RESEARCH PAPERS

NEW MEMBER STATES OF THE EUROPEAN UNION AND THE CURRENT TRENDS IN THE WORLD ECONOMY

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This paper describes the specifics of the current development of the world economy and discusses implications for new member states of the European Union, the EU NMS, with a small case study on the Czech Republic. The paper is divided into four parts: the trends, the EU NMS and the effects of the trends in the EU NMS and in the Czech Republic. The paper is based on a general economic analysis of data provided by the World Bank (WB), the International Monetary Fund (IMF), Eurostat, the European Central Bank (ECB) and by the Czech Statistical Office (CZSO). Being familiar with recent macroeconomic trends is nowadays important for Central and Eastern European managers in order to efficiently adapt their strategies to the constantly changing business environment.

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1 Introduction

The development of modern economies in the 2000s is different from the one observed in the 1970s, 1980s and also 1990s in view of the strengthening role of cross-border trade (especially of intra-industry trade, intra-firm trade etc.), foreign investment, internationalization and innovation, as well as multinational and transnational companies (MNCs and TNCs). In addition, the recent global financial, economic and partly "debt" crisis of 2008 (also called "the Great Recession") was the first and largest global economic downturn since World War II, in many dimensions comparable to the economic crisis of 1930s (the Great Depression). The crisis significantly affected the economies of the U.S. and of the European Union (EU), in the latter – in both the old member states and the recent adherents, the so-called EU new member states (EU NMS) who joined the EU in 2004, 2007 and 2013: Bulgaria, Croatia, Cyprus, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Romania, Slovakia and Slovenia. Growth has remained fragile since. This paper aims to describe, in a concise and informative manner, the specifics of the current development of the world economy and to discuss their effects in the mentioned EU NMS, with a short case study on the Czech Republic as one of the most developed economies.

2 Methods

The paper is divided into four parts, the trends, the EU NMS and the effects of these trends in the EU NMS with a special focus on the Czech Republic. The paper is based on general scientific methods of analysis, comparison, induction and synthesis in the form of general economic analysis performed on data from the World Bank (WB), the International Monetary Fund (IMF), the Organisation for Economic Co-operation and Development (OECD); from the European sources, Eurostat and the European Central Bank (ECB); and from the Czech Statistical Office (CZSO) and Czech National Bank (CNB). Not all data for the year 2013 was available in Q3 2014; therefore, Croatia is excluded from the EU NMS and EU list in tables. The most recent research on the topic was presented in (Baláž et al., 2010; Baldwin et al., 2009; Cihelková et al., 2009; Kalínská et al., 2010; Maddison, 2004; Pettis, 2013; Štěrbová et al., 2013), Chapter 1, and in (Bolotov, Čajka, Gajdušková, 2013), Chapters 1 and 3.

2.1 Trends in the Global Economic Development since 2000

Recent literature on the world economy, international business and international trade, e.g. (Maddison, 2004; Pettis, 2013), in the Czech and Slovak languages, e.g. (Baláž et al., 2010; Cihelková et al., 2009; Kalínská et al., 2010; Štěrbová et al., 2013), states that the world economy has become a complex socio-economic system characterized by two mutually interconnected processes, globalization – an increased interconnection and interdependence between the majority of economies in the world, and regional integration – region/continent-based free trade agreements, customs unions, common markets, currency unions etc. with the EU as a successful example. The mutual interaction of both processes has created five trends in the world economy at the start of the 21st century and especially in the current decade, 2010–2020, as described in (Baldwin et al., 2009; Štěrbová et al., 2013) and (Bolotov, Čajka, Gajdušková, 2013):

a) Continuous expansion of cross-border (international) trade in goods and services with an average growth rate of world exports and imports outperforming the growth of real world gross domestic product (GDP), 5.87-5.88% against 3.44% in 1991–2013 (IMF data, World Economic Outlook October 2014). This difference is mainly caused by the so-called compositional, synchronicity and statistical effects, as defined in (Baldwin et al., 2009; WTO, 2011, 2013), see Table 1.

Table 1: Three effects influencing the development of international trade

Effect	Significance
Compositional effect	Higher share of 'postponable' goods in the world trade than in GDP, the demand of which is more volatile than the aggregate demand in economies.
Synchronicity effect	Importance of internationalized supply chains, herd behavior.
Statistics / value-added effect	Rise in trade in intermediate goods that leads to counting the same value added more than once in cross-border trade flows.

Source: Bolotov, Čajka, and Gajdušková (2013), p. 13.

Durable goods dominate world trade with a greater share than the one of 50% (WTO data, 2014), therefore it experiences higher demand fluctuations compared to service-oriented GDP, where services account for ca. 2/3–3/4 (WB data, 2014). This is amplified by implementation of new telecommunication technologies in supplier-buyer networks and by on-going delocalization of industrial production and services towards Central and Eastern Europe, mainly the EU NMS, and towards Asia, notably China (and now also South-East Asia). The growth of trade is also spurred by liberalization through adoption of new regional trade agreements – for example, the new free trade agreements between the EU and the Republic of Korea (July 2011) and Peru and Columbia (March and August 2013) – and through long-term negotiation rounds within the framework of the World Trade Organization (WTO), currently the Doha Development Agenda (since 2001).

b) Increase in foreign direct investment (FDI) flows, which quadrupled from 2004–2007 and reached their historical maximum of ca. 2 billion USD in 2007. The outflow of FDI for 2014 is projected to be slightly over 1.5 billion USD (reaching ca 1.75 billion USD in 2016, according to UNCTAD's World Investment Report 2014). FDI strengthens the position of MNCs and TNCs – today approximately 1/3 of world trade is regarded as intra-firm conducted within MNCs and TNCs (UNCTAD data, 2013). According to an OECD study (Lanz and Miroudot, 2011), the extended MNCs' and TNCs' networks, based both on FDI and non-FDI types of relations, account for up to 2/3 of exports and imports of goods and services in a number of developed economies; consult also Machková and Taušer (2013).

c) Internationalization of production of goods and services that decreases the role of countries in international trade and strengthens the position of MNCs and TNCs and their global value chains (GVCs) (Evan, 2011; UNCTAD 2013), e.g. Levi Strauss & Co. produces cotton, fabric and clothes (jeans) in Mexico, Dominican Republic, Haiti, Egypt, which are later sold in the USA and Europe (Levi and Strauss, 2009). GVCs improve allocation of resources at the global level but their growth hampers the ability of international organizations, such as the WTO, UNCTAD and OECD, to accurately measure international trade as cross-border transactions include foreign value added. The share of foreign value added in cross-border exports, the strength of GVCs, varies from 3–7% in Saudi Arabia and Russia to almost 50 and 60% in Singapore and Luxembourg, according to OECD and WTO, TiVA data, 2014.

Table 2: Basic facts and figures on the EU NMS in 2012

Name / Code	Area	Population		GDP		In the EU since	In the euro area since
	th. sq. km	thousand	% of EU 27	million EUR	% of EU 27		
Cyprus	9.3	862.0	0.17	16,259	0.12	5/1/04	1/1/08
Czech Republic	77.3	10,505.4	2.10	149,855	1.14	5/1/04	-
Estonia	43.4	1,333.8	0.27	18,495	0.14	5/1/04	1/1/11
Hungary	93.0	9,931.9	1.98	98,048	0.75	5/1/04	-
Latvia	62.3	2,044.8	0.41	23,375	0.18	5/1/04	1/1/14
Lithuania	62.7	3,003.6	0.60	34,705	0.26	5/1/04	ERM II
Malta	0.3	417.5	0.08	7,109	0.05	5/1/04	1/1/08
Poland	312.7	38,538.4	7.70	388,644	2.96	5/1/04	-
Slovakia	49.0	5,404.3	1.08	72,791	0.55	5/1/04	1/1/09
Slovenia	20.1	2,055.5	0.41	34,955	0.27	5/1/04	1/1/07
Bulgaria	111.0	7,327.2	1.46	41,031	0.31	1/1/07	-
Romania	230.0	20,096.0	4.02	141,563	1.08	1/1/07	-
EU NMS	1071.1	1279.5	20.28	1026.83	7.81	x	x

Source: author, based on Eurostat data, 2014 and Europa.eu.

d) The growing share of developing and transitional econo-mies in the world economy, especially of the BRICS (Brazil, Russia, India, China and South Africa) – e.g. China became 2nd in terms of both nominal GDP and GDP in purchasing power parity (PPP) in 2010 (8.4 trillion USD in 2013) and is expected to become the 1st for PPP in 2014 (IMF data, 2014). Developing and transitional economies registered a total share of 42% in world trade in 2012–2013 and a greater than 50% share in global FDI inflows in 2013 with China and Russia being among top three investment destinations and top five investor nations (WTO and UNCTAD data, 2014). The share of the BRICS and of the EU NMS in the world GDP increased by 50–100% in 2000–2008 (prior to the Global Recession) and in the case of the BRICS, continues to grow, as indicated by (Bolotov, Čajka, Gajdušková, 2013, p. 16) (WB data, 2014).

e) Higher instability of financial markets and the lasting effects of the global financial, economic and partly debt crisis of 2008, in which the world economy experienced a ca. 0.7–2.2% contraction in GDP in 2009 (IMF and WB data, 2014) and a slowdown since 2011 with growing signs of recovery only in the USA in 2014. In 2014, the instability was amplified by geopolitical risks resulting in worsening relationships and sanctions between the USA, EU, Canada, Australia, Japan, Switzerland, Norway and Russia due to the Ukrainian crisis, as well as to other crises and problems, such as the Middle East (Iraq and Syria), Ebola outbreak, etc.

2.2 The New Member States of the European Union, the EU NMS

The EU NMS are a group of countries that acceded to the EU during the 2004, 2007 and 2013 enlargements (countries, which will accede in the future will be also added to the EU NMS list): Bulgaria, Croatia, Cyprus, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Romania, Slovakia and Slovenia. Ten of these countries are former socialist economies, part of which emerged in the beginning of the 1990s with the dissolution of the USSR (1991), Yugoslavia (1991–1992) and Czechoslovakia (1993). Hence they have undergone a profound economic transition since the 1990s, which has already finished in some countries, in Estonia, the Czech Republic, Slovakia and Slovenia (possibly also in Hungary and in Poland) and continues in the rest, consult Table 2. Cyprus and Malta share a different historical background and are considered to be developed economies by the IMF / WB.

The EU NMS vary greatly in size and in economic development, ranging from 0.3 to 312.7 thousand sq. km, from 0.4 to 38.5 million inhabitants and, in terms of GDP per capita in PPP, from 47 to 91% of the EU 27 level, consult Table 3. The same is valid for price levels: the lowest value corresponds to 49% and the highest to 88% of the EU 27 average.

Table 3: Comparison of economic level of the EU NMS and the EU 27 in 2012

	GDP per capita, PPP		Price level
	EUR	%	%
European Union (EU 27)	25600	100	100
EU NMS (average)	19098	75	71
Cyprus	23296	91	88
Czech Republic	20224	79	75
Estonia	17664	69	80
Hungary	16896	66	62
Latvia	15872	62	75
Lithuania	17920	70	66
Malta	22016	86	78
Poland	16896	66	58
Slovakia	19200	75	72
Slovenia	20992	82	85
Bulgaria	12032	47	49
Romania	12544	49	57

Source: author, based on Eurostat data, 2014.

The EU NMS are an economically developing segment of the EU: with approximately 24.8% of its territory and 20.3% of its population, in 2012 the EU NMS accounted for only 7.8% of the EU 27's GDP, 18.2% of its agricultural production, 10.7% of its industrial production, 10.6% of its total exports and 10.8% of its total import; consult Table 4 for indicators.

Table 4: Comparison of economic indicators of the EU NMS and the EU 27, 2004–2012

	EU 27	EU NMS
Real GDP growth, %	1.2	2.9
Inflation rate, consumer prices, %	2.4	4.1
Unemployment rate, % of labor force	8.9	9.1
Public debt, % of GDP	70.0	38.2
Current account deficit, % of GDP	0.3	-5.9

Source: author, based on Eurostat data, 2014.

2.3 The EU NMS and the Recent Global Trends in the World Economy

The lower price level, lower labor costs and important investment incentives enable production to be delocalized from developed countries in EU 27 and in the world to the EU NMS. By means of examples, in the 2000s, automotive companies like Volkswagen, PSA, and Toyota moved their production to the Czech Republic, Hungary and Slovakia, Danish toy producer LEGO to Poland etc. This renders the EU NMS an important part of global value chains (GVC). From Table 5 it can be observed that foreign value added in a EU NMS country's exports since 1995 – quadrupled for the Czech Republic, ten-folded for Estonia and increased 25 times in the case of Slovakia and was introduced in Lithuania where it was almost non-existent. The EU, however, remains their main trading partner and the largest investor in the new member states, as indicated by Eurostat data.

Table 5: Foreign value added in the gross exports of the selected EU NMS, million USD

	Total				Transport equipment			
	1995	2000	2005	2008	1995	2000	2005	2008
EU 27	91150.8	134550.1	237536.2	402394.5	10078.2	15704.8	25096.9	44557.3
Slovenia	3039.4	3834.2	8718.2	13628.4	481.5	637.5	1404.8	1803
Slovakia	3981.2	6838.2	17257.7	37530.7	429.8	1616	4047.9	10735.8
Poland	4750.4	10255.7	32996	61318.6	387.6	1740.2	7401.8	14109
Lithuania	990	1580.5	5478.8	11013.2	0	25.7	88.6	214
Latvia	431	762.8	2102.7	3943.6	9.1	14.7	42	84.6
Hungary	4939.1	14248.6	31857	50849.3	343.6	2650.8	6864.2	11321.9
Estonia	1065.1	2298.6	4931.1	6141.6	16.7	40.2	162.6	173.8
Czech Republic	8490.2	13387.3	32536.4	55300.6	890.6	2842.6	7446.1	9679

Source: author, based on OECD-WTO, TiVA, 2014.

The openness to trade in goods and services and to FDI inflows of the ten largest EU NMS also substantially increased since the 1990s. The most open economies in 2013 were Estonia, Hungary and Slovakia. For some countries, the share of total trade (sum of export and import) in GDP exceeded 180%, which means that 90% of what was produced within their territory entered cross-border trade. The share of FDI in GDP was smaller, nevertheless significant (5–10% of GDP) and played the role of stabilizer, as indicated in (Bolotov 2012, 2013). For the specifics of the EU NMS balance of payments, consult also Kondrashov and Šíma (2014).

2.4 Case Study of the Czech Republic

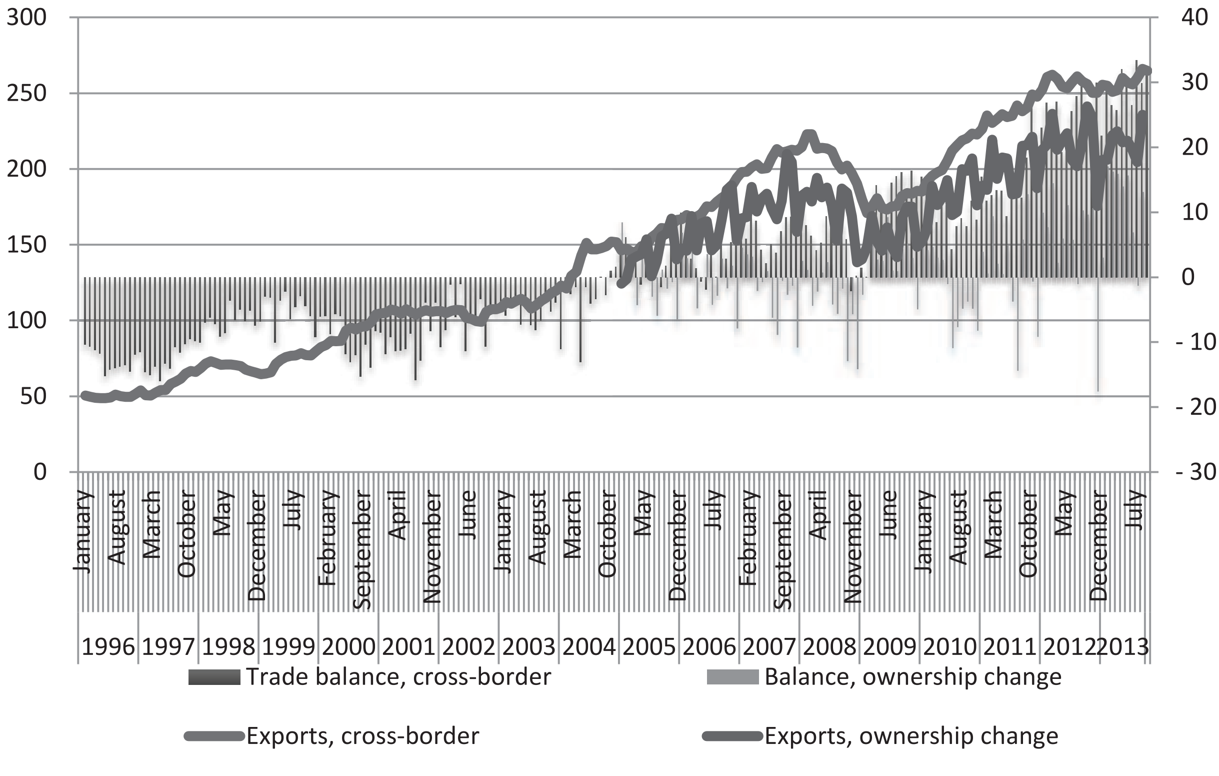
In 2013, the Czech Republic (CR) was the 15th largest and the 11th most populous member state in the EU 27 and EU 28, as well as its sixteenth largest and the 17th most developed economy in terms of GDP and GDP per capita in the purchasing power standard (PPS), according to Eurostat. The economic development of the CR since EU accession has been above par for all basic macroeconomic indicators, as displayed in Table 6. In general, the structure of the Czech economy has not been subject to major changes since 1993 except for ownership, followed by privatization and important FDI inflows. The CZSO (Dubská, 2012) states that foreign capital controls about 97% of assets in the Czech banking sector, and its share in manufacturing turnover surpassed 50% in 2002 and accounts for more than 80% in the automotive industry. Export-orientation and high productivity, a substantially greater share in production (value added, VA) compared with the one in employment, places foreign-controlled companies in a better position when compared to less efficient domestic ones.

Table 6: Economic indicators of the EU NMS and of the Czech Republic, 2004–2012

	EU NMS	Czech Republic
Real GDP growth, %	2.9	2.9
Inflation rate, consumer prices, %	4.1	2.7
Unemployment rate, % of labor force	9.1	6.7
Public debt, % of GDP	38.2	33.5
Current account deficit, % of GDP	-5.9	-2.9

Source: author, based on Eurostat data, 2014.

Figure 1: Statistical discrepancies in the Czech external trade, CZK bn., 1996–2013



Source: author, based on CZSO data, 2014.

The dual economy is especially perceived in retail trade of which, in 2010, 76.5% of turnover was created by the TOP 10 foreign-controlled firms (Machek 2012), while the share of all foreign-controlled companies in the industry's employment was seven times lower, approximately 10% in the same year. As other examples, the three largest Czech mobile operators were acquired by Telefonica / O_2, Vodafone and T-Mobile, and in 2013, 44% of Czech Airlines' shares were sold to Korean Air by the Czech government. Despite important market saturation, Czech industries remain lucrative for foreign companies due to investment incentives and lower labor costs, as indicated in (Bolotov, Čajka, Gajdušková, 2013, p. 71).

New trends in the world economy have had a specific impact on Czech external trade. The value added tax (VAT) registration in the CR enables non-resident EU-based companies to be viewed as Czech exporters and importers. Today, Hungary and the CR are the only EU NMS countries, which experience relatively large differences in cross-border / gross and national (ownership change, residents, non-residents) methods of calculation of external trade. In 2012 the corresponding difference constituted approximately 6% of Czech GDP, consult Figure 1. The main reasons for the discrepancies in the Czech foreign trade are 1) hire of storehouses by non-residents for re-export and transit trade business and 2) intra-firm trade inside multinational and transnational corporations (MNCs and TNCs), which leads to deviations between producer and exporter prices – e.g. automotive products are usually exported via TNC's special trade companies after being purchased from the producer ones in the CR.

3 Conclusion and Managerial Implications

The paper showed that the EU new member states possess certain specifics over the European Union as a whole: rapid development compared to the EU 27, lower general government and private debt, current account deficits and important inflows of foreign direct investment. Their engagement in the new trends of the world economy is, despite these differences, relatively high in terms of openness and foreign value added. They have become an important destination for outsourcing and hence a part of global value chains. It can especially be seen in the case of the Czech Republic, which has a significant share of foreign value added in its exports and is subject to differences between cross-border and national (residents–non-residents) trade.

The development of the world economy is rapid and its new trends represent opportunities in cost reduction or possible threats to companies. Being familiar with recent macro and business changes is important for Central and Eastern European managers in order to efficiently adapt their strategies to the constantly changing business environment and to overcome the current post-crisis slowdown.

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