to come by. The state administration did not have the resources and know how to commission or execute studies on the impact of EU legislation<sup>44</sup>. The line ministries and the chief negotiator had little quantitative material at their disposal.

The absence or lack of impact studies put downward pressure on the number and scope of the TPRs. The Czech Republic lacked hard evidence and data when discussing TPRs with the EC. For each TRP the EC required detailed arguments including time tables with intermediate targets. During the discussions Prague rarely withstood the EC's technical pressure: 'Not enough impact studies were performed to have exemption from the acquis. If you want to focus on EU accession under different conditions you need more studies, expertise and arguments, which we did not have. Our capacity compared to the EU was much more limited in that respect'<sup>45</sup>.

The EC's objective was to limit and reduce TPRs in the consecutive rounds of consultation before the negotiations<sup>46</sup>. The EC's general attitude was not to negotiate TPRs. There was not a willingness to increase their scope or duration: 'If they do not come up with it, we are not going to tell them. Quite often we were surprised that the applicant countries did not ask for TPRs in areas where the perception was that for 95 per cent they were not able to comply'<sup>47</sup>. During the many consultations between the EC and the Czech authorities the EC signalled that requesting TPRs meant the country was not ready for EU membership. The EC also made clear what was acceptable: 'One does ask for a TPR of five instead of 10 years. The goal was to join the EU, not to protect the national interests or to prevent, to reduce the impact of EU membership and certainly not the social impact it had. It was important for the Czech Republic to be as flexible as possible'<sup>48</sup>.

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<sup>43</sup> Interview by Author with Representative of the Ministry of Foreign Affairs of the Czech Republic, Prague, 04/05/2004b.

<sup>44</sup> Interview by Author with Representative of the Office of the Government of the Czech Republic, Prague, 04/05/2004d. Interview by Author with Representative of the Czech National Bank Prague, 04/05/2004a.

<sup>45</sup> Interview by Author with Representative of the Confederation of the Czech Industry, Prague, 03/05/2004.

<sup>46</sup> Interview by Author with Representative of the Ministry of Finance of the Czech Republic, Prague, 24/03/2004b.

<sup>47</sup> Interview by Author with representative of the EC's Delegation to the Czech Republic Prague, 24/03/2004a.

<sup>48</sup> Interview by Author with Representative 1 of the Negotiation Team of the Czech Republic, Prague, 23/03/2004a.

The finding follows what *Mayhew* calls *the precautionary principle* or the attempt by governments to reduce the number of TPRs to a minimum in order to speed up the negotiations<sup>49</sup>. Conformingly, the Czech administration had a tendency to limit or not to request TPRs: ‘If you want many TPRs you do not really want to become a member of the EU. You cannot ask for long and wide TPRs without endangering your accession. We had to compromise somehow as we could not give a bad impression’<sup>50</sup>. At the end of the screening exercise and the preparation of all position papers the Czech Republic counted between 100-150 problem areas where TPRs were warranted<sup>51</sup>. Quite a few were rejected, set aside, or their scope and duration reduced. The government even discussed whether the country really needed them<sup>52</sup>. Towards the end of the process the government’s benchmark to put through a request was based on the available time left, the politicised nature of the proposal and the budgetary impact of the TPRs: ‘At the end of the day the choice of the government came down to the budget and the financial aspects of enlargement. The Czech Republic had to be careful as it had just become member of NATO, which was very costly. EU membership will cost us even more’<sup>53</sup>.

Czech business representatives feared that TPRs would encourage the EU to take a similar approach. For instance the Austrian and German trade unions were conducive to lobbying their respective governments and raise the barrier for EU membership. Therefore, the social partners, chief negotiator and the government were very careful when putting more issues on the table<sup>54</sup>. The representatives of the business associations discovered that the EC’s reluctance and the government’s observance of the precautionary principle led to a reduction of TPRs before the negotiations had even started: ‘We did not want to take chances. Often we set aside TPRs where possible as most were not necessarily a cushion for the country but often the result of conflicting lobbies’<sup>55</sup>. Because Prague authorities’ reluctance to put TPRs on the table they advised large companies to contact the EU directly.

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<sup>49</sup> A. MAYHEW, *Enlargement of the European Union: an analysis of the negotiations with the central and eastern European candidate countries*, Brighton: University of Sussex, 2000., pp. 18-19.

<sup>50</sup> Interview by Author with Representative 3 of the Negotiation Team of the Czech Republic, Prague, 19/03/2004 and 22/03/2004.

<sup>51</sup> Interview by Author with Representative of the Ministry of Foreign Affairs of the Czech Republic, Prague, 04/05/2004b.

<sup>52</sup> Interview by Author with Representative of the Czech National Bank Prague, 04/05/2004a.

<sup>53</sup> Ibid.

<sup>54</sup> Interview by Author with Representative of the Czech Confederation of Trade Unions (CMKOS), Prague, 23/03/2004b.

<sup>55</sup> Interview by Author with Representative of the Office of the Government of the Czech Republic, Prague, 04/05/2004d.

The reluctance to endorse TPRs was also manifest on a sectoral level. Czech pharmaceuticals companies and subsidiaries of foreign companies active on the Czech market contacted the MoI. Czech companies asked for TRPs. Foreign subsidiaries pressed Prague to apply EU legislation retroactively. The ministry objected to a TPR. EU legislation in the area of pharmaceuticals was associated with the modernisation and sectoral progress. It was only at the end of the negotiations that the Czech chief negotiator, Mr. *Pavel Telicka*, changed his mind<sup>56</sup>. The process was similar for the steel industry. The administration was reluctant to pressure the EU. The EC's mandate on steel was very limited. It felt that the EU MS frequently asked the EC to inform them about progress on the industry<sup>57</sup>.

The Czech Republic initially agreed to full adoption of the transport acquis. Afterwards the EU requested a TPR for cabotage. Consultations between the employers, chief negotiator and the PM concluded that only affect 5 per cent of the drivers. Despite the fact that cabotage was a growth market the volume of business at the time proved too low. The MoT did not object to the EU's TPR and neither did the employers or trade unions<sup>58</sup>. Telicka attempted to use the EU's request as a bargaining chip in other sectors<sup>59</sup>. The MoFA together with the team prepared a new position paper. It subsequently presented it to the line ministry for a signature. It prolonged the transport negotiations with two months without results<sup>60</sup>.

#### **6.1.2.2. Hungary**

The institutional preparations for EU membership started in the mid 1990s. Many of the institutional structures for negotiating the EAs were adjusted for the preparations of EU membership (see Figure 34)<sup>61</sup>.

#### **Line Ministries**

For the 77 screening rounds in Hungary the line ministries established 31 (later 29) inter-ministerial groups corresponding to the 31 (29 chapters in the negotiations) chapters of the acquis. The line ministries appointed the five to ten member strong groups, including outside experts and representatives of interest groups. They were headed by a representative of the State

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<sup>56</sup> Interview by Author with Representative 3 of the Negotiation Team of the Czech Republic, Prague, 19/03/2004 and 22/03/2004.

<sup>57</sup> See European Commission, *Pre Accession Reports Czech Republic*, March 1998-September 2002.

<sup>58</sup> Interview by Author with Representative of the Ministry of Transport of the Czech Republic, Prague, 22/03/2004b.

<sup>59</sup> Interview by Author with Representative of the Czech Confederation of Trade Unions (CMKOS), Prague, 23/03/2004b.

<sup>60</sup> Interview by Author with Representative 1 of the Negotiation Team of the Czech Republic, Prague, 23/03/2004a.

<sup>61</sup> Interview by Author with Representative of the Ministry of Finance of Hungary, Budapest, 06/02/2004 and 18/02/2004.



Secretariat for Integration and Trade (SSI-T) of the MoFA. The groups performed the main preparatory work for the screening rounds and kept regular contact with their counterparts in the mission and the EC as well as with corresponding sectoral interests. The heads held the responsibility for one chapter of the acquis and the preparation of the first position paper. Meetings were held at least every two months with some 20-40 participants<sup>62</sup>. From 1998 the inter-ministerial working groups became expert groups which included experts with horizontal responsibilities from the MoFA, MoFI, and the MoJ. Representatives of these three ministries were always involved at every level of the domestic decision-making processes<sup>63</sup>.

The line ministries had the obligation to consult economic and social partners when formulating the position papers on matters within their competence. Expert groups were obliged to contact professional associations before finalising proposals. Most TPRs that later appeared in the position papers emerged at this level. The line ministries and expert groups stood close to the interests of the respective sectors. They were well informed and knew the sectoral concerns<sup>64</sup>.

#### **Inter-ministerial Committee for European Integration**

The inter-ministerial committee for European integration (ICEI) organised overall co-ordination and served as a channel of communication between ministries. It comprised several inter-ministerial working groups and representatives at State Secretary, Deputy State Secretary or head of department level with the head of the SSI-T from the MoFA at the helm. The ICEI met regularly during the screening process. It mobilised all the relevant actors in the ministries and discussed the preparations of EU-related government decisions. It reported to the government through the MoFA<sup>65</sup>. As the negotiations advanced the negotiation delegation and the MoFA gained in importance. The ICEI's power declined and its meetings became less frequent.

#### **European Integration Council (EIC)**

Economic and social partners had the opportunity to express their opinion in the European Integration Council (EIC). It was established in 1998 and counted 20 members from trade unions,

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<sup>62</sup> Co-ordination of accession negotiations, in: [www.mfa.gov.hu](http://www.mfa.gov.hu) (2004); A. PODRAZA, *Central Europe in the Process of European Integration. A comparative Study of Strategies of the Czech Republic, Hungary, Poland and Slovakia; Towards Deepening and Widening of the European Union*, Research Support Scheme, Open Society Support Foundation, 2000., p. 32-33.

<sup>63</sup> Interview by Author with Representative of the Hungarian Competition Office, Budapest, 05/02/2004.

<sup>64</sup> Getting Closer to EU Membership, An Interview with Endre Juhász, Ambassador of Hungary to the EU and Chief Negotiator for Accession, in: *The Hungarian Quarterly*, Autumn 2001, XLII(No. 163), pp. 10., p. 11.

<sup>65</sup> V.K. PYSZNA DOROTA, *The Management of Accession to the European Union in Poland and Hungary*, Budapest: Hungarian Academy of Sciences, October 2002., pp 60-61.

business associations, chambers of commerce, special interest groups and representatives from the political parties. The MoFA convened and chaired the meetings. It brought together organisations representing the widest possible interests and formulated the negotiation positions for the accession talks. Officially the EIC was the only formal body which had influence on the EU-related decisions of the government. Informally, however, some of the biggest firms directly approached the government when their specific interests were at stake<sup>66</sup>.

The government's and MoFA's concerted effort to consult business associations, industry confederations and trade unions worked well. All major sectors in the economy had an opportunity to express their opinion and put forward TPRs if they had not already done so on an expert level<sup>67</sup>: 'In order of importance the negotiations obviously included business interests, economic sectors and society. Questionnaires on the application and impact of the *acquis* were put forward. We asked industry which issues potentially could create a problem and how serious'<sup>68</sup>.

In the beginning the Hungarian institutional structures provided for a thorough consultation procedure on EU accession. The authorities accepted all the business associations' and economic sectors' TPRs. Later on in the process not every request was accepted. Conflict emerged between the line and the co-ordinating ministries, particularly with the MoFA, which rendered agreements with the associations difficult<sup>69</sup>. Once the negotiations started the MoFA kept the EIC on tight leash. The MoFA did not want the negotiations to derail because of business interests<sup>70</sup>.

Only in exceptional cases would some of the largest firms directly approach the government when their interests were at stake<sup>71</sup>. Sometimes large companies would use EU channels for their interest representation. For instance, 48 large companies heavily affected by EU tax legislation organised and lobbied the government, the EC and individual EU member states<sup>72</sup>.

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<sup>66</sup> Interview by Author with the Chief Negotiator of Hungary, Budapest, 09/02/2004.

<sup>67</sup> Getting Closer to EU Membership, An Interview with Endre Juhász, Ambassador of Hungary to the EU and Chief Negotiator for Accession, in: *The Hungarian Quarterly*, Autumn 2001, XLII(No. 163), pp. 10., p. 11.

<sup>68</sup> Interview by Author with Representative of Ministry of Foreign Affairs of Hungary, Budapest, 13/02/2004.

<sup>69</sup> Interview by Author with Representative of the Ministry of Finance of Hungary, Budapest, 06/02/2004 and 18/02/2004.

<sup>70</sup> Interview by Author with Representative of the Steel Trade Union of Hungary, Budapest, 10/02/2004b.

<sup>71</sup> Getting Closer to EU Membership, An Interview with Endre Juhász, Ambassador of Hungary to the EU and Chief Negotiator for Accession, in: *The Hungarian Quarterly*, Autumn 2001, XLII(No. 163), pp. 10., p. 11.

<sup>72</sup> Interview by Author with Representative of the Ministry of Finance of Hungary, Budapest, 06/02/2004 and 18/02/2004.

### **Negotiation Team and Chief Negotiator**

The negotiation team was responsible for relations with the EU. It counted 12 members with the Minister of Foreign Affairs at the helm. The negotiation team was a rather informal body meeting at least once a month in Budapest<sup>73</sup>.

The chief negotiator was the prime contact for the EU. Exceptionally among the applicant countries he had a double hatted function as the head of the Hungarian mission to the EU and as chief negotiator<sup>74</sup>. He evaluated and developed the strategy in the negotiations. He negotiated formally at deputy level during the accession conferences, substituted for the Minister of Foreign Affairs during intergovernmental negotiations at Coreper level and conducted informal negotiations<sup>75</sup>.

Based upon information from Brussels he prepared proposals for the government. He regularly modified the initial negotiation positions and formulated new positions on the spot. The PM or the Minister of Foreign Affairs would only take important decisions in consultation with the State Secretary for European Integration and the chief negotiator<sup>76</sup>.

### **Ministry of Foreign Affairs**

As Hungary did not have a Minister for European Affairs the MoFA played the key role in defining, co-ordinating and executing Hungary's EU accession policy. Within the MoFA the point of gravity for the accession process lay with the State Secretariat for Integration (SSI). It was headed by the State Secretary for Integration or the Deputy Foreign Minister. The SSI (about 80 officials) supported the negotiation team, inter-ministerial committee for European integration and the EIC. Under the *Medgyessy* cabinet the SSI became the SSI-T with expanded responsibilities. The new body resolved the problem of overlapping competencies and rivalry between the MoFA and the MoTI. Its structure ensured a single co-ordination between diplomatic and sectoral expert skills ensuring sufficient synergy in the preparations for membership. The

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<sup>73</sup> It comprised the Head of the SSI-T, chief negotiator and representatives of State Secretariat for Integration, the MoFI, MoJ, MoE, MoA, MoRD, MoI, MoTr, MoEn, PMO and the Hungarian National Bank, in: V.K. PYSZNA DOROTA, *The Management of Accession to the European Union in Poland and Hungary*, Budapest: Hungarian Academy of Sciences, October 2002., p 60.

<sup>74</sup> Only in Hungary did the chief negotiator take up the position of Ambassador to the EU.

<sup>75</sup> Coreper is the Committee of Permanent Representatives composed of the heads (coreper II) and deputies (coreper I) of the member states' permanent representations in Brussels.

<sup>76</sup> Getting Closer to EU Membership, An Interview with Endre Juhász, Ambassador of Hungary to the EU and Chief Negotiator for Accession, in: *The Hungarian Quarterly*, Autumn 2001, XLII(No. 163), pp. 10.

SSI-T became the key institution for EU related decision-making. It did not handle vertical or sectoral issues<sup>77</sup>.

The Minister of Foreign Affairs led the accession process and headed the Hungarian EU delegation. He represented the government in the Association Council and via the chief of the SSI-T in the Association Committee<sup>78</sup>. He also represented all EU accession related issues to the government and the Parliament<sup>79</sup>. As the main responsible for the EU accession process the Minister of Foreign Affairs would be criticised in the Parliament when negotiations stalled, particularly when the government was seen as unable to deliver on EU membership. The pressure contributed to the rising importance of the MoFA. Its increasing insulation from the other administrative structures. Furthermore, the MoFA was plugged into the negotiation game in Brussels and attempted to prevent any derailment of the process in the domestic arena. Some ministries failed to contact the MoFA for information on negotiations positions: ‘The MoFA privatised the accession negotiations’.

### **Prime Minister’s Office (PMO)**

The government approved all major decisions. Only in exceptional cases did it mediate technical issues during the preparatory phase. The Medgyessy government set up the European integration cabinet. It was headed by the PM and comprised the Minister of Foreign Affairs (vice-chair), Justice, Finance, Interior, Industry, Trade and Tourism and Agriculture. Other ministers could be invited. The integration cabinet was a preparatory body that met every fourth night and outlined conceptual issues, the national preparation, the work of individual ministries, the preparations for the eventual referendum and the communication strategy. The government approved all written negotiating positions in full plenary session according to a well-established procedure for normal government decision-making<sup>80</sup>.

### **Parliament**

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<sup>77</sup> V.K. PYSZNA DOROTA, *The Management of Accession to the European Union in Poland and Hungary*, Budapest: Hungarian Academy of Sciences, October 2002., pp 59-60.

<sup>78</sup> Getting Closer to EU Membership, An Interview with Endre Juhász, Ambassador of Hungary to the EU and Chief Negotiator for Accession, in: *The Hungarian Quarterly*, Autumn 2001, XLII(No. 163), pp. 10.

<sup>79</sup> V.K. PYSZNA DOROTA, *The Management of Accession to the European Union in Poland and Hungary*, Budapest: Hungarian Academy of Sciences, October 2002., p. 59.

<sup>80</sup> Getting Closer to EU Membership, An Interview with Endre Juhász, Ambassador of Hungary to the EU and Chief Negotiator for Accession, in: *The Hungarian Quarterly*, Autumn 2001, XLII(No. 163), pp. 10.

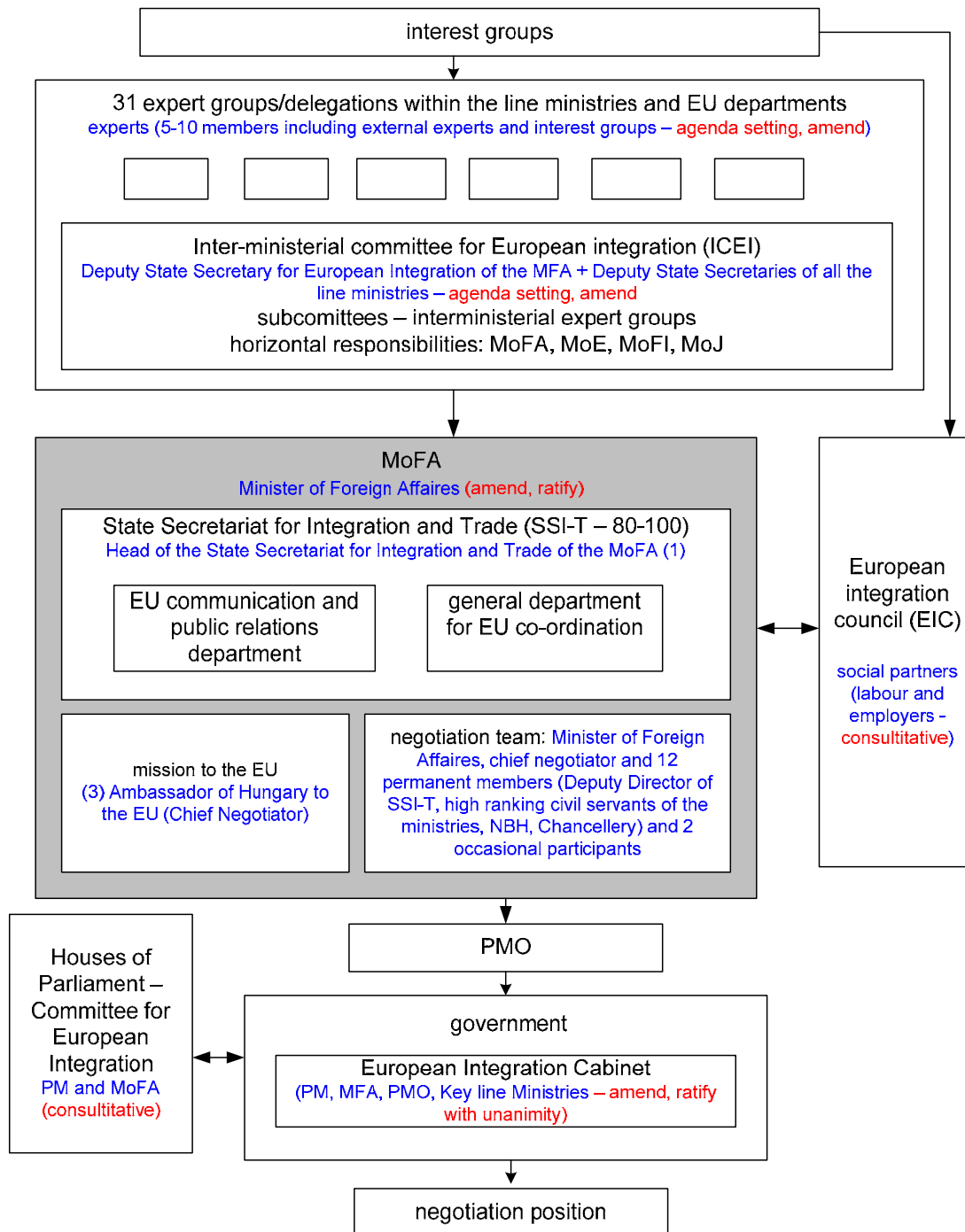
The single-chamber parliament established a standing Committee on European Integration in June 1992. It was responsible for all aspects in the relations with the EU. It established international contacts through the EU-Hungarian Joint Parliamentary Committee and the committees on European affairs of the other applicant countries<sup>81</sup>. Within the Parliament, the Committee for European Integration was the 6<sup>th</sup> most important committee out of a total of 23 committees.

The Parliament participated in the legal harmonisation process. It refrained from subjecting EU membership to a bi-partisan political struggle. In a joint declaration of September 2000 all political parties agreed on promoting legal harmonisation in the Parliament. The declaration prevented blockages of EU related matters as a result of party clashes. Furthermore, it had little say in the accession negotiations. MPs could express their views but without binding effect. From 1999 onwards MPs could scrutinise the government's EU accession drive during an annual debate in the plenary session. The Minister of Foreign Affairs introduced and the PM concluded the debate. Not one MP in his respective legal personality was represented in the executive institutional structure handling EU membership. In other words, while the parliament was necessitated to pass all EU related legislation over a relatively short period of time the accession process was overwhelmingly managed by the Hungarian executive and insulated from political or partisan pressures.

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<sup>81</sup> A. PODRAZA, *Central Europe in the Process of European Integration. A comparative Study of Strategies of the Czech Republic, Hungary, Poland and Slovakia; Towards Deepening and Widening of the European Union*, Research Support Scheme, Open Society Support Foundation, 2000., p. 33-34.

**Figure34: Policy Process for the Preparation of Hungary's Negotiation Position**



Note: Chief Negotiator = Head of the Hungarian Mission to the EU  
 Source: Own Compilation on the basis of interviews with ministerial and government representatives and literature: A. PODRAZA, *Central Europe in the Process of European Integration. A comparative Study of Strategies of the Czech Republic, Hungary, Poland and Slovakia Towards Deepening and Widening of the European Union*, Research Support Scheme, Open Society Support Foundation, 2000; V.K. PYSZNA DOROTA, *The Management of Accession to the European Union in Poland and Hungary*, Budapest: Hungarian Academy of Sciences, October 2002; Getting Closer to EU Membership, An Interview with Endre Juhász, Ambassador of Hungary to the EU and Chief Negotiator for Accession, in: *The Hungarian Quarterly*, Autumn 2001, XLII(No. 163).

### **Negotiation Positions**

Seven institutions were created to deal formally with the preparations of the EU enlargement. A negotiation position would generally be reached after making its way through four levels of government, i.e. the line ministries and expert groups, the ICEI, the MoFA and the European Integration cabinet. EU related decision making in Hungary was guided by three principles: (a) ministerial responsibility; (b) inter-ministerial co-ordination with a leading role for the SSI-T under the auspices of the MoFA; and (c) speaking with one voice to the EU. The principles resulted in a highly concentrated responsibility over EU accession at the MoFA. According to the chief negotiator the EU recognised that the system was highly efficient and recommended it to other applicant states<sup>82</sup>.

Preparations for the negotiation positions started during the screening rounds. By the end of 1998 Budapest was expected to identify the legislative gaps in the position papers. The position papers were the result of different rounds of well organised consultations and negotiations between the different parties including the EC. Sometimes these rounds were complemented by informal rounds at various levels. On a domestic level two questions prevailed: Was the status quo possible and for how long? And how to present TPRs when warranted? Decisions were made on the basis of evaluation papers, which resulted from the meetings with the sectoral representatives, firms and associations<sup>83</sup>.

The line ministries under the co-ordination of the MoFA and more specifically the SSI-T prepared the draft negotiating positions. The SSI-T adjusted the interests of the different ministries in the inter-ministerial committee, which proved to be an ideal forum for interest conciliation. Conflicts at the expert level were resolved politically. The Minister of Foreign Affairs presented the position papers to the government.

Within the MoFA the chief negotiator formulated the draft positions on the basis of the proposals of the expert groups in the line ministries. If a position had to be changed in the course of the negotiations the MoFA requested the government for a new mandate. The position papers were

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<sup>82</sup> Getting Closer to EU Membership, An Interview with Endre Juhász, Ambassador of Hungary to the EU and Chief Negotiator for Accession, in: *The Hungarian Quarterly*, Autumn 2001, XLII(No. 163), pp. 10.

<sup>83</sup> Interview by Author with Representative of the Hungarian Ministry of Economy and Transport, Budapest, 10/02/2004a.

forwarded to the government with final approval reserved for the PM and his cabinet. Governmental approval including the mandate to negotiate was automatic. The PM would only decide in rare and urgent cases: ‘Very few decisions went up to the Prime Minister or Prime Minister level’<sup>84</sup>. The chief negotiator would then present the adopted positions to the intergovernmental conference on accession. Throughout the process the position papers were kept confidential. Their content was only revealed *ex post*. Position papers were not public with the exception of the first official position papers. According to the chief negotiator confidentiality served flexibility: ‘you do not want to tie your hands in the negotiations. The EU’s common negotiation position was also confidential’<sup>85</sup>.

In the beginning almost all issues would go through the different administrative levels. As the negotiations progressed issues were informally decided. Agreed positions would receive clearance *ex-post*. Reaching a negotiation position would take around two weeks under a shortened procedure. Experts would make direct proposals to the negotiating team. The MoFA subsequently would make a decision whether the TPR would go forward. In the MoFA the benchmark for TPRs acceptance was related to the politicised nature of the proposal and its budgetary impact. At the end of the process the chief negotiator and members of the team agreed on negotiation positions on an ad hoc basis obtaining approval *ex post*<sup>86</sup>.

For each position paper the EC would be involved before it reached government level. The EC would receive all the draft position paper. According to the chief negotiator ‘the first draft position papers were in a sense an attempt to gauge what was realistically possible’. The EC let it known informally that TPRs of more than ten years in duration were unrealistic. The norm was five years. In some cases it was seven years. In exceptional cases it was more. After consultation with the EC the chief negotiator would confer with the capital and re-draft or re-submit the position paper: ‘It was a game of submit-re-submit in Brussels and Budapest. At maximum I

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<sup>84</sup> Interview by Author with the Chief Negotiator of Hungary, Budapest, 09/02/2004.

<sup>85</sup> Getting Closer to EU Membership, An Interview with Endre Juhász, Ambassador of Hungary to the EU and Chief Negotiator for Accession, in: *The Hungarian Quarterly*, Autumn 2001, XLII(No. 163), pp. 10.; Interview by Author with the Chief Negotiator of Hungary, Budapest, 09/02/2004.

<sup>86</sup> Interview by Author with Representative of the Ministry of Finance of Hungary, Budapest, 06/02/2004 and 18/02/2004.



would re-draft a position paper five times. The redrafting could involve two lines, two pages, 14 pages, or longer<sup>87</sup>.

Predominantly, TPRs were sectorally related. Their adoption depended on technical reasons and the government budget. In most cases TPRs were rejected or reduced<sup>88</sup>. Rarely would they be based on impact studies. The chief negotiation team had only a few impact studies at its disposal because of time pressure and related costs: ‘The issues involved were complex and mostly the study could only provide a best guess’<sup>89</sup>. Others concurred: ‘It was difficult to decide on the impact of the acquis and whether a TPR could address the issue and should be requested. When was the effect of the acquis excessive? There is simply no way of estimating the economic and social consequences of one EU directive; or the accumulative effect of a whole set of directives’<sup>90</sup>. The uncertainty of the impact of EU membership made it difficult for Hungary to make arguments stick, particularly in the absence of hard data.

The presence of TPRs would always cause the EC to request additional information and clarification along three phases: before the official position papers were put forward, after the official position papers were on the table and during the negotiations. The EU’s executive did not allow for large differences between the TPRs of different candidate countries and tried to limit their number and content. The scope of TPRs was never widened or its duration augmented: ‘There was a gradual approach which meant that TPRs were reduced in number, content and duration’<sup>91</sup>.

TPRs were regarded as counterproductive for the political commitment to join the EU. The strategy of the team was to have as few and short TPRs as possible: ‘I dropped many requests, including of sectoral interests, because it would burden the negotiations and the real important requests for Hungary would be endangered because of them. It is about priorities’<sup>92</sup>. Initially the position papers contained some hundred TPRs. The EC encouraged the negotiation delegation to reconsider the papers. Many were withdrawn, some re-grouped and others put aside. Their

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<sup>87</sup> Interview by Author with the Chief Negotiator of Hungary, Budapest, 09/02/2004.

<sup>88</sup> Interview by Author with Representative of the Ministry of Foreign Affairs of Hungary, Budapest, 04/02/2004b.

<sup>89</sup> Interview by Author with the Chief Negotiator of Hungary, Budapest, 09/02/2004.

<sup>90</sup> Interview by Author with Representative of the Ministry of Employment and Labour Affairs of Hungary, Budapest, 03/02/2004.

<sup>91</sup> Interview by Author with Representative of the Ministry of Finance of Hungary, Budapest, 06/02/2004 and 18/02/2004.

<sup>92</sup> Interview by Author with Representative of the Hungarian Ministry of Economy and Transport, Budapest, 10/02/2004a.; Interview by Author with the Chief Negotiator of Hungary, Budapest, 09/02/2004.

number came down to 60. Under influence of the government and the MoFA the counted less than 60 in the end<sup>93</sup>.

The strategy caused difficulties for the Hungarian government. It attempted to reconcile national interests of joining the EU with sectoral interest that were harmed by EU related legislation. For instance, 48 major multinationals representing a substantial part of the Hungarian GDP jointly protested the application of the *acquis* in the area of taxation. The companies had invested in regions with high unemployment in return for tax holidays. The tax holidays would be scrapped after EU enlargement. They appealed to the government for full compensation. With the general budget under pressure the Hungarian government was not forthcoming: ‘With the EU being very strict on the internal market *acquis* the Hungarian government ended up negotiating between the 48 companies and the EU’<sup>94</sup>.

A similar account developed in the area of pharmaceuticals. The sector was well organised. It had the capacity to make the government represent its interests in the enlargement process: ‘What mattered more was how the pharmaceutical sector represented its interests’. It made clear to Hungarian authorities that full application of the *acquis* would have a damaging effect on the health care budget. The association of Hungarian pharmaceutical producers had the support of the MoH and the MoFI: ‘The impact for Hungary is on the budget and the price of medicines. The impact on business is different’<sup>95</sup>. The sector’s public campaign contributed to a positive stance of the MoFA and the government: ‘Pharmaceuticals are important in Hungary’<sup>96</sup>. One official argued: ‘There were clear cut state interests for pharmaceuticals’. EU membership affected the price of medicines on the market with a direct impact on the population as well as the government budget. The TPR was symbolic in that sense, which was also the reason we opted for the domestic rather than the foreign industry’<sup>97</sup>.

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<sup>93</sup> Interview by Author with Representative of the Ministry of Employment and Labour Affairs of Hungary, Budapest, 03/02/2004.; Interview by Author with Representative of Ministry of Foreign Affairs of Hungary, Budapest, 13/02/2004, Interview by Author with Representative of the Ministry of Foreign Affairs of Hungary, Budapest, 04/02/2004b.

<sup>94</sup> Interview by Author with Representative of the Hungarian Ministry of Economy and Transport, Budapest, 10/02/2004a.

<sup>95</sup> Interview by Author with Representative of the Ministry of Finance of Hungary, Budapest, 06/02/2004 and 18/02/2004.

<sup>96</sup> Interview by Author with the Chief Negotiator of Hungary, Budapest, 09/02/2004.

<sup>97</sup> Interview by Author with Representative of Ministry of Foreign Affairs of Hungary, Budapest, 13/02/2004.

In contrast, the steel industry was generally regarded as a burden for the budget and associated with the Communist era. It was still in state hands. The government had attempted to reduce its subsidies and protection. In the accession negotiations the MoFA refused a TPR arguing that the EC would not allow it<sup>98</sup>.

The government was confronted by a well organised transport sector. The professional organisation of road transporters pushed for TPRs at the ministerial level. One large company just had been privatised. It was well represented. The sector feared competition from other applicant countries after EU accession<sup>99</sup>. After an extensive consultation procedure in co-operation with the MoT they arrived at 14-15 TPRs. At the MoT experts and the head of the working group made a comparison between the legislative package prevalent in the EU and Hungary with the EU legislative package comprising some 300 pieces of legislation. In the course of the consultations with the Hungarian authorities and the EC the number of TPRs fell to seven<sup>100</sup>.

### **6.1.2.3. Poland**

Poland had two distinct institutional structures dealing with the EU accession process. The first was the triangular institutional structure (PMO, UKIE, and MoFA) associated with the *Jerzy Buzek* government (1997-2001, see Figure 35). The second was the vertically integrated institutional structure (MoFA and PMO) associated with the *Leszek Miller* government (2001-2004, see Figure 36).

#### **Triangular institutional structure (March 1998 - September 2001)**

Before the elections of September 2001 a triangular institutional structure dealt with EU integration. Essentially, three institutions dominated the preparations and negotiations for EU membership: the PMO and the chief negotiator, the Committee for European Integration (KIE) supported by the Office of the Committee for European Integration (UKIE) and the MoFA.

#### **Line Ministries**

The line ministries carried out the preparations for EU membership. A large group of medium level civil servants at the director or Deputy Secretary of State-level took part in the screening

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<sup>98</sup> Interview by Author with Representative of the Iron and Steel Institute, Budapest, 04/02/2004a.

<sup>99</sup> Interview by Author with Representative of Ministry of Foreign Affairs of Hungary, Budapest, 13/02/2004.

<sup>100</sup> Interview by Author with Representative of the Hungarian Ministry of Economy and Transport, Budapest, 10/02/2004a.

process (April 1998-July 1999) and the preparations of the draft negotiation positions<sup>101</sup>. The officials and experts in the line ministries made the first proposals on the draft negotiation position in consultation with the respective partners such as sectoral associations. The consultations were difficult. Polish sectoral interests were fragmented and not always representative for the sector. Knowledge about the enlargement process in the line ministries was more advanced than that of the market unless the respective sectors were export oriented<sup>102</sup>. The line ministries presented the draft position papers to the ministers and the inter-ministerial team<sup>103</sup>.

### **Inter-ministerial Team**

The inter-ministerial team for the preparation of accession negotiations was set up in March-July 1998. It functioned as an advisory body to the PM. Within the inter-ministerial team 37 subgroups provided opinions on the draft negotiation positions. They were supported by an inter-ministerial task force including experts from ministries and governmental agencies. Interest groups and external experts organised in sectoral groups provided expertise during detailed technical discussions<sup>104</sup>. The most important responsibility lay with the ministry's experts. They consulted the sectors, knew the technical details and were involved in working out strategies during the political phase of negotiations. Most TPRs emerged at this level. Experts had vertical rather than horizontal responsibilities. They tended to represent the corresponding sectors of the ministries rather than take in account the horizontal implications of the *acquis*. After consultation within the subgroups individual negotiation proposals were presented to the negotiation team. The responsibility of the inter-ministerial team would decline after October 2001. The new government streamlined the procedures for the EU accession negotiations.

### **Negotiation Team and Chief Negotiator (PMO)**

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<sup>101</sup> Conference Proceedings on Europeanisation of Public Administration in Central and Eastern Europe in the process of transformation and integration, *Europeanisation of Public Administration in Central and Eastern Europe. The Case of Poland*, College of Europe Natolin: College of Europe Natolin, Jean-Monnet-Lehrstuhl für Politikwissenschaft Universität zu Köln, 11 January 2002, pp. 1-22., p. 12.

<sup>102</sup> *Interview by Author with Representative of the Ministry of Finance of Poland*, Warsaw, 30/04/2004.

<sup>103</sup> Conference Proceedings on Europeanisation of Public Administration in Central and Eastern Europe in the process of transformation and integration, *Europeanisation of Public Administration in Central and Eastern Europe. The Case of Poland*, College of Europe Natolin: College of Europe Natolin, Jean-Monnet-Lehrstuhl für Politikwissenschaft Universität zu Köln, 11 January 2002, pp. 1-22., p. 12.

<sup>104</sup> M. BRUSIS and J.A. EMMANOUILIDIS, *Negotiating EU Accession: Policy Approaches of Advanced Candidate Countries from Central and Eastern Europe*, Bertelsmann Foundation, Bertelsmann Group for Policy Research, Centre for Applied Research, July 2000., p. 10.

The position of chief negotiator and the negotiation team were set up in March 1998. The chief negotiator was State Secretary in the PMO. His responsibilities overlapped with those of the Minister of Foreign Affairs. The PM in consent with the MoFA and KIE selected the chief negotiator's tasks and placements. The chief negotiator reported directly to the PM. He was charged with the preparations and conduct of the EU accession negotiations. He formally led the negotiation team. His office was located within the PMO. He took part in meetings of KIE. The negotiation team comprised 19 members all appointed by the PM at the level of Secretary and Under-Secretary of State from the major ministries<sup>105</sup>.

Different department in the line ministries, the PMO and UKIE supported the chief negotiator and his team<sup>106</sup>. The mission to the EU channelled information between the team and the EC. The negotiation team met twice a week with at least 10 members present including the Chair and Vice-Chair. The members did not represent their respective ministries. Decisions were taken by consensus. The government reduced the team to eight members in the fall of 2001 to render the team more effective and reduce conflicts between horizontal and vertical issues<sup>107</sup>.

#### **National Council for EU integration (NCEI)**

The Prime Minister, Mr. *Jerzy Buzek*, set up the NCEI as a consultative body that reported directly to the PM. It established a high level of co-operation between the different groups of political actors and civil society<sup>108</sup>. It comprised 47 advisors and experts including NGOs, research institutes and interest groups. Its main function was to support the government's communication policy and to advise the PM on sensitive political issues related to EU accession. When the new government took office in the fall of 2001 this consultative body was abolished.

Consultation was not obligatory and written in the law. In the early phase of the EU accession process extensive consultations were held. Consultation procedures became less frequent later in the process because of the measured effect they had: 'Once the negotiations were well underway

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<sup>105</sup> Including the Chairmen of KIE, the Governmental Centre of Strategic Studies, the Office for the Protection of Competition and Consumers, the Ministers of Foreign Affairs, Interior and Administration, Finance, Justice, Economy, Environment, Agriculture, Labour and Social Policy and Transport and Communication. Other members of the team were the Government Plenipotentiary for Family Affairs, the head of the mission to the EU and the secretary of UKIE.

<sup>106</sup> *Closer, Closer, Close. The Way of Decision-Making*, The Warsaw Voice, No. 39 (622), 24 September 2000.

<sup>107</sup> *Interview by Author with Representative of the Committee for European Integration (KIE)*, Warsaw, 15/04/2004.

<sup>108</sup> Conference Proceedings on Europeanisation of Public Administration in Central and Eastern Europe in the process of transformation and integration, *Europeanisation of Public Administration in Central and Eastern Europe. The Case of Poland*, College of Europe Natolin: College of Europe Natolin, Jean-Monnet-Lehrstuhl für Politikwissenschaft Universität zu Köln, 11 January 2002, pp. 1-22., p. 14.

we did not have the time. We would have gone even slower and not been able to deliver any progress in the accession negotiations'<sup>109</sup>. The negative effects extensive consultation had on the accession negotiations were ascribed to the fragmentation of interest representation. Generally, the business community was not very much involved in the process. Often sectoral interest were dispersed and not representative for the entire sector. Representation in the NCEI reached approximately 20 per cent of all the Polish employers. Frequently they could not come to a common position. They were also not very well informed about EU legislation. Predominantly the authorities explained the *acquis* to sectoral interests rather than receiving input for the respective negotiation position. The capacity of the small companies to assess the impact of EU membership was limited: 'They did not have the personnel, infrastructure, language skills and funds to prepare for EU membership'<sup>110</sup>. When sectoral interests were given the possibility to address the impact of EU related legislation they did not. Most business associations were not a member of their European counterparts in Brussels. When they were they lacked a vote<sup>111</sup>.

The NCEI did not function very well<sup>112</sup>. The authorities had problems in receiving relevant information from the trade unions and the business associations. Sometimes information was contradictory: 'There were different bodies, different interests and different representatives. At times it was difficult for us to have an idea what they wanted.' As the negotiations progressed most associations improved their political assets and the dialogue matured. Nevertheless, the burden of the initiative and the management of the negotiations fell almost entirely on the administration<sup>113</sup>.

### **Ministry of Foreign Affairs**

Before October 2001 the Polish MoFA did not play a significant a role in the enlargement process. It represented Poland in relations with the EU. Four departments dealt with the EU: the Department of the European Union, European institutions, economic analysis and European integration which co-ordinated the activities of all the above mentioned departments. The Polish

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<sup>109</sup> *Interview by Author with Representative of the Committee for European Integration of the Republic of Poland (KIE)*, Warsaw, 14/04/2004.

<sup>110</sup> *Ibid.*

<sup>111</sup> *Interview by Author with the Chief Negotiator of Poland*, Warsaw, 26/04/2004b.

<sup>112</sup> *Interview by Author with Representative of the Committee for European Integration of the Republic of Poland (KIE)*, Warsaw, 14/04/2004.

<sup>113</sup> *Interview by Author with Representative of the Office of the Committee for European Integration (UKIE)*, Warsaw, 21/04/2004.

Mission to the EU ensured political representation, information flow and technical assistance in the negotiation process. Under the Buzek government its head was a member of the negotiating team. The mission was responsible for horizontal links with experts in the line ministries in the framework for the preparation of national negotiation positions. The task of the mission was to understand the position in Brussels<sup>114</sup>.

From October 2001 the MoFA gained responsibility for the EU accession process. Its workload increased considerably. The Secretary of State at the MoFA dealt directly with the details of the negotiation positions. And she was fully supported by the different departments at the MoFA<sup>115</sup>. The fact that the MoFA had no particular interest of its own relative to the line ministries facilitated its role in speeding up the accession process. Some criticised the MoFA for being too close to Brussels and disregarding Poland's interests<sup>116</sup>.

### **KIE and UKIE**

KIE was established in 1996. It was the main body responsible for EU accession<sup>117</sup>. It operated within the structure of the PMO. It set and co-ordinated EU accession policy. The PM or a member of cabinet chaired KIE. It presented its integration strategies to the government.

Until October 2001 UKIE implemented KIE's recommendations<sup>118</sup>. UKIE was a large institutional body with as many as 200 staff<sup>119</sup>. As the negotiations progressed UKIE increasingly added executive task to its competences. The number of internal organisations involved in European policy increased and presenting difficulties for internal co-ordination. KIE co-ordinated accession related legislation, monitored legislative compatibility and implementation. It also dealt with financial aid under the EAs. KIE and UKIE weakened the role of the Minister of Foreign

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<sup>114</sup> Interview by Author with Representative of the Committee for European Integration of the Republic of Poland (KIE), Warsaw, 14/04/2004.

<sup>115</sup> Interview by Author with Representative of the Ministry of Foreign Affairs of Poland, Warsaw, 27/04/2004.

<sup>116</sup> Ibid.

<sup>117</sup> Law of 8 August 1996 on the Committee for European Integration, in: *Journal of Laws*, 1996, 30 August 1996.

<sup>118</sup> Its membership was restricted to Ministers of Foreign Affairs, Home Affairs and Administration, Economy, Finance, Social and Labour Policy, Agriculture and Justice and three other representatives, in: A. PODRAZA, *Central Europe in the Process of European Integration. A comparative Study of Strategies of the Czech Republic, Hungary, Poland and Slovakia; Towards Deepening and Widening of the European Union*, Research Support Scheme, Open Society Support Foundation, 2000., p. 58.

<sup>119</sup> M. BRUSIS and J.A. EMMANOUILIDIS, *Negotiating EU Accession: Policy Approaches of Advanced Candidate Countries from Central and Eastern Europe*, Bertelsmann Foundation, Bertelsmann Group for Policy Research, Centre for Applied Research, July 2000., p. 9.

Affaires and indirectly contributed to the fragmentation of Polish EU policy<sup>120</sup>. Under the Buzek government conflicts emerged between the chief negotiator and UKIE. The EC complained that Poland send confusing signals to Brussels. Under a new structure this problem was eliminated<sup>121</sup>.

### **Government**

The PM's and cabinet's role in all questions concerning European integration rose inescapably between 1998 and 2002. The government approved all major decisions through several institutions subordinate to the PM. Only in exceptional cases did it directly mediate in technical issues. As the chairman of KIE the PM influenced all facets of Poland's policy towards the EU. The appointment and location of the chief negotiator and his team at the heart of the PMO only strengthened his position<sup>122</sup>. The presidium of the accession negotiations assisted the PM. It was some sort of steering committee that comprised the PM, MoFA, chief negotiator, and the chief of UKIE. They discussed tactics and strategy. Under the Buzek government the quality of the EU membership prevailed. Under the Miller government the strategy changed to joining the EU at the lowest possible financial costs<sup>123</sup>.

### **Parliament**

The rise of executive power was matched by a declining importance of the Houses of Parliament (Sejm and the Senate). Estimates indicate that between 1998 and 2002 one third of the parliamentary work was related to EU legislative harmonisation.

Prime Minister Buzek attempted to make the Parliament more relevant in the accession process. He set up a parliamentary consultation procedure and reinforced the role of the committees for European integration<sup>124</sup>. Three parliamentary committees played a key role in harmonization of Polish law to the EU: the European Integration Committee, the Foreign Affaires Committee and the ad hoc European Law Committee. The ad hoc European Law Committee was set up in 2000 in order to speed up the process of adoption of EU law. In the Senate two committees dealt with

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<sup>120</sup> V.K. PYSZNA DOROTA, *The Management of Accession to the European Union in Poland and Hungary*, Budapest: Hungarian Academy of Sciences, October 2002., p. 21.

<sup>121</sup> *Interview by Author with Representative of the Office of the Committee for European Integration (UKIE)*, Warsaw, 21/04/2004.

<sup>122</sup> V.K. PYSZNA DOROTA, *The Management of Accession to the European Union in Poland and Hungary*, Budapest: Hungarian Academy of Sciences, October 2002., p. 24.

<sup>123</sup> *Interview by Author with Representative of the Committee for European Integration of the Republic of Poland (KIE)*, Warsaw, 14/04/2004.

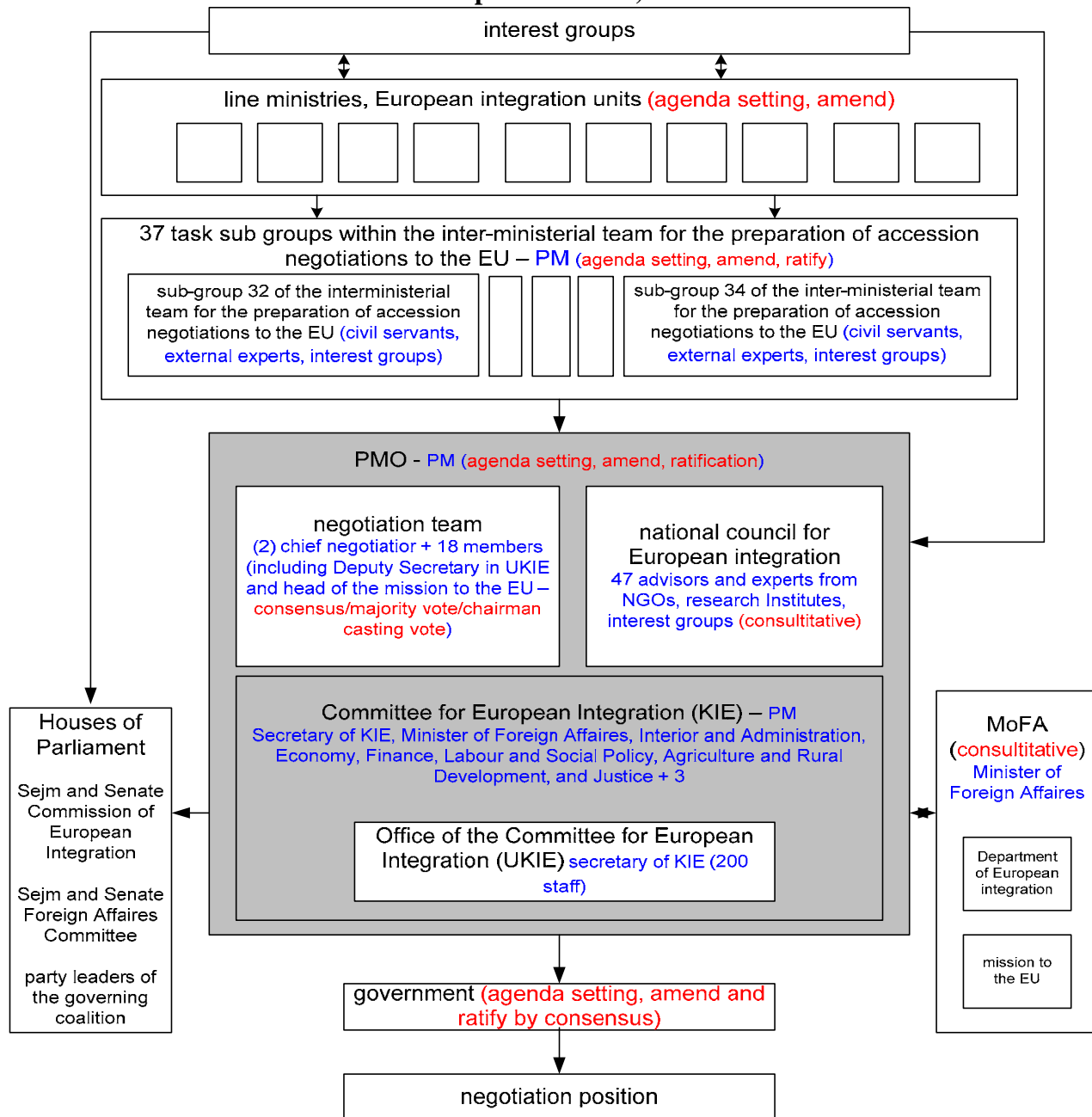
<sup>124</sup> Conference Proceedings on Europeanisation of Public Administration in Central and Eastern Europe in the process of transformation and integration, *Europeanisation of Public Administration in Central and Eastern Europe. The Case of Poland*, College of Europe Natolin: College of Europe Natolin, Jean-Monnet-Lehrstuhl für Politikwissenschaft Universität zu Köln, 11 January 2002, pp. 1-22., p. 14.



EU accession: the Foreign Affairs and European Integration Committee and the European Legislation Committee.

Despite their major responsibility and EU related legislative workload the political role of the Sejm and Senate remained limited. Not one MP in his respective legal personality was represented in the EU related executive institutional structure. The Sejm and Senate did not participate in the formulation of the negotiation positions. Political co-ordination was ensured by the inter-ministerial committee of European integration and the leaders of the political parties in the ruling coalition. Parliamentary debates were infrequent. Rarely would debates be held on European integration in the presence of the cabinet and the media. The Sejm's influence on the process declined further when the Miller cabinet took office in October 2001. It decided to speed up the negotiations process.

**Figure 35: Policy Process for the Preparation of Poland's Negotiation Position (Before September 2001)**



Note: Chief Negotiator = State Secretary in the Chancellery of the Prime Minister  
 Source: Own Compilation on the basis of interviews with ministerial and government representatives and literature: Government Plenipotentiary for Poland's Accession Negotiations to the European Union, Chancellery of the prime minister, *Accession Negotiations: Poland on the Road to the European Union*, Warsaw, 2000, pp. 108.; A. PODRAZA, *Central Europe in the Process of European Integration. A comparative Study of Strategies of the Czech Republic, Hungary, Poland and Slovakia Towards Deepening and Widening of the European Union*, Research Support Scheme, Open Society Support Foundation, 2000; Conference Proceedings on Europeanisation of Public Administration in Central and Eastern Europe in the process of transformation and integration, *Europeanisation of Public Administration in Central and Eastern Europe. The Case of Poland*, College of Europe Natolin, College of Europe Natolin, Jean-Monnet-Lehrstuhl für Politikwissenschaft Universität zu Köln, 11 January 2002; V.K. PYSZNA DOROTA, *The Management of Accession to the European Union in Poland and Hungary*, Budapest: Hungarian Academy of Sciences, October 2002; Government Plenipotentiary for Poland's Accession Negotiations to the European Union, Chancellery of the prime minister, *Accession Negotiations: Poland on the Road to the European Union*, Warsaw, 2000.

### **Vertically Integration (October 2001 – December 2002)**

In the first half of 2001 Poland began to trail the other applicant countries in the EU accession negotiations. As the Buzek administration refused or was unable to make concessions in the negotiations the EC decided to wait for a new government to take over<sup>125</sup>. Commentators as well as the political opposition in the Sejm argued for the need of a stronger centralised co-ordination mechanism able to counter intra- and inter-ministerial conflicts. The three nuclei of European decision-making, i.e. UKIE and KIE, the MoFA, and the chief negotiator at the heart of the PMO were said to complicate EU related decision-making. The new government that won the elections in September 2001 streamlined the EU-related institutional structure from October 2001 onwards (see figure 36). Effectively the Miller cabinet made a philosophical and an institutional U-turn. It replaced almost all top officials involved in the EU accession process. The new approach resulted in a new strategy on EU membership<sup>126</sup>.

The new government regarded the EU as a means to modernise Poland. Negotiating EU accession required flexibility to obtain membership under financially advantageous conditions. The main aim of the reform was to reduce the bureaucratic structure in order to increase its effectiveness. The PM, Mr. *Leszek Miller*, reduced and subordinated several bodies with overlapping responsibilities to the MoFA. The MoFA and UKIE were united in the double hatted function of Deputy Minister of Foreign Affairs (Secretary of State in the MFA), Head of UKIE, Secretary of KIE and Minister of European Affairs in the government. Ms *Danuta Hubner* took up the post. She became responsible for the whole integration policy. As a result the role of KIE was significantly reduced. Its regular meetings became less frequent and a statutory participation of the representatives of the opposition was no longer ensured. Only three independent experts were invited to become members of the KIE<sup>127</sup>.

More drastically, Mr. Miller appointed a new negotiating team and reduced its composition to 11 members and later to just 8 members. Only the representatives of the key line ministries kept

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<sup>125</sup> Interview by Author with Representative of the Committee for European Integration (KIE), Warsaw, 15/04/2004.

<sup>126</sup> Interview by Author with Representative of the Ministry of Foreign Affairs of Poland, Warsaw, 27/04/2004.

<sup>127</sup> Conference Proceedings on Europeanisation of Public Administration in Central and Eastern Europe in the process of transformation and integration, *Europeanisation of Public Administration in Central and Eastern Europe. The Case of Poland*, College of Europe Natolin: College of Europe Natolin-Lehrstuhl für Politikwissenschaft Universität zu Köln, 11 January 2002, pp. 1-22., p. 7.

their seat on the team. Just three key actors at the level of Deputy Minister under the former cabinet kept their positions. One of the most important changes was the appointment of a new chief negotiator. Mr. *Jan Kulakowski*, who had been in charge since 1998, was replaced by Mr. *Jan Truszczyński*, head of the presidential office for European integration and until February 2001 Ambassador to the EU. The government modified the resolution on the chief negotiator placing him within the structure of the MoFA. With Mr. Truszczyński at the helm the role of the chief negotiator became more technical and less autonomous. The PM kept its prime responsibility and continued to be the Chairman KIE<sup>128</sup>. He ensured his position as the most powerful decision-maker in the field of EU integration. Miller abolished the NCEI<sup>129</sup>.

The general view was that the old institutional structure harboured too many experts with their respective vertical interests. The new structure was geared towards strategy instead of a holistic approach. Several line ministries were excluded and the number of overall players was reduced. Continuity was of no importance. The idea was that EU membership would occur on the cheapest possible basis with a limited impact on the government budget prevailed. In contrast to the former cabinet Warsaw would show flexibility<sup>130</sup>. According to one policymaker: 'Originally 65 per cent of all decisions resembled the government's political priorities. The new structure reduced the government involvement to just 35 per cent'<sup>131</sup>. The EC appreciated the new institutional structure. It ensured better co-ordination of Polish EU integration policy as the MoFA, the PM, and UKIE presented unified views vis-à-vis EU<sup>132</sup>.

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<sup>128</sup> Ibid., p. 14.

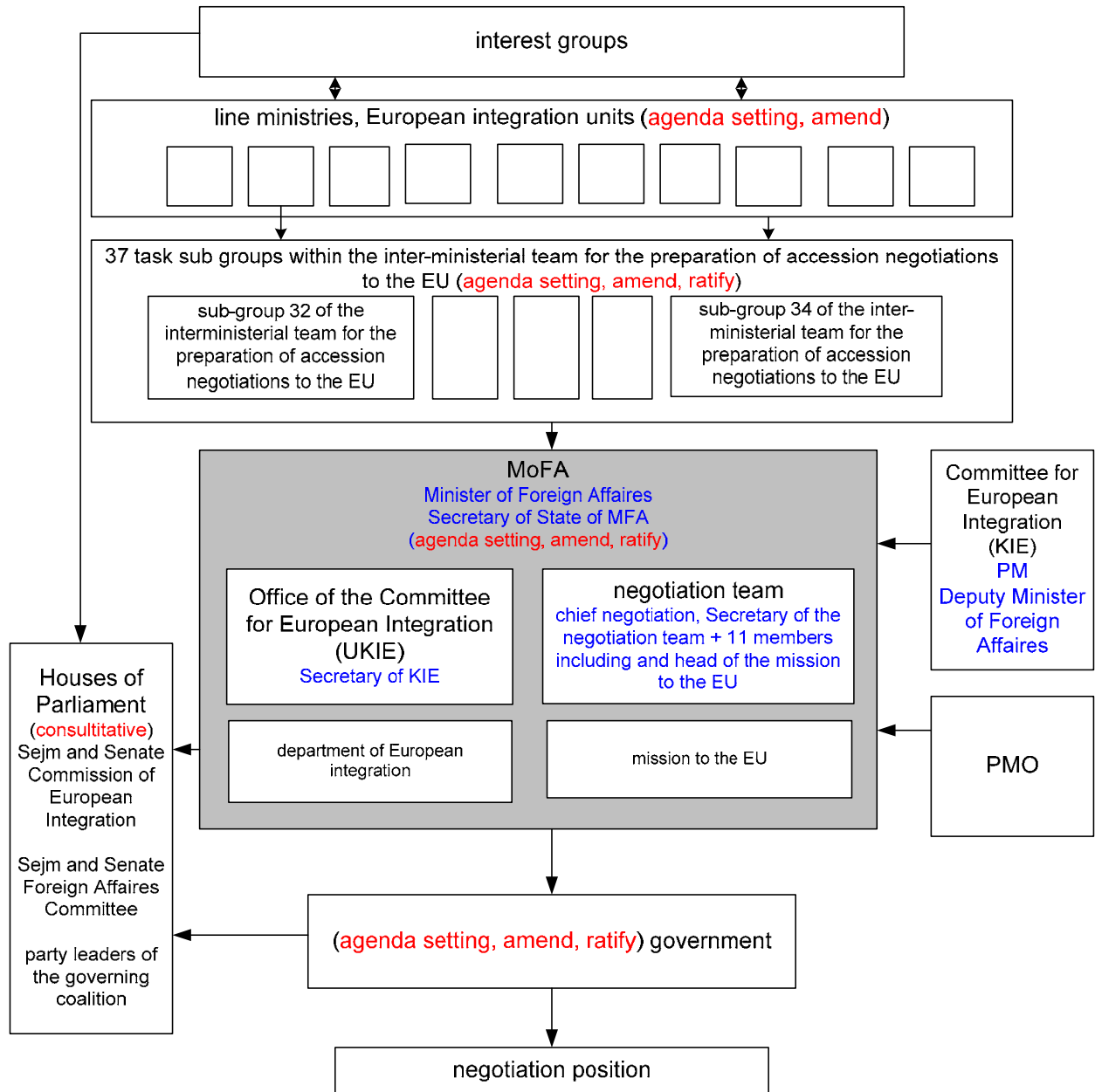
<sup>129</sup> M. BRUSIS and J.A. EMMANOUILIDIS, *Negotiating EU Accession: Policy Approaches of Advanced Candidate Countries from Central and Eastern Europe*, Bertelsmann Foundation, Bertelsmann Group for Policy Research, Centre for Applied Research, July 2000., p. 10.

<sup>130</sup> Interview by Author with Representative of the Ministry of Foreign Affairs of Poland, Warsaw, 27/04/2004.

<sup>131</sup> Ibid.

<sup>132</sup> Ibid.; Interview by Author with Representative of the Committee for European Integration of the Republic of Poland (KIE), Warsaw, 14/04/2004.

**Figure 36: Policy Process for the Preparation of Poland's Negotiation Position (After September 2001)**



Note: 1. Chief Negotiator = Undersecretary of State in the MFA (plenipotentiary of the government)  
 2. Secretary (Head) of the Committee for European Integration = Secretary of State of MFA = Minister for European Integration = Secretary of State of European Integration = Deputy Minister of Foreign Affairs

Source: Own Compilation on the basis of interviews with ministerial and government representatives and literature: A. PODRAZA, *Central Europe in the Process of European Integration. A comparative Study of Strategies of the Czech Republic, Hungary, Poland and Slovakia Towards Deepening and Widening of the European Union*, Research Support Scheme, Open Society Support Foundation, 2000; Conference Proceedings on Europeanisation of Public Administration in Central and Eastern Europe in the process of transformation and integration, *Europeanisation of Public Administration in Central and Eastern Europe. The Case of Poland*, College of Europe Natolin: College of Europe Natolin, Jean-Monnet-Lehrstuhl für Politikwissenschaft Universität zu Köln, 11 January 2002; V.K. PYSZNA DOROTA, *The Management of Accession to the European Union in Poland and Hungary*, Budapest: Hungarian Academy of Sciences, October 2002; Government Plenipotentiary for Poland's Accession Negotiations to the European Union, Chancellery of the prime minister, *Accession Negotiations: Poland on the Road to the European Union*, Warsaw, 2000.

## Negotiation Positions

Regardless of the presence of eight formal institutions a draft negotiation position passed through four levels of government for approval, i.e. the line ministries, the negotiation team, the committee for European integration and the cabinet<sup>133</sup>. The contours of a draft negotiation position formed in the line ministries during the screening process (1998-1999)<sup>134</sup>. Legislative inconsistencies were noted in the draft negotiation position papers of the line ministries and passed on to the inter-ministerial team after consultations with the representatives of firms and interests groups. Ministerial working groups of the inter-ministerial task force clarified the draft negotiating positions.

The negotiation team would discuss the draft negotiation position. During the examination of the preparatory position proposals the team drafted documents for negotiating alternatives in the bargaining process with input from the mission to the EU. The team together with two working groups controlled by the MoFI and the government Centre for Strategic Studies would verify budgetary and economic and social costs related to the position paper. These technical assessments occurred between 1999 and 2001<sup>135</sup>. On the basis of their analysis the negotiation team took a position<sup>136</sup>.

The position paper would end up on the desk of the inter-ministerial committee of European integration which would submit it to the cabinet for final adoption. The PM, who between 1998 and 2001 had the political responsibility for the negotiations, assisted by the Minister of Foreign Affairs and the secretary of the KIE decided based on political factors<sup>137</sup>. The chief negotiator presented the final paper to the Sejm's Commission for European Integration for consultation and

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<sup>133</sup> Interview by Author with Representative of the Committee for European Integration of the Republic of Poland (KIE), Warsaw, 14/04/2004.

<sup>134</sup> Conference Proceedings on Europeanisation of Public Administration in Central and Eastern Europe in the process of transformation and integration, *Europeanisation of Public Administration in Central and Eastern Europe. The Case of Poland*, College of Europe Natolin: College of Europe Natolin, Jean-Monnet-Lehrstuhl für Politikwissenschaft Universität zu Köln, 11 January 2002, pp. 1-22., p. 12.

<sup>135</sup> M. BRUSIS and J.A. EMMANOUILIDIS, *Negotiating EU Accession: Policy Approaches of Advanced Candidate Countries from Central and Eastern Europe*, Bertelsmann Foundation, Bertelsmann Group for Policy Research, Centre for Applied Research, July 2000.

<sup>136</sup> Interview by Author with Representative of the Committee for European Integration of the Republic of Poland (KIE), Warsaw, 14/04/2004.

<sup>137</sup> A. PODRAZA, *Central Europe in the Process of European Integration. A comparative Study of Strategies of the Czech Republic, Hungary, Poland and Slovakia; Towards Deepening and Widening of the European Union*, Research Support Scheme, Open Society Support Foundation, 2000., pp. 57-59.

for information. When the government approved the draft position papers they were presented to the EC, the EU Presidency and the Secretariat of the Council<sup>138</sup>.

This system changed after October 2001. Each position paper passed three levels of government instead of four: the negotiation team, KIE and the cabinet. The position papers from the former administration were adapted to new priorities, which solely concerned the government budget and access to EU funds. Otherwise the team was prepared to compromise on most TPRs when it could<sup>139</sup>. Under the new system with high demands on rapid decision-making and swift diplomacy the MoFA gained authority relative to the PMO<sup>140</sup>.

Under the Buzek administration TPRs originated at the level of the line ministries. They and were presented in consultation with the interest group representatives. The authorities complained that corporate structures were too dispersed for the provision of market information. Only well organised interest groups sent clear signals when they wanted TPRs<sup>141</sup>. Companies would use domestic channels to present their interest in the enlargement policy. The larger and international active companies were more effective in representing their interests. They had know-how and easy access to policy makers. The domestic market operators were much more limited in their reach<sup>142</sup>.

The Miller administration established priorities for maintaining TPRs, which centred on the government budget. In all other matters the new administration was prepared to make concessions<sup>143</sup>. Setting the criteria for the substance and length of TPRs was not straightforward. Authorities had difficulties in exactly determining the modalities for TPRs: 'If you do not know whether you need a TPR and how long it should be you ask for one that is near to the upper limit of the total possible length and scope. You could do the analysis or drop the TRP later in the

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<sup>138</sup> *Closer, Closer, Close. The Way of Decision-Making*, The Warsaw Voice, No. 39 (622), 24 September 2000.

<sup>139</sup> *Interview by Author with Representative of the Ministry of Foreign Affairs of Poland*, Warsaw, 27/04/2004.

<sup>140</sup> *Interview by Author with the Chief Negotiator of Poland*, Warsaw, 26/04/2004b.

<sup>141</sup> *Interview by Author with Representative of the Committee for European Integration of the Republic of Poland (KIE)*, Warsaw, 14/04/2004.

<sup>142</sup> *Interview by Author with Representative of the Committee for European Integration (KIE)*, Warsaw, 15/04/2004.

<sup>143</sup> *Interview by Author with Representative of the Ministry of Foreign Affairs of Poland*, Warsaw, 27/04/2004.

process'<sup>144</sup>. The Polish administration was well aware that it needed to justify its position with hard evidence.

Impact studies were important in this respect: 'They provided the gunpowder in the negotiations'. Without impact studies it was difficult to maintain TPRs during the negotiations. Impact studies were absent with exception for the steel industry, tobacco, and the environment chapter of the acquis. In the remaining sectors impact studies became available once the negotiations were finished<sup>145</sup>. It was easier to have impact studies on the budget, state aid and subsidies. Budgetary issues were more easily quantifiable.

To address this problem the authorities hoped that market operators and interest representations would have more data. However, decision-makers soon discovered that the NCEI did not function very well and that market operators were hoping for similar information for the authorities<sup>146</sup>. They did not provide the government and the team with much information to base its negotiation strategy on<sup>147</sup>.

When asking a TRP the EC would demand for a detailed justification, a plan with intermediate targets and expiration date for the TPR<sup>148</sup>. The EC also expected flexibility from Poland'<sup>149</sup>. 'We were told that too many and too long TPRs were a risk. They could be used as a pretext for EU MS not to proceed with the negotiations'<sup>150</sup>. When impact studies were available the negotiation team was usually more successful in defending its position. A case in point was the TPR for tobacco, which was supported by data coming directly from the industry. Poland also hired consultants for the steel industry, the environment chapter of the acquis and social policy<sup>151</sup>. It also appeared that when export or import oriented companies were involved the EC would listen more carefully. For instance Poland had special economic zones that provided tax exemption to

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<sup>144</sup> Interview by Author with Representative of the Committee for European Integration of the Republic of Poland (KIE), Warsaw, 14/04/2004.

<sup>145</sup> Interview by Author with the Chief Negotiator of Poland, Warsaw, 26/04/2004b.

<sup>146</sup> Interview by Author with Representative of the Committee for European Integration (KIE), Warsaw, 15/04/2004.

<sup>147</sup> Interview by Author with Representative of the Ministry of Finance of Poland, Warsaw, 30/04/2004.

<sup>148</sup> Interview by Author with Representative of the Office of the Committee for European Integration (UKIE), Warsaw, 21/04/2004.

<sup>149</sup> Interview by Author with Representative of the Ministry of Foreign Affairs of Poland, Warsaw, 27/04/2004.

<sup>150</sup> Interview by Author with Representative of the Office of the Committee for European Integration (UKIE), Warsaw, 21/04/2004.

<sup>151</sup> Interview by Author with Representative of the Committee for European Integration (KIE), Warsaw, 15/04/2004.



multinationals. These companies argued directly with the EU that Poland should make up for the losses they suffered from EU enlargement. The EC understood the plight of these companies and appeared more tolerant and forthcoming relative to Polish business<sup>152</sup>.

The EC was disappointed with the first position papers as to the substance and arguments: ‘They told us that we needed to argue better and pointed out the weaknesses in our argumentation’<sup>153</sup>. This view clashed with the philosophy of the Buzek administration on EU membership: The quality of EU membership was much more important than EU membership itself<sup>154</sup>. In the opening statement of the negotiations the EC argued that the applicant countries had to reconsider TPRs<sup>155</sup>.

Initially the priority would concern the economy. If the experts regarded the *acquis* was not conducive to economic growth a TPR would be written in the position paper. The effect on the budget would take second place. Joining the EU was important but not at all costs. It resulted in internal ministerial discussions with three ministers arguing that TPRs had to be longer and that some sectors had to be taken more into account. It resulted in big political discussions between the chief negotiator and the some sectoral representations, it slowed down the negotiations and to a certain extent blocked them<sup>156</sup>.

The MoH together with the pharmaceutical associations discussed the impact of the *acquis*. The process was lacklustre and issues were not crystal clear. The chapter was closed and EU legislation adopted in full. The Polish industry mobilised late in the negotiations upon initiative of their Hungarian counterparts. They lobbied strongly and several meetings followed between KIE and the associations<sup>157</sup>. The Polish pharmaceutical association together with KIE formulated

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<sup>152</sup> *Ibid.*

<sup>153</sup> *Interview by Author with Representative of the Committee for European Integration of the Republic of Poland (KIE), Warsaw, 14/04/2004.*

<sup>154</sup> *Interview by Author with Representative of the Committee for European Integration (KIE), Warsaw, 15/04/2004.*

<sup>155</sup> *Ibid.*

<sup>156</sup> *Interview by Author with the Chief Negotiator of Poland, Warsaw, 26/04/2004b.; Interview by Author with Representative of the Committee for European Integration of the Republic of Poland (KIE), Warsaw, 14/04/2004.*

<sup>157</sup> *Interview by Author with Representative of Polfarmed, Warsaw, 26/04/2004a.; Interview by Author with the Chief Negotiator of Poland, Warsaw, 26/04/2004b.*

a TPR. The MoFI was supportive because of the impact on the patient's reimbursement of the health budget<sup>158</sup>.

In the area of cabotage the MoT and the UKIE contacted the main road transport association to ask whether the EU's TRP formed an obstacle. The MoT and negotiation team received good feedback from the sectors association. Road transporters were well organised and expressed clear views. They did not consider restrictions on cabotage as problematic and did not mobilise<sup>159</sup>.

The authorities took a restrictive stance in the area of the steel industry: 'In the coal industry we were able to reduce subsidies in less than four to five years. Therefore we thought we could do it as well in the steel industry. We realised that the steel industry was not profitable and costly for the government. The EC made clear that Poland could not enter the EU with an uncompetitive and subsidised steel industry. Without EU pressure reform in the sector would have been difficult. The MoE and MoT shared our view'<sup>160</sup>.

#### **6.1.2.4. Slovakia**

The Slovak accession process started with almost two years delay. The country was excluded from starting negotiations in 1998 because of the authoritarian character of its government. Instead, negotiations began in February 2000. Slovakia found itself catching up with the other V-4 in the EU accession process. To catch up Slovakia's experts co-operated closely with their Czech counterparts. Both countries signed an intergovernmental agreement on 18 April 2000 for translating and transposing EU legislation<sup>161</sup>.

The Slovak institutional structure was barely six years old when it commenced the EU accession drive. It was the Czech Republic that had inherited the institutional set up of the Czechoslovak Federation. Just a minority of former Czechoslovak diplomats decided to work for the new Republic. The Slovak MoFA was new and untested. Bratislava looked at neighbouring countries and the EU for the creation of its European foreign policy structure. Guided by the EC's

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<sup>158</sup> *Interview by Author with Representative of the Office of the Committee for European Integration (UKIE), Warsaw, 21/04/2004.*

<sup>159</sup> *Ibid.*

<sup>160</sup> *Interview by Author with Representative of the Office for Competition and Consumer Protection of Poland, Warsaw, 16/04/2004.*

<sup>161</sup> European Commission, *Pre Accession Report Czech Republic*, December 2000.

questionnaires and screening process (1998) it set up a decision-making structure for negotiating EU membership<sup>162</sup>.

The institutional framework for negotiating EU membership comprised the ministerial council of the government for European integration and the departments of European integration at every ministry and central state administration (see figure 37)<sup>163</sup>. The aim of the structure was to improve co-ordination between these bodies<sup>164</sup>. The MoFA took the lead and shared most responsibilities with the government<sup>165</sup>.

### **Line Ministries**

The line ministries set up 29 sectoral negotiation working groups<sup>166</sup>. They carried out the main preparatory work during the screening and prepared the draft positions papers under the co-ordination of the chief negotiator. The line ministries, working groups and the chief negotiator kept close contact with their counterparts in Brussels as well those in the Czech Republic<sup>167</sup>. Because Slovakia was catching up its administrative structures were weaker relative to those of the other V-4. Sometimes one person with industry expertise and the required language skills dealt with the preparations of the sectoral body of EU legislation. It was the case for the transport chapter<sup>168</sup>.

As a result, experts in the line ministries had substantial impact on the position papers, particularly when sectoral difficulties emerged during the screening process. Unlike in the Czech Republic, Hungary or Poland the Slovak line ministries did not always consult the relevant sectors in the market place. There was simply not enough time to go through a consultation procedure. The EU departments in the line ministries together with MoFA would set up a joint process for the formulation of the position papers. The MoFA would co-ordinate between the different vertical interests of the line ministries.<sup>169</sup> For more difficult issues the MoFA informally

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<sup>162</sup> *Interview by Author with Representative of the EC's Delegation to the Slovak Republic*, Bratislava, 11/03/2004.

<sup>163</sup> Government of the Slovak Republic, *Government Action Plan* 14 January 1999.

<sup>164</sup> A. PODRAZA, *Central Europe in the Process of European Integration. A comparative Study of Strategies of the Czech Republic, Hungary, Poland and Slovakia; Towards Deepening and Widening of the European Union*, Research Support Scheme, Open Society Support Foundation, 2000., p. 85.

<sup>165</sup> *Ibid.*, p. 84-107.

<sup>166</sup> *Ibid.*, p. 93.

<sup>167</sup> *Interview by Author with Representative of the Slovak State Institute for Drug Control*, Bratislava, 12/03/2004b.

<sup>168</sup> *Interview by Author with Representative of Slovak Ministry of Transport*, Bratislava, 02/03/2004a.

<sup>169</sup> Ministry of Foreign Affairs, *Statute of the Chief Negotiator of the Slovak Republic for Negotiations on Slovakia's Accession to the European Union*, Bratislava, 1999.

organised a group comprising the corresponding departments and partners. The process became more singular towards the end of the negotiations when the chief negotiator, the MoFI and the PMO dealt with the position papers and negotiations<sup>170</sup>.

### **Working Committee**

The working committee was involved in the preparation of the sessions of the ministerial council for European integration. It was chaired by the chief negotiator and comprised the general directors of division of European integration of the government's office, the individual ministries and central bodies of the state administration. It also comprised the heads of the 29 working groups that operated in the line ministries. The working committee reported to the ministerial council for European integration and dealt with expert and technical questions related to the individual position papers<sup>171</sup>.

### **Consultative Committee**

The consultative committee of the ministerial council for European integration comprised the representatives of scientific institutions, trade unions, employers association and NGOs. It had an advisory capacity and was supervised by the deputy PM for European Integration and attended by the chief negotiator. It was a formal consultative body. Its conclusions were not binding.

It was required to be consulted. Often not enough time to go through such consultation procedure. The Committee rarely met. Economic and social partners were badly informed about the impact of EU membership. They would complain about not being consulted. Most of the information they received came from the press or the line ministries<sup>172</sup>. As a result, the EU accession process was insulated. Many partners were excluded because the government was under time pressure to meet the EU's deadlines. Only at the very end when the referendum on EU membership approached did the administration engage in a consultation procedure<sup>173</sup>.

### **Negotiation Team, Chief Negotiator and MoFA**

The government created the position of chief negotiator on 16 December 1999 at the heart of the MoFA. He was appointed by the government, acted as a State Secretary in the MoFA and was a

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<sup>170</sup> *Interview by Author with Representative of the Slovak Office of the Government, Bratislava, 12/03/2004a.*

<sup>171</sup> *Ibid.*

<sup>172</sup> *Interview by Author with Representative of the Chemicals Workers Union Slovakia, Bratislava, 30/02/2004.*

<sup>173</sup> *Interview by Author with Representative of the Confederation of Slovak Trade Unions (KoZ SR) Bratislava, 25/04/2004.*

member of the ministerial council for European integration and of the consulting committee. The chief negotiator shared the responsibility for negotiating EU membership with the Deputy PM for European Integration assisted by the horizontal services of the MoFI and MoFA.

The chief negotiator directed and co-ordinated all the activities of the working groups in the line ministries. Together with the line ministries, working groups and the working committee he prepared Slovakia's individual negotiating positions. The main responsibility for the position papers lay respectively with the chief negotiator and state secretary at the MoFA<sup>174</sup>. Operating within the MoFA the chief negotiator would together with the Deputy PM for European Integration present the government with proposals concerning Slovakia's negotiation strategy. Both would inform the single chamber parliament (National Council of the Slovak Republic) on the progress in the accession negotiations<sup>175</sup>. The chief negotiator maintained direct contact with the government and required approval for the negotiation positions particularly when they proved politically sensitive<sup>176</sup>. He received support from a ten member strong negotiating team<sup>177</sup>. Because of the heavy workload the team rarely met.

The MoFA was the main responsible ministry liaising with the EU. Within the MoFA the division for European integration was subordinated to the Minister of Foreign Affairs and the State Secretary for European Integration<sup>178</sup>.

### **Ministerial Council for European Integration**

The ministerial council for European integration was set up in December 1998. It was the key co-ordination and advisory body for the government headed by the deputy PM for European integration. It comprised the Minister of Foreign Affairs, Economics, Finance, Agriculture,

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<sup>174</sup> Interview by Author with Representative of the Slovak Office of the Government, Bratislava, 12/03/2004a.

<sup>175</sup> The Government of the Slovak Republic, *Statute of the Chief Negotiator of the Slovak Republic for Negotiations on Slovakia's Accession to the European Union*, December 1999., Article 1-5.

<sup>176</sup> Ministry of Foreign Affairs, *Statute of the Chief Negotiator of the Slovak Republic for Negotiations on Slovakia's Accession to the European Union*, Bratislava, 1999.

<sup>177</sup> The team comprised the head of mission to the EU, the general heads of the European affairs section of the PMO, the European integration section of the MoFA, the European integration department at the PMO, the chief negotiator department of the MoFA and the department for economic and legal relations with the EU of the MoFA. They were accompanied by eight coordinators appointed by corresponding government minister in consent with the chief negotiator.

<sup>178</sup> A. PODRAZA, *Central Europe in the Process of European Integration. A comparative Study of Strategies of the Czech Republic, Hungary, Poland and Slovakia; Towards Deepening and Widening of the European Union*, Research Support Scheme, Open Society Support Foundation, 2000., p. 85-86.

Interior and the chief negotiator<sup>179</sup>. The ministerial council for European integration would convene monthly at the PMO. The meeting would consist of a tour de table about the tasks and their implementation in attempt to reduce the risk that Slovakia would not make it into the EU. Once the meeting was over the members would report to the negotiation team and the government<sup>180</sup>. The ministerial council for European integration also prepared solutions for politically sensitive problems in the integration process.

### **Office of the Government (PMO)**

Within the PMO the Deputy PM for European Integration was responsible for co-ordinating the various aspects of integration policy. He supervised the division for European affairs which was divided into the department of European integration, the department of foreign assistance and the department of institution building<sup>181</sup>. The creation and position of the Deputy Prime Minister for European Integration was unique among the V-4. While he co-operated with the MoFA he had considerable sway over EU integration policy and was the prime responsible for the entire EU integration policy<sup>182</sup>.

### **Parliament**

Several bodies of the National Council were involved in the process of European integration such as the Foreign Affairs Committee, the Committee for European Integration, and the Joint Parliamentary Committee of the EU and the Slovak Republic. The Foreign Affairs Committee was primarily responsible for political relations with the EU while the Committee for European Integration, established in 1996, had more specific tasks such as the fulfilment of the Copenhagen criteria and the approximation of law and the usage of EU funds. Both committees co-operated closely and its membership overlapped. However, not one MP in his respective legal personality was represented in the executive institutional structure handling EU membership. The National Council did not participate in the formulation of the negotiation positions.

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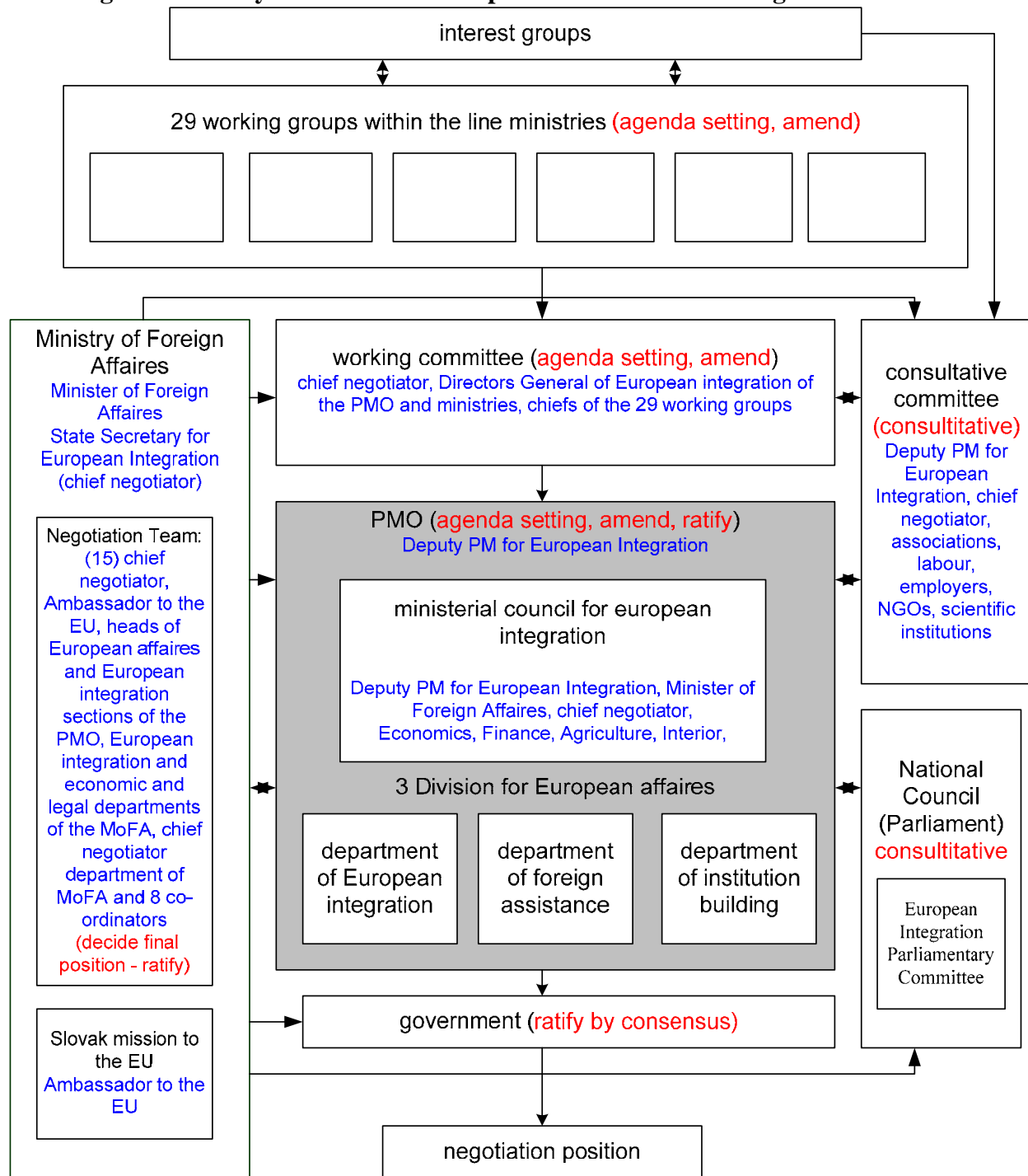
<sup>179</sup> Ibid., p. 85.

<sup>180</sup> Interview by Author with the Chief Negotiator of the Slovak Republic, Bratislava, 05/03/2003.

<sup>181</sup> A. PODRAZA, *Central Europe in the Process of European Integration. A comparative Study of Strategies of the Czech Republic, Hungary, Poland and Slovakia; Towards Deepening and Widening of the European Union*, Research Support Scheme, Open Society Support Foundation, 2000., p. 85-86.

<sup>182</sup> Interview by Author with Representative of the Slovak Anti-Monopoly Office, Bratislava, 24/02/2004.

**Figure 37: Policy Process for the Preparation of Slovakia's Negotiation Position**



Note: Chief Negotiator = State Secretary of European Integration at the MoFA  
 Source: Own Compilation on the basis of interviews with ministerial and government representatives and literature: Office of the the Government of the Slovak Republic, *Slovakia & European Union*, Bratislava, s.d; A. PODRAZA, *Central Europe in the Process of European Integration. A comparative Study of Strategies of the Czech Republic, Hungary, Poland and Slovakia Towards Deepening and Widening of the European Union*, Research Support Scheme, Open Society Support Foundation, 2000; Government of the Slovak Republic, *Government Action Plan* 14 January 1999; The Government of the Slovak Republic, *Statute of the Chief Negotiator of the Slovak Republic for Negotiations on Slovakia's Accession to the European Union*, December 1999.

### Negotiation Positions

Slovakia had eight institutions dealing formally with the preparations of EU enlargement. A negotiation position would generally be reached after making its way through three levels of government, i.e. the line ministries, the negotiation team and the PMO<sup>183</sup>. The initial draft position papers formed within the line ministries. Under time pressure the experts attempted to contact all the relevant partners. They would make a pre-review and present an opinion to the working groups. In parallel the experts would prepare consultative reports for the EC, which usually led to the negotiation position the EC anticipated<sup>184</sup>. Finally, the position would receive EC confirmation before closing the discussion in the working groups. According to some interviewees the line ministries accepted all the EUs advice even at the expense of sectoral interests: 'They wanted to show the EC that they were up to the job'<sup>185</sup>.

In the event of disagreement among experts the issue would be passed onto the chief negotiator and the head of the mission to the EU. Both would try to resolve the matter in consultation with the EC. The chief negotiator would re-arrange the draft position paper in co-operation with and approval from the MoFA. The MoFA was the most important institution that centralised all the preparations: 'We worked according to a centralised model built around the MoFA'<sup>186</sup>.

The position paper then would go to the PMO<sup>187</sup>. The PMO would produce two documents upon request of the EU. The first entailed a government declaration in which it would give the tasks for legislative implementation to the line ministries. To ensure implementation the PMO kept direct contact with the head of the working groups in the line ministries. Subsequently, it would inform the Deputy PM for European Integration whose task was to supervise the internal legislative process<sup>188</sup>. The government needed to approve every position paper which it turned into a negotiation mandate<sup>189</sup>. The MoFA would then send the negotiation position to the Slovak mission to the EU who would pass it on to the EC, the EU presidency, and the Secretariat of the Council.

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<sup>183</sup> Interview by Author with Representative of the EC's Delegation to the Slovak Republic, Bratislava, 11/03/2004.

<sup>184</sup> Interview by Author with Representative of the World Bank Slovakia, Bratislava, 02/03/2004b.

<sup>185</sup> Interview by Author with Representative of the Slovak State Institute for Drug Control, Bratislava, 12/03/2004b.

<sup>186</sup> Interview by Author with the Chief Negotiator of the Slovak Republic, Bratislava, 05/03/2003.

<sup>187</sup> Interview by Author with Representative of the Negotiation Team of the Slovak Republic, Vienna, 04/05/2004c.

<sup>188</sup> Interview by Author with Representative of the Slovak Office of the Government, Bratislava, 12/03/2004a.

<sup>189</sup> Interview by Author with the Chief Negotiator of the Slovak Republic, Bratislava, 05/03/2003.



Most TPRs based on consultations with the relevant sectors, but only after comparison with neighbouring countries<sup>190</sup>: ‘When we prepared our negotiation position we first looked at what neighbouring countries were doing and in particular the Czech Republic. Then our experts would get to work. They set concrete priorities’<sup>191</sup>. TPRs always came via domestic channels and predominantly via the line ministries. They originated at the firm level, particularly for agriculture and competition policy. For the other TPRs it was the state which took the initiative after comparison with the neighbour’s negotiation position and the common position of the EU-15 MS: ‘We had an understanding with the Czech Republic and studied their positions carefully and their experience in the negotiations.’<sup>192</sup>. ‘Because we were catching up we could learn from our neighbours. Nobody wanted to have a worse condition. Sometimes we were waiting to see what the others were requesting’<sup>193</sup>.

This tactic created difficulties for certain sectors. Companies would pressure the government to put forward TPRs. Among the employers only those sectors with international experience were well informed and prepared: ‘Generally, international companies were well received. It was not automatic but it had a slightly positive effect. Slovak companies on the other hand were not well informed and prepared. They had a disadvantage’<sup>194</sup>.

Usually the sector would ask for a TPR in the form of exemptions and a number of years. The government in this respect would not compromise and put forward TPRs to protect the interests of US Steel, VW Wolfsburg and the energy sector vis-à-vis the EU<sup>195</sup>.

Slovakia did not perform general impact studies on enlargement. The IMF, the OECD and the WB were the only institutions that performed impact studies: ‘There was too little time, a lack of expertise and funds to commission impact studies’<sup>196</sup>. Authorities were aware that the lack of

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<sup>190</sup> *Interview by Author with Representative of the EC's Delegation to the Slovak Republic, Bratislava, 11/03/2004.*

<sup>191</sup> *Interview by Author with Representative of the Ministry of Foreign Affairs of the Slovak Republic Bratislava, 03/03/2004.*

<sup>192</sup> *Interview by Author with Representative of the Negotiation Team of the Slovak Republic, Vienna, 04/05/2004c.*

<sup>193</sup> *Interview by Author with Representative of the Ministry of Foreign Affairs of the Slovak Republic Bratislava, 03/03/2004.*

<sup>194</sup> *Ibid.*

<sup>195</sup> *Interview by Author with Representative of the EC's Delegation to the Slovak Republic, Bratislava, 11/03/2004.*

<sup>196</sup> *Ibid.; Interview by Author with Representative of the Slovak Office of the Government, Bratislava, 12/03/2004a.; Interview by Author with Representative of the Negotiation Team of the Slovak Republic, Vienna, 04/05/2004c.; Interview by Author with Representative of the Negotiation Team of the Slovak Republic, Vienna, 04/05/2004c.*

impact studies was an important weakness in the negotiations: ‘To have good arguments is really important but also difficult as most legislation was new to us [...] Slovakia went to the negotiating table empty handed and badly prepared’<sup>197</sup>.

The only serious impact studies came out at the very last stage of the negotiations. The only certain information at the disposal of the chief negotiator was the impact of EU legislation on taxation and competition on public finances<sup>198</sup>. In these areas TPRs were substantiated by research and hard data. Expertise and arguments were important: ‘In several cases we would not have been able to push for TPR without data. In the case of the tobacco industry their reports and figures really helped us’<sup>199</sup>. ‘When we had sectoral impact studies, such as company data, we could build a case. Otherwise this would not be possible’<sup>200</sup>.

Some interviewees claimed that a cost benefit analysis of EU membership for Slovakia was politically too risky: ‘The political risk of a cost-benefit analysis was too high. If it [EU membership] was seen as too costly certain politicians could have seized on the studies and hijack Slovakia’s EU membership ambitions. After the EU’s first rejection in 1997 we did not want to take risks’<sup>201</sup>.

Slovakia held consultation with the EC before the draft position papers became official<sup>202</sup>. The bargaining space was limited and the EC would always ask for additional opinions and motivations when TPRs emerged. The EC generally took a very uncompromising attitude on TPRs. The ministries were generally not ready to protect the respective sectoral interests let alone go all the way in the negotiations: ‘If you want to become a member of the EU, a member of the club, it is up to you to be flexible. Slovakia had to give in. We felt that we were at the weak end. The EC reduced the requests and would not compromise’<sup>203</sup>.

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<sup>197</sup> Interview by Author with Representative of the Confederation of Slovak Trade Unions (KoZ SR) Bratislava, 25/04/2004.

<sup>198</sup> Interview by Author with Representative of the World Bank Slovakia, Bratislava, 02/03/2004b.

<sup>199</sup> Interview by Author with Representative of the Ministry of Foreign Affairs of the Slovak Republic Bratislava, 03/03/2004.

<sup>200</sup> Interview by Author with the Chief Negotiator of the Slovak Republic, Bratislava, 05/03/2003.

<sup>201</sup> Interview by Author with Representative of the Slovak Anti-Monopoly Office, Bratislava, 24/02/2004.

<sup>202</sup> Interview by Author with the Chief Negotiator of the Slovak Republic, Bratislava, 05/03/2003.

<sup>203</sup> Interview by Author with the representative of the National Bank of the Slovak Republic, Bratislava, 05/03/2004.

From observing neighbouring countries and the EC's opinion on the first draft position papers the Slovak negotiation delegation decided to respect the precautionary principle and restrict TPRs: 'It was in our interest to keep TPRs as short as possible. As a general rule the Ministries (MoFA) and the PMO would attempt to limit their scope and duration'<sup>204</sup>. The chief negotiator knew from the political discussions in Brussels what was feasible: 'We knew the range of the EC and we had a comparative advantage of catching up with the other applicant countries. We were learning from their mistakes, particularly from the Czech Republic'<sup>205</sup>. As an official concluded: 'One or two countries set up an extensive consultation process involving all the social and economic partners as well as the Parliament. We were wondering why they wanted to join the EU'<sup>206</sup>.

The administration's approach to limit TPRs conflicted with the interests of some well organised sectors. These sectors tended to be multinationals and very effective when lobbying the Slovak government and the EU. Given their impact on employment, GDP and the balance of payments they were too important for the government to ignore. According to the a World Bank representative US Steel and VW Wolfsburg, two companies that would lose their tax holidays after Slovakia's accession, were politically very important. The government wanted to please both companies because they represented the first large investments in the country and were assumed to be important for Slovakia's image abroad and their multiplier effect on FDI<sup>207</sup>. The EC representative in Slovakia agreed with this reading. These companies complicated Slovakia's EU accession drive. They contacted both the government and the EC. They were sitting at the table when Slovak representatives were negotiating with the EU: 'It made a difference whether a sector was internationalised and concentrated on the domestic market. Their sheer economic strength prevented the government from compromising on TPRs'<sup>208</sup>.

In the area of pharmaceuticals the chief negotiator refused to take in account the objections against full application of the *acquis* on property rights. When a representative of the pharmaceutical industry attempted to contact the MoH it had already formed an opinion without

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<sup>204</sup> Ibid.

<sup>205</sup> *Interview by Author with Representative of the Slovak Office of the Government, Bratislava, 12/03/2004a.*

<sup>206</sup> *Interview by Author with Representative of Slovak Ministry of Transport, Bratislava, 02/03/2004a.*

<sup>207</sup> *Interview by Author with Representative of the World Bank Slovakia, Bratislava, 02/03/2004b.*

<sup>208</sup> *Interview by Author with Representative of the EC's Delegation to the Slovak Republic, Bratislava, 11/03/2004.*

consulting the industry<sup>209</sup>: ‘They had approved of the position paper and closed the chapter in the negotiations. The government refused to reopen the position or the chapter’<sup>210</sup>. One official stated: ‘It was not a problem for Slovak pharmaceutical companies. Slovakia had little generic production’<sup>211</sup>.

In contrast, the negotiation delegation was prepared to fight for the steel industry and US Steel. Officials from the Slovak National Bank argued: ‘The chief negotiator had no other choice. Export oriented sectors had priority. The government looked at the balance of payments and the budget. Given that US steel had such a large impact on both it was obvious for the authorities what to do’<sup>212</sup>. US Steel was financially affected, mobilised aggressively and directly contacted the government: ‘We were using their analysis in the negotiations and their representatives attended the meetings in Brussels’<sup>213</sup>. US Steel was not aware how Brussels functioned. It assumed that the negotiation team acted against their interests. US Steel argued that because it was an American company it had a disadvantage: ‘Let us say that it did not help them, particularly when considering their case in the light of VW Wolfsburg where EU Commissioner *Gunter Verheugen* was personally involved in the negotiations’<sup>214</sup>.

The transport the working group in co-operation with the MoFA and PMO formulated the negotiation position. The road transport partners were consulted, but only after the position was final: ‘It was for comments at the end of the process’. One representative said: ‘We were invited by the MoT for a dialogue on EU enlargement. It was some sort of gentlemen’s agreement as the MoT wanted us to comply with the *acquis*. There was a clear understanding that the government wanted to close the chapter because Slovakia was catching up. Employers did not pressure the government because it was not necessary, certainly not in comparison to our Hungarian colleagues’<sup>215</sup>. In the end Slovakia did not formulate TPRs in the transport chapter: ‘The problems were the result of a spill over from the Czech Republic’<sup>216</sup>.

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<sup>209</sup> State Institute for Drug Control *Requirements and procedure for achieving compliance of marketing authorisations of medical products in the Slovak Republic with "acquis communautaire"*, Bratislava, guideline No. 05/2002.

<sup>210</sup> *Interview by Author with Representative of the Slovak State Institute for Drug Control*, Bratislava, 12/03/2004b.

<sup>211</sup> *Interview by Author with Representative of the Negotiation Team of the Slovak Republic*, Vienna, 04/05/2004c.

<sup>212</sup> *Interview by Author with the representative of the National Bank of the Slovak Republic*, Bratislava, 05/03/2004.

<sup>213</sup> *Interview by Author with the Chief Negotiator of the Slovak Republic*, Bratislava, 05/03/2003.

<sup>214</sup> *Interview by Author with Representative of the Negotiation Team of the Slovak Republic*, Vienna, 04/05/2004c.

<sup>215</sup> *Interview by Author with Representative of the Slovak International Transport Trade Union*, Bratislava, 26/02/2003.

<sup>216</sup> *Interview by Author with Representative of Slovak Ministry of Transport*, Bratislava, 02/03/2004a.

## **Institutional Comparison of the V-4 Countries**

The variation of formal or constitutional veto players among the V-4 in the enlargement process is minimal. The Czech Republic, Hungary, Poland and Slovakia had three constitutional veto players in place to negotiate EU membership, i.e. the president, the government and the parliament. The power to set the agenda and conduct foreign policy, rested with the president and the government. In all countries the president's power to conduct foreign policy was delegated to the government. He retained symbolic authority over EU enlargement policy but refrained from direct involvement.

The key political control for agenda setting and organising EU accession policy rested with the governments in Prague, Budapest, Warsaw and Bratislava.

The parliaments in the region had the constitutional right to ratify the EU accession treaties negotiated by their respective executives. They all decided to delegate the ratification authority by passing legislation for a referendum on EU membership. In the Czech Republic ratification of the accession treaty meant the approval by a simple majority of those participating in the referendum. After numerous proposals the Hungarian Parliament settled for a referendum that required the endorsement of '25 plus 1' per cent of those participating. Only in Slovakia and Poland was the bar in the EU accession referenda raised to a quorum of the electorate under a simple majority.

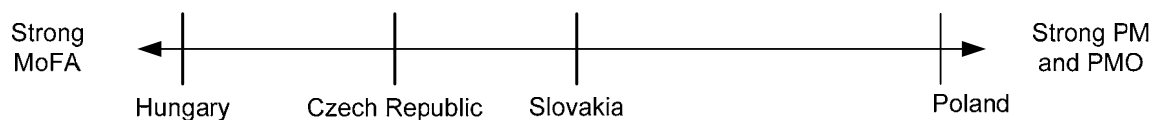
The formal political power to negotiate EU membership rested with the national executives. Each set up an institutional framework for negotiating EU membership. Despite different national traditions, institutional structures inherited from Communism and those for negotiating the EAs, these institutional frameworks turned out to be remarkably similar across the applicant countries. And, they converged under pressure of the accession negotiations between March 1998 and December 2002.

These findings are somewhat contradictory to those of *Brusis* and *Emmanouilidis* who claim that 'advanced candidate countries [...] developed [...] quite different institutional arrangements in

response to the negotiation task posed by the EU<sup>217</sup>. It qualifies their findings to the extent that the administrative structures were not static over the four years of EU accession negotiations. The heavy demands and pressures emanating from the preparations for and progress in the accession negotiations resulted in rather drastic changes in policies, procedures and executive institutions. Finally, institutional frameworks differed as to the supply of protection for interest groups in some crucial aspects. Also here did the V-4 countries converge.

According to the distribution of power one can place the V-4s formal institutions and administrative structures (1998, see Figure 33, 34, 35, 36) for transposing the *acquis* and negotiating EU membership along a continuum (see Figure 38) in a two dimensional space. At one extreme of the line a strong co-ordinative and decision making role is reserved for the PM, the PMO and subordinate agencies and institutions. At the outset of the negotiations Poland represented this model. At the other extreme one finds the model based upon a strong MoFA. Hungary perfected this model. The EC recommended it to the other candidate countries. In the Czech Republic the MoFA dominated the conduct of the accession negotiations, however, it was not as powerful as in Hungary. Slovakia occupied the middle ground. The Bratislava authorities struck a balance between the government and the MoFA with the creation of a special Minister of European Integration at the heart of the PMO.

**Figure 38: Distribution of power among EU Decision Making Institutions of the V-4 (1998)**

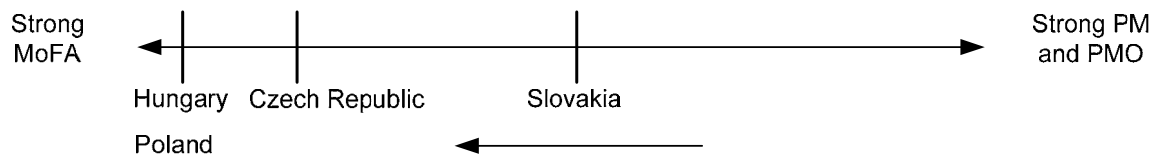


As the negotiations progressed the Czech Republic and more radically Poland changed the institutional set up dealing with the EU accession process (see Figure 39). In February 2000 Prague initiated a limited reform of the central government decision-making bodies streamlining the procedures indirectly favouring the MoFA. The MoFA wanted to speed up the negotiations and keep the road to EU membership clear of obstacles. Warsaw changed the institutional structure drastically as a result of the government changeover after the general elections of

<sup>217</sup> M. BRUSIS and J.A. EMMANOULIDIS, *Negotiating EU Accession: Policy Approaches of Advanced Candidate Countries from Central and Eastern Europe*, Bertelsmann Foundation, Bertelsmann Group for Policy Research, Centre for Applied Research, July 2000., p. 22.

September 2001. The Polish MoFA gained substantial powers at the expense of the more politicised agencies under the authority of the PM and PMO.

**Figure 39: Distribution of power among EU Decision Making Institutions of the V-4 (2000-2001)**

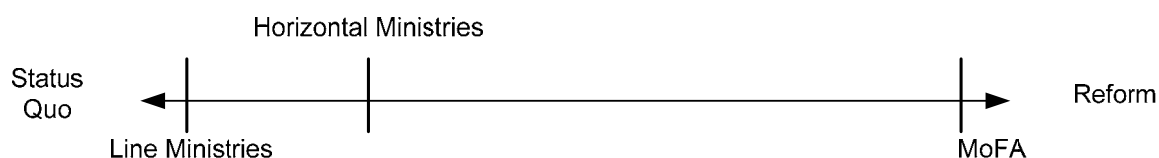


The skewed power distribution towards the MoFA resulted in sharply reduced responsibilities for the line ministries with vertical (sectoral) interests. Concentration of power in the MoFA came at the expense of other ministries with horizontal responsibility such as the MoFI, the MoI or MoE in all V-4.

EU membership took absolute priority for the MoFA. It was directly plugged into the EU accession game in Brussels and of all national institutions stood closest to the EC’s point of view. The MoFA was more ignorant about and insulated from societal pressures such as sectoral interests. It represented the case for reform.

In contrast, the line ministries would be less insulated from sectoral interests and more susceptible to maintaining the status quo. They were positioned at the opposite end of the two dimensional space (see Figure 40) and would maintain vertical (sectoral) contacts with the respective sectoral interests at the expert level. They generally would be more inclined to understand the potential impact of EU legislation on the market.

**Figure 40: Preference Formation of EU Decision Making Institutions**



Members of ministries other than the MoFA such as the MoFI, MoI or MoE with horizontal responsibility understood the position of the line ministries better. They were more concerned

with the quality of EU membership. Unlike the MoFA they were less inclined on joining the EU at all costs.

The strong role of the executive and the rise of the MoFA's responsibility were mirrored by a declining role of national parliaments. While the Houses of Parliament in the V-4 were required to pass over 80,000 pages of EU legislation ahead and during the negotiations, they were given no or only limited powers in the area of negotiating EU membership. Not one MP or Senator in their own legal personality had an executive position in the EU accession policy making process between 1998 and 2002 in all the individual V-4. Moreover, under the banner of efficiency and time pressure governments in the V-4 attempted to limit political oversight of the Parliament on the EU accession process.

In the Czech Republic the government attempted to adopt a constitutional law, which would have allowed EU related legislation to pass by decree. In 2000 it succeeded in reducing parliamentary procedures that required three readings for EU-legislation to pass. In Hungary, the single chamber Parliament refrained from subjecting EU membership to a bi-partisan political struggle. In the joint declaration of September 2000 all political parties agreed on promoting legal harmonisation in the Parliament. The declaration prevented blockages of EU related matters as a result of party clashes. In Poland and Slovakia Parliament could only express its opinions on EU integration in the presence of the government during one annual debate. As I will show in Chapter 7 the shadow of the Houses of Parliament loomed large over the process in Poland and Slovakia in contrast to the Czech Republic and Hungary. Regardless, governments in the region were at pains to make sure Parliament would not put any obstacles on the road to EU membership.

The growing insulation of the EU related decision making processes in the V-4 as a result of (a) the convergence of formal veto players; (b) the reinforced role of the executive and the MoFA; and (c) the declining influence of the line ministries and sectoral preferences, resulted in a general reduction of TPRs both in content and duration.



Opposition to the status quo was complemented by the EC's insistence on the adoption of the full acquis. The V-4 government's feared that TRPs would indicate their unwillingness to comply with the acquis, and hence that they were ill prepared for EU membership. The inexperience with EU legislation, the lack of impact studies and hard data reinforced the reduction of TPRs in the position papers. The V-4 chief negotiators found it hard to counter the EC when good arguments were lacking. Following the so-called *precautionary principle* the V-4 limited TPRs before they were officially presented in the position papers.

The V-4 countries differed most at the outset of the negotiations. Hungary had set up a specific institution, the EIC, to consult sectoral interests, the market and the social partners. It went to the negotiations after a well organised concerted effort to consult the different sectoral interests. The system worked well. Sectors were generally well organised and the line ministries, experts and teams received a good deal of input.

In the Czech Republic the consultations occurred in the working team for European integration. There were more of an informative nature and were not used to the full by employers and labour associations. Moreover, the precautionary principle dominated the talks on the position papers making the partners reluctant to put TPRs on the table.

The Polish policy makers set up a system at the heart of the PMO chaired by the chief negotiator with the purpose of collecting information from sectoral interests about the potential impact of EU related legislation. The NCEI did not function well. Sectoral interests were too fragmented and did not speak with a single voice. The chief negotiator and other institutions were keen on sectoral input. Instead, they often were confronted with a plethora of interests. The consultative committee in Slovakia set up with a similar purpose turned out to be a paper tiger and was rarely used. There was simply not enough time for a consultation procedure.

In this area the V-4 converged between 1998 and 2002. In Hungary consultations increasingly occurred directly between the MoFA and the experts and sectoral interests. While the meetings were relatively frequent in the Czech Republic they became increasingly informative. In Poland the government abolished the NCEI after October 2001. In Slovakia limited consultation

occurred between the chief negotiator, the government and the sectors when they mobilised politically.

Under a growing insulation of the institutional process and the decline of organised consultation predominantly large export oriented companies and well organised sectors were able to gain access to EU related institutions. It did not mean that governments and the MoFAs had difficulty in controlling sectoral interests as Brusis and Emmanouilidis claim<sup>218</sup>. On the contrary, the insulation was designed to reduce interference from society and went hand in hand with reducing the number and scope of TPRs in all the V-4.

Governments prioritised and picked TPRs on a case by case basis in the position papers following the logic of destructive and constructive interference. Chapter 6 shows that priorities took shape according a combination of the *acquis*' impact on the government budget, the political salience of issues and the strength of the sectoral interests that lobbied for the status quo. Sectoral businesses that (a) were well organised; (b) could produce good arguments for TPRs; (c) and had direct access to the government or alternatively could set up an effective lobbying campaign, would generally have their interests represented in the position papers. As chapters 3, 4 and 5 have shown these sectors had an international outlook and tended to be export oriented.

The effect TPRs would have on the budget and the potential for political salience contributed to the already well organised pharmaceutical sector's strength in Hungary and Poland but not in the Slovakia and the Czech Republic. In contrast, the TPRs in the steel industry had a negative effect on the government's budget and its political significance was concentrated. In the area of road transport a TPR would have no effect on the budget and its potential for political salience was negligible.

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<sup>218</sup> *Ibid.*, p. 23.

## **Conclusion**

In chapter 6 I demonstrate that the number of institutional veto players in the Czech Republic, Hungary, Poland and Slovakia has an important influence on states' acceptance of sectorally solicited TPRs analysed in chapter 3, 4 and 5. The relationship between the number of TPRs – the likelihood of maintaining the status quo – and the number of veto players is dynamic and acceptance of TPRs follow the logic of constructive and destructive interference.

That is to say, between 1998 and the end of 2002 the number of institutional domestic veto players in the EU enlargement process declined and partisan veto players' preferences systematically converged on the case for reform, i.e. full EU membership. The presidents in the V-4 delegated their power to the governments in the area of EU foreign policy. Despite being the workhorses of the enlargement policy passing over 80,000 pages of EU related legislation Parliaments under influence of their respective government's voluntarily gave up their say on the direction of EU enlargement policy. Under much wavering and many delays they delegated the ratification constraint on EU membership to the electorate under a surprisingly low threshold in the Czech Republic and Hungary. Only in Poland and Slovakia was the referenda constraint maintained. Overall, this allowed the executives to increasing their grip on enlargement policy.

In parallel, within the executive the distribution of power changed in favour of those ministries that directly represented the case for reform, i.e. full EU membership as early as possible. The MoFA gained in responsibility at the expense of those ministries concerned about the sectoral and overall costs of EU enlargement such as the line ministries and the MoFI, MoE or MoI which were less willing to compromise on the status quo.

The reduction of veto players and the convergence of the preferences among partisan veto players did not give the executive a free hand in enlargement policy. The ratification constraint of the referendum combined with the presence of strong sectoral interests, encouraged government's to consider TPRs according to the logic of constructive and destructive interference. Governments prioritised and picked TPRs on a case by case basis according to a combination of the acquis' impact on the government budget, the political salience of the issues at hand and the strength of the sectoral interests that lobbied for the status quo.

Governments' did have little other means to gauge the impact of the acquis as impact studies were rare. During a meeting of the Luxembourg Six countries one chief negotiator asked about the presence of impact studies in other countries. The reply of the Cypriot chief negotiator summarises the situation well: 'If you had prepared impact studies about the political, social and economic effects of the 1989 revolutions you would never have embarked upon a revolution'<sup>219</sup>. It meant that cost benefit calculations were few and probably would have come out against the benefits. As a result, candidate countries usually would lose the argument over TPRs with EC because they had little hard evidence to make requests stick.

The effect TPRs would have on the budget and the potential for general political salience contributed to the already well organised pharmaceutical sector's strength in Hungary and Poland but not in the Slovakia and the Czech Republic. In contrast, the TPRs in the steel industry had a negative effect on the government's budget and its electoral political significance was concentrated. In the area of road transport a TPR would have no effect on the budget and its potential for political salience was negligible.

In other words, domestic institutions mediated the sectoral demand for the status quo in the enlargement process and set the bargaining space for governments and their chief negotiators at the international negotiating table, which I will discuss in chapter 7.

Among the accession states, the lack of a separate turnout requirement placed Hungary alongside the Czech Republic and contrasted with the 50 per cent turnout required in Poland and Slovakia.

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<sup>219</sup> *Interview by Author with Representative of Ministry of Foreign Affairs of Hungary, Budapest, 13/02/2004.*

## CHAPTER 7: STRATEGIES

How and why applicant countries were able to negotiate sectoral exemptions from the *acquis*? Negotiation theory predicts the acquiescence of applicant states in the negotiations when confronted with the EU's dominant bargaining power. Chapter 6 attempts to answer this final part of the research puzzle. It also attempts to find an explanation for the presence of TAs where sectors did not politically mobilise (see Part II) or countries did not support TPRs in the respective position papers (see chapter 6)?

An appraisal of the enlargement negotiations and their distributional outcomes requires an understanding of the bargaining power of its participants. The chapter makes the argument that *the ability to realise the national negotiation positions at the international bargaining table is related to the level of the negotiator's domestic negotiation constraint*<sup>1</sup>. According to Schelling's paradox of weakness variation in the size of the domestic win sets affects the room for manoeuvre of governmental negotiators in the international arena and their bargaining advantage.

To add weight to this conjecture the chapter engages with: (a) the institutional characteristics of the accession negotiations; (b) the institutional framework for the EU to arrive to its common negotiation position; and (c) the domestic constraints on and strategies of the V-4 at the negotiating table. It demonstrates how these three factors affect the international negotiation mandate and bargaining power in the enlargement negotiations. I find that the presence of at least one domestic veto player in the V-4 has a clear impact on the distributional outcomes in the EU enlargement negotiations.

### Introduction

In the EU enlargement and negotiations literature structural power asymmetry is assumed to be the cause of distributional outcomes among the negotiation parties<sup>2</sup>. In contrast, I have shown in chapter 1 that structural power derived from the economic weight and population is neither a

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<sup>1</sup> T.C. SCHELLING, *The Strategy of Conflict*, Cambridge, Massachusetts: Harvard University Press, 1960., p. 22.

<sup>2</sup> C. PRESTON, *Enlargement & integration in the European Union*, London; New York: Routledge, 1997., p. 19-22. Helen Wallace describes the power asymmetry as a core assumption of the enlargement literature as follows: (a) Enlargement is an asymmetrical process in which the incumbent members, in the driving seat, engage with the candidates, which are supplicants and dependants; (b) the issue for the incumbents is whether or not the candidates are desired or desirable partners in terms of their fit with the existing and established patterns of integration, in: H. WALLACE, EU enlargement: A neglected subject, in: M. G. COWLES, *The State of the Union: Risks, Reform, Resistance, and Revival*, Oxford: Oxford University Press, 2000, pp. 149-63.

necessary nor a sufficient condition to explain the presence of TAs and their distribution among the applicant states<sup>3</sup>.

Despite the presence of fundamental power asymmetries, reinforced by the negotiation framework, the Schelling conjecture predicts, *ceteris paribus*, that the most constraint negotiator is likely to do better at the negotiating table when his opponent's hands are less tied. Schelling argued that if 'the executive branch is free to negotiate the best arrangement it can, it may be unable to make any position stick and may end up by conceding controversial points because its partners know, or believe obstinately, that it [the United States] would rather concede than terminate the negotiations. But if the executive branch negotiates under legislative authority, with its position constrained by law [...] then the executive branch has a firm position that is visible to its negotiating partners'<sup>4</sup>.

The dynamic in the fifth EU enlargement negotiations appears largely similar to this logic. The chief negotiator in the accession process might choose to encourage and make public his negotiation constraints present in the form of sectoral interests or a binding referendum to increase her bargaining power at the international level. Conversely, the chief negotiator might choose to have a decision mandate that is loosely defined. She might chose to keep her negotiation position secret indicating to her opponent that she is prepared to compromise. A case in point is Hungary's accession negotiation strategy whereby the negotiation positions were kept secret even to the legislature: 'You do not want to tie your hands in the negotiations to maintain a capacity to negotiate'<sup>5</sup>.

Exploring whether a negotiator benefits from domestic constraints helps us explaining the variation in international outcomes, particularly when traditional accounts are unsatisfactory.

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<sup>3</sup> Cyprus, Estonia, Malta, Latvia and Slovakia are the most obvious counter intuitive cases. Poland and Malta are cases at the opposite end of the power spectrum where aggregate economic and popular weight are inadequate predictors of the presence and number of TAs when not used in conjunction with other explanatory factors. As Thomas Schelling argues: 'These qualities [more financial resources, more physical strength, more military potency or more ability to withstand losses] are by no means universal advantages in bargaining situations; they often have a contrary value', in: T.C. SCHELLING, *The Strategy of Conflict*, Cambridge, Massachusetts: Harvard University Press, 1960., p. 22. This leaves the door open for alternative explanatory factors. See also S. MEUNIER, What Single Voice? European Institutions and EU-U.S. Trade Negotiations, in: *International Organization*, 2000, 54(1), pp. 103-35.; CLARK W.R, DUCHESNE E and MEUNIER S, Domestic and International Asymmetries in United States-European Union Trade Negotiations, in: *International Negotiation*, 2000, 5(1), pp. 69-95.

<sup>4</sup> T.C. SCHELLING, *The Strategy of Conflict*, Cambridge, Massachusetts: Harvard University Press, 1960., p. 28.

<sup>5</sup> Interview by Author with the Chief Negotiator of Hungary, Budapest, 09/02/2004.

Following Schelling paradox of weakness it would be plausible to argue that domestic institutional contexts such as the number of veto players and their preferences would have an influence on the respective bargaining power and ultimately the level of success judged by the nature of the TAs in the EU enlargement negotiations<sup>6</sup>. Therefore, to understand the presence of TAs and their distribution across the applicant countries requires an insight of the influence of domestic institution's on the bargaining behaviour of international actors.

In the following sections I first disentangle the origins of the institutional power asymmetries in the EU-V-4 negotiation relationship. Subsequently, I draw a simple two dimensional spatial model indicative of the explanatory power of the role of domestic institutions in the distributional outcomes of the enlargement negotiations. Finally, I provide a litmus test of the model by demonstrating the influence of domestic veto players (see chapter 6) on the negotiations' outcomes for three sectors across four countries (see chapter 3, 4 and 5).

## **7.1. Institutional Characteristics of the Accession Negotiations**

While keeping the EU constant it is useful to consider the origins and mechanisms of the EU's dominating bargaining power in the enlargement negotiations. In the following sections I describe the institutional setting of the negotiations followed by an analysis of the determinants of the EU's international bargaining capacity including its common negotiation position, the supranational voting rule, and the level of delegation in the negotiations. I supplement the analysis with a number of idiosyncratic elements present in the accession negotiations.

### **7.1.1. Institutions**

The EU accession negotiations concern over 80.000 pages of EU legislation. For the negotiations the legislation is divided into chapters, each representing one policy area and its corresponding legislation. For each chapter the applicant countries formulate position papers, which they present to the Council of the EU (henceforth Council) in Brussels. In response the EC draws up the draft common (negotiation) positions (DCP), which it submits to the Council for consultations. Within the Council the DCP is discussed in the enlargement working group where most of the decisions

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<sup>6</sup> I attempt to avoid the functionalist fallacy to the extent that I do not automatically assume that the negotiator can shape his domestic constraints.

on the negotiations positions are taken<sup>7</sup>. This group usually comprises the officials from the Permanent Representations of the EU member states in Brussels. It reports to the Committee of Permanent Representatives (COREPER) in the Council, which has the overall responsibility for preparing the CPs. The DCP is also discussed in the capitals of the member states. On the basis of the DCP the Council decides a Common (negotiation) Position (CP) and presents it to the candidate countries. Henceforth the chapter can be opened for negotiation (see Figure 41)<sup>8</sup>.

The accession negotiations have an intergovernmental character (see Figure 41). They take place in many intergovernmental conferences (IGCs) with a leading role for the governments of the EU member states and the Council. The Council creates these temporary IGCs as an official forum for conducting the accession negotiations. In the IGCs the EU MS act as a collective negotiator. Their positions are represented by the current Presidency of the EU<sup>9</sup>. It is the Presidency which presents the CP to the candidate countries and speaks for the EU in the negotiations. It also decides which chapters should be tackled first, which is a not a small prerogative<sup>10</sup>.

Notwithstanding, the recurrent necessity for common solutions the IGCs are structured along a single negotiation framework with parallel bilateral negotiations between the EU and each candidate country. The Council convenes the IGCs with each of the applicants, which meet at ministerial and ambassadorial level with the former at the level of the heads of delegations (Ministers of foreign affairs of the candidate state and the member states) and the latter at the level of the deputy heads of delegations (chief negotiator and permanent representatives). The more important negotiating rounds are those at the deputy level. The chief negotiators from the applicant countries and the EU Brussels ambassadors meet formally to open chapters for negotiations and decide which negotiation chapters can be provisionally closed<sup>11</sup>. The IGCs are a formal with each side presenting its meticulously prepared negotiation position, which is usually

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<sup>7</sup> Frequently the EU replied to the position papers of the candidate with a long series of further questions often leading to new position papers and new common positions. This resulted in frustration on the applicant country side. One interviewee said: 'The EC was very inventive in formulating additional questions to the line ministries', in: *Interview by Author with Representative of the Ministry of Finance of Hungary*, Budapest, 06/02/2004 and 18/02/2004.

<sup>8</sup> A. MAYHEW, *Enlargement of the European Union: an analysis of the negotiations with the central and eastern European candidate countries*, Brighton: University of Sussex, 2000., Annex 1, pp. 68-71.

<sup>9</sup> The Presidency of the EU is a rotational chairmanship of the meetings of the Council performed for six months successively by all EU member states.

<sup>10</sup> The Swedish Presidency in this respect presented a watershed in the negotiations. It pressured the EC and the Council to speed up the process. It made enlargement a priority and speeded up the negotiations by opening many chapters.

<sup>11</sup> *Interview by Author with Representative of the EC's Delegation to the Slovak Republic*, Bratislava, 11/03/2004.



preceded by much posturing: ‘At the IGCs the CPs were read out and we would accept them’<sup>12</sup>. The sessions of negotiations mostly lasted less than 60 minutes<sup>13</sup>.

In the entire process the EC assists the MS in their EU accession related work. It makes preparations for the negotiations and explores solutions for specific problems during the negotiations at the Council’s request<sup>14</sup>.

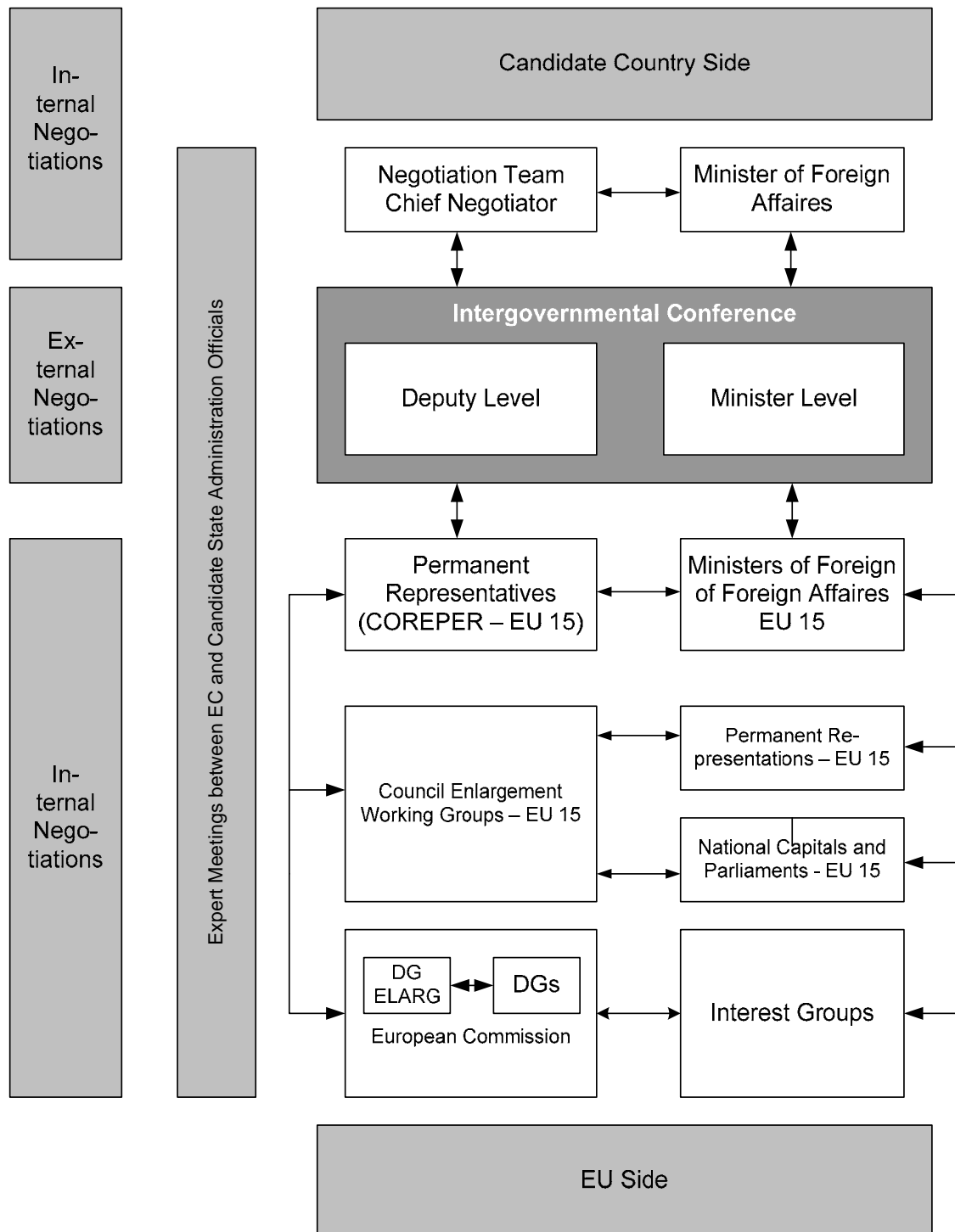
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<sup>12</sup> *Interview by Author with Representative of the Office of the Government of the Czech Republic, Prague, 04/05/2004b.*

<sup>13</sup> A. MAYHEW, *Enlargement of the European Union: an analysis of the negotiations with the central and eastern European candidate countries*, Brighton: University of Sussex, 2000., p. 8.

<sup>14</sup> Government Plenipotentiary for Poland’s Accession Negotiations to the European Union, Chancellery of the prime minister, *Accession Negotiations; Poland on the Road to the European Union*, Warsaw, 2000, pp. 108., p 31.

**Figure 41: The Formal EU Enlargement Negotiation Framework**



Note: For a more detailed analysis of the EU Negotiation Process see: GRANELL, F., The European Union's Enlargement Negotiations with Austria, Finland, Norway and Sweden, in: *Journal of Common Market Studies*, 1995, 33(No. 1), pp. 117-41, p. 124

## 7.1.2. Procedures

### 7.1.2.1 The Common Position

Before the EU opens the accession negotiations on a particular topic its member states need to reach a CP that they will defend with a single voice *vis-à-vis* the applicant states. The CP is characterised by a triple unanimity. It is a daunting threshold for any opponent wishing concessions. One option is to influence the sectoral pivot state among the EU-15.

#### Triple Unanimity

For EU enlargement the member states agreed to retain their individual veto power over every single CP adopted. The unanimity rule makes the EU a tough bargainer. Because each individual member state needs to give his consent the bargaining outcome of the common position stands at or close to the ideal point of the most conservative member state<sup>15</sup>: ‘If one EU MS would have a problem with a TPR or have a view on an issue it usually had a real chance having its position adopted. It was listened to very carefully by the other MS’<sup>16</sup>. ‘Solidarity prevailed among the EU MS. When it occurred they [the EU-15] tried to support the most sensitive country’<sup>17</sup>. ‘There was always one EU MS objecting while the rest was neutral. It resembled a division of labour in the Council. If one EU MS was prepared to fight the others would follow’<sup>18</sup>.

This happens because all other member states are not harmed by the individual position of the lowest common denominator and are unlikely to object to its position: ‘The position of the lowest common denominator counted particularly when the other member states did not care’<sup>19</sup>. While theoretically plausible it is unlikely within the Council that the pivot is composed of only one member state. For instance, it is rare for an individual member state to hold the CP of the Council hostage to its interests. In practice the ideal point of the lowest common denominator is approximated by several member states: ‘Most of the time 2 or 3 EU MS would react and express strong opinions’<sup>20</sup>. One official stated: ‘Usually there were three groups of countries for each

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<sup>15</sup> S. MEUNIER, What Single Voice? European Institutions and EU-U.S. Trade Negotiations, in: *International Organization*, 2000, 54(1), pp. 103-35., p 104.

<sup>16</sup> Interview by Author with Representative 3 of the Negotiation Team of the Czech Republic, Prague, 19/03/2004 and 22/03/2004, Interview by Author with Representative of the Ministry of Finance of Hungary, Budapest, 06/02/2004 and 18/02/2004.

<sup>17</sup> Interview by Author with the Chief Negotiator of the Slovak Republic, Bratislava, 05/03/2003.

<sup>18</sup> Interview by Author with Representative of Ministry of Foreign Affairs of Hungary, Budapest, 13/02/2004.

<sup>19</sup> Interview by Author with Representative of the Office of the Committee for European Integration (UKIE), Warsaw, 21/04/2004.

<sup>20</sup> Interview by Author with Representative of the Hungarian Ministry of Economy and Transport, Budapest, 10/02/2004.

issue on the table. The first would hold strong preferences. The second group would hide behind the first. And the third would be totally indifferent to the issue. Because of the strong solidarity in the Council things would usually go the way of the first group<sup>21</sup>. Sometimes this process would be repetitive: ‘All MS agreed on a CP. Then one would raise an objection and the position would be re-opened, sometimes 20 minutes before the deadline’<sup>22</sup>. In other words, the MS representing the lowest common denominator corresponds to the EUs collective interest in the CP, which the EU subsequently presents with its combined weight internationally.

The EU domestic institutional set up reinforces the unanimity rule. Once a CP is reached it is very difficult to change: ‘It was technically difficult. They [the EU-15] had to agree with 15. Hungary on the contrary could change its position in one day, in 24 hours’<sup>23</sup>. The common positions are the result of a complex and difficult balancing act between the member states that takes place across two levels, i.e. at national and supranational level. At the national level interest groups, parliaments and governments might be involved. They each might prepare reports on distinctive aspects of the negotiations. These feed into the national positions and the negotiations between MS in the enlargement working groups and COREPER<sup>24</sup>.

At the supranational level the negotiations leading up to the CP involve the EC, the EP and in particular the Council. *Mayhew* writes that the ‘capacity of individual EU member states to fight for their national interest in the negotiations leading up to the common negotiation positions should not be underestimated’<sup>25</sup>. This is particularly the case since the norm in for Council decision making is consensus: ‘Everyone’s interest would be catered for with the lowest common denominator taking precedence’<sup>26</sup>.

In addition to the unanimity rule for the CP the outcome of the negotiations is weighed down by the shadow of an *ex post* unanimity ratification constraint. The results of the EU accession negotiations are made in the form of a draft provision of the accession treaty. The draft to the

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<sup>21</sup> Interview by Author with Representative of the Office of the Government of the Czech Republic, Prague, 04/05/2004b.; Interview by Author with Representative of the EC's Delegation to the Slovak Republic, Bratislava, 11/03/2004.

<sup>22</sup> Interview by Author with the Chief Negotiator of the Slovak Republic, Bratislava, 05/03/2003.

<sup>23</sup> Interview by Author with the Chief Negotiator of Hungary, Budapest, 09/02/2004.

<sup>24</sup> A. MAYHEW, *Enlargement of the European Union: an analysis of the negotiations with the central and eastern European candidate countries*, Brighton: University of Sussex, 2000., pp. 68-71.

<sup>25</sup> *Ibid.*, p. 17.

<sup>26</sup> Interview by Author with Representative of the Ministry of Foreign Affairs of Poland, Warsaw, 27/04/2004.

Treaty is subsequently submitted for approval to Council and the EP<sup>27</sup>. For the second time, the Council consents unanimously to the full accession treaty. Subsequently, the treaty makes its way to individual EU member states for submission to the national parliaments and in some member states to a national referendum. The treaty becomes only effective upon ratification by all member states and the applicant country.

As a result of these institutional constraints the bar in the accession negotiations is raised very high. Each individual member state must be satisfied as well as the entire club complemented by an individual member state domestic ratification constraint. It sends a very strong and credible signal to the negotiating partners that the CP is difficult to alter. As a result, the EU's collective bargaining power relative to the applicant countries is directly more significant than its structural bargaining power in terms of economy or population. The EU uses this institutional constraint to encourage its opponent to accept as much as is possible.

### **Opponents Options**

It is worthwhile to look at the constraint of the triple unanimity vote from the perspective of the EU's negotiation partners. They are well aware that the intricacies of reaching a CP reinforces the EU's negotiation position at the international level. They are suspicious that the CP serves the EU as an excuse for frequently refusing concessions: 'It is like negotiating with a black box. We did not know what was happening on the EU's side. We had to be very flexible while the EU was not flexible at all. Mostly the negotiations were simple declarations of the CPs. As the EU-15 agreed on a position it was made clear that it was impossible to change. It would mean to get the 15 back around the table and make them re-agree. That would almost not happen'<sup>28</sup>. The EU's opponent usually reconciled with the deal on the table for fear of a breakdown of the negotiations. Moreover, under the opponent's request to improve upon and re-open an existing CP, EU negotiators regularly use veiled threats of the possibility that an inferior CP might emerge relative to the one on the table.

Nevertheless, the EU's negotiating adversary may attempt to influence the lowest common denominator in the Council: 'The key [...] was to influence the DCP at every stage before it

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<sup>27</sup> The EP votes with a simple majority and falls within the veto player set of the Council and is therefore less relevant.

<sup>28</sup> *Interview by Author with Representative of the Ministry of Finance of Hungary, Budapest, 06/02/2004 and 18/02/2004.*

reached the CP'<sup>29</sup>. In this sense the lowest common denominator becomes the breakpoint country or pivot in the negotiations. Only when the pivot improves upon his offer will the common negotiation position move in the opponent's direction. When the pivot agrees to lift his veto it is likely that other member states with less direct interest at stake would consent: 'If a solution would be found for the MS with a strong position the others would follow'<sup>30</sup>.

Often influencing the pivot within the Council was the only viable strategy for the chief negotiators constraint by their respective capitals to negotiate exemptions from the *acquis*. Interviews have shown that the chief negotiators were well aware of the existence of pivots in the Council: 'The only way to influence the CP was to go to the capitals of the EU MS and influence the individual positions of those countries that had an interests'<sup>31</sup>. For instance, for the pharmaceutical, iron and steel and international road freight transport sectors the Ministers of foreign affaires and the chief negotiators would identify the pivots in the Council, sometimes upon advice of the EC or other MS like the UK, the Netherlands or the Nordic countries: 'Sometimes the EC would indicate which MS was objecting. A change was possible when we influenced that position in the Council through directly talking to the individual MS'<sup>32</sup>.

### **Sectoral Pivots**

In the area of pharmaceuticals 'the Council took a much stricter position than the EC'<sup>33</sup>: 'The EC knew that most of the pharmaceutical companies were subsidiaries of EU companies. It advised the Hungarian team to directly negotiate with the MS, with the capitals and the permanent representatives in Brussels'<sup>34</sup>. Particularly the UK proved important as it was the MS within the Council that had taken charge of the negotiations on pharmaceuticals. It was seen to have strong interests in the area. 'The UK was very active, which was unusual. It generally took a favourable position on EU accession in the Council'<sup>35</sup>. The Hungarian chief negotiator travelled to the capitals of the UK, France and Germany – in that order of importance – to influence their

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<sup>29</sup> *Interview by Author with the Chief Negotiator of Hungary, Budapest, 09/02/2004.*

<sup>30</sup> *Interview by Author with Representative of the Ministry of Foreign Affaires of Poland, Warsaw, 27/04/2004.*

<sup>31</sup> *Interview by Author with Representative of the Office of the Government of the Czech Republic, Prague, 04/05/2004b.*

<sup>32</sup> *Interview by Author with Representative of the Ministry of Finance of Hungary, Budapest, 06/02/2004 and 18/02/2004.; Interview by Author with Representative of the Ministry of Foreign Affaires of Poland, Warsaw, 27/04/2004.*

<sup>33</sup> *Interview by Author with Representative of the Ministry of Finance of Hungary, Budapest, 06/02/2004 and 18/02/2004.*

<sup>34</sup> *Interview by Author with the Chief Negotiator of Hungary, Budapest, 09/02/2004.*

<sup>35</sup> *Interview by Author with Representative of the Committee for European Integration of the Republic of Poland (KIE), Warsaw, 14/04/2004.*

individual negotiation position<sup>36</sup>. ‘It was certain that without negotiating individually with the MS, no solution would have emerged’<sup>37</sup>.

In the area of basic iron and steel production it was the EC that put the pressure on the applicant states: ‘One could distinguish the countries hiding behind the ECs tough stance. They were Luxembourg, Belgium, France, the UK, Spain and Germany – in that order of importance’<sup>38</sup>. ‘I do not know whether there was a concerted action, however, it appeared so. During the negotiation process different EU MS with an interest in the steel industry consecutively raised objections and new issues. Too many EU member states were asking for reconsideration’.

In the area of road freight transport Austria and Germany objected on the DCP. Later the Netherlands joined this group. It had substantial interests in the sector and a substantial share of the German cabotage market<sup>39</sup>. ‘They refused to sign the final deal if the CP would not change. Subsequently the EC started negotiations with Austria and Germany’<sup>40</sup>. ‘The position in Germany and Austria was politically motivated. Elections loomed in Germany and their associations feared EU enlargement. [German Chancellor Gerhard] Schröder wanted to show that he protected their interests’<sup>41</sup>.

#### **7.1.2.2. Level of Delegation**

In the area of EU trade policy a limited negotiating delegation ensures that the final outcome does not diverge from the CP. In the field of EU enlargement the Council does not delegate its negotiating authority to the EC. It is the Presidency of the EU that negotiates with the applicant countries. Hence, the CP adopted by Council sets the limits of the mandate, which the Presidency

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<sup>36</sup> The names of the pivots being the UK, France and Germany were provided by all interviewees concerned and in similar order of importance by six interviewees directly involved in the negotiations at state level. For the remainder of the interviews the position of France and Germany oscillated.

<sup>37</sup> *Interview by Author with the Chief Negotiator of Hungary*, Budapest, 09/02/2004.

<sup>38</sup> *Interview by Author with Representative of the Ministry of Foreign Affairs of the Czech Republic*, Prague, 04/05/2004a. The names of the pivots being the Luxembourg, Belgium, France, the UK, Spain and Germany were provided by all interviewees concerned. Six interviewees directly involved in the negotiations at state level cited these countries in similar order of importance.

<sup>39</sup> *Interview by Author with Representative of the Ministry of Foreign Affairs of Poland*, Warsaw, 27/04/2004.; *Interview by Author with Representative of the Committee for European Integration (KIE)*, Warsaw, 15/04/2004.; *Interview by Author with Representative of Slovak Ministry of Transport*, Bratislava, 02/03/2004a.

<sup>40</sup> The names of the pivots being Germany and Austria were provided by all interviewees concerned at state level.

<sup>41</sup> *Interview by Author with Representative of Slovak Ministry of Transport*, Bratislava, 02/03/2004a.

defends as the EU's collective interest. According to *Avery* the Presidency is not authorised to do other than what the member states agree in advance<sup>42</sup>.

In this respect the EC's role in the negotiations is theoretically endogenous to the voting rule in place. It has agenda setting powers and formulates the DCP to the EU in response to the position papers of the applicant states<sup>43</sup>. The EC is aware of the voting rule and the EU member states' preferences. It has to consider what the member states will be prepared to agree among themselves. As a result, it is unlikely to make proposals to the Council that are far of the mark of the Council's pivot(s). Otherwise it might risk further delays in the negotiations and lose the trust of the Council's members in the process<sup>44</sup>.

### **7.1.3. General and Idiosyncratic Aspects**

A number of additional institutional elements in the enlargement negotiations strengthen the EU's bargaining power. These can be grouped under the headings of sequencing, grouping and uncertainty. Principles of equality and reciprocity mitigated power asymmetry in the negotiations.

#### **7.1.3.1. Sequencing**

It is common for negotiations to progress whereby the most difficult issues wait until last. Negotiators concentrate first on those issues that would be easier to resolve while keeping the hard ones until later<sup>45</sup>. In the accession talks the EU decided upon the chronology of the chapters to be opened for negotiation. Despite being common practice the sequencing of negotiations is by no means neutral. It leaves fewer opportunities for logrolling. In the case of the fifth enlargement it meant that the applicant countries would take on the obligations of EU membership and bear the costs of adjustment without knowing the level of financial support they would receive from the EU to meet these obligations.

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<sup>42</sup> G. AVERY, *The Commission's Perspective on the EFTA Accession Negotiations*, Brighton: University of Sussex, 1995., pp. 2-4.

<sup>43</sup> With the exception of issues relating to common foreign policy and security and third pillar issues.

<sup>44</sup> This is essentially an analogy of the argument on delegation on American trade policy made by M. Gilligan in: M.J. GILLIGAN, *Empowering exporters: reciprocity, delegation, and collective action in American trade policy*, Ann Arbor: University Of Michigan Press, 1997., pp. 4-6 and chapter 3, pp. 35-57.

<sup>45</sup> H. RAIFFA, J. RICHARDSON and D. METCALFE, *Negotiation analysis: the science and art of collaborative decision making*, Cambridge, MA, London: Belknap Press of Harvard University Press, 2002., pp. 479-480.



It was a catch-22 as the applicant countries' TPRs depended on information about financial support. Without it they did not know how long it would take to adjust because it remained unclear to what extent the EU would meet the costs of applying EU legislation. One negotiating official dubbed this EU strategy as 'pulling the rope at both ends. We were shooting at a moving target. The EU was manoeuvring us in a position whereby we had to take on the obligations of EU accession, reduce TPRs while it delayed any information about the privileges. You could say we jumped in the swimming pool without knowing whether there was water'<sup>46</sup>.

Others argued: 'Some chapters were kept hostage by others. As long as they were not closed we could not move on. We contested the salami tactics and wanted to introduce the-put-aside-method. A delegation went to the capitals of the EU member states but without success'. 'We asked the Portuguese Presidency to change the sequence of the negotiations. We wanted to know about the financial package in order to have a better idea about the funds we needed to set aside for meeting adjustment costs of EU membership. The EU member states refused to accept that idea. It argued that we were not ready for such thinking'<sup>47</sup>.

The EU's sequencing and delaying tactics in the negotiations was a bone of contention for the applicants. They attacked the EC and EU MS for failing to set out their positions in more detail on the more difficult but important chapters: 'I was really upset and raised the matter regularly with the EU but the EU would reply: On this issue the EU will adopt its position later'<sup>48</sup>.

### **7.1.3.2. Group Dynamic**

The negotiations between the EU and the individual applicant countries were conducted separately but in parallel whereby the progress of each country in the overall negotiations was judged on its own merit. The 12 IGCs, one each between the EU and the applicant countries, operated individually while the meetings among the two groups of countries, the Luxembourg Six and the Helsinki Six, often took place chronologically and immediately after each other with similar issues on the table. It allowed the EU to pick and choose among the applicant states' proposals and obtain concessions which the other countries were then under pressure to follow:

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<sup>46</sup> Interview by Author with Representative of the Committee for European Integration (KIE), Warsaw, 15/04/2004.

<sup>47</sup> Interview by Author with Representative of the Office of the Committee for European Integration (UKIE), Warsaw, 21/04/2004.; Interview by Author with Representative of the Committee for European Integration of the Republic of Poland (KIE), Warsaw, 14/04/2004.; T. SIMON, War of words erupts over enlargement, in: *European Voice*, 23/03/2000.

<sup>48</sup> Interview by Author with the Chief Negotiator of Hungary, Budapest, 09/02/2004.

'Time and time again the EU approached and selected the most convenient partner. It then proposed the solution to the others'<sup>49</sup>.

The EU's supremacy by preventing the applicant countries from joining forces could perhaps have been counteracted by a common front of applicant countries in numerous policy domains where interests overlapped. Despite the regular contacts between the applicant states the EU was never presented with a firm common negotiation position of all EU applicants<sup>50</sup>. The common front failed because of the policy of active differentiation. The EU and certain candidate countries stressed that EU accession should be based upon the individual merits of each applicant country. The approach of differentiation was seen as a means to encourage reform in the EU applicant countries, however, it served also as a contention for some countries' perception of being held back by neighbours that were catching up in the process.

The lack of co-operation was related in part to historical factors and perceived competition. Collaboration was flawed by the doubt that co-operation with others could be beneficial for their own EU membership. This perception was strengthened by the EU's decision to add the Helsinki six to the race for membership in 1999. The Luxembourg Council strengthened the competition element by adding another group of countries. There was a belief among the applicants that EU enlargement would consist of only a small group of countries<sup>51</sup>. It prevented real co-operation with the exception of the Czech and Slovak Republics: 'We wanted to join the EU and the Czech Republic wanted us to join too. There were natural benefits for the Czech Republic. Their advice helped us to be realistic'<sup>52</sup>. The competition element made the chief negotiators regard the enlargement process as a beauty contest amongst the applicants. They spoke of co-operation on an informative basis only. The negotiations essentially revolved around the perceived national interests of each individual applicant.

The EC encouraged this dynamic through the naming and shaming of the applicant countries in the annual reports on progress towards accession (1998-2002)<sup>53</sup>. Through the publication of the

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<sup>49</sup> Interview by Author with Representative of the Committee for European Integration (KIE), Warsaw, 15/04/2004.

<sup>50</sup> G. AVERY, *The Commission's Perspective on the EFTA Accession Negotiations*, Brighton: University of Sussex, 1995. pp. 11-12.

<sup>51</sup> Interview by Author with Representative of the Office of the Government of the Czech Republic, Prague, 04/05/2004b.

<sup>52</sup> Interview by Author with the Chief Negotiator of the Slovak Republic, Bratislava, 05/03/2003.

<sup>53</sup> Interview by Author with Representative of the Office of the Government of the Czech Republic, Prague, 04/05/2004b.

reports judged the candidates' progress towards EU membership. The annual publication of the progress reports was similar to a school teacher handing out the results of the annual exams that would allow the applicants go over to the next year. As a result, a media frenzy erupted in the fall of each year between 1998 and 2002 when the progress reports were published. The media accused the executives for not being able to deliver when they were lagging behind in the negotiations: 'During the negotiations progress in the chapters provisionally closed was almost always front page news'<sup>54</sup>.

Among the business and banking community progress in terms of number of chapters closed was an indication for reform and progress towards EU membership. Some economists even believed that the number of chapters closed was positively correlated to the inflows of FDI in the applicant states<sup>55</sup>. It was another reason for the applicants not to co-operate on EU membership since they were competing over financial assistance and FDI<sup>56</sup>.

*Berglof and Roland* portray the practice as 'the race for EU membership'. EU membership was regarded as 'tournament' prize where only the best can win<sup>57</sup>. The race had a similar dynamic on all countries. It made them drop TPRs to advance in the negotiations and close chapters. It prevented them from co-operating. This logic is confirmed by the individual country strategies at the negotiating table in Brussels. In contrast, the EU-15 individual negotiation positions were institutionally well co-ordinated and resulted in the CP, the mirror image of the EU as a bloc of 15 states.

### **Czech Strategies**

The Czech Republic was still coping with the financial crisis when it commenced the accession negotiations<sup>58</sup>. Prague assumed that early EU membership was on the cards particularly in the view of its successful transition process. Proud of its achievements its Prime Minister, Mr. *Vaclav Klaus*, had declared the transition process over in 1996 only to be woken up by the

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<sup>54</sup> Interview by Author with Representative of the Negotiation Team of the Slovak Republic, Vienna, 05/05/2004.

<sup>55</sup> A. BEVAN, H. GRABBE and S. ESTRIN, in: *The impact of EU accession prospects on FDI inflows to Central and Eastern Europe*, Brighton: University of Sussex, Sussex European Institute, 2001, pp.

<sup>56</sup> R. KEOHANE and S. HOFFMANN, Conclusion: Structure, Strategy, and Institutional Roles, in: R. O. KEOHANE, J. S. NYE and S. HOFFMANN, *Integrating the Two Halves of Europe: Theories of Interests, Bargaining, and Institutions*, Cambridge: Harvard University Press, 1993, pp. 381-404., p. 393.

<sup>57</sup> E. BERGLOF and G. ROLAND, *From Regatta to Big Bang, Impact of EU accession strategy on reforms in central and eastern Europe*, Washington: IMF Working Paper, 2000.

<sup>58</sup> Interview by Author with representative of the EC's Delegation to the Czech Republic Prague, 24/03/2004a.

financial meltdown of its banking system. The aftermath proved difficult for Prague and had its effect on the EU accession process: ‘In 1999 reports emerged that we were dropping out of the first group [the Luxembourg group]. We feared that the costs for joining the EU would rise as we would be relegated’<sup>59</sup>. The Czech negotiation delegation used the competition element strongly: ‘We were direct competitors’<sup>60</sup>. The first regular report, which criticised the Czech Republic for its lack of reform, encouraged the competitive dynamic. In 2001 the chief negotiator, Mr. *Pavel Telicka*, gave public speeches on the strategy of his country to join the EU. He insisted on the principle of differentiation in the negotiations and declared to drop TRPs to speed up the process. Only towards the end of the negotiations did Prague change its strategy and pursued quality of EU membership<sup>61</sup>: ‘Only in the last six months we realised that speed did not matter. At the end the dynamic changed whereby the results of the negotiations were compared’<sup>62</sup>.

### **Hungarian Strategies**

In Budapest early membership was perceived as the best possible way to serve national interests. The Hungarian delegation wanted to be the best among all the applicant countries. Swiftness in the negotiations was its prime strategy. Like in *the battle of the sexes* Budapest set precedents for other countries: ‘Being the first was an advantage. I was afraid of setting bad precedents. Of course, it involved the risk that other countries could criticise your position’<sup>63</sup>. ‘Hungary did not try to emulate other countries. Speed was the prime objective and strategy. I still believe that Hungary could have joined earlier. When concluding the EAs I thought that Hungary could have joined the EU by 2000. If that was the objective, why delaying it’<sup>64</sup>.

The competitive spirit prevented Hungary from forming a common front with other candidates on common problems in the negotiations: ‘We exchanged views [on the negotiations], however, always ex post, after the positions were put forward. In certain cases there was co-operation, however, no common standpoints were put forward’. ‘The Luxembourg Six met regularly and exchanged papers. The group was set up in Copenhagen. They met in each others capitals in total around 20-30 times. The exchange of [position] papers happened after submitting the papers not

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<sup>59</sup> Interview by Author with Representative 1 of the Negotiation Team of the Czech Republic, Prague, 23/03/2004.

<sup>60</sup> Ibid.

<sup>61</sup> Interview by Author with Representative of the Negotiation Team of the Slovak Republic, Vienna, 05/05/2004.

<sup>62</sup> Interview by Author with Representative of the Office of the Government of the Czech Republic, Prague, 04/05/2004b.

<sup>63</sup> Interview by Author with the Chief Negotiator of Hungary, Budapest, 09/02/2004.

<sup>64</sup> Ibid.

before. The reason for such behaviour was that technically this was impossible. There was a rush; and it was problematic because of logistical reasons'<sup>65</sup>. After Helsinki (10-11 December 1999), this form of limited co-operation did not longer work as other countries were brought into the group. The EU decided that the second group was allowed to catch up with the first group. 'It slowed the negotiations down. I remember that in 2000, at some point, we did not close one, or just one, chapter'<sup>66</sup>.

### **Polish Strategies**

Among the V-4 only Poland did not share the fear of its neighbours that the EU door would be shut and that they would not be allowed in after the first wave. Under the *Buzek* administration (1997-2001) quality of membership prevailed over early entry at all costs: 'We negotiated on our own terms'<sup>67</sup>. 'The race did not matter, we were enlargement'<sup>68</sup>. 'Joining the EU at the lowest costs was our prime objective'<sup>69</sup>. Despite these perceptions the EU cajoled Poland in the race for EU membership as it did with other candidate countries. During a meeting between PM Buzek and EC President *Romano Prodi* the latter argued that he wanted 'Poland in the first group of countries to join the EU, although he said that the outcome could not be guaranteed because it depended on the negotiations'<sup>70</sup>.

Delays in the negotiations resulted in a change of strategy after a government turnover in September 2001 and Warsaw followed in step. Poland had come under considerable pressure from the EU to accelerate the pace: 'Even Slovakia was further ahead in the negotiations. We were frightened of not being in the first group because we were lagging behind'<sup>71</sup>. 'When we waited too long for the EU to come up with a better proposal in the negotiations the public climate went against us. The press would begin to ask questions why our neighbours had closed the chapters while we did not. There was a general perception that we needed to deliver. To leave open the negotiations when others moved ahead was political suicide. The electorate would argue

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<sup>65</sup> Ibid.

<sup>66</sup> Ibid.

<sup>67</sup> Interview by Author with the Chief Negotiator of Poland, Warsaw, 26/04/2004.

<sup>68</sup> Interview by Author with Representative of the Ministry of Foreign Affairs of Poland, Warsaw, 27/04/2004.

<sup>69</sup> Interview by Author with Representative of the Committee for European Integration of the Republic of Poland (KIE), Warsaw, 14/04/2004.

<sup>70</sup> Poland presses EU on accession timing, in: *Financial Times*, 03/04/2000.

<sup>71</sup> Interview by Author with Representative of the Ministry of Foreign Affairs of Poland, Warsaw, 27/04/2004.

that the government could not deliver'<sup>72</sup>. One chief negotiator called it 'chapter-ology' saying it exerted pressure on the applicant states that otherwise would have been absent'<sup>73</sup>.

Despite the competitive dynamic the Polish delegation co-operated on an informative basis only: 'Among the Luxembourg Six there was a cosy atmosphere but rather *ex post* and never *ex ante*. Before the meetings we had little interaction because there was too little time for a common front. It was time consuming and the pace was too high. Some basic loyalty existed but there was never any strong agreement'<sup>74</sup>.

### **Slovak Strategies**

Being part of the second wave Slovakia was catching up: 'we were being treated differently because we were part of the second wave. For us speed [in the negotiations] prevailed for almost all issues. We politically had decided to join the EU as fast as was possible'<sup>75</sup>. 'It [Slovakia] followed the tactics of the neighbouring countries, which enabled it to catch up'<sup>76</sup>. 'In the negotiation delegation we shared the belief that there was a serious risk for Slovakia not to be allowed in the first group that would join the EU. We were together with Romania and Bulgaria in the group. From a geographic point of view I thought it was impossible for us to be excluded, however, after talks with officials from the EC and the EU-15 we changed our view. They send us signals that a failure to comply with the conditions would prevent Slovakia from joining'<sup>77</sup>.

Simultaneously Bratislava had little use of bad news coming from Brussels: 'We had a serious political difficulty in Slovakia at the time. The opposition would act upon the fact that were not doing well in the negotiations. It is difficult to argue in front of the public that you are holding out in the negotiations because you want to improve upon the deal. Politically it was impossible and very risky to do'<sup>78</sup>.

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<sup>72</sup> Interview by Author with Representative of the Committee for European Integration of the Republic of Poland (KIE), Warsaw, 14/04/2004.

<sup>73</sup> Interview by Author with Representative of the Committee for European Integration (KIE), Warsaw, 15/04/2004.

<sup>74</sup> Interview by Author with Representative of the Ministry of Foreign Affairs of Poland, Warsaw, 27/04/2004.

<sup>75</sup> Interview by Author with Representative of Slovak Ministry of Transport, Bratislava, 02/03/2004a.

<sup>76</sup> Interview by Author with Representative of the EC's Delegation to the Slovak Republic, Bratislava, 11/03/2004.; Interview by Author with Representative of the Ministry of Foreign Affairs of the Slovak Republic Bratislava, 03/03/2004.

<sup>77</sup> Interview by Author with Representative of Slovak Ministry of Transport, Bratislava, 02/03/2004a.

<sup>78</sup> Interview by Author with Representative of the Negotiation Team of the Slovak Republic, Vienna, 05/05/2004.

‘The media played on the element of competition. They were looking for form [the number of chapters] and not so much substance. If the level of competition would have been lower, it would have increased their power at the negotiating table. Political pressure came also from the electorate heavily supportive of EU membership. It resulted in bad legislation. In addition, Slovakia felt the pressure to close chapters in the negotiations as it had the impression that closing chapters drew in FDI flows: ‘In Slovakia we felt a clear influence of the business community watching the number of chapters closed. The more chapters we closed, the closer we got to EU membership, the more FDI came into the country. Perhaps it is coincidence, although, we failed to attract FDI before’<sup>79</sup>. ‘The turning point was 2000 [...] The role of FDI in the competition element cannot be underestimated’<sup>80</sup>.

Members of the delegation admitted that apart from co-operation common positions or agreements in the negotiations did not hold. It increased the leverage of the EU, reduced TPRs and the number of effective TAs: ‘There was exchange of information *ex post*. The chief negotiators would meet every 3 months in the capitals in alphabetical order but agreed positions did not stick in the negotiations. Countries would break ranks with each other on numerous occasions<sup>81</sup>. Being in the second group and attempting to catch up Slovakia benefited from the exchange of information among the candidates.

### 7.1.3.3. Uncertainty

Despite the uncertainty of not having a date for EU membership the applicants had to make working assumptions for entering the EU in the negotiation position papers, particularly for the formulation of TPRs. It meant that applicant countries had been shooting a flying target while being encouraged to be precise in its timing of adjustment<sup>82</sup>. Most negotiating governments recognised the need to withdraw TPRs as they would expire ahead of EU membership: ‘Many TPRs became obsolete because the negotiations took that long’<sup>83</sup>. Not one applicant country worked according to an EU entry assumption in its position papers of ‘n+1’ with ‘n’ being equal

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<sup>79</sup> Ibid.

<sup>80</sup> Interview by Author with Representative of the World Bank Slovakia, Bratislava, 02/03/2004b.

<sup>81</sup> Interview by Author with the Chief Negotiator of the Slovak Republic, Bratislava, 05/03/2003.; Interview by Author with Representative of the Negotiation Team of the Slovak Republic, Vienna, 05/05/2004.

<sup>82</sup> A. MAYHEW, *Enlargement of the European Union: an analysis of the negotiations with the central and eastern European candidate countries*, Brighton: University of Sussex, 2000., p. 45.

<sup>83</sup> Interview by Author with the Chief Negotiator of Hungary, Budapest, 09/02/2004.

to the year of EU entry. For the EU it was most conceivable that the applicants would apply costly EU legislation ahead of membership even if this would go against its economic interest.

Without the certainty about the end of the negotiations each applicant country made assumptions about EU entry. For the Czech Republic the initial working assumption was 2000, later revised to 2002 with effective membership on 1 January 2003<sup>84</sup>. The Hungarian assumption for joining was the year 2000. Budapest had the strong conviction even after the Luxembourg Council that the EU would take in only a limited number of countries<sup>85</sup>. ‘These assumptions did not hold. The EC asked us how much time we needed for adjustment. We were required to be specific both in time and content and strongly advised not to reconsider. As the date for EU membership slipped we lost TPRs as we were applying EU legislation ahead of EU membership’<sup>86</sup>. ‘The real break through for us was the political time table, the so-called road map, decided in June 2001 in Goteborg’<sup>87</sup>.

For Poland the initial assumption date was 31 December 2000, later adjusted to 31 December 2002 and again to a new working assumption of 31 December 2003<sup>88</sup>: ‘We did not work according to the ‘n+1’ formula. This was our mistake. The EU on the contrary counted from a fixed date enforcing EU legislation sooner rather than later’<sup>89</sup>. Of all the applicant countries Slovakia had set its working assumption closest to the effective date of EU membership of 1 May 2004. In 1999-2000 the Slovak delegation set 1 January 2004 as a working assumption: ‘We assumed that we could harmonise our legislation with the *acquis* by 2003 and built in a buffer zone of one year in case additional problems would emerge. In the end we went faster’<sup>90</sup>.

#### **7.1.3.4. Equality and Reciprocity**

Despite the voting rule, the institutional difficulties associated with the CP and the absence of delegation a dynamic of equality and reciprocity in the negotiations worked against the EU’s dominant power in the negotiations. Some leeway was present in the negotiations because of

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<sup>84</sup> *Interview by Author with Representative 1 of the Negotiation Team of the Czech Republic, Prague, 23/03/2004.; Interview by Author with Representative of the Office of the Government of the Czech Republic, Prague, 04/05/2004b.*

<sup>85</sup> *Interview by Author with Representative of the EC's Delegation to Hungary, Budapest, 02/02/2004.*

<sup>86</sup> *Interview by Author with Representative of the Hungarian Ministry of Economy and Transport, Budapest, 10/02/2004.*

<sup>87</sup> *Interview by Author with Representative of Ministry of Foreign Affairs of Hungary, Budapest, 13/02/2004.*

<sup>88</sup> *Interview by Author with Representative of the Office of the Committee for European Integration (UKIE), Warsaw, 21/04/2004.*

<sup>89</sup> *Interview by Author with Representative of the Committee for European Integration (KIE), Warsaw, 15/04/2004.*

<sup>90</sup> *Interview by Author with the Chief Negotiator of the Slovak Republic, Bratislava, 05/03/2003.; Interview by Author with Representative of the Negotiation Team of the Slovak Republic, Vienna, 05/05/2004.*



three reasons. First, once the EU decided to open the negotiations it was unlikely to break them off, which gave room for compromise. Second, the EU was willing to temporarily deviate from its own rules. It put TPRs on the table according to the wishes of its individual member states. These were proposed on a take it or leave it basis and allowed for reciprocity and flexibility towards the applicant countries<sup>91</sup>. If the EU would put a TPR on the table the applicant countries could always make similar requests even if they were meaningless such as in the area of cabotage.

Finally, when one applicant country set a precedent in the negotiations it usually was followed by the others<sup>92</sup>. An issue specific TA for one country would almost automatically be extended to the other applicant countries when they were confronted by similar issues: 'The EU would certainly take more notice when several countries were putting forward similar TPRs'<sup>93</sup>.

The principle of equality and reciprocity was only applied if the negotiators made a request. 'Countries would not get a better deal if they would not ask for it'<sup>94</sup>. The chapter in question would be re-opened and a similar TA inserted. 'When there were similar TPRs on the table for other countries we would look whether they were obtaining similar deals in the negotiations. When they got more we would ask for the same. In that respect being the first was the most difficult as it was the ice breaker for the others'<sup>95</sup>.

In the EU this dynamic called common concessions: 'Chief negotiators would look at other countries. When they noticed the others obtained something their country did not have they would re-open the chapter or highlight it to the EU. The EU would then usually provide the concession. The negotiations on pharmaceuticals are a clear cut case of zero cost concessions'<sup>96</sup>. 'Because the EU and the EC were short on resources relative to the scale of the exercise in a way

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<sup>91</sup> A. MAYHEW, *Enlargement of the European Union: an analysis of the negotiations with the central and eastern European candidate countries*, Brighton: University of Sussex, 2000., p. 14-17.

<sup>92</sup> G. AVERY, *The Commission's Perspective on the EFTA Accession Negotiations*, Brighton: University of Sussex, 1995., p. 5

<sup>93</sup> Interview by Author with Representative of the Office of the Government of the Czech Republic, Prague, 04/05/2004b.

<sup>94</sup> Interview by Author with Representative of the Ministry of Foreign Affairs of Poland, Warsaw, 27/04/2004.

<sup>95</sup> Interview by Author with Representative of the Office of the Government of the Czech Republic, Prague, 04/05/2004b.

<sup>96</sup> Interview by Author with Representative of the EC's Delegation to the Slovak Republic, Bratislava, 11/03/2004.

they negotiated in bulk. They sought one solution for the entire group of countries'<sup>97</sup>. This contributed to the equality principle.

Equality and reciprocity explains the presence of TAs in areas where sectors did not mobilise or countries did not request TPRs. 'There were general spill over effects from other countries in the negotiations. Deals were extended'<sup>98</sup>. 'The negotiations were bilateral in the constitutional and legal sense. Otherwise they were multilateral with spill over effects on the EU's side. The EU did not deal with country specificities. It generalised solutions to all the other countries. The Helsinki Six – excluding Bulgaria and Romania – did not really negotiate. They accepted the solutions put forward by Luxembourg six'<sup>99</sup>.

## **7.2. Second Image Constraints**

The previous section described the bargaining setting and procedures of the accession negotiations. It established the institutional determinants of the EU's dominant bargaining power in the accession negotiations. The analytical task in the following section is to provide an explanation for the presence and variation of TAs in the presence of the EU's dominant bargaining power. I do this by introducing a simple two dimensional spatial model and applying it to the fifth enlargement negotiations rounds for pharmaceuticals, iron and steel production, and road freight transport in the V-4.

### **7.2.1 The Model**

Negotiation theory suggests that under certain conditions it is possible for the applicant states to use domestic constraints in order to gain concessions from the EU to maintain the status quo (TAs) in the negotiations. According to Schelling's conjecture, binding oneself domestically can be useful for extracting concessions internationally. In analogy, I argue that the presence of domestic constraints in the form of at least one veto player has a profound influence on the bargaining behaviour of the chief negotiator at the international level. This veto player can be a political actor or a domestic ratification constraint.

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<sup>97</sup> Interview by Author with Representative of the Negotiation Team of the Slovak Republic, Vienna, 05/05/2004.

<sup>98</sup> Ibid.; Interview by Author with representative of the EC's Delegation to the Czech Republic Prague, 24/03/2004a.

<sup>99</sup> Interview by Author with Representative of Ministry of Foreign Affairs of Hungary, Budapest, 13/02/2004.; Interview by Author with the Chief Negotiator of the Slovak Republic, Bratislava, 05/03/2003.

In addition, Schelling argues that public posturing *ex ante* can confirm the international agent's bargaining position: 'when national representatives go to international negotiations knowing that there is a wide range of potential agreement within which the outcome will depend on bargaining, they seem often to create a bargaining position by public statements, statements calculated to arouse a public opinion that permits no concessions to be made. If a binding public opinion can be cultivated and made evident to the other side, the initial position can thereby be made visibly «final»'<sup>100</sup>.

It is important to have a clear set of plausible assumption about the bargaining context. First, I characterise the entry talks as repetitive and integrative negotiations concerned with a deal whereby the parties pursuing an agreement<sup>101</sup>. The negotiating parties attempt to avoid the breakdown of the negotiations. Second, I assume the negotiation positions of the bargaining parties are apparent. The EU is well informed about the applicants because of the screening and preparatory phases that lead up to the opening of the negotiations: 'We thought the EU was receiving information from different sources. There was no point in fooling each other'<sup>102</sup>. The situation on the applicant countries side was somewhat different. It had little contact with the Council to the extent that some considered it a ghost or a black box<sup>103</sup>. Nevertheless, the applicant states were well aware of the intricacies of the CP, the negotiation positions of the individual member states including the pivots and the position of domestic sectoral interest groups (see chapters 3, 4 and 5).

The implication from apparent information is that posturing in the sense of bluffing or profitably fooling one's negotiating opponent is likely to yield little results because the opponent is likely to know one true reservation price.

Third, in contrast to the candidate countries the EU is a unitary actor having only one institutionally constrained negotiation position. For the present purpose it suffices to know that its

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<sup>100</sup> T.C. SCHELLING, *The Strategy of Conflict*, Cambridge, Massachusetts: Harvard University Press, 1960., p. 28.

<sup>101</sup> H. RAIFFA, J. RICHARDSON and D. METCALFE, *Negotiation analysis: the science and art of collaborative decision making*, Cambridge, MA, London: Belknap Press of Harvard University Press, 2002., pp. 191-193., 81-98.

<sup>102</sup> in: *Interview by Author with Representative of the Hungarian Ministry of Economy and Transport*, Budapest, 10/02/2004. The situation on the applicant countries side is somewhat different. It is unaware of the CP, the potential EU accession dates as well as the position of the other applicant countries.

<sup>103</sup> *Interview by Author with Representative of the Ministry of Finance of the Czech Republic*, Prague, 24/03/2004b.

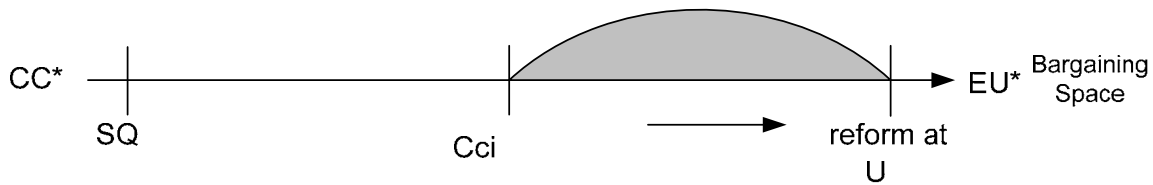
position is uniform to the reformist case across all issues. Finally, I assume variation in the preferences of the candidate countries to the degree of reform. Unless political pressure is exerted the status quo is always preferable over policy change in the negotiations.

Under these assumptions how does Schelling's reasoning translate to the EU accession negotiation context? Imagine the candidate country (CC\*) and the EU (EU\*) entering into accession talks (see Figure 42). They both agree on the outcome of the negotiations, i.e. EU membership, and are unlikely to sustain a general breakdown of the entry talks. They also have a set of preferences for the conditions under which EU membership would take place. For the EU\* the ideal point of its reservation price in the negotiations is equivalent to complete reform or full application of EU legislation in CC\*.

As shown in the previous section the EU's reservation price in the CP under unanimity stands at the position of the most conservative member state. As a result, the EU\*'s CP under unanimity (U) at the international bargaining table is identical to complete reform (reform at U).

For the CC\* the ideal point of its reservation price in the negotiations is likely be to closer to the status quo (SQ) as applying EU legislation might be costly for a number of domestic actors. While pursuing EU membership the CC\*'s international negotiator (Cci) might want to try to extract concessions (TPRs) from the EU\*. While Cci is prepared to accept reform in some areas it prefers SQ over reform at U. Therefore the ideal point of Cci lies somewhat in between SQ (reform at U). In Figure 42 the ideal points of the reservation prices of Cci and reform at U are the outer limits in the bargaining range of potential agreement between CC\* and EU\*.

**Figure 42: Bargaining under the absence of a domestic veto player**



Legend: SQ = status quo  
 CC\* = candidate country  
 EU\* = EU  
 Cci = candidate country international  
 U = Common position (CP) under unanimity

The location of the negotiators reservation points (Cci and reform at U) in the bargaining space determines the size of the win set in the negotiation round. At the bargaining table any agreement must lie within the win set (highlighted in grey). Taking in account the asymmetrical distribution of bargaining power between the CC\* and the EU\* the point of any potential agreement is likely to move in the direction of reform at U than of Cci. Moreover, due to the absence of any domestic constraint in CC\* and the dedication of Cci to have an international deal, Cci can move without restraint along the bargaining space in the direction of reform at U. Therefore, the most likely agreement will be identical to the EU\*'s reservation point.

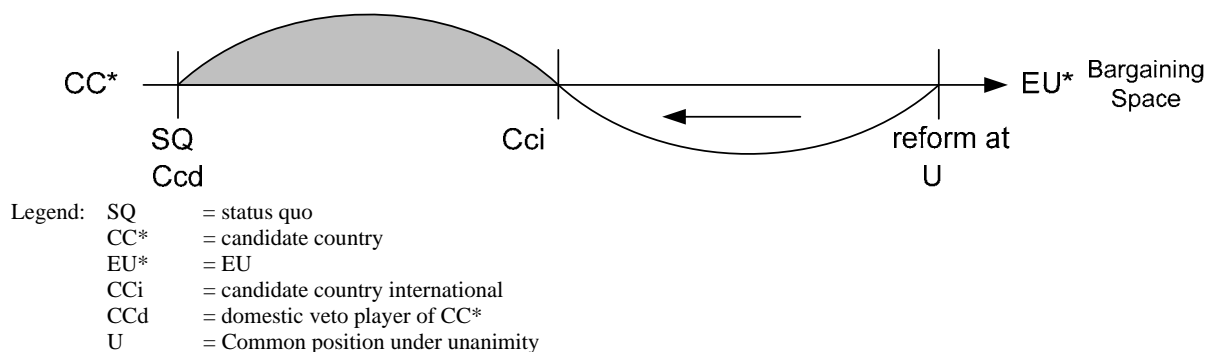
Does the size of the win set and the point of agreement vary when introducing a domestic constraint, i.e. under the presence of a domestic veto player? Following *Robert Putnam's* two level game metaphor an international negotiator requires the agreement at the domestic level and the international level to be successful. Putnam argued that 'the politics of many international negotiations can be usefully conceived as a two-level game. At a national level, interest groups pursue their interests by pressuring the government to adopt favourable politics. At an international level, governments seek to maximize their own ability to satisfy domestic pressures, while minimizing the adverse consequences of foreign developments. Neither of the two games can be ignored by central decision-makers, so long as their countries remain interdependent, yet sovereign'<sup>104</sup>. In the present context the metaphor entails that a successful agreement only can be

<sup>104</sup> R.D. PUTNAM, *Diplomacy and Domestic Politics: The Logic of Two-Level Games*, in: *International Organization*, 1988, 42(3), pp. 427-60., p. 434.

achieved provided it lies at the intersection of both the domestic and the international win sets – the set of alternatives to no agreement.

Concurringly, in the presence of a domestic veto player in Figure 43 any potential agreement point lies left of or is identical to the reservation point of Cci and closer to SQ. It is the only intersection of both the domestic and the international win sets that prevents breakdown of the negotiations. Imagine again that CC\* and EU\* are haggling over the conditions of EU entry in a similar setting as the one described above. The reservation prices of Cci and reform at U are the same as in Figure 42 only now Cci is confronted with a domestic constraint in the form of a veto player in CC\* (CCd). Because the costs of applying the *acquis* prove prohibitive for CCd her reservation price for any agreement (a TPR) is higher than that of international negotiating agent Cci who is keen on an international accord. The location of CCd's reservation point therefore lies left of that of Cci and closer to SQ. As a result, the size of the domestic win set (=Cci-CCd) is smaller under the presence of Ccd relative to the win set depicted in Figure 43, which is identical to the win set of Cci<sup>105</sup>.

**Figure 43: Bargaining in the presence of a domestic veto player**



The point of any potential agreement under the presence of a domestic veto player is therefore likely to move in the direction of the SQ rather than reform at U. Even if Cci is keen on an international agreement it cannot lower its reservation price because of the presence of a domestic veto player.

<sup>105</sup> Note that a domestic constraint can only be present if Ccd's win set is smaller than that of Cci.

Posturing and public announcements by CC\* and Ccd ahead of the negotiation rounds indicate to EU\* that the international bargaining agent Cci comes with his hands tied to the negotiating table. In such situation EU\* has two options. Either it decides to hold out hoping for Ccd to come its way risking a breakdown of the negotiations; Or it decides to lower its reservation price and move in the direction of Cci. According to this logic any agreement must lie within the win set of Cci-Ccd or between the reservation points of Cci and Ccd at SQ (highlighted in grey in Figure 43).

Taking in account the asymmetrical distribution of bargaining power between the CC\* and the EU\* the most likely agreement will be identical to the Cci\* reservation point, which is the closest point to reform at U within the win set. The finding is in agreement with *Clark et al* who argue that ‘if the domestic win set is smaller than the international win set, then the outcome is likely to be independent of the latter’<sup>106</sup>.

### **7.2.2. External Impact of Domestic Constraints in the V-4**

How does the degree of domestic constraints in the V-4 affect the room for manoeuvre of governmental negotiators in the international arena? How do national institutional constraints and/or the number of domestic veto players and their respective preferences affect international outcomes?

I test the model across three sectors and four countries in the accession negotiations (see Figure 44 cases 1 to 12). To gauge the influence of sectoral veto players on international negotiations the section engages with key political actors and their preferences over EU accession policy. It draws the attention to the legislature, the government and public opinion. The distribution of decision-making power among these institutions (see chapter 6) and the extent to which their preferences diverge over joining the EU defines the number of veto players in the applicant states. It also determines their responsiveness to the sectoral preferences discussed in chapters 3, 4 and 5.

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<sup>106</sup> CLARK W.R, DUCHESNE E and MEUNIER S, Domestic and International Asymmetries in United States-European Union Trade Negotiations, in: *International Negotiation*, 2000, 5(1), pp. 69-95.

### 7.2.2.1. Czech Constraints

In contrast to the international road freight transport sector interest groups for the pharmaceutical and basic iron and steel sectors carried strong preferences and mobilised politically. EU patent legislation would seriously damage the Czech pharmaceutical industry. The basic iron and steel industry would see its state aid banned after EU membership. The government listened to the concerns of the basic iron and steel industry in the accession negotiations.

The two centre-left Social Democratic (CSSD) governments that were in power between 1998 and 2002 were staunchly pro-EU. They could count on an alternating parliamentary majority to pass EU related legislation (see Table 24). The opposition in parliament would not be punished for their support of government EU policy. The electorate was supportive of EU membership throughout Prime Minister *Milos Zeman*'s tenure (1998-2002) with 54 per cent in favour and just 18 per cent against<sup>107</sup>. The government was confident enough in 2001 to openly state that it intended to hold a referendum on EU accession; and in the run up to the negotiations it was sufficiently under public pressure to yield in the accession talks. It would repeatedly ignore domestic interests groups and drop TPRs when they did not have a positive impact on the general government budget and/or had the potential to turn into a politically salient issue.

The TPR from the domestic pharmaceutical producers did not make it into the position paper. The impact of patent legislation on the government's budget and the electoral ramification were piecemeal. From the three sectors in the sample the government went into the negotiations with only one domestic veto player (see Figure 44, cases 1, 5 and 9).

Waning public support for EU membership in 2001 and 2002 to just 50 per cent with 19 per cent against prompted the new CSSD government headed by *Mr. Vladimir Spidla* to withdraw the draft law on an EU referendum in the Chamber of Deputies on 14 February 2001<sup>108</sup>. Instead the executive proposed and passed a law for a referendum with a low ratification threshold. The Spidla cabinet adjusted its strategy on EU membership from joining the EU at all cost to securing

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<sup>107</sup> European Commission, *Candidate Countries Eurobarometer (Fieldwork October 2001)*, Brussels, March 2002.

<sup>108</sup> European Commission, *Candidate Countries Eurobarometer: Public opinion in the countries applying for European Union membership (Fieldwork: September-October 2002)*, Brussels, December 2002.



good entry conditions. It protected more vigorously the interests of the steel industry which was a traditional bastion of CSSD electoral support.

The chief negotiator, Mr. *Pavel Telicka*, attempted to fool the EU in hiding his true reservation price in the talks on international road transport. In the absence of sectoral political mobilisation he pursued access to the German and Austrian cabotage markets in return for his acceptance of the EUs TPR on international road freight transport. Refusing to close the transport chapter he held out for two additional months. The strategy failed: ‘We wanted a bilateral deal with Germany and Austria. The chief negotiator went to Berlin and Vienna to broker a deal but came back empty handed. He obtained a largely symbolic reciprocity clause on cabotage’<sup>109</sup>.

The EU was aware of Telicka’s true reservation point in the negotiations. In the absence of a domestic veto player the outcome could only go towards the EUs preferred outcome unless the Czech Republic would favour the breakdown of the accession talks (see Figure 44, cases 1,5 and 9). The Czech Republic was the last to close the transport chapter in the accession negotiations (see Table 25).

Telicka backed the steel industry and was the third last country to close the negotiations on competition policy. In the presence of a strong domestic veto player the EU caved in to the Czech demands and allowed it to continue state aid for its ailing steel industry after EU membership.

#### **7.2.2.2. Hungarian Constraints**

Well organised sectoral interest groups mobilised in all three sectors. The strong Hungarian pharmaceutical industry would lose its domestic and foreign markets under EU legislation. The international road freight industry and the basic iron and steel producers feared foreign competition after EU membership. The government took note of the concerns of the pharmaceutical and road freight industry.

Regardless of the composition of the government in the single chamber parliament, becoming a full member of the EU had been a top priority of Hungarian foreign policy practically since 1990.

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<sup>109</sup> Interview by Author with Representative of the Office of the Government of the Czech Republic, Prague, 04/05/2004b.

The general elections in May 1998 brought a new centre-right government headed by Mr *Viktor Orbán* to power with a comfortable majority of 20 seats in parliament (see Table 24). Moreover, all six parliamentary parties were in favour of EU membership and energetically co-operated on EU legislation. Regular opinion polls showed that Hungary was among the most pro EU membership candidate states. In 2001, 70 per cent of those polled were supportive of EU membership rising to 77 per cent in 2002 with 10 and eight per cent respectively opposing the process<sup>110</sup>. The accession process nevertheless left policy makers nervous enough to allow a referendum with a low ratification constraint.

With a substantial parliamentary majority and favourable public opinion polls the government cleared most obstacles on the road to EU entry. It dropped TPRs during the negotiations and ignored sectoral interests groups such as the basic iron and steel industry. It would hold on to TPRs that would have a positive impact on the budget and/or had the potential for a high level of political salience, which was the case for pharmaceuticals and the international road freight transport sector. These dynamics did not change after the general elections of April 2002, which resulted in the formation of a centre-left cabinet with a five seats majority in Parliament under the leadership of *Peter Medgyessy*.

The two well organised sectors constrained the government in the accession talks. The Hungarian chief negotiator, *Mr. Endre Juhász*, held out in the negotiations on company law which had an impact on pharmaceutical production. Hungary closed the chapter as the last but one among the candidate countries, which was unusual. In the area of road freight transport Budapest was among the last four to close the negotiations and obtained a TA for its sector (see Figure 44, cases 2, 6 and 10). The deals in pharmaceuticals and international road freight transport were subsequently extended to other applicant countries under the principle of equality in the negotiations.

### **7.2.2.3. Polish Constraints**

The sectoral interest groups mobilised in the pharmaceutical and the basic iron and steel industry sectors but not in the road freight industry. The latter was competitive and dominated the market. In contrast, the basic iron and steel industry would see its state aid slashed after EU membership.

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<sup>110</sup> European Commission, *Candidate Countries Eurobarometer (Fieldwork October 2001)*, Brussels, March 2002.; European Commission, *Candidate Countries Eurobarometer: Public opinion in the countries applying for European Union membership (Fieldwork: September-October 2002)*, Brussels, December 2002.

The pharmaceutical industry would see its cost base rise and export markets evaporate under EU membership. The government paid attention to both sectoral concerns.

When the negotiations commenced the PM, Mr. *Jerzy Buzek*, headed a centre-right coalition government of the Solidarity Electoral Action (AWS) and the liberal Freedom Union (UW) with a comfortable majority of 31 seats in the Lower House (Sejm – see table 2). It was unequivocal pro-EU membership, however, feuding between the coalition partners and a lack of internal party discipline among rivalling factions of the AWS slowed EU related legislative work.

The government's priority was the quality of EU membership rather than EU entry at all costs. EC officials expressed concern over the lack of control the government had over the behaviour of its members in parliament, 'who often tinker with legislation to such an extent that the final version is completely out of line with EU laws'<sup>111</sup>. When the UW decided to leave the coalition in June 2000 the Buzek cabinet was left to govern as minority government. It depended upon the support of opposition parties to pass EU legislation.

The EU accession negotiations suffered from the political instability and pork barrel politics for the passage of EU legislation in the Sejm. By the first half of 2001 Poland fell behind in the negotiations relative to its neighbours. It was held hostage by demands from interest groups and rivalling AWS factions in the run-up to the September 2001 elections. Instead of acquiescing the EU decided to hold out in the negotiations and waited for a new government to take office.

The 23 September 2001 elections proved a watershed for Polish politics. They resulted in an obliteration of the ruling centre-right AWS. Instead three right wing and outright anti-EU parties made it into the Sejm with a combined vote of over 25 per cent and 123 seats (see Table 24). A new eurosceptic centre-right party, Citizens Platform (PO), took the middle ground with 63 seats. Poland was now the only country in the region with outright Euro-sceptic and anti-European parliamentary parties. The victory of the eurosceptic and anti EU parties was in part related to domestic reforms that had been blamed on EU accession.

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<sup>111</sup> T. SIMON, War of words erupts over enlargement, in: *European Voice*, 23/03/2000.

The victor of the elections was the pro-EU centre-left SLD-UP. It fell short of a parliamentary majority and struck an uneasy coalition agreement with the Polish Peasants Party (PSL). The new cabinet with the SLD Premier, Mr. *Leszek Miller*, at the helm made EU accession negotiations the domestic and foreign policy priority number one. It streamlined and insulated the institutional structures dealing with the EU and changed the chief negotiator and most of the executive personnel associated with the negotiations. In a clear break with the previous government the new negotiation strategy called for closing all negotiation areas not directly linked with money<sup>112</sup>.

Despite the eurosceptic vote in the elections the growing popularity of EU membership supported the new EU strategy. In 2001 54 per cent of those polled were supportive of EU membership while 26 per cent opposed it. By December 2001, 56 per cent was in favour of EU membership and 24 per cent against. And in 2002 this figure had risen to 61 per cent in favour with 18 per cent against<sup>113</sup>.

Strong party discipline and a rising wave of popular support for EU membership made the government clear most obstacles on the road to EU membership. It dropped TPRs where they did not have a positive impact on the budget or might damage popular support. As a result, the government supported the pharmaceuticals and iron and steel industry in the negotiations. In the area of company law the Poland's new chief negotiator, Mr. *Jan Truszczyński*, kept his resolve and closed the negotiations on pharmaceuticals as the last candidate country (see Table 25). In fact Poland re-opened the chapter on pharmaceuticals for its industry. In the area of competition policy which dealt with the basic iron and steel subsidies it closed the chapter last. Finally, Warsaw took over the deal on international road freight transport from Hungary under the principle of equality in the negotiations (see Figure 44, cases 3, 7 and 11). Throughout the negotiations Poland's negotiators were supported by a strong ratification constraint in the form of a referendum.

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<sup>112</sup> Accession: New Negotiation Strategy, in: *The Warsaw Voice*, 25 November 2001.

<sup>113</sup> European Commission, *Candidate Countries Eurobarometer (Fieldwork October 2001)*, Brussels, March 2002.; European Commission, *Candidate Countries Eurobarometer: Public opinion in the countries applying for European Union membership (Fieldwork: September-October 2002)*, Brussels, December 2002.

#### 7.2.2.4. Slovak Constraints

In Slovakia the executive decided to ignore the domestic pharmaceutical producers. EU legislation would have a limited impact on the market and the government budget. The international road freight transport sectors did not hold strong preferences over EU membership. It was one of the most competitive road transport sectors in the region. The basic iron and steel industry, however, was furious at the prospect of losing a lucrative tax holiday because of EU membership. It mobilised politically and left the executive little choice than to fight for its interests at the international negotiating table.

Following the September 1998 elections the centre-left, populist and eurosceptic Movement for a Democratic Slovakia (HZDS) became the biggest political force in the single chamber parliament (National Council). It was consigned to opposition following the formation of the ideologically diverse coalition government comprising four parties with Prime Minister Mr. *Mikulas Dzurinda* in the driver's seat. It commanded a three-fifths parliamentary majority (see Table 24). The Dzurinda I cabinet was keen to put EU accession back on track after the EU had refused to open accession negotiations with Slovakia because of the authoritarian nature of the previous government. During his inaugural speech in November 1998 Mr. Dzurinda declared that '[...] the strategic goal and one of the most important political and economic priorities of the Slovak Republic is the membership in the European Union'<sup>114</sup>. The elections of November 2002 maintained the essential dynamic of Slovakia's EU membership drive. The Dzurinda II cabinet held on to a three seat majority in the National Council.

A strong and rising pro-EU membership popular opinion supported the Dzurinda I&II governments in their accession drive. Eurobarometer opinion polls indicated that 66 per cent of the Slovak electorate was supportive of EU membership with 11 per cent opposing it in 2001. By October 2002 this number had risen to 69 per cent with 11 per cent opposing<sup>115</sup>.

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<sup>114</sup> E. SLIVKOVA, *Slovakia's Response on the Regular Report from the European Commission on Progress towards Accession*, Bonn: Zentrum für Europäische Integrationsforschung, Center for European Integration Studies Rheinische Friedrich Wilhelms-Universität Bonn, 1999., pp. 5-6.

<sup>115</sup> European Commission, *Candidate Countries Eurobarometer (Fieldwork October 2001)*, Brussels, March 2002.; European Commission, *Candidate Countries Eurobarometer: Public opinion in the countries applying for European Union membership (Fieldwork: September-October 2002)*, Brussels, December 2002.

Slovakia was catching up in the negotiations. It did not go through an concerted industry consultation exercise. It emulated the strategy of the neighbouring countries and concentrated on the budgetary implications and political salience of TPRs.

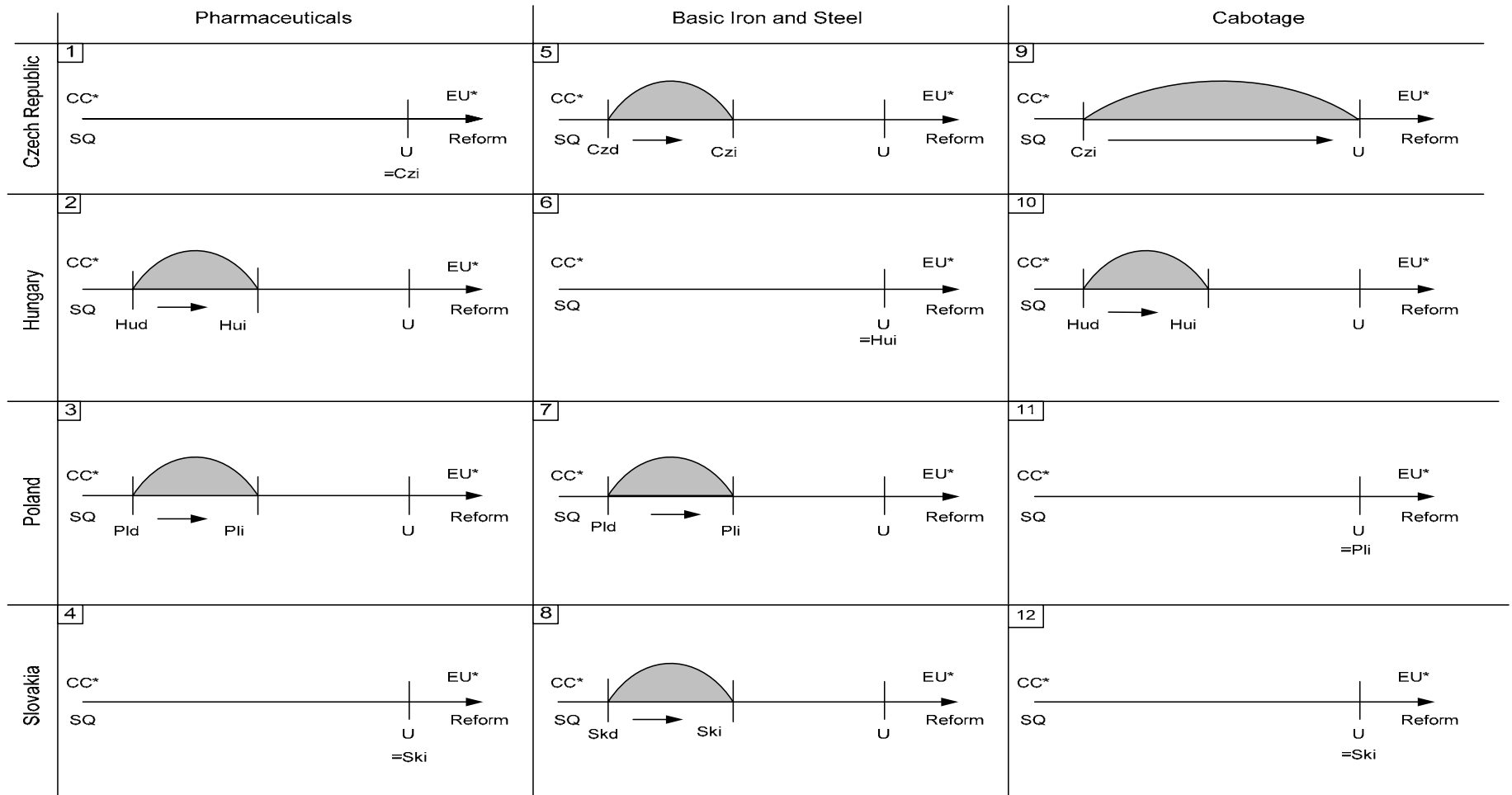
In the absence of veto players in the area of pharmaceuticals and cabotage Slovakia closed the negotiations in company law and transport as second and fifth respectively among the applicant states (see Table 25). The swiftness of closing these chapters is a remarkable feat knowing Slovakia started negotiating only in 1999. In the area of transport it held out because it did not want to break ranks with the Czech Republic: ‘The Czech Republic waited to close the chapter. While Slovakia and the Czech Republic had a similar starting position, the Czechs waited to close a chapter in order to have a better deal. This was not always an optimal solution because there might be a spill over from another country that had already closed. We had to be careful not to have a negative effect from not closing. For us it made no sense to leave a chapter open until the end’<sup>116</sup>.

In competition policy it went to the negotiations constraint of the large steel producer, US Steel. It proved to be the longest of all negotiation rounds between Bratislava and Brussels. The EU gave in to Slovak chief negotiator, Mr. *Jan Figel*, who obtained an 11 year tax holiday exemption from the EU treaty (see Figure 44, cases 4, 8 and 12).

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<sup>116</sup> Interview by Author with the Chief Negotiator of the Slovak Republic, Bratislava, 05/03/2003.

Figure 44: Domestic Constraints at the EU Entry Talks for the V-4



Legend: CC\*=candidate country; EU\*=EU; SQ=status quo; U=EU\*'s reservation point under unanimity (reform at U); Czi=Czech Republic international; Czd=Czech Republic domestic; Hui=Hungary international; Hud=Hungary domestic; Pli=Poland international; Pld=Poland domestic; Ski=Slovakia international; Skd=Slovakia domestic  
 Source: chapters 3, 4, 5 and 6

**Table 24: Governments and Parliamentary Majorities in the V-4**

Country	elections	cabinet	party	position	vote (%)	seats	coalition parties	majority	majority 1	majority 2			
Cz	19/06/1998 14/06/2002	Zeman I	CSSD (Czech Social Democratic Party)*	CL-P	32.2	74	1	-26(37)'	18.50	-13.00			
			ODS (Civic Democratic Party)	CR-S	27.7	63	1	-26(37)'					
			KSCM (Communist party of Bohemia and Moravia)	L-S	11	24	1	-26(37)'					
			KDU-CSL (Christian Democrats-Czech People's Party)	CR-P	9	20	1	-26(37)'					
			US (Freedom Union)	CR-P	8.6	19	1	-26(37)'					
total				88.5	200	1/2	-26(37)'						
	14/06/2002 02/06/2006	Spidla I	CSSD (Czech Social Democratic Party)*	CL-P	30.2	70	2	1	n.a.	n.a.			
			ODS(Civic Democratic Party )	CR-S	24.5	58	2	1					
			KSCM (Communist party of Bohemia and Moravia)	L-S	18.5	41	2	1					
			Coalition (KDU-CSL & Freedom Union)*	CR-P	14.3	31	2	1					
			total				87.5	200	2	1			
Hu	10-24/05/1998 27/04/2002	Orban I	Federation of Young Democrats-Hungarian Civic Party (Fidesz-HCP)*	CR-P	29.4	148	3	20	5.18	n.a.			
			MSZMP (Hungarian Socialist Party)	CL-P	32.9	134	3	20					
			SP (Independent Smallholders Party)*	CR-P	13.2	48	3	20					
			AFD (Alliance of Free Democrats)	CL-P	7.6	24	3	20					
			MIEP (Hungarian Justice and Life Party)	R-P	5.5	14	3	20					
			HDF (Hungarian Democratic Forum)*	CR-P	2.8	17	3	20					
			total				91.4	385	3	20			
	7-21/05/2002 09/05/2006	Medgyessy I	MSZMP (Hungarian Socialist Party)*	CL-P	46	178	2	5	1.30	n.a.			
			Federation of Young Democrats-Hungarian Civic Party (Fidesz-HCP)	R-P	48.6	188	2	5					
			AFD (Alliance of Free Democrats)*	CL-P	5.2	20	2	5					
			total				99.8	386	2	5			
Pl	21/09/1997 23/09/2001	Buzek I	AWS(Solidarity Electoral Action)*	CR-P	33.83	201	2(1) June 2000	31(-29)	6.74	-6.30			
			SLD(Democratic Left Alliance)	CL-P	27.13	164	2(1) June 2000	31(-29)					
			UW (Freedom Union)*	CR-P	13.37	60	2(1) June 2000	31(-29)					
			PSL (Polish Peasant Party)	CR-N	7.31	27	2(1) June 2000	31(-29)					
			ROP(Movement of Poland's Reconstruction)	CR-P	5.56	6	2(1) June 2000	31(-29)					
			German Minority		0.61	2	2(1) June 2000	31(-29)					
			total				87.81	460	2/1	31(-29)			
				23/09/2001 25/09/2005	Miller I	SLD-UP(Democratic Left Alliance-Labour Union)*	CL-P	41.3	219	2(1) March 2003	31(-11)	6.74	-2.39
						PO (citizens Platform)	CR-P	12.7	63	2(1) March 2003	31(-11)		
						Samoobrona (Self Defence)	L-S	10	53	2(1) March 2003	31(-11)		
PiS (Life and Justice Party)	R-S	9.8				47	2(1) March 2003	31(-11)					
PSL (Polish Peasant Party)*	CR-N	8.8				42	2(1) March 2003	31(-11)					
LPR (League of Polish Families)	R-S	7.7				34	2(1) March 2003	31(-11)					
German Minority		0.61				2	2(1) March 2003	31(-11)					
total							90.3	460	2/1	31(-11)			
Sk	26/09/1998 20/09/2002	Dzurinda I	HZDS (Movement for a Democratic Slovakia)	CL-S	22.5	43	4	18	12.00	n.a.			
			SNS (Slovak National Party)	R-S	7.6	14	4	18					
			SDL (Party of the Democratic Left)*	CL-P	12.2	24	4	18					
			SMK (Hungarian Coalition)*	CR-P	7.6	14	4	18					
			SDK (Slovak Democratic Coalition)*	CR-P	22	42	4	18					
			SOP (Party of Civic Reconciliation)*	C-P	6.7	13	4	18					
			total				78.6	150	4	18			
				20/09/2002 17/06/2006	Dzurinda II	HZDS (Movement for a Democratic Slovakia)	CL-S	19.5	36	4	3	2.00	n.a.
						SDKU(Slovak Democratic and Christian Union)*	CR-P	15.1	28	4	3		
						Smer (Direction)	CL-P	13.5	25	4	3		
SMK (Hungarian Coalition)*	CR-P	11.2				20	4	3					
KDH (Christian Democratic Movement)*	CR-P	8.3				15	4	3					
ANO (Alliance of the New Citizen )*	CR-P	8				15	4	3					
KSS (modern Communist Party of Slovakia)	R-S	6.3				11	4	3					
total				81.9	150	4	3	2.00	n.a.				



**Table 25: Duration of the Accession Negotiation Rounds (March 1998-December 2002)**

Chapter/Country	Cy	Cz	Es	Hu	Lv	Lt	Mt	Pl	Sk	Sl
Chapter 1: free movement of goods	17	6	18	23	0	0	0	21	0	21
Chapter 2: free movement of persons	13	17	22	13	0	5	0	19	0	19
Chapter 3: free movement of Services	22	20	19	19	10	11	4	16	10	16
Chapter 4: free movement of Capital	0	0	0	0	0	0	0	n.a.	0	0
Chapter 5: Company Law	30	30	21	33	11	11	2	36	7	18
Chapter 6: Competition Policy	37	41	30	43	18	18	25	43	29	30
Chapter 7: Agriculture	30	30	30	30	18	18	12	30	18	30
Chapter 8: Fisheries	12	1	12	0	12	2	20	38	0	0
Chapter 9: Transport Policy	18	37	28	25	13	13	7	31	17	25
Chapter 10: Taxation	29	25	31	19	13	10	18	28	9	25
Chapter 11: Economic and Monetary Union	0	0	0	0	0	0	0	3	0	0
Chapter 12: Statistics	3	3	3	3	2	2	2	3	1	3
Chapter 13: Employment and social Policies	6	20	13	14		4	0	18	3	14
Chapter 14: Energy	0	0	0	0		0	0	20	0	0
Chapter 15: Industrial Policy	0	0	0	0	0	0	0	6	0	0
Chapter 16: Small and Medium-sized enterprises	1	1	1	1	0	0	0	1	0	1
Chapter 17: Science and Research	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Chapter 18: Education and Training	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Chapter 19: Telecom and IT	7	6	6	19		5	0	7	5	8
Chapter 20: Cultural and Audiovisual Policy	1	32	24	44	10	7	5	25	6	31
Chapter 21: Regional Policy	24	24	26	27		15	16	30	16	27
Chapter 22: Environment	19	18	18	18		7	16	22	9	15
Chapter 23: Consumer Protections	1	1	1	2	0	0	0	1	0	1
Chapter 24: Justice and Home Affairs	19	19	22	18	12	10	9	26	12	19
Chapter 25: Customs Union	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Chapter 26: External Relations	0	0	0	0	0	0	0	6	0	0
Chapter 27: CSFP	0	0	0	0	0	0	0	17	0	0
Chapter 28: Financial Control	0	0	0	0	0	0	0	2	0	0
Chapter 29: Finance and budgetary Provisions	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Chapter 30: Institutions	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Chapter 31: Other	0	0	0	0	0	0	0	0	0	0

Source: Own compilation

## Conclusion

Chapter 7 spelled out the institutional origins of the EU's dominant bargaining power in the negotiations. It established a two dimensional spatial model based on the Schelling conjecture for understanding the role of domestic constraints in international negotiations. The application of the model to the accession negotiations between the EU and the V-4 in the area of pharmaceuticals (EU company law), basic iron and steel (EU competition policy) and international road freight transport (EU transport law) confirmed its main predictions. Its findings are in line with Schelling's paradox of weakness under complete information, that is binding oneself domestically can be useful for extracting concessions internationally.

The chapter finds that regardless of the EU's dominant bargaining power derived from institutional characteristics applicant countries were able to negotiate sectoral exemptions from the *acquis* when confronted with at least one domestic veto player. Despite a strong motivation to

clear obstacles on the road to EU membership, governments in the region observed sectoral interests when their demands contributed positively to the general budget. In addition, negotiators were wary of issues that might damage popular support for EU membership particularly in the view of a post ratification constraint.

In contrast, in the absence of a domestic constraint the outcome of the negotiations would resemble the preferences of EU negotiators. In other words, negotiators were prepared to stretch but not overstretch domestic political support.

The chapter also elucidated the presence of TAs where sectors did not politically mobilise (see Part II) or countries did not support TPRs in the respective position papers (see chapter 6). The dynamic of equality and reciprocity between the negotiating parties worked against the EU's dominant institutional power. When one applicant country struck a deal it set a precedent in the negotiations usually followed by the others, which the EU extended upon request. While the negotiations were bilateral in the constitutional and legal sense they were multilateral in practice with spill over effects on the EU's side of the bargaining table. The EU did not deal with country specificities and generalised solutions to the other negotiating parties.

## ANALYTICAL SUMMARY

### **The Puzzle and Questions?**

The topic of this dissertation has been the varying sectoral conditions, i.e. transitional arrangements (TAs), under which the applicant states joined the EU in May 2004. These arrangements delay the application of the body of EU legislation.

The presence of TAs is puzzling for three reasons. First, EU membership presupposes the full application of the *acquis communautaire* in the applicant states. The presence of TAs in the applicant countries for certain economic sectors suggests the opposite. Second, given that TAs ease the adjustment cost of EU membership, they are present in economic sectors and countries where we least expect them. Finally, it is surprising that the applicants were able to negotiate exemptions from applying EU legislation given the power asymmetry in the accession negotiations.

Therefore, the two central research questions that lie at the basis of this dissertation are: Why and how do sectoral conditions for joining the EU vary for the individual applicant states? And, what do the transitional arrangements reveal about sectoral and state interests' ability to influence the enlargement process?

### **Why Is It Important?**

Studying these sectoral conditions present an opportunity for the comparativist interested in EU decision making processes. TAs are the distributional outcome of the EU enlargement process. Their variation tells us something about the EU accession negotiations and the sectors and countries to which they apply. They provide us with a handle on the conceptually and analytically elusive phenomenon of EU enlargement.

Treating TAs as *explanadum* allows us rigorously to test hypotheses pertaining to the behaviour of sectors and states to which they apply, and the respective strategies for pursuing them.

## How Did I Choose to Solve It?

Conventional accounts that solely refer to the EU traditional manner of expansion and the strategic calculus of the member states and their counterparts are inconclusive when applied to this puzzle. The former cannot explain the specificities of the variation of TAs across countries and sectors. The latter is unable to provide a convincing and conclusive explanation for their presence.

Instead, I have used insights from *modern political economy*, *comparative politics* and *negotiation theory*. The theoretical framework allows for the exploration of how and why sectors, states, and their strategies at the negotiating table affect distributive outcomes and mediate the EU membership talks.

The research design has been structured around two building blocks to isolate the independent variables (sectors, states and strategies). Each has a logic of its own and relates to a different explanation. Are the sectoral conditions under which the EU enlarges influenced by sectoral interests? Or alternatively, do they reflect the underlying pattern of aggregation of those sectoral interests in the public arena?

Modern political economy corresponds to the demand side of the argument. It expects that TAs and their variation are the result of sectoral interests' preferences shaped by patterns of interdependence, i.e. their position in the economy. It allows for the formulation of clear hypotheses to analyse the effect of EU integration on sectoral incomes and the ensuing intensity of preference formation. It also permits the analysis of the strength of sectoral organisations and their propensity to exert political pressure.

The state and strategy-centred approach attributes less importance to these groups. It considers state preferences and the strategic bargaining in the negotiations as the main explanatory variables. The supply side of the argument explores how institutions aggregate and influence sectoral preferences in the public arena.

The interaction between both explanatory variables follows the logic of *constructive and destructive interference*. States and international organisations act as constraints upon sectoral preferences when their interests are not aligned, i.e. destructive interference. Conversely, when sectoral interests and institutional preferences are aligned states and strategies sustain or amplify societal preferences. This is what I refer to as constructive interference.

In other words, this study takes a comparative perspective that stands in contrast to the assumptions of a purely pluralist model of interest politics. It assumes that the accommodation of sectoral preferences is not inevitably concomitant to sectoral political mobilisation. It is explicit about public institutions. As a result, this study separately considers the mediating effect states and international organisations have on sectoral interests.

### **The Implementation of the Study**

The study devised two different tests to assess economic sectors' demands for protection in enlargement policy; and governments and international organisations' mediation of those demands.

In the first test (Part I) I quantitatively compare the universe of cases, i.e. all 47 economic sectors across all ten applicant states in the fifth EU enlargement (1998-2004) according to their trade, factor and asset specificity.

The second is a qualitative test (Part II and III) of specified sectors and countries. The logic of *Mill's* comparative method guided the cases selection. The most dissimilar system design has allowed inference on the importance of the sector on a country level, and the role of the country across similar sectors on a cross-country level. Modern political economy guided the selection of sectors.

The case studies are the pharmaceutical, basic iron and steel and international road freight transport industries for the Visegrad Four, i.e. the Czech Republic, Hungary, Poland and Slovakia. They have been based on sector and country-specific literature and 82 positional and structured interviews.

## **Findings**

### **Part II: Sectors – the Demand Side**

Enlargement policy had a redistributive influence on incomes that resulted in preference formation and political mobilisation along sectoral lines. Sectors asserted their interest in the accession negotiations when particular terms of EU enlargement were debated. This confirms the underlying argument that the presence and variation of different sectoral conditions (TAs) for EU entry is due to sectoral interests and their ability to influence EU enlargement policy.

The hypotheses based on an asset specific theory combined with assumptions about asymmetric lobbying hold up well for the prediction of preference formation and political mobilisation. Following *Frieden, Rogowski* and *Gilligan*, an asset and factor-specific theory usually picks up changes in sectoral economic positions and in ensuing socio-economic institutions over *la longue durée*. Given the short period this research studies, i.e. 1989-2004 and more specifically 1998-2002, the theory performs remarkably well. It continues to pick up the EU enlargement effect in transition countries experiencing drastic economic changes.

When considering preference formation and the likelihood of political mobilisation, the framework explains up to 83 per cent of the cases, or ten out of 12 cases. Those sectors that are more factor and asset specific hold stronger preferences; and have a higher propensity to exert political pressure.

The assumptions about the influence of insider status in the policy process and ownership structures on the likelihood of success do not hold up. In fact, the causality travels in the opposite direction.

### **Preference Formation**

Sectoral conflicts that occur because of the income redistribution induced by market integration have strong effects on preference formation. First, in the sample preference formation occurred along sectoral lines. Second, sectors characterised by a progressive comparative disadvantage are more likely to form preferences than those with a comparative advantage. The former were more likely to oppose strict application of the *acquis* and the redistributive effect it had on their income.

Third, anticipated loss of income provoked stronger preferences over EU enlargement policy than anticipated gains. In the sample those sectors which expected benefits did not form strong preferences and failed to mobilise. This chimes with claims stressing the uncertain nature of gains relative to losses. Economic actors only know that some markets will open up, not whether they will be able to capitalise on this opportunity in the face of international competition. Moreover, actors tend to react more strongly to losses than gains, again favouring losers in the mobilisation dynamic. Very few actually lobbied for opportunities in the enlargement process.

Fourth, exporters with a comparative advantage that stand to lose because of changing policies hold the strongest preferences. They tend to mobilise most intensely. Because of their international exposure they know precisely what they will be losing as a result of EU integration. This enhances their incentives to mobilise politically. Relative to those actors exclusively focussed on the domestic market, they are also more likely to mobilise internationally.

### **Political Mobilisation**

Sectoral socio-economic assets contribute to the ability of actors sharing a common interest to overcome collective action problems critical to the effects of political capacity.

Political capacity was highest for the basic iron and steel industry as it could mobilise to overcome collective action problems at the lowest marginal cost. The steel trade disputes throughout the 1990s and early 2000s are a case in point. Concentration in the pharmaceutical industry was lower and the marginal costs for overcoming collective action problems were higher. In the pharmaceutical industry, collective action problems were compounded by sectoral division between local producers and foreign subsidiaries. The dispersed road hauliers industry had the lowest sectoral concentration. Road haulers had difficulty in mobilising their vast and geographically spread membership at short notice, which EU accession negotiations required.

Cross-sectorally, the Hungarian pharmaceutical and Slovak basic iron and steel sector held the highest national and regional score for asset specificity. They had invested heavily in anticipation of continuing sales. All other comparable asset-specific industries exerted political pressure except for the Slovak drugs industry. Czech, Polish and Slovak road haulers whose asset

specificity was the lowest failed to mobilise. Their Hungarian counterparts put pressure on the authorities. They were assisted by one regionally and nationally dominant road freight enterprise.

While theoretically plausible, the assumption that factor specific sectors are more likely to hold better organised political assets was empirically ambiguous in the sample. Despite the variation in asset specificity and empirical evidence of lobbying, all three sectors appeared to have equally well-organised sectoral associations. It was empirically difficult to gauge asset specificity or political capacity on the basis of institutional characteristics.

The empirical research also established that membership of European or international associations did not contribute to the weight of political assets of the V-4 industries. European or international associations protected the interests of their respective insiders. They opposed those of its new Central European associative members.

Therefore, this research concludes on the basis of the sample that preference formation rather than political capacity is decisive for political mobilisation and its intensity.

### **Insider Status and Ownership Structures**

A state-owned firm is likely to have a higher insider status compared to a private firm. The former would be more successful in protecting its interests relative to the latter. A foreign-owned firm is more of an outsider relative to a domestically-owned one. The former is more successful in protecting its interests relative to the latter.

Both assumptions have proven to be incorrect, both within and across sectors. While state ownership provided direct access to policy makers in the enlargement process it did not necessarily result in a better protection of the firm's interests. Empirical evidence from the sample suggests that private owners were less inclined to compromise on the preferences they held than publicly-owned enterprises and sectors. Firms in foreign hands, and particularly those with a strong, and rising presence in international markets, held strong preferences and mobilised both nationally and internationally. They also tended to be politically more effective.



Finally, relative economic and political strength on a national and regional level is a good indicator for the supply of protection when political mobilisation occurred. When controlling for economic size and population, the effect of a large industry in a small country continues to be overriding. Political mobilisation in the V-4 predominantly occurred within the national context.

### **Empirical Discrepancies**

Social inference on the basis of a factor and asset specific theory is less clear cut (66 per cent or in eight out of 12 cases) when taking into account the supply for protection. On many occasions respective state institutions decided to ignore sectoral political preferences.

The discrepancies between preference formation, political mobilisation and national negotiation positions rise to almost one in two in the sample when taking into account the eventual policy outcomes. Grace periods appear for sectors that did not hold strong preferences or mobilise, and for states that did not ask for TAs.

The implicit political model of economic pluralism in modern political economy has its strengths. It performs well in anticipating political mobilisation of economic sectors. The presence and the degree of political pressure is a function of economic conflict shaped by actor's preference formation and weighted by their socio-economic organisational capacity.

It performs less well in its assumptions that the effects of market integration on sector's preference formation and mobilisation will automatically feed into institutional arrangements. Policy outcomes are not automatically a result of sectoral preference formation and political mobilisation as predicted by 'demand side' international political economic theory.

### **Part III: States and Strategies – the Supply Side**

Part III demonstrates that states and international organisations and the strategies of actors occupying these institutions mediate sectoral interests according to what I call *the logic of destructive and constructive interference*. States and international organisations act as constraints on societal preferences at the negotiating table when their interests are not aligned. This is 'destructive interference'. Conversely, when societal interests and institutional preferences are aligned states and strategies sustain or amplify societal preferences at the negotiating table. This I refer to as 'constructive interference'.

More specifically, Part III finds that the following all have mediating effects for international outcomes: the number of domestic veto players and their preferences; the degree of institutional insulation from sectoral preferences; and the respective national strategies at the international negotiating table. They limit, sustain or amplify the scope for international sectoral agreements; and allow for their extension to sectors and countries that did not pursue them.

The hypotheses based on the theory of veto players, combined with assumptions about executive preference formation and insulation of the policy process, perform surprisingly well. The institutions in the applicant countries were more receptive to sectoral pressures the higher the number of institutional actors whose assent was required for a policy change. In fact, the V-4 countries reduced their number and insulated the EU-related policy process from sectoral pressures to clear obstacles on the road to EU membership. The sample also confirms the conjecture that the executive's majority in Parliament and the proximity to the next general elections loomed large over enlargement policy. All three findings have been consistent across the cases.

Finally, in contrast to the general assumption of power asymmetry in the enlargement negotiations, the Shelling paradox of weakness has been confirmed by the sample. A high domestic ratification constraint for the applicants' individual chief negotiators provided for a bargaining advantage at the negotiating table in Brussels. This has been the case across sectors and countries. Additionally, this finding has been corroborated by a test of revealed preferences in the negotiations for the 12 case studies.

### **Veto Players**

Institutions are likely to be more receptive to societal pressures the higher the number of institutional actors whose assent is required for a policy change. All countries reduced the number of veto players, leaving only the executive and the electorate with a post-ratification constraint. The rising national disregard of demand for protection confirms the hypothesis. It demonstrates that the number of institutional veto players in the Czech Republic, Hungary, Poland and Slovakia had an important influence on the status quo or states' acceptance of sectorally-solicited protection.

Variation of formal veto players in the V-4 countries for EU accession policy was minimal. The presidents in the V-4 delegated their power to the governments in the area of EU foreign policy. Despite passing over 80,000 pages of EU-related legislation, national Parliaments voluntarily gave up their say on the direction of EU enlargement policy. In addition, they delegated their ratification constraint on EU membership to the electorate under a surprisingly low threshold in the Czech Republic and Hungary. Only in Poland and Slovakia was a normal referendum constraint maintained.

Minimizing the veto constraint allowed the executives to strengthen their grip on accession policy. The preference function of the executives in Prague, Budapest, Warsaw and Bratislava was influenced by their majorities in Parliament and the proximity to the next elections. The larger the executive's majority and proximity to the next general elections the less likely sectoral preferences prevailed in national EU accession policy.

Minimizing vetoes allowed government's to prioritise and pick sectoral demands for protection on a case-by-case basis according to a combination of the *acquis'* impact on the government budget, the political salience of the issues at hand and the strength of the sectoral interests that lobbied for the status quo. As a corollary to Part II, sectoral businesses that were well organised, could produce good arguments for the negotiation positions, and could set up an effective lobbying campaign, would generally have their interests represented in the negotiation positions.

Finally, within the executive the distribution of power changed in favour of those ministries that directly represented the case for reform, i.e. full EU membership as early as possible. The Ministry of Foreign Affairs (MoFA) gained responsibility in all V-4 countries at the expense of those ministries and governmental offices that were more concerned with the sectoral costs of EU enlargement. These were the line ministries and those with horizontal responsibilities such as Ministry of Finance (MoFI), Ministry of Economy (MoE) or the Ministry of Industry (MoI). They were less willing to compromise on the status quo.

### **Insulation of the Policy Process**

The more decision-making authority over policy was insulated from sectoral pressures the less policy change was associated with changes in sectoral preferences and their political mobilisation. In all V-4 countries the executives progressively insulated the EU-related decision-making processes from sectoral pressures.

The more politicised executive institutions, i.e. the Prime Minister's Office (PMO) and line ministries, gave up authority over enlargement policy in favour of those more insulated from sectoral pressures (the MoFA). The MoFA represented the case for reform. It was directly plugged into the accession game in Brussels and stood closest to the EU's point of view. Concentration of power in the MoFA came at the expense of other ministries less insulated from national sectoral interests and more susceptible to maintaining the status quo.

A similar evolution became visible with regard to the national consultation of sectoral interests. Hungary went to the negotiations after a well-organised, concerted effort to consult the different sectoral interests. In the Czech Republic the tripartite consultations were more informative. Sectoral interests did not use the consultations to the full because of the *precautionary principle*, i.e. a deliberate attempt to limit demands for protection so as to make an international deal more likely. Polish policy makers set up a system at the heart of the PMO chaired by the chief negotiator with the purpose of collecting information from sectoral interests about the impact of EU legislation. It did not function well. The authorities were often confronted with a plethora of interests that did not speak with a single voice. The consultative committee in Slovakia set up with a similar purpose turned out to be a paper tiger. It was rarely used.

Also in this area the V-4 converged between 1998 and 2002. In Hungary consultations increasingly occurred directly between the MoFA and the experts and sectoral interests. The meetings in the Czech Republic became increasingly informative. In Poland the government abolished the consultative body after October 2001. In Slovakia consultation occurred directly between the chief negotiator, the Minister of European Integration and the mobilising sectors.

Under a growing insulation of the institutional process and the decline of organised consultation, predominantly large export-oriented companies and well-organised sectors were able to gain

access to EU-related institutions. This did not mean that executives had difficulty in controlling sectoral interests. On the contrary, the insulation was designed to reduce interference from society. It went hand in hand with reducing the influence of demands for protection on policy formation according to the logic of constructive and destructive interference.

The growing insulation of decision making processes as result of the convergence of formal veto players, the reinforced role of the executive and the MoFA, and the declining influence of the line ministries (and hence also sectoral preferences), resulted in a general reduction of demand for protection in the national negotiation positions.

### **International Strategies and the Paradox of Weakness**

National strategies at the international negotiating table have mediating effects on sectoral preferences to the extent that they limit or amplify the scope for international sectoral agreements. They also allow for their extension to sectors and countries that did not pursue them.

These findings are in line with Schelling's paradox of weakness under complete information, that is binding oneself domestically can be useful for extracting concessions internationally. Domestic institutions set the bargaining space for governments and their chief negotiators at the international negotiating table. Regardless of the EU's dominant bargaining power derived from institutional characteristics, applicant countries were able to negotiate sectoral exemptions from the *acquis* when confronted with at least one domestic veto player.

Despite a strong motivation to clear obstacles on the road to EU membership, governments in the region observed sectoral interests at the international negotiating table when their demands contributed positively to the general budget. In addition, negotiators were wary of issues that might damage popular support for EU membership particularly in view of a post ratification constraint. In contrast, in the absence of a domestic constraint, the outcome of the negotiations would resemble the preferences of EU negotiators.

The empirical test of the Schelling conjecture based on the duration of issue-specific negotiations between the individual applicants and the EU states corroborated these results.

Last but not least, EU accession negotiations have been characterised by a dynamic of equality and reciprocity between the negotiating parties. When one applicant country struck a deal, it set a precedent in the negotiations usually followed by the others. The EU extended these precedents upon request to the other applicants.

## CONCLUSIONS

The purpose of this study has been twofold. First, it has analysed how EU membership influenced the income of economic sectors in the applicant states. It explained whether and how they responded. Second, it clarified how the governments in the applicant states balanced the demands from sectoral interests with the broader objective of joining the EU.

In both cases the analysis has centred on the distributive outcomes of the enlargement negotiations, i.e. the presence and variation of sectoral conditions under which the applicant countries joined the EU. These conditions allow for a rigorous test of hypotheses pertaining to the behaviour of sectors and states to which they apply, and the respective strategies in the enlargement process for pursuing them.

The theoretical framework on the demand side has been provided by insights from modern political economy. It places economic interests, more specifically sectors, their preferences and political mobilisation at the centre of the argument. On the supply side, veto player and negotiation theory, combined with assumptions about political preference formation, provided hypothetical guidance. They considered the role of states (governments) and international organizations (strategies) as exogenous to elicit the aggregation and translation of sectoral demands for protection into national and international outcomes.

To this end I first contrasted the universe of cases, i.e. 47 economic sectors across all ten applicant states in the fifth EU enlargement (1998-2004) according to their trade, factor and asset specificity. Subsequently, I compared three economic sectors, i.e. pharmaceuticals, basic iron and steel and international road freight transport, across four applicant states, i.e. the Czech Republic, Hungary, Poland, and Slovakia.

While they were all keen to obtain EU membership, applicant states responded differently in the EU accession negotiations. This resulted in different national and international outcomes. Measured by the economic sectors to which they apply, the Czechs obtained 30 exemptions from the *acquis communautaire* and the Hungarians 29. The Poles negotiated 53 exemptions and the Slovaks just 25. These exemptions predominantly took the form of market regulations followed

by exclusions from EU tax and state aid law. They touched on approximately 13 per cent of the Czech economy and 11 per cent of Hungarian GDP. They covered as much as 33 per cent of Polish GDP compared to only 9 per cent of the Slovak economy.

My leading account for these varying outcomes is based on the role of sectoral interests. Sectors asserted their interest in the accession negotiations when particular terms of EU enlargement were debated. EU enlargement affected their incomes, their preferences and propensity to exert political pressure demanding protection from their governments. Those sectors with more specific factors and assets held stronger preferences as they would lose more from EU integration. They were also more likely to mobilise politically. Surprisingly, very few actually lobbied for opportunities in the enlargement process.

However, their success in the enlargement process was not inevitably concomitant to political mobilisation. Sometimes sectors carried strong preferences and mobilised politically without success. This was the case for the Czech pharmaceutical industry or the Hungarian basic iron and steel sector. For some sectors political mobilisation was absent while they obtained exemptions from EU law. The Slovak pharmaceutical industry and the Czech road freight transport sector are a case in point.

Therefore, I explicitly considered public institutions and the way they aggregated demand for protection in the public arena. States and international organisations and the strategies of actors occupying these institutions mediated societal interests along what I call *the logic of destructive and constructive interference*. States and international organisations act as constraints upon societal preferences at the negotiating table when their interests are not aligned, i.e. destructive interference. Conversely, when societal interests and institutional preferences are aligned states and strategies sustain or amplify societal preferences at the negotiating table, i.e. constructive interference.

Governments observed sectoral interests when their demands for protection reduced government expenditure for EU entry. Also, government negotiators' were wary of issues that might have damaged popular support for EU membership in view of the referenda on EU entry.



The effect that demand for protection would have on the budget and the potential for political salience contributed to the already well-organised pharmaceutical sector's strength in Hungary and Poland but not in the Slovakia and the Czech Republic. In contrast, demand for protection in the steel industry had a negative effect on the government's budget but its political significance was substantial and concentrated. In the area of road transport, protection would have no effect on the budget and its potential for political salience was negligible, except in Hungary.

On an international level, government negotiators found it easier to extract concessions from the EU when constrained by at least one domestic veto player. And last but not least, the EU would extend these concessions to other countries that requested them under the banner of equality and reciprocity.

In conclusion, this study has provided a framework for analysing EU accession negotiations. It highlights several relationships in the enlargement process that have been inadequately studied in the past. It stresses the role of structural factors for the understanding of the EU enlargement process, which essentially pertains to the extension of EU market regulations. In this study these structural factors have been market integration and their interaction with political institutions. In my view they are fundamental to the understanding of the EU enlargement process.

This study also demonstrates that exclusive accounts of economic interests are insufficient. The aggregation of interest groups' preferences in the public arena provides a necessary complement to insights provided by demand-side political economy accounts. In short, while sectoral preference formation and political mobilisation are necessary conditions for explaining international outcomes in the enlargement process, states and international organizations provide the sufficient conditions for their presence and distribution.

This study does not claim to provide an all-encompassing account or explanation of the EU accession process. EU enlargement is simply too large a political and economic event that affects nearly all facets of society. This study does, however, call for a more systematic analysis of the structural factors underlying enlargement. These are easily missed or misinterpreted by more traditional accounts that focus solely on the role of the states under a closed polity; or the role of EU enlargement policy as *sui generis*.

It is possible to analyse the EU accession process systematically in a comparative perspective. And there are important lessons to be learned from the experience of the countries that joined the EU on 1 May 2004. To that extent this study has offered an internally consistent theoretical framework that can predict the sectoral difficulties and the extent to which agreement is possible over them in the EU enlargement process.

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*Interview by Author with Representative of the Czech National Bank Prague, 04/05/2004a.*

*Interview by Author with Representative of the Czech Research Based Pharmaceutical Industry Prague, 25/03/2004b.*

*Interview by Author with Representative of the Czech Trade Union of the Steel Industry, Prague, 22/03/2004b.*

*Interview by Author with representative of the EC's Delegation to the Czech Republic Prague, 24/03/2004a.*

*Interview by Author with Representative of the EC's Delegation to the Slovak Republic, Bratislava, 11/03/2004.*

*Interview by Author with Representative of the Hungarian Competition Office, Budapest, 05/02/2004.*

*Interview by Author with Representative of the Hungarian Ministry of Economy and Transport, Budapest, 10/02/2004a.*

*Interview by Author with Representative of the Hungarian Pharmaceutical Manufacturers Association, Budapest, 06/02/2004.*

*Interview by Author with Representative of the Iron and Steel Institute, Budapest, 04/02/2004a.*

*Interview by Author with Representative of the Ministry of Employment and Labour Affairs of Hungary, Budapest, 03/02/2004.*

*Interview by Author with Representative of the Ministry of Finance of Hungary, Budapest, 06/02/2004 and 18/02/2004.*

*Interview by Author with Representative of the Ministry of Finance of Poland, Warsaw, 30/04/2004.*

*Interview by Author with Representative of the Ministry of Finance of the Czech Republic, Prague, 24/03/2004b.*

*Interview by Author with Representative of the Ministry of Foreign Affairs of Hungary, Budapest, 04/02/2004b.*

*Interview by Author with Representative of the Ministry of Foreign Affairs of Poland, Warsaw, 27/04/2004.*

*Interview by Author with Representative of the Ministry of Foreign Affairs of the Czech Republic, Prague, 04/05/2004b.*

*Interview by Author with Representative of the Ministry of Foreign Affairs of the Slovak Republic Bratislava, 03/03/2004.*

*Interview by Author with Representative of the Ministry of Transport of the Czech Republic, Prague, 22/03/2004c.*

*Interview by Author with Representative of the Negotiation Team of the Slovak Republic, Vienna, 04/05/2004c.*

*Interview by Author with Representative of the Office for Competition and Consumer Protection of Poland, Warsaw, 16/04/2004.*

*Interview by Author with Representative of the Office of the Committee for European Integration (UKIE), Warsaw, 21/04/2004.*

*Interview by Author with Representative of the Office of the Government of the Czech Republic, Prague, 04/05/2004d.*

*Interview by Author with Representative of the Polish Confederation of Private Employers, Warsaw, 15/04/2005.*

*Interview by Author with Representative of the Slovak Anti-Monopoly Office, Bratislava, 24/02/2004.*

*Interview by Author with Representative of the Slovak International Transport Trade Union, Bratislava, 26/02/2003.*

*Interview by Author with Representative of the Slovak Office of the Government, Bratislava, 12/03/2004a.*

*Interview by Author with Representative of the Slovak State Institute for Drug Control, Bratislava, 12/03/2004b.*

*Interview by Author with Representative of the Steel Trade Union of Hungary, Budapest, 10/02/2004b.*

*Interview by Author with Representative of the World Bank Slovakia, Bratislava, 02/03/2004b.*

*Interview by Author with the Chief Negotiator of Hungary, Budapest, 09/02/2004.*

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Annex 1: TAs per Chapter of the Acquis and Country

Country	Cy	Cz	Es	Hu	Lv	Lt	Mt	Pl	Sk	Sl	Total/chapter
Chapter 1: free movement of goods	1	0	1	0	0	1	2	2	0	1	8
Chapter 2: free movement of persons	0	1	1	1	1	1	0	1	1	1	8
Chapter 3: free movement of Services	1	0	2	1	2	2	0	3	1	3	15
Chapter 4: free movement of Capital	1	2	1	2	1	1	1	2	1	0	12
Chapter 5: Company Law	0	0	0	0	0	0	0	0	0	0	0
Chapter 6: Competition Policy	1	1	0	4	0	0	5	4	2	0	17
Chapter 7: Agriculture	7	5	5	7	9	9	10	10	4	7	73
Chapter 8: Fisheries	0	0	0	0	0	0	0	0	0	0	0
Chapter 9: Transport Policy	1	1	1	4	3	4	3	3	1	0	21
Chapter 10: Taxation	8	6	5	7	4	3	6	8	7	5	59
Chapter 11: Economic and Monetary Union	0	0	0	0	0	0	0	0	0	0	0
Chapter 12: Statistics	0	0	0	0	0	0	0	0	0	0	0
Chapter 13: Employment and social Policies	0	0	0	0	3	0	2	1	0	3	9
Chapter 14: Energy	1	2	2	0	1	1	1	1	1	1	11
Chapter 15: Industrial Policy	0	0	0	0	0	0	0	0	0	0	0
Chapter 16: Small & Medium-sized enterprises	0	0	0	0	0	0	0	0	0	0	0
Chapter 17: Science and Research	0	0	0	0	0	0	0	0	0	0	0
Chapter 18: Education and Training	0	0	0	0	0	0	0	0	0	0	0
Chapter 19: Telecom and IT	0	0	0	0	0	0	0	1	0	0	1
Chapter 20: Cultural and Audiovisual Policy	0	0	0	0	0	0	0	0	0	0	0
Chapter 21: Regional Policy	0	0	0	0	0	0	0	0	0	0	0
Chapter 22: Environment	4	3	6	4	8	4	7	10	7	3	56
Chapter 23: Consumer Protections	0	0	0	0	0	0	0	0	0	0	0
Chapter 24: Justice and Home Affairs	0	0	0	0	0	0	0	0	0	0	0
Chapter 25: Customs Union	0	0	0	1	0	0	1	0	0	0	2
Chapter 26: External Relations	0	0	0	0	0	0	0	0	0	0	0
Chapter 27: CSFP	0	0	0	0	0	0	0	0	0	0	0
Chapter 28: Financial Control	0	0	0	0	0	0	0	0	0	0	0
Chapter 29: Finance and budgetary Provisions	0	0	0	0	0	0	0	0	0	0	0
Chapter 30: Institutions	2	2	2	2	2	2	2	2	2	2	20
Chapter 31: Other	1	1	1	1	1	1	1	1	1	1	10
<b>Total/country</b>	<b>28</b>	<b>24</b>	<b>27</b>	<b>34</b>	<b>35</b>	<b>29</b>	<b>41</b>	<b>49</b>	<b>28</b>	<b>27</b>	<b>322</b>
<b>Total/country excluding chapters 29, 30 and 31</b>	<b>25</b>	<b>21</b>	<b>24</b>	<b>31</b>	<b>32</b>	<b>26</b>	<b>38</b>	<b>46</b>	<b>25</b>	<b>24</b>	<b>292</b>

Source: European Commission, 31 December 2002



## **Annex 2: Interviews**

This study is in part based upon 82 positional and structured interviews of between 45 minutes and two hours according to a sectoral (Form A) and a state (Form B) based template. Almost 80 per cent of all interviews were recorded between 10 January 2004 and 31 May 2004 in Hungary, Slovakia, the Czech Republic and Poland respectively (see table below). Between one and four interviews were carried out per day.

### **Sectors (see Form A)**

For the sectoral template the interviews were solely requested when interviewees were representative for the sector and when they directly had participated in the EU integration process between 1998 and 2002. Otherwise the interview was discarded. Interviews were carried out on the level of the firm, sectoral employers association and sectoral trade unions as well as peak associations.

On a state level the interviewees were the direct counterparts of their sectoral colleagues. For instance, the head of the pharmaceutical association in country x usually had a number of interlocutors in the Ministry of Finance and Institute for Drug Control. For the basic iron and steel sector the corresponding state administrations were the Ministry of Economy, Industry, Finance and the Office for Competition. The Ministry of Transport was the interlocutor for the road transport sector.

Interviews that follow this methodological and technical pattern provided at least two observations per sector, i.e. one for the sector and one in the corresponding administration. In our case the sectoral interview comprised two observations, i.e. employers and labour, resulting in at least three observations per sector. On a cross country level the completion of the interviews resulted in saturation from the third country onwards (Czech Republic).

Positional and structural interviews following this type of analysis exclude the reasonable possibility of cheap talk and prevent the inflation of credible speech. It also resulted in the exclusion of interviews whereby one interview failed the confirmation of his counterpart. When the sectoral representative made a claim it required a counter response in the state administration.

### **States and Strategies (see Form B)**

I complemented the sectoral level with interviews on a horizontal or state level. The interviewees were either members of the negotiation team, those in charge for EU accession in the ministries (Ministry of Foreign Affairs, Finance, Economy and Transport) depending on the country's singularity, and/or members of the government. They represented a third observation point.

The transcripts of the interviews are available upon request from the author. Upon request interviewees remain anonymous throughout this study.

## **Form A: Firm/Sectoral Level**

### **1. Interest and Preferences of firms/sectors on EU enlargement**

- Firm/Sectoral details
  1. Average level of education of employees in the sector (nr. years)?
  2. Are skills of employees specific the job/employment when hired (yes/no)?
    - Do employees receive additional education in the sector/firm (yes/no)?
    - How many years?
    - Level of R&D expenditure in the sector/firm (US\$/Euro)?
    - Has the expenditure risen or declined over time (yes/no)?
- Trade
  - Is/was the sector export or import oriented (yes/no)?
  - Has the sector/firms gained/lost income in the process of EU enlargement (yes/no)?
  - Why?

### **2. Likelihood of Political Mobilisation**

- Nr. of companies operating in the sector representing 80 % or more of market share (nr.)?
- Name of companies?
- Has the number of companies operating in the sector remained the same since 1989(yes/no)?
- Do companies regularly enter/exit the sector (yes/no; nr.)?
- Are all firms operating in the sector member of the association/federation (yes/no)?
- Which ones not?
- Membership of the association in terms of market share (%)?
- Are other associations/organisations operation in the sector (yes/no)?
  - If so, what is their market share (%)?
- Is there a strong incentive for a company to join the association/organisation (yes/no)?
- If so, why?
- What is the budget of the association/organisation (in US\$ or Euro)?
- What are other organisational resources of the association?
- Is the association a member of an international/European federation (yes/no)?
- If so, which one(s)?
- What are the most important benefits of joining an international association /federation?
- Did such relationship have any impact on the outcome of the EU enlargement negotiations for the sector (yes/no)?
- Why?

### **3. Likelihood of Success**

- Have there been long established contacts/channels with government /ministries in the sector (yes/no)?
- If so, which ones?
- Is the association/organisation consulted for information and expertise in the sector by the government/ministries (yes/no)?
- How many times per set of legislation?
- Does consultation by the ministries/government happen at a firm level as well (yes/no)?

- Could the government implement legislation in the sector without the help or consultation of the association/organisation (yes/no)?
- Could the government implement EU related legislation (*acquis communautaire*) in the context of EU enlargement (yes/no)?
- Has the association been consulted on EU enlargement (yes/no)?
- If so, how many times?
- When?
- How many times has the association been involved in EU enlargement negotiations and which government/policy levels?
  - Number of times
  - Number of Levels
- What is the ownership structure of the firm/sector for the companies representing more than 80 % of market share?
- Does the ownership structure of the firms in the sector influence access to policymakers?
  - Local
  - Regional
  - National
  - European
- Did the EU enlargement process in the sector receive much attention in the press (yes/no; comment)?
- Was EU enlargement in the sector a politicised issue (yes/no)?
- If so, why?
- Did politicisation/press attention have an influence on the position of the government in the sector (yes/no)?
- If so, why?

#### 4. Policy Process

- Did the firm/sector/peak organisation contact policy makers to highlight a preference on EU enlargement (yes/no)?
- If so, why?
- Did the government/ministries contact the association/federation to ask its view/preference on EU enlargement issues related to the sector (yes/no; comment)?
- If so, how many times?
- Which levels?
  - Local
  - Regional
  - National
  - European
    - i. European Commission
    - ii. EU Member States
    - iii. European Council
  - European Federations/Associations?
    - i. Did it have an effect?
    - ii. Which One?
  - Foreign Embassies/chambers of commerce
  - Other
- Did you have easy access to policy makers?
- Has it been costly in time and resources?

- Do you recommend talking to other people?

## **Form B/Model B: State Preferences**

### **1. Before the negotiations: State/Sector/Firm**

- A. How were the position papers composed?
- B. What did the impact studies argue?
- C. How many levels of government were involved generally before a final position was reached?
  - 1   2   3   4   5   6   7
  - Which were they?; and what were the levels of consultation with the respective firms, sectors, interest representations affected by EU legislation?
- D. Did the preparations and the EU accession negotiations influence the form of the government/administrative structure in dealing with the EU (yes/no)?
- E. If so, how?
- F. Did requests for TAs originate at the firm level and/or state level?
- G. How did you determine the substance and length of TPRs?
- H. Did guidelines exist of what could pass and what not?
- I. Where did these guidelines originate (national, EU)?
- J. Was there consultation with the EU (EC/Council/other FMS and EU MS, etc.) ahead of the presentations of the position papers?
- K. If so, on what?
- L. Did the position papers of other FMS have any influence on the position papers (spill over effects)?
- M. Did the companies/sectors/interest organisations contacted the EC/EU MS directly or did they work always through domestic channels?
- N. Did it make a difference whether a firm/sector was domestically or foreign owned for the government's position on a particular issue?
- O. Did the fact that EU MS subsidiaries were operating in the country have any influence on the position of the firm/sector in the country?
- P. On the implementation of the acquis?

### **2. Strategy in the position papers?**

- A. In balancing preferences in the position papers, did other pref. override the objective of joining the EU?
- B. What prevailed?
- C. What was the strategy of the government in formulating the position papers?
  1. Were requests always real?
  2. Were requests strategic?
  3. What was the strategy?
- D. Where their instances when request were put aside because of other interests?
- E. What was the government's preference function in the position papers?
  1. Joining the EU?
  2. Satisfying domestic interest groups?
  3. Satisfying foreign interest in the country?
  4. Satisfying its electorate and staying in power?
- F. Were negotiators saying different things on a national and international level?

### **3. Position of the EC**



- A. What was the initial position of the EC on the position papers of the country on TAs requests?
  - B. Was the position of the EC different from those of the EU member states/Council in the negotiations?
  - C. Did the EC's position change over time?
  - D. Where certain issues unacceptable relative to others?
- 4. Position of the EU Member States**
- A. Where certain member states expressing clear opinions on certain issues? On the sectors; firms?
  - B. Did MS in the country take different positions (embassies) than they would in Brussels; or diverging from the EU's common position?
  - C. Was the EU always negotiating with the country or in fact negotiating with itself at times?
- 5. Position of the European Council, Coreper?**
- A. How was Coreper/Council formulating the common EU negotiation position?
  - B. Did its negotiation position change over time?
  - C. Where certain EU MS positions regarded as a lowest common denominator followed by other MS on certain issues?
  - D. Which issues?
- 6. Negotiations – Strategic Calculus**
- A. Did a government strategy on the accession negotiations exist (yes,no)?
  - B. What was the government's strategy in the negotiations?
  - C. Did the strategy change over time (change of government)?
  - D. Was the government adamant about its demands for TAs and/or was it ready for compromise/concessions?
  - E. Where TAs being dropped as part of the 'race' or strategy
  - F. If so, which ones?
  - G. Did other FMS's position have any effect on the country's position?
  - H. Was there a time effect (spill over)?
  - I. Was it a dis/advantage of being the first/middle/last to negotiate a chapter and close it? (yes/no)?
  - J. If so, why?
- 7. Are you aware of deals being struck between different issue areas (package deals)?**
- A. Was the government's overall goal reached at the outcome of the negotiations?
  - B. In Copenhagen Dec 2002?
  - C. Do you recommend talking to other people?

### Positional Interviews V-4 (10 January 2004-31 May 2004)

Level/Country	Hungary	Slovakia	Czech Republic	Poland
Chief Negotiator	X	X		X
Team of the Chief Negotiator	X	X	X	X
	X	X	X	X
		X	X	X
			X	X
			X	X
				X
Government/Office of the Government	X	X	X	
			X	
Ministry of Foreign Affairs	X	X	X	X
		X		
Ministry of Finance	X	X	X	X
Ministry of Economy		X	X	X
Ministry Transport	X	X	X	
National Bank		X	X	X
		X		
Competition Office	X	X		X
		X		
Office of Drug Control		X		
Pharmaceutical Association	X	X	X	X
	X		X	X
Pharmaceutical TU	X	X		
Steel Association	X	X	X	
		X	X	
Steel TU	X	X	X	
Transport Association	X	X	X	X
Transport TU		X	X	
Confederation TU		X	X	
		X		
Confederation Employers		X	X	X
			X	
World Bank officer		X		
European Commission	X	X	X	
<b>Total</b>	<b>15</b>	<b>28</b>	<b>23</b>	<b>16</b>

#### Legend

x =interview  
 grey =absent