The Czech Republic – impacts of and experience with EU membership

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Abstract

This paper analyses the impact of the post-accession experience of the Czech Republic in the years 2004-2011. In particular, it focuses on the integration into the EU internal market, preparation for Eurozone accession, transfers from the EU budget and the formulation of the EU energy policy. In each policy area, both the impact of the existing EU regulatory framework and Czech preferences for its reforms are covered. The last section of the paper (chapter 6) describes the Czech institutional adaptation to the EU membership, in particular the 2009 Czech presidency experience.

Key words: Czech Republic, European Union enlargement, internal market, Presidency of the Council of EU, transition periods, EU energy policy, EU budget.

JEL Classification: F15, F36, O52, Q4

1. Introduction

The objective of the following text is to map several areas where the EU accession of the Czech Republic has changed the political, economic and regulatory environment in the Czech Republic. In particular, the text will concentrate on three factors of the post-accession development which will receive a particular attention.

The first one is the importance of the regulatory change as a result of the shift from the asymmetric association status to full membership for the Czech Republic through the 2004 accession. From this perspective, the major challenge for the post-accession Czech Republic seems to be the transition to the position of an active player in the EU's decision-making regulatory structures.

The second element of the Czech post-accession experience, which will be demonstrated later in the text, was that the impact of the post-accession

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experience on the economic situation in the Czech Republic was not radical. The post-accession development can be interpreted primarily as an extrapolation of the pre-accession association status in combination with the mitigation impact of the transitional periods contained in the accession acquis.

The third feature analysed is the dynamic of the process of the Czech experience as a EU member when the Czech government has undergone some radical shifts in its position regarding several key EU projects, such as Eurozone, during the six post-accession years.

2. Czech adaptation to the EU's internal market

The Czech Republic is usually described as a "small open economy". The Czech export is directed primarily towards the European Union (e.g. 85% of total export in 2008, 84% in 2009) with Germany as the dominant export target (30% of total export in 2008, 32% in 2009), followed by Slovakia (9% of total exports in 2008, 8% in 2009), France, Poland, and Austria (Czech Statistical Office, 2011). The inter-connection between Czech and German economy has reached such intensity that the Czech Republic has been even labelled as *"another German Lander"*.[1]

In the first years after the EU accession, the Czech economy experienced an unprecedented growth since the beginning of the economic transformation at the beginning of the 90s[2]. The growth was accompanied by an increase in labour costs and by the strengthening of the Czech crown.

The impact of the crisis of 2008-2011 has been relatively limited. The major reason is the conservative approach of Czech banks in the pre-crisis period. Therefore, no governmental bank rescue package has been required. Furthermore, the vast majority of the Czech private (household) debt has been denominated in Czech crowns, which made the financial situations of households less vulnerable to the currency fluctuation and has prevented problems experienced, for instance, by Hungary since 2008.

As an export-oriented economy, however, the Czech Republic has been very sensitive to the consumption trends of its EU neighbours, particularly in Germany. The export to Germany dropped almost by 10% in 2009 in comparison with previous years (Czech Statistical Office 2011) and the economic recovery in Germany in 2010 was reflected in the growth of Czech exports. The impact of the crisis onto the Czech Republic has also been

[1] Zámečník, Miroslav. Sedmnáctá spolková? Euro, January 24, 2011.

[2] GNP growth in the post-accession years was as follows: 4.5 % (2004), 6.3% (2005), 6.8% (2006), 6.1% (2007), 2.5% (2008), -4.1% (2009), 2.3% (2010); estimation for 2011 is 2.5% . In contrast, in the pre-accession years 1999-2003, the GNP growth was between 1.3% (1999) and 3.6% (years 2001 and 2003) (Czech Statistical Office, 2011).

mitigated by the relatively low public debt of the Czech state, albeit the pessimistic dynamics of its development. In 2010, the public debt of the Czech state reached 36.6% GNP (in comparison to 21.1% in 2004) and the estimate for 2011 is 42% of GNP (Czech Statistical Office, 2011). Against the general trend in the EU, the position of public finances of the Czech Republic was „upgraded“ by Standard & Poor's from the "A" to "AA-" category in August 2011.

The EU membership has been generally considered as a significant, if not the major, factor of the Czech post-accession economic growth. However, it can be argued that the most influential factor of the post-enlargement economic environment has not been the formal opening of the internal market *per se*. Since the tariff barriers and quotas for industrial good were removed even before the Czech accession (as result of the association regime) and significant barriers in the free movement of services survived even in the post-accession period, the increase in the credibility and predictability of the regulatory environment in the Czech Republic and the removal of some technical and administrative barriers against mobility due to the EU membership can be identified as the most significant impact of the Czech accession to the EU (Marek and Baun, 2011, pp.106-108).

As an EU member, the Czech Republic has gained a potential to influence the regulatory framework of the internal market as an active player, in contrast to the position of a passive recipient of acquis in the pre-accession period. The experience of the first post-accession years has demonstrated with great clarity the importance of defining and pursuing national interests within the EU structures. In several cases, new EU rules have created significant problems to the corresponding segments of the Czech economy – a frequently used example is the impact of the new EU regulatory framework for sugar which caused a radical implosion of the sugar production industry in the Czech Republic.

The Czech Republic has pursued two major trends in the internal market during its post-accession years. The first has been the support for liberalization within the internal market; in other words for removing the remaining national barriers within internal market. Examples of this strategy include Czech calls for a termination of transitional periods, for the free movement of workers and/or support of the EU initiatives for further liberalization of the free movement of services. In the latter case, the Czech representatives criticized the gradual reduction of the originally ambitious liberalization plan contained in the Commission's proposal of the "Bolkestein directive" (directive on free movement of services) during the legislative process in the European Parliament and the Council; however, the Czech MEPs voted even for the final, less ambitious, version of the directive since even the final version of the directive had eliminated some existing problems and clarified several rules of the service mobility within the internal market.

The second trend within the internal market, which has been supported by the Czech Republic since its accession to the European Union, has been the opposition against new regulatory initiatives establishing new EU standards, particularly in the domain of taxation or employment policy. Czech politicians consistently vetoed EU's initiatives for higher tax harmonization in the EU (quite symbolically, the first Czech veto was applied in the debate on an increase of the consumption tax on beer). At the same time, the Czech Republic has not adopted explicit declarations or (quasi)legislative measures stating the *"national sovereignty"* in tax policy, as the Slovak Republic did in 2007.

The EU's impact on the labour market and mobility of workers in the Czech Republic deserves further elaboration. The full mobility of Czech workers to other EU states was limited (until 1st May 2011) by transitional periods negotiated in the accession treaties. The impact of transitional periods was weakened by the fact that no new EU state in Central Europe and only some old EU states actually used the regulatory potential contained therein and the list of EU states applying the transitional periods has been gradually narrowing since 2004[3]. Furthermore, citizens of the Czech Republic used the potential of the intra-EU mobility less intensively than citizens of its neighbours. Reasons behind are primarily better economic performance of the Czech Republic in both pre- and post-accession years and traditional less pro-mobility socio-economic patterns in the Czech society.

At the same time, the Czech Republic has developed into a significant recipient county of labour mobility streams in the post-accession period. The most important countries of origin of foreign workers employed in the Czech Republic include both EU states (Slovakia, Poland) and non-EU countries (Ukraine, Vietnam). The EU accession does not seem to have a significant impact on the structure of the inflow of foreign workers and major initiatives in this domain remain under autonomous decision of Czech policy makers. For instance, the Czech Republic opted not to apply transitional periods in the most recent enlargement (Bulgaria and Romania).

The Czech position towards the liberalization of transport services has its specificity, similar to those which emerged in Austria. The Czech situation is primarily influenced by the location of the Czech Republic on the major transport corridors within the European Union. In particular, the land transport (haulage) tests the limits of the Czech transport infrastructure (highways) capacity and generates a financial burden for the Czech budget as a result of the construction and maintenance costs. The Czech Republic reacted by an attempt to transfer part of these costs to the transport operators; and the existence of the

[3] The United Kingdom, Ireland and Sweden has not used transitional periods at all, Spain, Finland and Portugal opened their labour markets to Czech workers in 2006 and France in 2008.

EU limits on the price of vignettes (toll stickers) for heavy trucks has been one of the factors for the Czech decision to introduce a road-toll system, calculated for each vehicle according to the distance actually travelled, where the EU provides more discretion for individual member states.

3. Eurozone and economic governance

The Czech Republic did not become a (full) member of the Eurozone at the moment of its accession to the EU. The experience of delayed accession to the Eurozone has been shared also by other new EU members. What distinguishes the Czech Republic from other new members of the enlarged EU is the fact that the approach of the Czech Republic to the European monetary integration project had experienced a radical shift since 2004.

Originally, the Czech executive expressed the intention to join the Eurozone within a relatively short time framework/horizon, with target dates of January 1, 2010 (based on the plan of the Social Democratic government in 2005). Later, the updated governmental strategies for the Eurozone postponed the target date for 2012 while the Czech National Bank stressed its neutral position regarding the date of the Eurozone entry (Šlosarčík et al, 2011, pp. 101-102, Beneš and Braun, 2008, p. 65). The only vocal critic of the Eurozone project in the Czech Republic at the moment of the Czech accession to the EU was the President of the Republic, Václav Klaus (Beneš and Braun, 2008, p. 82).

A major argument in favour of the Eurozone accession was the expected stabilization impact on the Czech industry and the export-oriented industrial lobby (e.g. car producers) was also the most vocal supporter of a prompt replacement of the Czech national currency by the Euro, particularly with the objective to increase the stability and predictability of the business environment in the Czech Republic.

However, the Czech government, since the very beginning of the Czech EU membership, has expressed a need to balance the impact of the future Eurozone accession onto different actors in the Czech Republic. It has also stressed the political nature of the timing of the Czech accession to the Eurozone, regardless of the formal obligation of the Czech Republic to make steps towards the Eurozone accession, as provided in the Accession Treaty. To identify and evaluate the impact of the Eurozone accession on different socio-economic actors in the Czech Republic was also the key objective of the major analytical advisory study commissioned by the Czech government in 2007 (Lacina, 2007).

However, the Czech position has changed radically since 2008 and debate about plans to join the Eurozone, or even about a target date, have virtually disappeared at present (Beneš and Braun, 2011, pp. 59-60). Reasons behind this development are threefold. The first is the change in composition of the Board of Governors (Banking Board) of the Czech National Bank, a body co-responsible (together with the Ministry of Finance) for Czech preparation for the Eurozone membership. Members of the Board of Governors are appointed by the President of the Republic for a six-year term and the appointment(s) are exclusively within discretion of the President (i.e. no approval of the government is required). As President Václav Klaus has been in office since 2003, he has directly appointed all serving members of the Board of Governors by the end of the decade. Logically, President Klaus appointed economists with an approach to the Eurozone similar to his own, i.e. primarily sceptical to the viability of the Eurozone project.

The second reason behind the decline in the Czech support of Eurozone membership is the impact of the 2008-2011 economic crisis on the Czech Republic. As demonstrated above, the impact of the crisis on the Czech public finances was relatively limited. However, even the limited impact of the crisis has moved the Czech public budget outside the limits of the convergence criteria necessary for the Eurozone accession. The present (2011) Czech government declares itself the „government of financial responsibility“ and the Greek crisis was used by centre-right political parties as an argument against the centre-left political parties during the 2010 election campaign. However, the obligation to comply with the Eurozone convergence criteria does not occur in the governmental argumentation for fiscal responsibility and/or austerity measures; the arguments used are primarily focused on the need for the stability and sustainability of the Czech national budget.

The third reason for the Czech sceptical approach to the Eurozone is the 2010-2011 Eurozone internal crisis. In general, the Czech Republic tended to adopt the “wait and see“ tactics towards the crisis and refused to make any long-term commitments regarding its future participation in the Eurozone project. In line with this passive approach is the Czech decision not to participate in the European financial mechanisms formed during the crisis, such as the European Financial Mechanism which was joined by all non-Eurozone countries with the exception of the United Kingdom, Sweden, Hungary and the Czech Republic. (Beneš and Braun, 2011, pp. 66-67).

Thus, the statement of the President Klaus that, in contrast to his refusal of the Czech accession to the Eurozone, he could imagine his support of the Czech accession to a post-Eurozone monetary union of the northern EU states linked with the German economy (“Markozone“) is a rather anecdotic comment. In a more general and serious analysis, the President of the Republic frequently comments on the unsuitability of the Eurozone membership for the EU states with lower economic productivity (Klaus 2011).

4. Energy policy

The energy policy of the Czech Republic is relatively complicated, reflecting both the historical and geographical context of the Czech state. The energy mix of the Czech Republic includes domestically produced coal, imported gas and crude oil, nuclear energy and a limited amount of renewable resources (water, solar, wind).

The governmental energy policy has to balance the mutually competing disadvantages of the individual elements of the energy mix which include the supply interruption risk (gas, crude oil), negative impact on the environment (coal) and ideologically driven criticism (nuclear energy). In the post-accession years, the Czech Republic has experienced problems both with the interruption of supplies from Russia (e.g. gas crisis in January 2009) and inter-state tension linked with the nuclear energy (in particular, diplomatic tension and public protests in Austria).

The Czech energy policy at the EU level thus follows two directions. The first one is a call for more efficient EU external policy focused on the stability of energy supplies, including EU support for infrastructure projects (Czech support for Nabucco gas pipeline or for strengthening the intra-EU electricity grid) and for firm EU position(s) during negotiations with third-party countries. However, the Czech Republic supports primarily EU funding of specific infrastructure projects instead of creation of a general EU financial framework for energy infrastructure (such as Connection Europe Facility) that is perceived as a threat to a scope of EU funding of general policy of social and territorial cohesion.

The second direction of the Czech activity at the EU level is the opposition to the attempts to regulate the nuclear energy and the relatively sceptical approach to the EU carbon emission policy (Beneš and Braun, 2010, pp. 66-67).

5. The EU budget

The expected financial transfers from the EU budget were frequently used as the argument in favour of the Czech accession to the EU. As a state with a GDP per capita bellow the EU average, the Czech Republic had a strong potential to turn into a significant beneficiary of the intra-EU transfers. This potential has materialized in the first post-accession years when the Czech Republic developed into a net recipient from the EU budget, particularly in the domain of economic and social cohesion (and only gradually in the CAP, as described later). From the short-term perspective, the major problems linked with the EU budget in the Czech Republic concerned the technicalities of the utilization of funds allocated to the Czech Republic, such as setting the respective administrative bodies in the Czech Republic, negotiating the agreement(s) with the European Commission on the cohesion policy priorities, the red tape linked with project implementation, the co-financing required by the EU rules or occasional corruption connected with financial transfers. Insufficient extraction of the EU funds caused by a lack of quality programs and by the intensive administrative burden on private applicants is usually identified as the major problem in the first post-accession years.

At the same time, the Czech Republic has been a critic of the structures and priorities of the EU budget, particularly opposing the allocation of resources to the Common Agricultural Policy at the expense of other policy areas, such as education or modern infrastructure. The critique of the CAP spending by the Czech Republic has been simplified by the relatively small size of the Czech agricultural sector, in comparison with other new EU states. On the other hand, the Czech position regarding the EU spending is more pragmatic than ideologically-driven and the Czech Republic proved to be able to lobby in favour of specific Czech agriculture interests, such as the important role of large farms in the Czech agriculture (Dostál, Karásek, Thim, 2011, p. 120).

Since it belongs to the more advanced and richer part of the new EU states, it is not clear whether the Czech Republic will be net-recipient or net-payer in the medium term perspective, such as after 2020.

Therefore, the Czech position towards the budget seems to be trapped between two colliding objectives. The Czech priority is the general expansion of the EU budget, where the Czech Republic would benefit as a net-recipient. The second one is the pressure on the reform of the EU spending structure which would more properly correspond to the Czech priorities and to the fact that, in the medium term perspective, some Czech regions are likely to cease their eligibility to a significant number of segments for the EU's funding.

6. Institutional adaptation, the 2009 Czech Presidency and ratification of the Lisbon Treaty

Two events in the Czech Republic distinguished themselves among the generally low profile activities of the Czech state within the EU. The first was the Czech presidency of the European Council and the Council of the EU in the first half of year 2009; the latter was the ratification process of the Lisbon Treaty in the second half thereof.

The Czech Presidency demonstrated both strong features and weaknesses of the Czech behaviour within the European Union. The Czech Presidency adopted a relatively moderate program focused on internal EU economic liberalization, energy security and Eastern dimension of the EU foreign policy. Within these priorities, the Presidency focused on practical policy initiatives (e.g. launching the summit of the Eastern Partnership organized in Prague) and concrete legislative measures. At the same time, the Presidency activities were from the very beginning "hijacked" by unexpected events outside the EU (interruption of gas supplies caused by the dispute between Russia and Ukraine, escalation of Gaza crisis).

In the economic sphere, the Czech presidency regarded its primary role as the opponent and/or corrector of massive use of spending power of the EU states

(Beneš and Karlas, 2010, pp. 74-75). Prime Minister Mirek Topolánek gained even some unwelcomed attention from global media when he criticized the US financial crisis plan as "road to hell" in his speech before the European Parliament in March 2009. The Czech presidency also criticized, among others, the national financial schemes stimulating purchasing of new vehicles (Beneš and Braun, 2010, pp. 65-66). Paradoxically, the Czech car industry was a significant beneficiary of the stimulation programs introduced by its neighbours (particularly by Germany and Slovakia) when its export to the countries in question had increased as a result of the stimulation programs introduced by local Slovak and German governments.

From the external perspective, however, the major event of the Czech Presidency was the fall of the government in the middle of the presidency. This political crisis, caused primarily by domestic political competition, significantly weakened the performance of the Czech executive during the second half of the Presidency, and seriously damaged the reputation of the Czech state.

The Czech Republic was a relatively active player during the preparation of the Treaty establishing the Constitution for Europe. This pro-active approach has not, however, continued during the preparation and ratification of the Lisbon Treaty. The new Czech centre-right government did not belong to the most ardent supporters of the treaty reform but, ultimately, the Lisbon Treaty was approved by the Czech government. The following ratification procedure was then interrupted twice by reviews before the Constitutional Court and further delayed by the insistence of the President of the Republic that the Lisbon Treaty should include guarantees against destabilization of the property regime in the Czech Republic. This requirement has been tackled, albeit in a legally very opaque form, at the EU level and the Czech Republic has been the last EU state ratifying the Lisbon Treaty in the autumn of 2011.

7. Conclusions

EU has not turned into a panacea for all shortcomings of the Czech state. At the same time, major fears of the EU's impact on the vulnerable elements of the Czech economy or society have not materialized either.

Within the EU, the Czech Republic had to learn how to formulate and defend national interests within the EU structures. After a relatively short post-accession learning phase, the Czech Republic started to systematically pursue those elements of the EU integration which correlated with its export-oriented economy and (allegedly) relatively low level of labour and welfare regulation.

However, while the Czech Republic proved to be a relatively skilful learner in coping with the more technical and short-term policy objectives, debates about the Lisbon Treaty and turmoil of the post-2008 crisis demonstrated that the Czech Republic still keeps a rather low profile within the long-term trends of the European integration project.

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