

UNICE TASK FORCE ON ENLARGEMENT

**2002 REPORT ON CANDIDATE COUNTRIES' PROGRESS
TOWARDS EU ACCESSION**

CZECH REPUBLIC

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Executive summary

This report presents an analysis of the Czech Republic's progress towards EU accession based on companies' experience of doing business in the Czech Republic.

The Czech Economy has maintained relatively strong growth rates throughout 2001, despite the world economic slowdown, with economic indicators painting a positive picture - not least in terms of Foreign Direct Investment, which remains at record levels. From the business standpoint, the Czech Republic offers an attractive business environment in which companies can prosper. This encouraging outlook is reflected in the Czech Republic's progress towards meeting the requirements of EU accession, which continues in a positive manner.

Nevertheless, further measures must be taken to create a business environment conducive to further economic growth and to ensure that when the Czech Republic joins the EU, it does so without any distortion to the single market. Issues of particular importance to business are:

- Strengthening the Czech Republic's administrative capacity
- Ensuring full legal enforcement of EU rules
- Continuing the fight against corruption

Sustained progress in these areas is pivotal to setting sound foundations for the Czech Republic's accession to the EU. Meeting the above requirements will also depend upon a more consistent and efficient approach to government consultation of stakeholders, of which business is a key constituent.

This report provides an overview of the Czech Republic's progress in key areas. It argues that:

- Speeding up reforms of the legal system – including an improved system of commercial courts and
- Creating a more efficient public administration, with an improved regulatory and law enforcement process
- Improving the competitiveness of the Czech economy through both economic and regulatory measures
- Pursuing the drive against corruption

will all be critical for successful accession to the EU.

Introduction

The Czech Republic continues to fulfil the Copenhagen political and economic criteria for EU membership. It is a functioning market economy and should be able to cope with competitive pressure and market forces within the Union, provided it keeps up the pace of reforms.

The European Commission's 2001 Progress Report on the Czech Republic paints an accurate picture of how much is being done to meet the Acquis communautaire but with uneven progress across the board. This is certainly to be expected, meeting all the Acquis is no easy task. But the business community stands ready to play its part in facilitating the accession process.

The Czech Republic faces election this summer but any changes to the composition of the government are unlikely to reduce the commitment to accession.

Looking to the economy, annual GDP growth declined marginally over the course of 2001 from 3.8% in the first quarter to 3.2% in the fourth. Nevertheless, the average annual growth rate of 3.6% was the fastest annual rate growth in GDP since 1997. Growth largely reflects ongoing gains in manufacturing output offsetting a relative weakening in domestic demand.

Manufacturing output growth rate slowed down over the course of 2001, falling from at an annualised rate of 12.3% in the first to 6.4% by the last quarter. Nevertheless, manufacturing growth for 2001 stood at 7.9% compared with the 4.2% recorded in 2000. Domestic demand also declined throughout 2001, from 5.73% in the first quarter to 4.62% in the fourth. However, in contrast to the manufacturing average, the average growth in domestic demand during 2001, at 5.3% was almost half of the 9.5% recorded in 2000.

Inflationary pressures have built up in the Czech economy, with consumer prices for the whole of 2001 standing at 4.8%, higher than the average of 3.9% in 2000.

On average, unemployment levels have declined moderately as a result of the faster rate of economic growth. In 2001 the unemployment rate averaged around 8.6% compared with 9.0% over the whole of 2001. Worryingly, there was an increase in the fourth quarter of last year to 8.7% from the 8.5% that was recorded in each of the first three quarters of 2001. Whilst relatively high, the Czech average unemployment rate for 2001 is in line with the corresponding European average of 8.3%.

The Czech Republic: the business perspective

From a business perspective, the Czech Republic is already proving a very attractive market and this for a number of reasons. Geographically, the Czech Republic has ready access to both Western and emerging Eastern markets. Furthermore, it benefits from good transport and infrastructure links with both Western and Eastern Europe and 70% of its trade is now with the EU. It has a highly educated workforce with strong engineering skills. IT and R&D spending per capita is the highest in Central and Eastern Europe (and higher than some EU countries). It also benefits from excellent language skills amongst its labour force and competitive labour costs. With liberalisation of the Czech economy, the opportunities are promising.

That said, significant improvements and adjustments are required before the Czech Republic can successfully accede to the EU.

The Czech Republic's Progress towards EU accession

Last year, the UNICE Task Force on enlargement identified a number of key business priorities to ensure successful accession of the Czech Republic to the European Union. These were:

- Intensification of measures against corruption, including better legislation, enforcement, institutional co-operation and border controls
- A faster pace for reforms of the legal system, an improved system of commercial courts and a more efficient public administration
- Reform of the state budget to improve the country's fiscal performance
- Continued progress with privatisation of the banking sector
- Enhanced co-operation with business in introducing regulations
- Improved system for protecting commercial data

A year on, we look back to assess progress in meeting business expectations. We believe that in three key areas, the Czech Republic's current deficiencies are a matter of concern. They do not have the potential to distort the single market, however, companies could be at a competitive disadvantage if the situation is not redressed in time for EU accession. For the business community the priorities for 2002 are twofold:

- Intensifying the fight against corruption,
- A faster pace for reform of the administrative and legal framework.

2002 being an election year should be used as an opportunity to address these priorities and not be used as an excuse to dodge them. These are the expectations of the business community. Without significant progress in these three areas, the Czech Republic's accession to the EU will not prove successful.

Intensification of measures against corruption in the Czech Republic

The Czech authorities have taken a number of measures to fight corruption but the situation continues to be of concern. Companies in the Czech Republic identify corruption as a significant obstacle, if not a threat, to their operations and business interests. Corruption acts as a deterrent to business activity by making it more difficult and costly for companies to operate and thus undermines the competitiveness of the Czech economy.

Although much has been done to facilitate investigation and prosecution of corruption and economic crime, efforts to achieve an effective policing system must be redoubled. The forthcoming elections provide an opportunity to further raise the profile of the fight against corruption.

A faster pace for reform of the administrative and legal framework

The Czech Republic has experienced a changeable legislative framework and this has worked against establishing a level playing field by EU standards. Although the Czech Republic's efforts to meet the Acquis are progressing, an inefficient administrative framework and regulatory process undermine this progress. The issue of commercial registers is a case in point. Administrative inefficiency results in higher operating costs to business, which reduces competitiveness.

There is a climate of legal uncertainty, which works against the Czech Republic's successful accession to the EU. This problem has been visible in the context of the Czech Republic's commercial code. Frequent amendments to the regime and varying jurisprudence across the country create a contradictory system for Czech business law. Legal redress in the Czech Republic must be made more efficient and the UNICE Task Force on Enlargement supports the recommendations of Sir Anthony Colman to have specialist commercial judges and a wholesale review of the hearing process as well as better training for the Courts.

Better regulation is no doubt an area where even the EU has yet to deliver higher standards, nevertheless some of the laws in the Czech Republic do nothing to improve the legislative framework. Present bankruptcy provisions in the Czech Republic need to be reformed in line with the European Commission and the World Bank's own recommendations. Serious legislative reviews need to be carried out in the field of competition policy. The Czech Republic has good anti-trust laws but they need to be implemented more effectively and a stronger infrastructure needs to be developed to administer the laws. Procurement rules need to be restructured to create greater flexibility. Furthermore, greater transparency in the way in which the Czech authorities operate would go a long way towards improving the legislative environment. Consultation with stakeholders is still insufficient across the board and Czech regulators need to be more open in their dialogue with the business community.

Conclusions and recommendations

UNICE supports the Czech Republic's accession to the EU as soon as it has fulfilled all the Acquis communautaire. Progress is still required where problems remain and the current report identifies priority areas:

- Speeding up reforms of the legal system – including an improved system of commercial courts.
- Creating a more efficient public administration, with an improved regulatory and law enforcement process.
- Improving the competitiveness of the Czech economy through both economic and regulatory measures.
- Continuing the drive against corruption.

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