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## The Promises and Perils of European Union Membership

by Wess Mitchell

On May 1, 2004, the European Union absorbed 10 new members, comprising 250,000 square miles, 80 million citizens and \$444 billion in gross domestic product (GDP) — the largest expansion in territory, population and wealth ever achieved by a government in peacetime.

Eastern enlargement was supposed to be a winning proposition for everyone involved: Western Europeans would gain access to the East's abundant markets and cheap labor; Eastern Europeans would gain access to Western jobs, investment and EU subsidies. The result would be two prosperous and increasingly equal halves of a formerly divided continent. So ran the official line, and anyone from the accession countries who questioned this orthodoxy — such as Czech President Vaclav Klaus or Hungarian Prime Minister Viktor Orban — was dismissed as a visionless “euroskeptic.”

But now, less than a year into the venture, Eastern Europeans find themselves in an increasingly autarkic regional cartel where second-class citizenship, economic centralization and political bullying — all stark reminders of the communist system jettisoned in 1989 — are once again the order of the day.

**Second Class Citizenship.** The EU Commission had little difficulty convincing Eastern Europeans they would be richer and freer inside the union. In the run-up to accession, EU officials told Eastern politicians that there would be three clear-cut benefits from membership:

■ **Labor mobility:** Eastern Europe's populous workforce would no longer be restricted from migrating westward in search of jobs.

■ **Agricultural aid:** Like Spanish and Greek farmers before them, the newcomers would be eligible for the EU's extensive farm subsidies.

■ **Structural funds:** The East's poorest regions would receive handsome allotments from the EU's massive regional development program.

The prospect of lower unemployment and rural development spurred Eastern European governments to make the sacrifices necessary to comply with the 97,000-page collection of rules and regulations required for membership. However, when it came time for the EU to keep its part of the bargain, Western leaders made an abrupt about-face:

■ **Labor immobility:** Fearing a rush on their lavish entitlement programs, most Western governments placed last-minute restrictions on the entry of Eastern workers.

■ **Limited farm funds:** Pressured by French farmers, the EU cut subsidies to the newcomers by 75 percent. At the current rate, Polish farms must wait a decade to receive the same support French farmers get today.

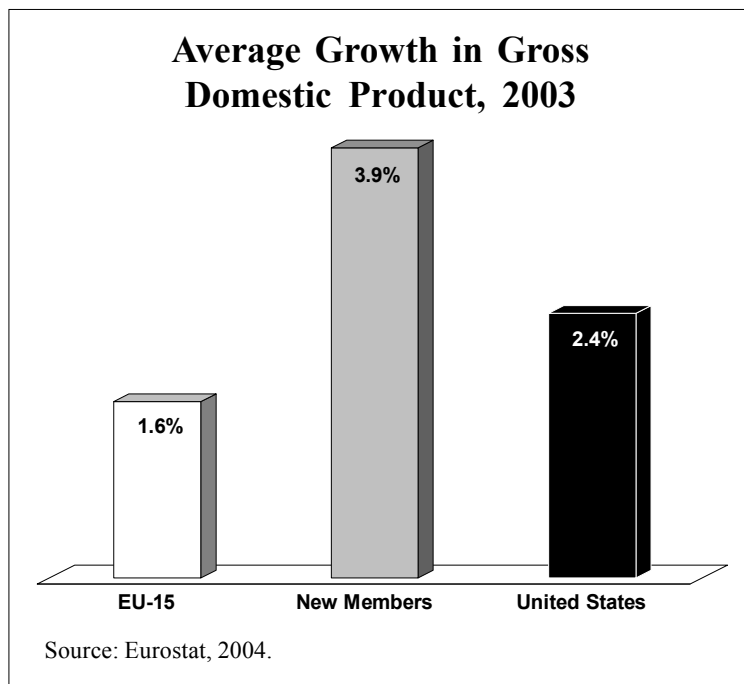
■ **Limited regional aid:** Although the Commission promised to cover most of the \$120 billion spent on accession, it has doled out a paltry \$1.8 billion, and

plans to give Eastern countries far less aid than Greece and Spain received after the last expansion.

**Economic Centralization and Decay.** EU membership has so far been a disappointment to Eastern Europeans, with high upfront costs and slow-to-materialize benefits. Nor can the citizens of Warsaw and Prague console themselves with the knowledge that they are joining, in the EU Commission's words, the world's “most dynamic trade bloc.”

■ Since the early 1990s, European unemployment has averaged 11 percent, compared to 4 percent in the United States.

■ According to the Organization for Economic Cooperation and Development, EU countries have not



created a single, net private sector job since 1970, compared to 50 million jobs added in the United States.

The roots of Europe's malaise can be traced to protectionist trade practices and heavy taxes that fuel government growth and impair private-sector job creation. By comparison, the new members — who spent the past 15 years dismantling socialism — have pioneered innovative pro-growth policies:

- In January 2004, Poland cut its corporate tax rate from 27 to 19 percent, followed by Hungary (down to 16 percent) and Slovakia (19 percent).
- The average corporate tax rate in Eastern Europe is 21 percent, compared to 33 percent in Western Europe as a whole and 38 percent in Germany.
- Three of the new members have adopted flat income tax rates — Estonia (26 percent), Latvia (25 percent) and Slovakia (19 percent) — and Poland and the Czech Republic plan to do so.

Thanks to their willingness to liberalize, the Eastern countries are outperforming the original EU-15 at every turn:

- The average Eastern European growth rate in 2003 was 3.9 percent of GDP — more than double the 1.6 percent average in Western Europe and significantly higher than the 2.4 percent growth in the United States [see the figure].
- The largest Eastern member (Poland) has enjoyed higher growth rates than the largest Western member (Germany) for each of the past nine years, averaging 3.8 percent annually.
- Hungary's growth has averaged 5 percent, with unemployment at 3 percent and wages up 17 percent in 2003.
- And the star performers among the accession countries — the flat-taxers — have enjoyed average GDP growth of 6.1 percent.

**Political Bullying.** In an effort to prevent the Easterners from out-competing Western firms, the EU is pressuring them to abandon pro-growth policies in favor of Western-style “third way” economic planning.

- Prior to accession, the EU forced the Easterners to give up the special incentive programs they had used to attract foreign investment.
- Following accession, Germany threatened to withhold aid unless new members raise their corporate tax rates to match Western levels.

- In the aftermath of the Iraq crisis, in which the Eastern countries supported Washington, EU leaders warned them that they will have to side with Brussels on future disputes with the United States — both in matters of trade and security.

**Looking Forward.** At present, the Eastern Europeans are caught in a classic Catch-22. On one hand, they must forgo EU subsidies, while on the other, they are told to abandon the pro-growth practices that would enable them to survive without the subsidies. As long as they want to receive future aid, Easterners will have to accept this arrangement and — as one author put it — “march to the beat of the German drummer.” However, doing so will only drag them into the EU's steadily deepening economic pit and weaken their ties with the United States, without conferring any offsetting financial or political benefits. In fact, a recent report from the pro-EU French think-tank IFRI suggests that if the Easterners play by the EU's rules, Europe is headed for economic atrophy. The study predicts that if current trends continue, the EU will become a second-rank economic power by 2050 and begin an “inexorable movement onto history's exit ramp.”

**Conclusion.** This is clearly not the future Eastern Europeans envisioned during their long, difficult push for EU membership. Rather than sacrificing the hard-won gains of the past 15 years and submitting to French and German dictates, a growing number of Eastern leaders believe their countries should retain sovereignty over economic policy — even if it means restricted access to aid. In March, representatives from the accession countries signed the “Bratislava Declaration,” in which they reaffirmed their commitment to free market policies.

Faced with a choice between economic growth and EU subsidies, Eastern Europeans have — at least for the moment — chosen the former. If they are able to withstand Western pressure, their success may provide a model for the rest of the EU and help breathe new life into an ailing continent. Herein lies the ultimate irony: countries where minimalist government and free enterprise have existed for so short a time may be instrumental in returning those concepts to countries where they originated but have lately fallen out of fashion.

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