Perspectives for Economic Cooperation
Between Russia and the
Countries of Central and Eastern Europe
in the Light of the Enlargement of the European Union

by
ANDRÁS KÖVES
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Introduction and Summary

This paper argues that Eastern enlargement of the European Union, which is to be accomplished \textit{de jure} as of May 1, 2004, will \textit{not} bring about any further significant changes in trade and economic cooperation between Russia and the former socialist countries of Central and Eastern Europe (CEE).\footnote{For the purposes of this paper, the term „Central and Eastern Europe” (CEE) covers mostly the former CMEA members (or their successor states) now (or, in the course of some more years) about to accede to EU – from Poland in the North to Bulgaria in the South, as well as Slovenia. CEE-6 are Central and Eastern European trading partners of Hungary. In some tables „CEE” include Yugoslavia’s other successor states and Albania as well, but not the Baltic states. As a matter of course, a large part of the narrative is based on Hungarian data and experiences.} Most of the really important changes related to the European integration and re-orientation have already occurred in the period following 1989, and there is little left for the future. On the other hand, economic and political stabilization in the CEEs – of which full membership in the EU should be an important phase – may contribute to better conditions (than in the turbulent transition period) for the development of relations with Russia (and other CIS countries outside the scope of the paper) as well.

\textit{De facto} integration of CEEs in (Western) Europe started as early as 1989-1990, concurrently to political change and economic transformation. Of all fields of integration, trade was the first to start. Trade re-orientation was an organic part of transformation (as a consequence of both the collapse of the CMEA and the rapid rise of trade with the West), and was an accomplished fact in most of the CEEs as soon as early 90s. By the end of the millennium, the share of the 15 present member countries of the European Union in total trade of most of the CEEs reached the point of culmination (a share between two-thirds and three-quarters in exports; somewhat less in imports). This is a unique feature of Eastern enlargement (as compared to previous cases of enlargement): trade-creating and trade-diverting effects of joining the European Union had emerged in their entirety \textit{before} full membership of the newcomers was attained. It would make no sense (what is more, it would be even counter-productive) to aim at further increase of those shares.\footnote{Actually, the EU’s exports shares decreased somewhat in some CEEs in 2000-2002.}

Parallel to the growing volumes of trade, and in accordance with the „Europe Agreements” concluded in early 90s, trading systems and trade policies of now acceding countries have gradually approached those of the Union. Therefore, coming change from national trading systems, regulations and policies of the CEEs, and also from nationally concluded trade agreements with third countries, to the acceptance of the common commercial policy of the Union will result in minor changes only, as far as conditions of trade, including those with third (non-member) countries are concerned. Also, according to calculations, in case of Hungary for example, the change from national regime of Most-Favoured-Nation treatment of Russia to the GFS treatment extended to Russia by the Union will not imply any significant alteration of conditions of bilateral commerce.

From another perspective, the only beneficiaries of the fundamental changes of geographical (regional) composition of CEE’s trade following the political transformations of more than a decade ago were developed countries (formerly called „developed capitalist” ones), foremost the countries of Western Europe. The rest were mostly losers. In physical terms, overall trade
among the former socialist countries of Europe, taken together, does not seem to have reached the level of 1989 at the onset of this century.3

It is sometimes left unsaid that trade among CEEs has lost some significance (trade shares of CEEs declined) in the past decade. While decline of relations between Russia (and other CIS countries) on one hand, and the CEEs on the other, is the most dramatic development in foreign economic relations of post-socialist countries, the lack of dynamism and continuing relegation to the background of intra-CEE trade is a most surprising one. As a matter of fact, mutual trade among CEEs has been of relatively limited significance for most of the last century. Before the war, this situation could be explained by unneighbourly relations among them, protectionism and strivings for mutual isolation. In the socialist period, the reason was simple as well: CMEA cooperation had „radial” character. All the CEEs had robust relations with the Soviet Union (not only the political and military center of the grouping but a vast selling market for CEEs’ manufacturing goods and – in some cases – food, and a source of imports of needed energy and raw materials), while trade among the smaller member-countries was neglected. In post-socialist times, despite discontinuation of CMEA, and the establishment of the CEEs’ own – however, temporary – „small” integration within the framework of the CEFTA, integration in (Western) Europe in each of them had preference over integration with the other CEEs. From a somewhat different perspective: while integration of some or most CEEs in Europe and the global economy progressed quite well, European integration of the CEE region as a region was less dynamic.

As a consequence of what has happened after 1989 in and around post-socialist countries, the structure and character of their economic relations with each other changed immensely.

Firstly, as a consequence of reorientation to the West of trade of all former CMEA member countries (and their successors) following political changes, as well as the either attained or planned membership of the majority of former European CMEA members in the NATO and the European Union, the former CMEA lost all the characteristics of being an economic or trade bloc or group. As shown by trade statistics, the center of gravitation for economies of all (or, at least, of the great majority of) sometime socialist countries lies outside the former bloc – in Western Europe.4

Secondly, contrary to the CMEA period, and notwithstanding the above-mentioned and other factors, which act as a constraint to development of the economic relations among Central European countries, intra-CEE trade of the CEE countries is now larger than trade with Russia (or even trade with the whole CIS). This is especially the case with exports of CEEs.

Thirdly, trade between CEEs and Russia, while generally losing much of its former significance, has become excessively asymmetrical as far as exports and imports are concerned. Russian exports of oil, gas, and some other raw materials to CEE have, at a lower level in any case, survived into the twenty-first century, while „traditional” (ie. developed specifically for exports to the Soviet Union) CEE exports of manufactures and food – have not.

There is a mutual dependence on Russian exports of energy to CEE. For the CEEs, Russia is a cheap (relative to alternative sources), reliable, geographically near-by supplier of most of

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3 In the case of Hungary, despite a long process of trade reconstruction that had started in early 90s, exports to transition countries (CIS, Baltics and CEEs) in 2001 were below the level of 1989 in volume terms, imports from those countries – only 2 percent above the level of the year of political transformation. During the same period (1989 –2001) exports to developed countries increased more than four times, imports from those countries – 3.7 times (see later).

4 Except for some CIS countries
their needed imports of energy, with established and well-functioning transport infrastructure. For Russia, CEE remains the market outlet for a large part of its exports of oil and gas, and one of the important transit routes for its actual and potential energy exports to Western and Southern Europe, as well as Asia Minor. CEE is also an area for promising foreign investments of leading Russian oil and gas companies.

Just the opposite seems to be the case with CEE exports to Russia: in macroeconomic sense, present trade data are witness of mutual „independence”, following the not-so-long process of smashing and deconstruction of large-scale business relations of the CMEA period. The Russian share in CEE exports is about 2 percent\(^5\), while about 6 percent of total Russian imports come from CEE (the six former CMEA members). In such a situation it is simply irrelevant to raise the question of eventual further negative implications of CEEs’ full membership in the European Union. This is not to ignore the highly protectionist and divisive policies of the Union, aimed, first of all, at imposing more administrative controls and restrictions on crossing its borders by nationals (inhabitants) of non-member states, at limiting cross-border (shuttle) trading and employment (legal and illegal). The injurious negative human (regional) implications of those policies, the eventual difficulties of business as usual notwithstanding, the macro-economic impact of the measures for Russia-CEE trade seems to be limited. By all means, they should not conceal the deeper, basic causes of the decay in relations.

However, following Eastern enlargement, uncertainties facing Russian exports to CEEs, and, especially energy, may increase, if the Union’s endeavours at securing energy supplies are not made consistent with the interests of Russia in establishing secure and long-term legal and physical infrastructure for exporting energy to Europe. The question relates very much to enlargement. The issue that may touch upon Russia-CEE relations is the share of the gas (and perhaps other energy) supplies the EU is prepared to allow from any one source. Officially, there are no restrictions on this amount, but it is recommended that not more than 30 percent of gas imports should derive from one source, given the dependency which the future EU members have for Russian gas (Grigoriev-Chaplygina, 2003).\(^6\) It is well-known that the present share of Russian gas in CEE imports is much higher. The eventual enforcement of the restriction (which, under present circumstances, does not seem to correspond to interests of the Union’s security of supply) would seriously impair Russian exports to CEEs, energy situation of the latter, as well as the realisation of the EU-Russia energy partnership.

Whatever should come of the energy problem, or of other possible dangers and uncertainties of Russia-CEE trade, the most important thing is to have a clear conception of the factors behind the present situation in trade. The problems are different in character. A lot of important problems of Russia-CEE trade have nothing to do with the EU (they have to do with the Russian economy as a whole), and full membership of CEEs will not change them even an iota. Other current problems (related to the competitive positions of CEE’s firms in the Russian markets) may even be easier to deal with, when Central Europeans will be fully within the EU. A third category of problems (determining geographical and commodity pattern of CEE’s trade) relates to the globalization of economies of the region, or, some characteristics of the present global division of labour.

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\(^5\) With the exception of Poland, where 2.9 percent of exports in 2001, and 3.2 percent in 2002 went to Russia. The corresponding shares in the Czech exports were 1.5 percent and 1.4 percent, in Slovakia – 1.0 percent in both years, and in Hungary – 1.5, respectively 1.3 percent.

\(^6\) For a broad view on Russian-CEE relations, in the context of Eastern enlargement, see Strany…(2002), especially Chapter 3, pp. 42-65.
However onerous the difficulties caused by eventual restrictions on energy trade may be, the real problem is structural weakness of Russian exports (and of Russian industry), the lack of internationally competitive manufacturing industry, and the consequent large-scale dependence of economic growth on development of international oil prices. Also, because of inherited from Soviet times weaknesses and the protracted crisis of the 1990s, the size of Russian import market is much smaller than usually presumed. In 2000-2002, Russia imported less goods from the world than Poland. (We will return to those issues later.)

Some CEEs were losing positions on the Russian markets not only after 1989-1990, but following the financial crisis of 1998, to the EU and other countries. In some cases, political difficulties might have played a role. Generally speaking however, CEE exporters are squeezed out of the market because of lack of competitiveness as far as, for example, financing is concerned. In this respect, EU exporters of agricultural products are in far better position than CEEs. Countries with a large share of food in exports to Russia (Hungary in 1996-1997) have suffered a significant decline. Full membership may even help to improve competitive positions in this respect.

Finally, CEE trade with the world is mostly dominated by multinationals. Multinational companies established in CEEs are part of complex global production, assembly and marketing networks. They export and import mostly through the channels of intra-company transactions (or: their intra-company transactions via national borders are called exports and imports); to the degree that those channels are keeping away from Russia because of the relatively slow joining of this country into multinational division of labour, neither their products do get (at least, directly from CEEs) to Russia.

Re-orientation in Hungary and Central and Eastern Europe

Trade reorientation in Hungary, as in many other countries, was very swift. At all means, it had been carried out much earlier than the economic crisis called by János Kornai (1994) transformational recession reached its nadir. In 1991, the year of the gravest fall of the Hungarian economy, the share of market (formerly: non-socialist) economies in total trade already reached three-quarters, that of the developed capitalist countries (according to the previous terminology) – two-thirds.

In this paper, we present some data about trade reorientation in Hungary according to volume changes. In this way, we get rid of distortions caused by significant price changes, including those related to discontinuation of transferable rouble. As Figure 1 (below) shows, in early 1990s total Hungarian exports had decreased sensibly (however not dramatically), and it was in 1995 only that the level of 1989 was restored. The most important factor behind the decline of total trade was the collapse of exports to former socialist countries. The latter touched bottom in 1993, and have not recovered since. According to data of 2002, exports to transition (formerly „socialist”) countries are still 6 percentage points below those of 1989 and 11 points below the level of 1985. Similar were the changes in exports to developing countries, which overtook the 1989 level in 2000-2002 only (as a consequence of a change in statistical definitions: namely, China was put into the category of developing countries), but remained below the level of 1985. Exports to developed countries, in volume terms, grew largely unbroken (the only break happened in 1993, at the time when the country’s GDP was at its nadir). It is due to the rapid growth of exports to developed countries that total exports declined relatively (relative to the great shocks of transition) less and briefly. In 1995, total exports surpassed the level of 1989, while exports to former socialist countries reached the half of the earlier volume, but exports to developed world doubled: that circumstance was
both obvious sign and consequence of a fundamental reorientation that had taken place in the meantime.

Figure 1

![Hungarian Exports to Main Partner Regions](image1)

Note: HSO is for Hungarian Central Statistical Office

Figure 2 indicates that oscillations of imports were smaller than those of exports. Total imports increased as early as 1993. True, that was due to a non-recurring event: soaring imports of military equipment (aircraft) from Russia in payment for the old Soviet debt. Imports from transition countries – unsimilar to exports – reached the level of 1985 by the end of the millennium. Starting 1992, imports from developed countries have grown continuously (volumes increased almost fourfold during a period of somewhat more than a decade, and levelled out in early 2000s). Imports from developing countries increased even more rapidly, than imports from developed countries, due to recent dynamics of imports from China, in the first place.

Figure 2

![Hungarian Imports from Main Partner Regions](image2)
As early as 1991 the (then) European Community became the biggest trading partner of most CEEs. The Community’s share of both exports and imports in Poland and Hungary exceeded 50 percent. In 1992, foreign trade of Czechoslovakia featured the same percentage shares. In 1993, a majority of Hungarian, Polish, the Czech and Slovenian trade was with the EC. In Slovakia, the smaller successor state of disunited Czechoslovakia, external economic relations with the Czech Republic were dominant in the first years of independence. It was only closer to the end of the decade that EU became the overwhelming partner of the country, for a lasting time on exports side, while in imports EU’s share decreased once again to below 50 percent in 2000-2001. Among the remaining countries, the percentage share of trade with EU grew more slowly in Romania, however, the share reached the CEE „norm” in recent years. In Bulgaria, the trade role of the EU remains relatively low; this is due to geographical situation of the country, respectively, the country’s significant trade flows to/from south and south-east. The changing role of EU15 in exports of some CEE countries is shown in Figure 3 (below).

In sum, by the end of the 1990s trade integration with the Union, in the quantitative sense, ie. as regards percentage shares of the 15 present EU countries in total foreign trade of CEEs, reached the zenith. Further increase of shares would be aimless and senseless, perhaps even counter-productive. (10 countries joining the EU in 2004 will mean increase of intra-EU trade – or of trade with the EU – as a percentage share of CEEs’ total trade.) The share of the Union – about 70 percent in exports, and about 60 percent in the majority of cases in imports – is more than satisfactory. (The lower percentages in imports are reflection of the fact that Russia’s share in imports of CEEs is higher than in exports.) It is remarkable that Hungary’s dependence on exports to EU is the highest among the comparable countries.

Figure 3

According to some calculations (Piazolo, 2001, pp. 23-24), the present share of trade with EU15 in total trade of CEE, on average, largely corresponds to the situation of the late 1920s. There is „a surprising coincidence in the geographical composition” with that of those years. The author from the Kiel Institute explains that the trading pattern „mirrored cultural affinity with Western European countries”, and „was subject to many of the same determinants as today: differences in natural resource and factor endowments, production complementarities, cultural and language links, and geographical proximity”. His approach suggests that
following the political transformation in 1989-1990 some „normal” situation, historical order was restored – in relation to which the period following the second world war should be considered a long anomalous deviation.

However, this comparison is mistaken. It is questionable, for example, whether there exists something like „normal order” in world trade. Further: if the answer is yes, why the inter-war period should be regarded as such, and not the period before the first world war. The policies of some CEEs between the two wars were characterized by a lot of features (strivings for self-sufficiency, isolation from one another, authoritarian government, domestic policies that foreshadowed fascism, etc.), which can not be regarded normal.

Other conditions have changed, too. Between the 1970s and the millennium the weight of Western Europe (EU15) in world trade has significantly diminished (diminution continued also in the decade after political changes in former socialist countries). At the same time, economic significance of some other regions (South-East Asia, China) increased. It would be „normal” on the part of CEEs to more intensively trade with the latter. There are few signs for such a change, at least as far as direct inter-regional trade is concerned. True, Western Europe, as a trading partner, plays a somewhat different role in CEEs in today’s „globalized” international economy than before. Namely, it is not only a final sales market and the original source of supply, but an intermediate stop for exports to other markets and imports from other sources.

Anyway, the share of trade with EU15 in total trade of acceding countries is higher than the share of intra-EU trade in total trade of many present members (Figure 4). In Hungarian exports for example, the EU’s percentage share is higher than the share of intra-trade in all EU countries save the Benelux and Portugal (In 2002, the Netherlands, Luxemburg, and Portugal only). Bulgaria is the only CEE country with a trade share of EU clearly under 60 percent, while there are six EU countries with an intra-trade share below 60 percent in 2002. In total trade of EU15, intra-EU exports amount to 61 percent of the whole.

*Figure 4*

![Intra-EU Trade as a Percentage of Total Exports of EU-15 (2002)](chart)

Source: IMF
That is to say, all the accession countries (Baltic states included) have oriented their trade (and external economic relations generally) unequivocally towards the European Union before becoming full member of the Union. Regarding trade, they have become de facto part of the Union. In this respect, accession will not alter the situation.

However, high share of EU in CEEs’ foreign trade not only indicates their organic ties within a regional integration, and degree of trade integration into the Union. Besides that, the said high shares indicate, how intensively exporters from acceding countries participate in global networks of multinational companies. It is simply impossible to know, which countries – near or far-away – the final destination of the commodities exported to EU according to statistical information are. On the other hand, it is also not very important to know. It is quite the same whether the engines produced in some Central European country will become part of a car in Columbia or Germany. In this respect, our traditional perceptions of the geographical or regional pattern of a country’s foreign trade should certainly be modified in a globalized world.

Nevertheless, I am afraid that that trade with „third”, ie. non-EU countries (at least those outside the developed world) is neglected in CEEs. This is part of the story, why trade with Russia is at a very low level now. The simple reason behind this unfavourable phenomenon is that overwhelming part of their foreign trade is in the hands of multinational companies. They play a most important role in modernization and integration of acceding countries. Recently however, not only general and long-term problems (bringing into existence of dual economies, growing social inequalities) related to the dominating role of multinationals have come to the fore. Some new factors, which manifest themselves concurrently, also indicate short-term problems of this situation. Those factors are among others: international recession, geographical reorientation of demand for up-to-date electronic products and machinery to Asia, appreciation of the euro against the dollar, appreciation of the currencies of CEEs linked in some way to euro (and reducing CEEs’ competitiveness vis-à-vis Asian countries currencies of which are linked to the depreciating dollar), as well as rising costs of labour.

**After Re-orientation**

We continue by presenting two tables on Hungarian foreign trade, which span over the periods of two great transformations and re-orientations – more than 70 years. The conclusions pertain to the situation and problems of the years following 1989 – probably, in all CEEs.
Table 1

Geographical Pattern of Hungarian Exports 1930–2003
(total exports = 100)

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Source: HSO

Table 2

Geographical Pattern of Hungarian Imports 1930–2003
(total imports = 100)

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</tr>
<tr>
<td>Slovakia</td>
<td></td>
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<td>Romania</td>
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<td>9.8</td>
<td>4.7</td>
<td>4.3</td>
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<td>1.6</td>
<td>0.7</td>
<td>1.1</td>
<td>1.3</td>
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<tr>
<td>Bulgaria</td>
<td>1.4</td>
<td>0.8</td>
<td>1.4</td>
<td>1.3</td>
<td>2.1</td>
<td>1.3</td>
<td>0.9</td>
<td>0.1</td>
<td>0.1</td>
<td></td>
</tr>
<tr>
<td>Above 4 (5) countries</td>
<td>34.9</td>
<td>18.6</td>
<td>21.7</td>
<td>22.1</td>
<td>18.1</td>
<td>12.3</td>
<td>10.9</td>
<td>6.8</td>
<td>7.8</td>
<td></td>
</tr>
<tr>
<td>CEE</td>
<td>40.0</td>
<td>23.1</td>
<td>24.0</td>
<td>24.6</td>
<td>20.1</td>
<td>14.9</td>
<td>14.5</td>
<td>7.8</td>
<td>8.8</td>
<td></td>
</tr>
</tbody>
</table>

Source: HSO

There are at least three important points inherent in the above tables as far as the message of the paper is concerned. 1. Following the transformation of 1989, Germany has not only become Hungary’s trading partner number one. Its present weight is outstanding in historical perspective, too. Its share in Hungarian exports of recent years is higher than that of the Soviet Union during the CMEA years. Taking account of overvaluation of the transferable rouble (the accounting currency of most of intra-CMEA trade) before 1989, the numbers are
especially striking. 2. The share of CEEs both in exports and imports has been almost continuously subsiding for the whole period shown; today it is less than before the political changes. This statement holds for each CEE one by one, for the group of former (smaller) CMEA members, and, finally, for CEEs in the broader sense. Some consolidation seems to be occurring in recent years. 3. The most striking change following transformation is contraction of trade with Russia, first of all, of exports to Russia.

In the CMEA period, The Soviet Union was the dominant power of „socialist integration”. Now, we also have a predominant trading partner for acceding countries, Hungary included. It is Germany. The German share of Hungarian exports to EU is close to 50 percent. Comparing Germany’s role in total trade of EU countries with its share in trade of accession ones (Figure 5), it is conspicuous that among all EU countries it is in Austrian foreign trade only, that Germany’s role (expressed quantitatively as a percentage of whole trade) is similar to that in Hungary, the Czech Republic and Poland.7

Figure 5

![Graph showing trade with Germany as a percentage of total trade of selected countries.](source: IMF)

Obviously, the present „radial” relations of CEEs with Germany are different in content from radial relations with the Soviet Union in CMEA times. Most importantly, for CEEs Germany is not a market for exports of non-saleable elsewhere manufactures and imports of elsewhere non-purchasable raw materials at relatively favourable prices.8 On practical examination (concerning technical attributes, prices, terms of delivery, company strategies, etc.), exports to, and imports from, Germany can at any point of time be replaced by exports to other destinations, or imports from other sources, what is more, by domestic products. Trade with Germany is accounted for in really existing (convertible into other currencies) foreign exchange, and it is not centrally managed by state authorities. It is an important door to international economy.

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7 Here, geography and existing transport infrastructure of mostly land-locked countries plays an important role, too. Geographical patterns of trade of accession countries that are more remote from Germany – Slovenia, Romania, Bulgaria – is more diversified. In those Mediterranean and Black Sea countries. Italy (from among EU countries) and the Mediterranean in general play a significant trade role.

8 However, at strongly deteriorating terms-of-trade (For this author’s views on static and dynamic advantages and disadvantages of intra-CMEA [CEE-Soviet] trade see Köves, 1984.)
However, large-scale concentration of CEE trade on Germany is also risky, and it lies heavily on them. The concentration means a strong dependence on development and state of German economy, on the latter’s place in the world and the European Union. Advantages and disadvantages of trade are function of situation and policies of multinational companies, which have their European headquarters in Germany, or which belong in German (majority) ownership. Whether those firms consider CEE an important – or not so important – site for manufacturing/assembling and/or selling market. Whether those firms decide to invest or disinvest in CEEs, how they decide, in which activities, on base of what considerations to invest or disinvest. Under today’s circumstances (slow growth in Europe, stagnation/recession in Germany, trans-Atlantic tensions), advantages from trade with Germany are less than desirable.

Intra-CEE trade

As previously noticed, countries between the East (the Soviet Union, Russia or CIS) and the West of Europe have played a limited role in Hungarian trade during the most of the twentieth century. The situation did not change following political and economic transformation in the countries concerned. The share of CEEs (whether in a narrow or broader sense) in Hungarian trade is now lower than in the inter-war or the socialist period. It is but a fraction of trade with EU, or, within it, Germany. True – as contrary to the CMEA years when trade with the Soviet Union was larger than that with the small CMEA countries together –, present level of Hungarian exports to CEFTA (CEE in the narrow sense) is much (in 2002: six times) higher than that to CIS. There are four CEE countries, Hungarian exports to which were higher than those to Russia in 2002 and 2003.

However, tendency of longer-term reduction of trade shares holds not only for the group as a whole, but for each and every country of the group (Poland, Czechoslovakia, respectively both of its successor states, Romania and Bulgaria), and, in the majority of cases, both for exports and imports. Partial exception is Hungary’s trade with Romania: against continuously disappointing imports, exports seem strengthening. Losses are the most astounding in trade with Czechoslovakia (respectively, its successor states), which was among the most important trading partners of Hungary during the large part of the period between the two wars, and even for some time after the war. All in all, in 2002 Hungary exported to the smaller former European CMEA countries little more than one-tenth (10.7 percent) of value of its exports to EU15. Former Yugoslavia’s successors included, the sum adds to 15.2 percent. Compared the above numbers with those of trade with Germany, exports to the former (smaller European) CMEA amounted to 23 percent, Yugoslavia’s successor states included – 32 percent in 2002. To compare: even in 1988, a year of decay, Hungarian exports to smaller CMEA countries totalled 61.9 percent of exports to the Soviet Union; the former GDR not included – 42.7 percent of those exports.

Patterns of Hungarian trade with other CEEs are very much similar to the general pattern of intra-CEE trade. The CMEA cooperation’s „radial” character, the dominant role of exchange of raw materials for manufactures, autarky having existed on the national levels allowed slight scope for relations among the smaller countries. In the CMEA, states and their authorities were inter-connected, they made decisions about the structure and quantities of trade, prices, international investment (mostly into fuel and raw materials sectors of the Soviet Union). Firms, with few exceptions, were only executing higher-level decisions despite slogans that insisted on the development of „direct relations” between enterprises. That was not enough by far to develop trade in manufacturing and integration in production of manufactured goods dynamically.
All that has changed following 1989. In theory, transformation and reorientation of these countries on one hand, globalization of the world economy on the other, could have proved highly favourable developments for trade among CEEs. Intra-CEE trade could be supported by tremendous global flows of foreign direct investment, by transferring the non-competitive in developed countries production into other, less developed countries, by geographical separation of different stages of homogenous or inter-linked production, by turning intra-firm processes of production into quasi international trade – everything that has really happened in the international economic relations of the last decade. Establishment of CEFTA could also have been a favourable circumstance for deeper relations, as well as the coincident ambition of CEEs to enter the EU. As a matter of fact, tendencies have not changed to the better.

There are different plausible explanations for the relatively low level (or simply: moderate dynamics) of intra-CEE trade. One of them may relate to development of machinery trade within the region. To demonstrate, the single biggest group in Hungarian exports (as well as imports) to (and from) CEE is machinery. It is very much the same as in total exports. Exports of machinery to CEE are increasing lively, its share in exports has doubled between 1997 and 2002. However, while 59 percent of total Hungarian exports consist of machinery, in exports to CEE the corresponding share is 28 percent only. (Machinery amount to 52 percent in total imports and 30 percent in imports from CEE.) Obviously, percentage shares of machinery in trade of a given country today do not indicate, at least, not in the first instance, the level of its economic development, the level of its labour force, the quality and structure of the value added it is producing. What it mostly indicates is how intensively the country in question is taking part in multinational division of labour in manufacturing. The most well-known feature of that division of labour is that different phases of internationally integrated production are settled in different countries. The relatively low intensity of intra-CEE trade plus the low share of machinery trade among the countries of the region (while the machinery share of total trade of many CEE countries is high by any international standards) support the conclusion that while some (most of the) CEE countries, one by one, are important partners in the multinational division of labour, the region as a region is not. In other words: (at least, as far as machinery trade is concerned) integration of production does connect those countries one with another in a much lesser degree than with the West, or, the „world” in a general sense. (We return to this issue below, see Table 3.)

Trade with Russia

As Table 1 and 2 (above) show, 1.3 percent of Hungarian exports went to Russia (0.8 percent to Ukraine and 2.4 percent to the whole of CIS taken together) in 2002, while 6 percent of imports originated in Russia (7.8 percent in CIS as a whole). Following some improvement in bilateral relations (and the cyclical downturn in Western Europe constraining the growth of Hungarian exports to the EU), Russian share in Hungarian exports grew to 1.5 percent in 2003. Imports from Russia reached 6.2 percent of total Hungarian imports last year. As mentioned, the difference between the shares of exports and imports comes from the fact that while the former declined very seriously as compared to pre-1989 situation, the most of primary energy continues to be imported from Russia. Due to strong discrepancies between imports and exports, the most of the trade deficit is taking its origin in trade with Russia (59.6 percent in 2001, 55.9 in 2002 – but only 46 percent in 2003). Comparing fresh data with those of some years earlier, as far as exports is concerned, the losses are disquieting even relative to low data of the first half of the 1990s. (In 1996-1997, share of Russia in Hungarian exports was about 5 percent.) While trade with other former CMEA countries also is not showing a
rosy picture, in 2002 Hungary exported to the Czech Republic, Poland, Slovakia and Romania each more than to Russia. In imports, because of deliveries of energy, Russia has remained a partner of decisive importance, however its role is changing in so far as imports from CEE (former CMEA), in aggregate, surpass those from Russia. Figures below show that after 1997, trade with Russia took an unfavourable turn for the second time in a decade, and the paths of changes in trade with Russia differ seriously from the general pattern of Hungarian trade, and even from that of trade with Central European countries.

As shown below (Figures 6 and 7) following the financial crisis of 1998, Hungarian exports to Russia in dollar terms decreased to one-third in two years before showing some moderate increase recently. Although direction of change in each year (and in the whole of the period between 1997-2002) conformed to that of the total Russian imports, the original fall was heavier, the consolidation following 2000 – more sluggish than in Russian trade with most countries. While in 1997 1.74 percent of Russian imports originated in Hungary, in 2001 the corresponding percentage was 1.07. Total imports of Russia (in terms of USD) in 2001 was 78 percent of the value of 1997; imports from CEE6 – 60 percent; from Hungary – 48 percent. In other words, while patterns of Russian imports have changed to the detriment of CEEs, Hungary has fallen backwards even within the group of CEEs. From a Hungarian point of view, the big problem with that is that the decline (especially after 2000) has coincided with a more general slow-down in exports and industrial growth.

**Figure 6**

![Hungarian Exports to Russia, World and CEE 6](image)

**Figure 7**

![Hungarian Imports from Russia, World and CEE 6](image)
As for the specific factors behind the backfall of Hungarian exports, two kind of possible reasons are usually mentioned: first, some estrangement in bilateral political relations (which is surely over with the social-liberal coalition coming to power in Hungary); and second, the specifics of Hungarian export pattern to Russia. By 1996-1997, food (SITC categories 0+1) became the most important commodity group in Hungarian exports, comprising 40.4 percent of the total in 1996, 36.7 – in 1997. Following the financial crisis, the conditions for Hungarian food exports very much deteriorated. As a consequence of that, Hungary’s food exports to Russia in 2002 last year were about half of its value in 1996.¹

The above developments indicate that decline in trade relations following 1998 is not only due to the problems of Russian economy. However, longer-term trade trends between CEEs and Russia depend basically on the situation of Russian economy and the size of Russian import market. Following the grave, almost 50 percent decline of GDP between 1991-1998, the economy is on a dynamic stage now, even if the production level of 1989 is a way off. Dynamism is nourished by political stability, the depreciation of the rouble after 1998 (making many important segments of the domestic production competitive with the imports) and the high international oil prices. However, structurally, the economy is weak. As a singular case in the world outside the OPEC, number one mover of economic development is high oil prices, although Russia can not influence their level. Russian (formerly: Soviet) intentions to develop internationally competitive manufacturing and abolish quasi-monoculture of fuel exports have been known for about three decades, however no changes have followed. Therefore, Russian dependence on the international oil and gas markets is very high: 55 percent of its exports consist of fuels.

Table 3

<table>
<thead>
<tr>
<th>Categories</th>
<th>Exports</th>
<th>Imports</th>
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<tr>
<td>Food, beverages and tobacco (0+1)</td>
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<td>14.7</td>
</tr>
<tr>
<td>Raw materials (2+4)</td>
<td>2.0</td>
<td>2.9</td>
</tr>
<tr>
<td>Fuels (3)</td>
<td>1.6</td>
<td>4.0</td>
</tr>
<tr>
<td>Manufactures (5+6+8+9)</td>
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<tr>
<td>Machinery and Transport Equipment (7)</td>
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<td>28.4</td>
</tr>
<tr>
<td>All Commodities</td>
<td>100</td>
<td>100</td>
</tr>
</tbody>
</table>

Source: HSO

¹ According to a Hungarian interpretation, the development of Hungarian agricultural exports was interrupted at the time of the Russian financial crisis in spite of the parallel food crisis as a consequence of the catastrophic harvest. Indeed, the market loss of Hungarian firms was caused by the latter. As a matter of fact, large-scale aid by US and EU laid the foundation of big commercial deals for the companies of the donor countries concerning, among others, produce of strong interest for Hungarian firms. In the meantime, import price rises in Russia did strongly incited multinational companies in food industry and trade to settle in Russia. Trade channels and ways of financing, which are operated by those companies, contribute to hold off and press back the more traditional exporters. (Lányi, 2003)
Table 3 shows strikingly different patterns of Hungarian trade with the world, CEE6 and Russia. While some specifics of trade with CEE (relatively low level of trade in machinery) were mentioned above, commodity structure of trade with Russia differs even more from the average (trade with the world). Food (despite reduction of deliveries following 1998) continues to dominate exports. Machinery exports are relatively unimportant even in the context of generally low level of exports to Russia. (Before 1989, almost 50 percent of Hungarian exports of machinery went to the Soviet Union.) In imports, four-fifth of trade consist of fuels, while all other commodities are practically unimportant.

Moreover, not only structural weaknesses and eventual instability make future development of Russian economy somewhat uncertain, but the country’s potential to import, although widening, is relatively limited for the time being. According to UN data (UN Monthly Bulletin of Statistics, November 2003), in 2001, Russian imports from the world (about USD 42 billion) were less than Polish ones (50 billion) and little more than Hungary’s imports (34 billion). Correspondingly, Russia’s share in world imports was 0.72 percent as compared to Poland’s 0.87 and Hungary’s 0.58 – or to the country’s own 1.72 percent share in world exports. No significant change occurred in 2002. Russian imports reached USD 46.2 billion (0.76 percent of world imports) as compared to Poland’s 55.1 billion (0.91 percent) and Hungary’s 37.8 billion (0.62 percent).10

Figure 8

![Percentage Shares of Selected Transition Countries in World Exports](chart.png)

Source: UN

10 The numbers given by IMF (IMF Direction of Trade Statistics Yearbook 2003) differ to a minimum extent from above. According to the latter, in 2002, Russia was responsible for 0.69 percent of world imports (USD 45.5 billion) as compared to Poland’s share of 0.83 (USD 55.1 billion) and Hungary’s 0.56 (USD 37.3 billion). Russian Goskomstat data, referred to in some other international publications (for example, in ECE Economic Survey of Europe), are different as they include trade flows not crossing the Russian borders (such as off-board fish sales) and estimates of value of goods exported or imported by individuals within an approved duty-free quota.
The statistics, on basis of which the above figures are constructed, may be somewhat distorting. Perhaps they do not take account of some differences in content of numbers given. They may lead to certain mistaken conclusions. For example, when comparing Hungarian and Russian trade, it should be considered that a significant part of Hungarian imports do not serve domestic uses but target export-oriented production. The latter is a negligible part in Russian imports. However, the essential thing is that as far as its import potentials are concerned, Russia today belongs to the same class of countries as Poland, and some other CEEs. Of course, the situation may change in a short period of time. Some of the questions pertaining are: will the present rate of growth of Russian economy persist, economic uncertainties inside the country subside, terms-of-trade steadily improve and trade growth accelerate. Even in such case, Hungarian exports (as well as exports of other CEEs) to Russian markets may remain limited for a longer period of time as development needs of the Russian economy will mostly be covered by deliveries from the most advanced countries, while China will remain an inexhaustible as well as the cheapest source of imports of mass consumption goods. Eventual advancement of multinationals in Russian economy may lead to growing role of foreign investors in the selection of trade channels and trading partners.

**No basic changes**

No basic changes as a consequence of full membership should be expected, as far as trade orientation of CEEs (Hungary included), and the prevailing role of the Union (respectively Germany) in external relations is concerned. Of course, there are a lot of unanswered (unanswerable) questions related not so much to the effects of *de jure* membership, than to economic development of EU25 and the future of European integration. The recent recession, with Germany as its epicenter, slowed down the development of EU trade, and signs of recovery are not distinct yet. Unfavourable economic developments (slow-down of GDP growth, unabating unemployment, lower competitiveness, simultaneous exodus of many multinationals) are to be seen in some CEEs as well. As far as foreign economic relations of CEEs are concerned, those developments may have a negative impact on trade with EU. That means, that for cyclical reasons among others, trade with EU in CEEs having grown rapidly in the period of candidacy, may slow-down, paradoxically, at the time of accession. In that case, intra-CEE trade, as well as trade with Russia and „third” countries in general will be of growing importance for us.
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