European Café

The Euro Dilemma: Success in the Baltics, Concerns in the V4

by

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Mr. István Újhelyi, an MEP from Hungary's Socialist Party published an online petition this summer urging a debate on Hungary's accession to the eurozone. Some media reported on the initiative, but a truly groundbreaking public debate has not followed. Since then, the interest has grown: conferences and panel discussions address the euro-dilemma, from various perspectives. Some tend to emphasize the negative experiences of some South-European countries and warn about the risks of giving up controll of the exchange rate. Others point out the inevitability of joining the common currency at a certain point and the vital interests of Hungary's economy being connected to the core of Europe. The pro-euro attitude has a significant public support: despite the anti-Brussels rhetoric of the Fidesz government, the European Union is still popular in Hungary and even the euro enjoys support. According to the latest polls, 52 percent of Hungarians would prefer the common currency and 41 would oppose it.

The governing party, Fidesz, once a keen supporter of the idea of early eurozone accession, is refraining from all public debates. The government is proud of its - self-proclaimed - successful economic record of the last years, which would theoretically enable Hungary to join the eurozone. However, its sovereign decision is not to do so. As the Ministry of National Economy often states, independent monetary policy helped the country overcome the financial crisis, therefore Hungary does not wish to enter the fixed exchange rate mechanism. The introduction of the euro can become only relevant if Hungary's economic development approaches the average of the eurozone, "Momentarily, the introduction of the euro in Hungary is not on the agenda" - reads the official statement of the ministry. Mr György Matolcsy, the President of Hungary's National Bank, also indicated that he saw no urgency and forecasted the date of accession no sooner than 2031.

The Visegrad concerns

Similar arguments are heard in the two other non-euro Visegrad countries, with the notable difference that the euro is suprisingly unpopular in both the Czech Republic and in Poland among citizens and the political elite. While in eurozone-member Slovakia the enthusiasm for the common currency is high, with 80% of popular support, in the Czech Republic only 20% of the society would like to adopt the euro, with 77% refusing it. The image of the euro in Poland is not much better: 32% of the public would vote for it, while 61% are against. One explanation could be that the multiple crises in the euro area undermined faith and questioned the operability of the monetary union. Furthermore, many politicians firmly believe that without an independent monetary policy, keeping their country economically on track would have been significantly harder. Others refer to the unquestionable role of Germany in the decision-making process. As both Czechs and Poles are allergic to alleged German dominance, the euro is often portrayed as a weapon for Berlin to push its economic and political interest through, at the expense of other members states.

It is also worth remembering that the financial crisis itself caused political crises both in the Baltics and in Slovakia, and resulted in the collapse of the Radicova government. This first-hand experience increased poitical concerns regarding the price of hasty accession to the monetary union. It is not only Hungarian PM Viktor Orbán or Polish PiS Leader Jaroslaw Kaczinsky, who are both against deeper integration to the European Union, but the pro-European Tusk government was also hesitant to introduce the common currency in Poland.

Yet long-term perspectives for the euro project in the V4 states are not so gloomy. Out of the three countries, the example of the Czechs is the most interesting. For many, the catching-up of neighboring and often looked down Slovakia with the EU is shocking and enviable. The majority of the public also acknowledge that sticking to the Crown was perhaps not the best idea: it took two more years for the Czech economy to recover, due to the unnecessary devaluation of the Crowns, which was unable to show same adaptive capability as the euro. Business circles also started to criticize the exchange-rate losses, and a number of politicans would be ready – in case of public support – to move towards the European currency. Still, there is a long way ahead: support to join the monetary union has further diminished in the last years.

It is precisely the difference in public support which would enable a Hungarian, a Romanian or a Croatian politial leader to openly stand up for introducing the Euopean currency. The same is not easy in Bulgaria, Poland and in the Czech Republic, due to the negative feelings of the population. Theoretically speaking, and from a purely political perspective, Prime Minister Orbán, if considering the possible financial merits of the latest package offered by the European Commission, could even gain popularity by introducing the issue of joining the eurozone during the upcoming election campaign. However, he is most likely not do so.

The Baltic success stories

Interestingly, the Baltic experiences are rarely referred to in the Hungarian public debate, although the three post-Soviet countries are considered as the prime success stories (along with Slovakia) of the euro accession. Yet it is important to emphasize that all three countries had been hit hard by the economic crisis of 2007-2009 before they adopted the common currency. Stabilization was fast and almost brutal, but - contradicting well-known economic experts like Paul Krugman - effective. In contrast to the often mentioned "bad pupil" of the eurozone, Greece, the three Baltic countries recovered growth and competitiveness in a relatively short time.

In all three countries - Estonia joined the euro in 2011, Latvia in 2014 and Lithuania in 2015 -

it was a clear political decision to adopt the euro and cement their ties to the EU, even defying public opinion which was not convinced about the benefits of giving up the national currency. In Latvia, for example, in 2013 only 45 % of the population supported the euro, but it grew to 53%, after the change of currencies. Latvia is a remarkable success story: the country of 2 million was hit the hardest by the crisis, its GDP falling in three consecutive years by 22%, but already recovering in 2011 with a robust, 6,4% growth, and growing ever since, although with a more moderate rate. Estonia and Lithuania showed the same trajectory but recovered from an equally deep crisis in only two years. Per capita income grew in all three countries and they have been catching up fast with the EU. In 1995 they stood at a mere 28% of EU average, in 2004, when joining the EU, they stood already at 44%, and by now they reached 70% - overtaking Hungary and Poland. Many experts warned about low wages, and skyrocketing prices, but actually wages have increased dramatically: in 2018, Estonia will have a minimum wage of EUR 500; Latvia - EUR 430 and Lithuania - EUR 400. This a considerable

increase if compared with 2016, when minimum wages were set at EUR 430 in Estonia, EUR 370 in Latvia and just EUR 350 in Lithuania.

The average gross monthly wage in Estonia was EUR 1,242 in 2017, Latvia's average gross wage amounted to EUR 927 and in Lithuania it increased to EUR 838. Just to compare it to Hungary: no other country in the CEE region has produced such sluggish development since the transition as Hungary. Starting of as an eminent student in the end of the 1980s, Hungary's per capita GDP stood at 43% of the EU average in 1993, but has climbed only to 63 % by 2015, stagnating for years. Sceptic economist Mr Zoltán Pogácsa often argues that growth will slow down inside the eurozone hindering the process of real convergence or catching up – but the experiences of the Baltics do not confirm this. Another frequent argument is that success stories of small countries (less than 5 million) cannot serve for middle-size economies.

In a regional context, however, the adoption the euro seems like a race. Romania and Bulgaria, which vowed to enter the waiting room of the eurozone, the ERM, would not like to remain on the periphery. Many see the current revitalization of the French-German tandem as a push for deeper integration in Europe, and there seems to be a rush to join the so called "core-Europe", built on the current eurozone. Slovakia already stated that it wants to sit at the Brussels/Frankfurt table where vital decisions on the future of the EU are to be taken. This would clearly weaken the Visegrad Four project. Hungary and Poland (and the countries outside the eurozone) have recently received an "irrefusable offer" from Brussels, a proposal of new funds to accelerate the preparation for the eurozone - but not much official reaction came so far from the government.

Questions:

1. To what extent is joining the eurozone a political or an economic decision? What was the role Russia and a potential Russian threat played in the Baltic decision to join the eurozone?
2. What are the risks to be taken into consideration/is there a price to be paid? And the benefits? Does size matter?
3. How important is public support and can the political elite achieve a wind of change, if yes, how?
4. Is the euro an obstacle of growth and real convergence? What are the perspectives of the Visegrad region if staying outside the eurozone?
5. Would the recent offer from the European Commission make any difference?