An Chomhairle Náisiúnta Eacnamaíoch agus Shóisialta
National Economic & Social Council
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BACKGROUND PAPER

6. The Fifth EU Enlargement and Ireland

by John Sweeney

An Oifig Náisiúnta um Fhorbairt Eacnamaíoch agus Shóisialta
National Economic & Social Development Office NESDO

An Chomhairle Náisiúnta Eacnamaíoch agus Shóisialta
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Abbreviations

CAP
Common Agricultural Policy

CEEA
European Economic Area

EU
European Union

EU-10
The member states that joined the EU in 2004: Czech Republic, Cyprus, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovakia, Slovenia

EU-12
The member states that joined the EU in the enlargement of 2004 and 2007: i.e.: the EU-10 plus Bulgaria and Romania

EU-15
The member states that comprised the EU before the enlargement of 2004: Austria, Belgium, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Luxembourg, Netherlands, Portugal, Spain, Sweden, and United Kingdom

FDI
Foreign Direct Investment

GDP
Gross Domestic Product

NMS
New Member States

ODI
Overseas Direct Investment

OMC
Open Method of Co-ordination

OMS
Old Member States

PPS
Purchasing Power Standards

PWD
Posted Workers' Directive

SM
Single market

TA
Transitional Arrangements

UK
United Kingdom

USA
United States of America

USSR
Union of Soviet Socialist Republics

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BACKGROUND PAPER

The Fifth EU Enlargement and Ireland

6.1 Introduction

This Chapter opens (Section 6.2) with a summary reflection on the significance of the EU's Fifth Enlargement which embraced twelve new states in 2004 and 2007.[1] Section 6.3 reviews the impact of this Enlargement on economic prosperity across the region, paying specific attention to its effects on trade and investment flows and to the significance of East-West labour migration. Further sub-sections discuss the impacts of this labour migration on national labour market standards and national welfare states respectively, and articulate some of the challenges that still attend 'bedding down' this recent Enlargement successfully at the EU level. Section 6.4 explores how Ireland has been affected and examines, in first place, the impact on trade and investment flows. Labour migration from the new Member States increased Ireland's workforce at a much faster rate than elsewhere—four times faster than in the UK, the second most affected country, and some fourteen times faster than the average for the EU 15[2]. The scale, composition and impacts of East-West migration into Ireland and how it is now being impacted by recession are, therefore, given extended treatment. A final Section 6.5 underlines the need for public policy and public opinion be prepared well in advance for further enlargements of the EU, and for Ireland to play a proportionate role in influencing their timing and circumstances.

6.2 The historic nature of the Fifth Enlargement

In 1993, an EU Summit in Copenhagen opened formal negotiations on membership with twelve countries, ten of whom - in Central and Eastern Europe - had only recently emerged from communist government, central planning and tutelage to the former USSR. It was the most ambitious and far-reaching enlargement the EU had yet attempted. Economic objectives were secondary to political concerns such as the need to consolidate democracy, the rule of law and political stability on the Union's eastern borders. It was not the first enlargement driven by political rather than economic concerns. In the early 1980s, negotiations on membership had opened with Greece, Spain and Portugal to support their fledgling democracies – the three countries had recently emerged from dictatorships - as well as on grounds of mutual economic interest. In 1993, however, it was more apparent still that the EU was

1 Formally termed the 'fifth' enlargement, it occurred in two steps - 2004 when Cyprus, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovakia and Slovenia acceded and 2007 when Bulgaria and Romania followed. The four previous enlargements were the UK, Denmark and Ireland (1973); Greece (1981); Spain and Portugal (1986); and Austria, Finland and Sweden (1995).

2 See Table 6.10.

acting primarily out of geo-political concerns and a sense of historical obligation rather than as an economic bloc. Negotiations followed that the acceding countries found difficult and disillusioning at times, as the EU 15 sought to protect their own economic and social achievements and ensure that the candidate states would be able to comply with the obligations of membership. But the fifth enlargement went ahead primarily because it was 'the right thing to do' and not because major economic and social gains could be demonstrated for the EU 15 in an EU of 27.

With a significance that became apparent only with time, the year in which the green light was given for the Fifth Enlargement coincided with the beginning of Ireland's 'Celtic Tiger' period. During the twelve years in which the candidate states negotiated and prepared for entry, Ireland's economy grew strongly, Irish living standards converged on, and then surpassed, the average for the EU 15, and significant progress was made in bringing Ireland's infrastructural endowments to the levels of its EU neighbours. By the time the formal accession of ten of the states occurred under an Irish presidency in 2004, the Irish economy was considered one of the most impressively performing in the EU 15. This status contributed to the government decision of the time to seek no postponement in opening Ireland's labour market to nationals from the new member states (one of only three existing member states to do so, along with the UK and Sweden). The scale of labour mobility into Ireland from the new member states that subsequently occurred was not only unforeseen but became one of strongest reminders for Irish people of the deep nature of the EU (comparable, for example, to the adoption of the euro, travel without frontiers, etc.).

The EU's fifth enlargement was a risk, for several reasons.

In the first place, it risked reigniting tensions between the deepening and widening of the EU. The emergence of the states of Central and Eastern Europe from behind the 'Iron Curtain' had taken the political leadership of the European Union by surprise. At the time, they were focused on the programme to complete the Internal Market, an agenda for 'deepening' that was to advance and include monetary union and institutional change. Germany, the most natural and powerful ally of eastern enlargement, had to concentrate for a period on the challenges of unification. In the initial years, therefore, it was pressure from the new leaders in the east that ensured membership rather than a new 'EFTA for the east' or some other form of privileged association became the objective. But the potential remained for some time for EU 15 elites to split between those who considered that enlargement would slow down further integration in the Union and those who gave priority to extending the area of peace and stability in Europe (Mayhew, 2007).

In second place, the EU was admitting new members whose living standards were further behind those of existing Member States than in previous enlargements. At the time of the southern enlargement, Greece, Spain and Portugal had per capital income levels (PPS adjusted) around 65 per cent of the existing Member States. By contrast, the ten States acceding in 2004 had an average per capita income some 45 per cent of the EU 15 level, ranging from as low as 34 per cent in Latvia to 70 per cent in Slovenia. Romania and Bulgaria who acceded in 2007 were poorer still with GDP per capita (PPS) 30 per cent of the *EU 25* average in 2004.

In third place, the fifth enlargement was a risk because no previous enlargement had increased the complexity of the EU's decision-making and operational procedures to the same extent. Increasing the number of Member States from 15 to 27 had myriad consequences for meeting formats, official languages, decision-making, and other formerly settled procedures (Hagemann *et al.,* 2007). It also entailed the particular challenge for the Community's institutions and the new member states of jointly recognising and addressing particular legacies of their communist pasts in multiple areas of their civic and political life. The proportionate increment in the EU's population brought about by this enlargement was large but not unprecedented. The population of the EU 27 is some 26 per cent larger than that of the EU 15 (though the new states added only 7 per cent to the latter's GDP). This is more than the 20 per cent the southern enlargement added to the then EU 12 but smaller than the 34 per cent increment that the entry of the UK, Denmark and Ireland brought to population of the founding Six in 1973. In absolute terms, however, the recent enlargement has been unprecedented for the absolute number of people who became EU citizens and, thus, in its scale impact on the Single Market.

A final reason why a risk element can be considered to have attended the eastern enlargement is that, despite its strong historical and moral underpinnings, there was significant popular apprehension in the existing Member States at some of the likely 'costs'. For example, in 2002, only 29 per cent of the EU-15 citizens believed that enlargement would help create jobs in their country, 48 per cent believed it would trigger a major wave of migration from Central and Eastern Europe, and 70 per cent were worried that such a development would lead to an increase in unemployment and crime, and a lowering of living standards (Eurobarometer, 2002).

Partly in recognition of these popular misgivings, existing Member States – as they had first done when Greece, Spain and Portugal joined the EU in the 1980s - applied for a temporary exemption from having to open their labour markets to job-seekers from the acceding Member States. 'Transitional arrangements' (TAs) allow existing Member States to continue to require work permits of nationals of the new Member States, in temporary contravention of the EU's principle of free movement for workers.[3] Twelve of the EU 15 Member States adopted TAs, motivated by a concern that the large gap in earnings and living standards would prompt labour inflows on a scale that could disrupt their labour markets.[4] An associated concern was that seeking work would masquerade as a tactic for accessing the benefits of their welfare states. The UK and Ireland, though not applying TAs, introduced new restrictions on accessing means-tested benefits; in keeping with EU law, these new restrictions did not discriminate against claimants from the NMS but applied to everyone.[5]

3 The TAs were based on a 2-3-2 formula: for the first two years following accession, access to the labour markets of the OMS depended on their national laws and policies; these national measures could be extended for a further three years; after five years, should a MS find that its labour market had been severely disrupted, the measures could be extended for a final two years.

4 Member States which adopted TAs in 2004 towards the EU 8 have lifted them as follows: Greece, Spain, Portugal and Finland (May, 2006), Italy (July, 2006), the Netherlands (May, 2007), Luxembourg (November, 2007), France (July, 2008), Belgium and Denmark (May, 2009), Germany and Austria continue to impose labour mobility restrictions until 2011 [Kahanec & Zimmermann, eds., 2009: 5].

5 Britain closed off welfare benefit to nationals from Accession states for a period of two years. Ireland followed with the 'habitual residency condition'. It imposes a two year residency requirement within the Common Travel Area on *anyone* seeking application for a range of social assistance (non-contributory) payments: "it shall be presumed, until the contrary is shown, that a person is not habitually resident in the State at the date of the making of the application concerned unless he has been present in the State or any other part of the Common Travel area for a continuous period of two years ending of that date")Section 246 of the Social Welfare Consolidation Act 2006).

6.3 Enlargement and the EU's economy

6.3.1 An overview

Despite the elements of risk in the Fifth Enlargement and the extent of popular misgivings in the EU 15, overall assessments of its economic impact, on the EU as a whole and on old and new Member States (OMS and NMS) considered separately, are positive. Important questions remain, however, as to how equitably the aggregate net benefits have been distributed within Member States. In particular, as the literature on the economic impact of migration would lead one to anticipate, concerns attach to the position of low-skilled workers in the EU 15. They have faced particularly intense competition from the mobile low-skilled in the NMS *and* from higher educated NMS migrants who have been willing to work in the OMS in relatively low skilled occupations.[6]

The key elements that emerge from a detailed analysis by the Commission of the economic achievements and challenges five years after the 2004 Enlargement (European Commission, 2009a)[7] are as follows.

(i) The enlargement increased the overall weight of the EU-27 in world GDP (by around 2.5 percentage points in purchasing power standards), and augmented the scale of the Single Market (SM). This has strengthened the voice of the EU in global economic governance. In particular, by introducing greater heterogeneity and diversity within the EU, the enlargement has enhanced the potential for the SM to function as a standard- and performance-setter and, thereby, to contribute indirectly to strengthening the capabilities of companies, workforces and national institutions in confronting globalisation. It has accelerated economic restructuring and factor flows (capital and labour) within the SM, improving efficiency and keeping some resources within the EU that otherwise would have moved outside it. These synergies and greater economic dynamism continue to hold out the prospect that Member States and the Union are being spurred by the on-going challenges of this enlargement to find better answers to the challenges posed by globalisation.

(ii) The new Member States (NMS) have reaped clear political benefits that started from the time the prospect of membership first came on the agenda of their governments. These benefits include the increased security on key frontiers, the strengthening of democracy and the rule of law, and the increased responsiveness of their public institutions to citizens.

(iii) The NMS have also reaped significant economic benefits. The Cohesion funds, CAP transfers, and preparation for, and participation in, respectively, the Single Market, the Stability and Growth Pact and the Lisbon OMC have fostered market reforms, company restructuring and labour market policies that have strengthened their economies. These have become more open to trade, received much larger inflows of foreign investment and benefited from stronger institutional frameworks they were required to develop. Headline indicators of relative EU 10 success include:

6 It is not always noted that these 'incumbent' low-skilled workers frequently include significant numbers of non-EEA migrants who had arrived earlier.

7 'Five years of an enlarged EU. Economic achievements and challenges'. *European Economy 1/2009*.

- Income per capita in the new Member States rose from 40 per cent of the EU 15 average in 1999 to 52 per cent in 2008;
- Their economic growth rate increased from an annual average of between 3.5 per cent, 1999-2003 to 5.5 per cent in 2004-08;
- Employment has grown robustly at about 1.5 per cent per annum since 2004; and
- Their earnings have risen, while remaining highly competitive. Wages per employee rose from 14 per cent of the EU-15 average in 1999 to 26 per cent in 2007.

(iv) The principal economic benefits to the old Member States (OMS) arise from how companies based in them have responded to the geographic extension of the Single Market and to the faster growth and rising incomes in the NMS. In effect, the EU 10 have stimulated and sustained growth in the EU 15, nearly all of whom run large trade surpluses with them. The Commission's study found that many EU-15 industries and companies took advantage of the favourable cost differentials of the new Member States, good location opportunities and cultural ties to split their production chains and engage in vertical specialisation (prominent examples are the automotive and ICT industries). It further notes that, while the prospects for relocation are largest in the efficiency-seeking manufacturing sector, some 70 per cent of the outward direct investment from the old to the new Member States has been in the services sector and of the market-seeking type. Generally, the Commission's findings on ODI by the EU 15 in the EU 10 support the more generalized finding that companies which engage in it frequently retain higher value home operations that then subsequently expand.[8]

(v) The prospect of major East-West migration, as noted, was - and remains - a major concern of many people in the EU. In effect, the overall level of migration over the first five years was significant but in line with the more conservative predictions (though the destinations of migrants were different than predicted). There was an estimated increase of 1.1 million in the number of EU 10 nationals living in the EU 15 over the period 2004-08, and a similar increase in the number of Romanians and Bulgarians through they joined as late as 2007. For the EU 15 as a whole (though not for Ireland as will be discussed below), the increase in the resident population of third country nationals (those from beyond the EU 27 and EEA) was larger still and rose by an estimated 3.4 million. The evidence on the specific impact of the increased intra-EU migration will be reviewed in 6.3.3 below.

6.3.2 Impacts on trade and investment

The decade of the 1990s was the more intense period of economic transformation in Eastern Europe. In the nineties, most of the liberalization in trade with the EU 15 took place and a strong shift of trade flows was recorded. Enlargement in 2004 added an additional impetus to a process that was, therefore, well underway. A further

8 The Commission also believes that the repatriation of profits from ODI had a significant countercyclical element. Between 2003 and 2006, for example, higher domestic demand growth in the EU 15 appears to have been accompanied by lower growth in income from FDI, suggesting it was less necessary to repatriate profits to smooth income. They speculate that, come a severe downturn in the mature economies, income from ODI will rise to compensate for smaller profits in the home economies.

contextual factor affecting the search for specific enlargement impacts on trade and investment is that, for reasons quite independent of EU developments, 2004 marked the transition from a period of subdued world trade to a period of stronger growth. In most regions in the world, trade grew faster after 2004 than in the preceding five-years, and this was the EU experience also. Trade volumes in the OMS increased from an annual average growth rate of 4.4 per cent between 1999-2003 to 6 per cent between 2004-2007, and from 6 per cent to 12.8 per cent in the NMS (European Commission, 2009a: 59). The greater weight of global over EU developments in driving EU trade is confirmed by the fact that extra-EU trade grew by an annual average rate of 10.4 per cent over the period 2004-'07 compared to 8.7 per cent for intra-EU trade.

The specific effects of enlargement on Ireland's trade and investment flows will be examined below. It is worth noting at this stage, though, that several Member States have a higher degree of reliance on trade with markets outside the EU than Ireland. In 2007, 34 per cent of Ireland's total goods trade (exports and imports) was outside the EU 27, and the remaining two-thirds within it (Eurostat, 2008)[9]. Seven Member States had a higher reliance on extra-EU trade than Ireland, the UK the most (44 per cent) followed by Italy, Greece, Bulgaria and Finland (all with shares of 40 per cent or over). On the other hand, one-half of the MS had a greater reliance on EU markets than Ireland; the share of total trade that was intra-EU was as high as 80 per cent in the Czech Republic, Slovakia and Luxembourg. The relative reliance of Ireland's goods trade on markets inside and outside the EU, therefore, was approaching 'normal' and similar to Germany, Sweden, the Netherlands and France.

These observations underline how important links with the emerging new regions in the global economy (China, India, Brazil and Russia, etc.) are to the development of trade and investment flows in many Member States (in particular among the EU 15). At the same time, the observed pattern in developments is also consistent with the thesis that the increased scale and diversity which enlargement has brought to the Internal Market is positive for the competitiveness of EU-based businesses in the global economy.

Export destinations and market shares

Changes in the destinations of the exports of the old and the new Member States since 2004 and the extent to which they are increasing or losing market share can throw some light on how 2004 has affected the integration of the OMS and NMS economies with each other and with the rest of the world.

Table 6.1 establishes that, for the OMS as a group, exporting to each other has declined in significance (by four percentage points between 1999 and 2007) and that most of the difference was made up by the growth in importance of the NMS (up three percentage points). For the NMS as a group, the significance of OMS markets for their exports declined by a full nine percentage points, while the significance of exporting to each other increased by over six percentage points. This acceleration in export trade among the NMS almost all occurred after enlargement, 2004-2007. Both the OMS and NMS recorded a slight decline in the significance of the USA as an export market but more than a doubling (though from a small base) in the significance of China. The NMS record much the stronger shift towards export markets elsewhere in the world (up by nearly four percentage points) than the OMS (a rise of 1.4 points).

9 Eurostat (2008), 'International Trade of the EU in 2007'. *Statistics in Focus* 92/2008

The progress being made by the NMS emerges more clearly in Table 6.2. It shows that the NMS increased their share of export markets most of all among themselves (an increase from 10 per cent to 17 per cent over the period 1999 to 2007) but also in the Old Member States (up 3 percentage points)and the rest of the world (up 1.8 points). Their increase in export market share in the EU-15 occurred primarily before accession but the pattern of stronger regional integration through trade among themselves that was significant before 2004 became even stronger in the following years. By contrast, the Old Member States have been losing export market share everywhere – admittedly from high levels – with the decline sharpest in the NMS and the Rest of the World and least in trade among themselves.[10]

International trade and investment links that grow primarily because overseas markets are expanding and providing opportunities for indigenous companies to increase business are welcomed by those representing domestic labour interests. The extent of the gap in wages and living standards between the NMS and the OMS, however, (as already noted) generated concerns that significant trade distortion and not just trade creation could occur if companies in the OMS switched the base of their operations from their relatively high-cost home countries to the NMS and

Table 6.1 Geographical Destination of Exports, Old and New Member States, 1999-2007

	1999	2003	2007
Old Member States (OMS)	%	%	%
To OMS	63.4	62.1	59.5
To NMS	4.7	5.7	7.5
To USA	8.7	8.6	7.3
To China	0.9	1.6	2.0
To Other	22.3	22.0	23.7
	100	100	100
New Member States (NMS)			
To OMS	68.6	67.1	59.7
To NMS	13.2	14.1	19.5
To USA	3.6	3.2	2.1
To China	0.3	0.6	0.7
To Other	14.3	15.0	18.0
	100	100	100

Source European Economy 1/2009: Tables III.1.3 and 4.

10 Not shown in the Table, but commented on by the Commission (op. cit, 63-64), is the divergence of OMS experiences. For example, of the larger OMS, the Netherlands increased its world export share, while Germany maintained a relatively stable position and the United Kingdom, France and Italy recorded significant slippage. Prominent factors that help explain this divergence, the Commission believes, include the stronger ties of some OMS countries to dynamic emerging markets and their more intensive engagement with the recomposition of global supply chains (e.g. by off-shoring).

Table 6.2 Export Market Shares of New and Old Member States, 1999, 2004 and 2007

%	World			Old Member States			New Member States			Rest of the World		
	1999	2004	2007	1999	2004	2007	1999	2004	2007	1999	2004	2007
NMS	2.10	3.28	2.90	3.83	5.97	6.98	10.35	13.50	17.29	0.64	1.05	1.30
OMS	39.49	37.84	34.33	66.67	64.87	61.10	68.95	59.77	58.30	21.08	20.43	18.24

Source European Economy 1/2009: 63.

chose to export from there onwards to third country destinations and back into their home markets. Countervailing arguments were put forward to assuage these concerns, principally that it is the productivity of labour in the NMS which determines whether they are 'low cost' locations and not their absolute earnings levels, and that rapid wage increases in the NMS could be expected to erode any initial advantage arising from earnings alone quite quickly.

One way of testing whether the relatively low wage levels in the NMS have been a major factor driving the growth in their exports is to examine the composition of those exports. Prior to enlargement, it was expected that the new Member States would take advantage of their lower labour costs and become more specialised in labour-intensive products. As Table 6.3 confirms however, the expectation was not borne out by what subsequently happened. While there is significant diversity among them (as the contrast between Hungary and Poland in the Table shows), the NMS as a group have seen a decline of eight percentage points in the share of their goods exports classified as 'labour-intensive' from 28 per cent in 1999 to 20 per cent in 2006. At the same time, the shares classified as 'capital-intensive' and 'easy-to-imitate research-intensive' increased to 25 per cent (up three) and 15 per cent (up four) respectively. The share classified as capital-intensive goods also rose from 22 per cent to 25 per cent between 1999 and 2006, surpassing the share for the OMS. This is attributed mainly to the FDI-induced rise of the automotive sector in the NMS. Potentially of particular interest to Ireland, given that trade flows are more likely to occur between economies with similar structures than between those which are dissimilar, is the fact that the shares of exports classified as 'difficult-to-imitate research intensive' had become similar in the NMS and the OMS by 2006 (with Romania achieving the most rapid progress).[11]

Role of foreign direct investment (FDI)

The fifth enlargement of the EU was expected to result in increased foreign direct investment in the new Member States for a variety of reasons. Some were common to all the NMS from Central and Eastern Europe, i.e., increased investor confidence, the improved business environment and the expectation of strong growth in the region as a whole. Some were specific to individual countries, i.e., the size and dynamism

11 When the Commission use a different but related metric, i.e., the technology-intensity of manufacturing exports, is used, the same high degree of convergence in the export composition of the NMS and OMSs is seen to have taken place over the period 1999-2006 is observed (and the greater variance among the NMS than between the two groups) (Appendix Table 6A.1).

of their domestic markets and their proximity (geographical and cultural) to the home country of the investing company ('gravity models' have, in fact, explained a significant part of the FDI that occurred across the NMS). Some of the FDI was by companies in the OMS that either shifted labour intensive parts of their production to the NMS to contain costs and strengthen their ability to compete globally, or sought to supply markets in the NMS (for goods and services) by establishing there rather than exporting. Finally, some of the FDI came from outside the EU as companies in other parts of the world chose these member states as their preferred foothold inside the Internal Market or were newly encouraged by their accession to supply NMS home markets by establishing a presence there rather than exporting.

Inward foreign direct investment (FDI) as a proportion of gross fixed capital formation has been consistently much higher in the NMS than in the OMS since the mid-1990s. Following enlargement in 2004, it further increased in the NMS (as a percentage of GDP) and decreased in the OMS (Figure 6.1) as companies from the OMS and the rest of the world responded to the improved investment climate and relatively strong economic growth in the region. The Commission considers that the proportion of this inward FDI that was a straightforward relocation from OMS has been small to date and taken the form of efficiency-seeking in selected manufacturing industries, and that this type of investment was far from being 'a common or prevailing pattern' (op. cit. 96). Since 2004, in fact, FDI to the NMS has grown more rapidly in services than in manufacturing, most of which is considered to be market-seeking rather than export-oriented. However, of particular interest to Ireland may be the observation that the NMS ' are becoming increasingly popular locations for [European] shared services centers' (supplying accounting, HR admin, software maintenance and sometimes research to subsidiaries across the EU owned by the same parent company) (op. cit.. 92).[12]

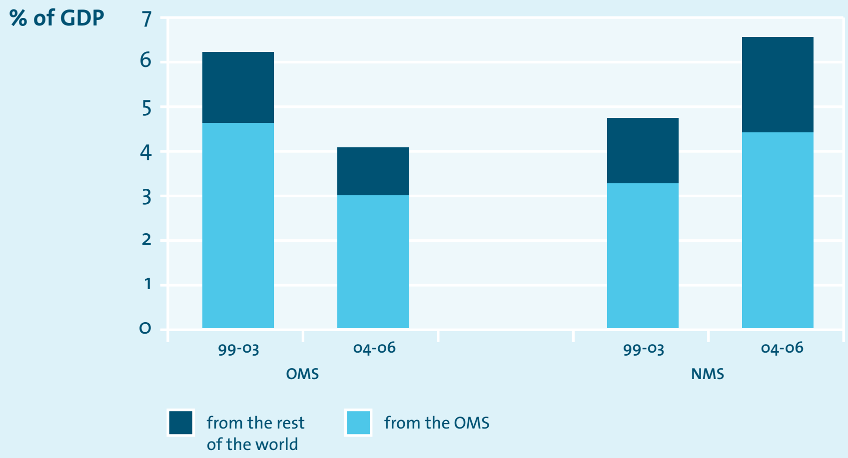
While the surprisingly high technological composition of exports from the NMS is attributed in a major way to the scale of the inward investment they received, the

Table 6.3 Break down of Total Exports by Factor Intensity

	Raw-material-intensive goods (RMI)			Labour-intensive goods (LI)			Capital-intensive goods (CI)			Research-intensive Goods: Difficult-to-imitate (DIR)			Research-intensive Goods: Easy-to-imitate (EIR)		
% of total	1999	2004	2006	1999	2004	2006	1999	2004	2006	1999	2004	2006	1999	2004	2006
NMS	14	14	14	28	23	20	22	23	25	25	26	26	11	14	15
OMS	12	13	15	19	17	15	22	23	23	29	28	27	19	19	20
HU	11	10	9	18	12	10	15	13	16	30	32	35	26	33	30
PL	18	16	16	34	25	22	21	25	27	21	26	26	7	7	9
RO	18	16	19	47	41	32	16	18	20	16	20	25	4	5	5

Source European Economy 1/2009: Table III.1.5.

Figure 6.1 Inward FDI in the Old and the New Member States



Source European Economy 1/2009: 38.

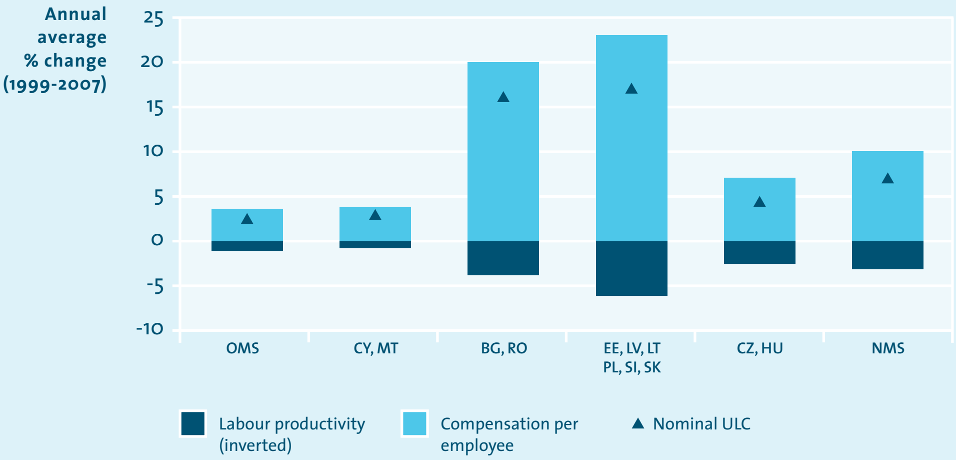
attractive power of the NMS has to be set against the continuing attractiveness of other locations in the world economy for EU-based companies engaging in overseas direct investment (ODI). The most recent data suggest that such locations have been exercising the greater attraction; the share of ODI of Member States that has gone elsewhere in the EU decreased from 61.5 per cent to 55 per cent over the five years, 2004-'08 (Eurostat, 2009). Ireland's experience was near the EU average in this also, with just over one-half of Irish ODI going elsewhere in the EU 27 in 2008 (op.cit.).[13]

In addition to its significant direct effects in boosting output and the level and quality of NMS exports, FDI is considered to have had important indirect effects in boosting the productivity of indigenous NMS firms. It has done this by stimulating them to imitate the products and organizational methods that inward investors brought with them, 'passing on' experienced employees (a consequence of churn in the labour market), and buying from and selling to indigenous businesses (backward and forward linkages).

A significant consequence of this FDI influence on the composition of exports is that the NMS have been able to record the significantly increased export market shares described above despite a *decline* in their cost competitiveness (Figure 6.2). Tightening labour market conditions (caused by the strong growth in GDP and the migration of workers) boosted earnings beyond what productivity gains could offset and the NMS were unable to retain their initial levels of cost competitiveness. However, by transforming the composition of exports from the NMS to the degree described above, FDI contributed to countering the effects that the sharp acceleration in nominal wages in the NMS might otherwise have

13 When the related but different question is asked, i.e., what share of foreign direct investment (FDI) coming into the Member States comes from elsewhere in the EU and what share comes from beyond it, the same pattern is evident. The share of FDI coming into the MS from elsewhere in the EU declined from 76 per cent to 65 per cent over the period, 2004-'08, and the corresponding share coming from beyond the EU rose from 24 per cent to 35 per cent.

Figure 6.2 Nominal Unit Labour Costs and its Components



Source European Economy 1/2009: 127.

had on their capacity to export. By contrast, the old Member States lost market share though the deterioration in their cost competitiveness was much smaller than in the NMS. The correlations between market share developments and price and cost competitiveness of the two groups of countries have, if anything, been counterintuitive.

By way of summary to this subsection, evidence on the destinations and composition of goods exports points to a convergence in economic structures taking place quite rapidly between the NMS and OMS[14]. An examination of foreign direct investment flows confirms the major role of FDI in driving this convergence. Before enlargement, it was expected that the new Member States would increase specialisation in labour-intensive products to take advantage of their lower labour costs. Contrary to expectations, large flows of FDI led to a significant increase in the technological content and product quality of the export basket of the new Member States. This qualitative upgrading of production in the NMS is one of the most characteristic impacts that EU accession has had on their economies.

6.3.3 Impacts of East-West migration

The Commission has informed its assessment of the specific impacts of the large East-West movement of workers triggered by enlargement by conducting simulations using its QUEST model of the EU economy (D'Auria *et al.*, 2008).[15]

14 There is greater variation among the NMS in the composition of their exports by factor intensity than between the NMS and OMS as groups. For example, over one-half of Romanian exports were either 'raw-material-intensive' or 'labour-intensive' in 2006, but less than 20 per of Hungarian exports, while Romania and Poland had much smaller shares of their exports termed 'easy-to-imitate research-intensive' than Hungary (under 10 per cent as against 30 per cent).

15 It is important to note that models do not describe what actually happened or seek to predict out of sample. Rather, they seek to provide insight into the contributions that key factors made to the actual historical outcome, however much other events and factors not captured (or capturable) by the model may also have impacted. They seek to isolate and quantify the specific effects of changes in selected variables of interest on the basis of a structural model of the economy which incorporates the best available knowledge on how the actual economy works.

As Table 6.4 shows, the GDP effect on the EU25 as a whole of the recent intra-EU mobility appears substantial and positive and is estimated to be 0.27 per cent of GDP. The study's authors note that this implies it was more potent, in economic terms, than a one percentage point increase in the EU25's investment to GDP ratio. However, whilst positive for the EU25 as a whole, both the literature and empirical research suggest that that migration has potentially less clear-cut effects for the sending (NMS) and receiving countries (OMS) when they are considered as separate groups.

Considering the NMS on their own, the simulation results point to the possibility that the labour outflow had a negative effect on aggregate GDP but positive effects on real wages, productivity and GDP per capita (Table 6.4). The latter effects would have been brought about by induced capital deepening (D'Auria *et al.*, 2008). The results also suggest (not shown) that, by contributing to emerging labour shortages, the labour outflow prompted a (temporary) increase in inflation in some of the main sending countries.

For the OMS, the simulation results suggest migration from the EU10 countries increased aggregate GDP. However, the effect on GDP per capita is slightly negative (-0.12, Table 6.4), reflecting the lower productivity / lower real wages associated with the migration shock as labour became more abundant relative to capital and provoked a reduction in the capital intensity of production.

In a separate simulation, the Commission team replaced the assumption that migrants work in jobs with the same skills composition as the local population with the assumption that they are more concentrated in lower skilled employments. The results then confirm what the literature leads one to expect,[16] i.e., higher rates of unemployment and lower real wage growth for the low skilled in the EU15.

Despite this, generally, non-alarmist picture of the impact of enlargement on employment and living standards in the OMS, there is evidence that the new element of labour mobility which it introduced across the EU continues to cause concerns, particularly in the OMS. Public perception appears to consistently over attribute migration to push factors and underestimate the role that the demand for labour in its own country is playing (Beutin *et al.*, 2007). Perceptions of migrants and their integration interact. Where people perceive migrants are in their country uninvited and not needed, the integration of the migrants is more difficult (op. cit). A follow-up Eurobarometer survey on enlargement carried out in 2006 found that several of the concerns voiced prior to enlargement still remained (Eurobarometer 2006). It believed that broader concerns with the consequences of globalization appeared to be functioning as a prism through which populations in the EU 15 were viewing the effects of enlargement. The comprehensive 2009 Commission study concurs with this. It believes enlargement has reinforced 'a family of issues that have emerged through Europe's encounter with the broader process of globalisation' (European Commission 2009a: 25).

16 "As a rule of thumb, natives in the receiving countries tend to win if the migrant labour force has at least the same skill level as the native labour force, and to lose in the converse case" (Brücker, 2007). If the receiving country employs a substantially higher share of the migrants than of native workers in low skilled jobs then "those at the bottom of the income distribution in the recipient countries tend to lose through lower wages and higher unemployment".

Table 6.4 Medium-term Economic Effects of Recent Intra-eu Mobility Flows on Receiving and Sending Member States

Changes in percent from baseline	GDP	GDP per capita	Productivity	Real Compensation of Employees	Employment Rate
NMS	0.38	-0.12	-0.13	-0.12	0.01
OMS	-2.23	0.28	0.42	0.46	-0.14
EU	0.27	0.27	0.27	0.28	0.04

Notes (i) The core assumption is that there is no change in skill distributions between migrants and the local population. (ii) NMSs except Bulgaria and Romania. (iii) Employment rate: change in percentage.

Source D'Auria, Mc Morrow and Pichelmann, 2008 (cited in European Economy 1/2009: 137).[17]

The study concluded that making an economic and social success of the recent enlargement will equip the EU better to meet the challenges of globalisation: 'in reality, 'the adjustment challenge posed by the fifth enlargement is not so very different from the structural changes that are called for in the vigorously unfolding process of globalisation' (op.cit. p25).

6.3.4 Enlargement and labour market standards

Independently of the Fifth Enlargement, there was unfinished business in some areas regarding how to reconcile the autonomy of national labour market institutions and regulations with Treaty-mandated free movement for workers and freedom to provide services.

On the one hand, each Member State is sovereign in the regulation of its own labour market. On the other hand, the EU is committed to ensuring that workers should be free to move and take employment in Member States other than their own, on equal terms to nationals of the State in which they work, and that service providers (including the self-employed) should be free to provide services temporarily - or establish themselves - in other MS without facing any obstacles arising from their nationality.

The requirements and functioning of the Internal Market have entailed some interpretation and qualification of the autonomy of national labour markets from the outset. From the earliest years of the Community, health and safety standards in the workplace and the relative pay of women were accepted as needing EU 'hard law' to ensure that businesses did not enjoy a competitive advantage based on less stringent requirements for health and safety and/or a greater tolerance of paying women less than men. In more recent years, the consultation of workers when

17 D'Auria, F., K. Mc Morrow and K. Pichelmann (2008), 'Economic impact of migration flows following the 2004 enlargement process: a model based analysis', *European Economy - Economic Papers*, No. 349, Economic and Financial Affairs DG, European Commission.

companies restructure to take advantage of the Internal Market was accepted as a third area in which binding EU requirements on domestic labour law are necessary in order to help keep competition within the Internal Market as beneficial and fair. Ireland is a prominent example, but not alone, of a Member State indebted to EU legislation for the manner in which its labour market standards in these areas were improved and benefited from a general 'levelling up' across the Union. The penetration of European legislation into these areas of national labour market regulation was sometimes controversial[18] but, generally and until the recent enlargement, took place through procedures that largely retained the trust of the social partners and of governments of different hue in the Member States, while protecting the integrity and functioning of the Internal Market.

In areas other than health and safety, equal pay for women and men, and workers' consultation, the EU continues to have no *direct* competence in labour market affairs. It is to 'support and complement' the labour market policies of the MS in fields summarised as eleven in Article 153 (1) of the Lisbon Treaty[19], but the MS remain sovereign – in theory at least – over such core issues as wage levels, national minimum wages, types of labour contract, job qualifications and the conduct of industrial relations. Some observers highlight the limited ambition of the EU Treaties where national labour markets are concerned by comparison to goods and capital markets. While the purpose of free movement for goods is that producers might compete fairly on price, the purpose of free movement of workers, by contrast, is simply to eliminate all discrimination based on nationality when workers are being recruited and services purchased. The intention is to afford the worker from one Member State the freedom to work in any other Member State under the same conditions as its own nationals, not to encourage wage competition. Pelkmans (2006), for example, reflects that 'the Treaty's approach to free movement is not concerned at all with the actual possibilities and economic incentives [for workers] to move across intra-EU borders, only with the legal right to do so' (180). It conceives of the mobility of EU workers as taking place *between* national labour markets and not within an 'EU labour market'. Pelkmans, in fact, is emphatic that the latter does not exist, is not envisaged by the Treaties and would not be a popular or feasible project given public opinion in many Member States.

In support of this perspective that the EU intends primarily a network of national labour markets - admittedly with a strong vested interest in seeing that each one is dynamic and flexible and that the ensemble is coordinated - it can be noted that diverse and complex national labour laws continue to govern minimum wage rates, hiring and firing, labour contracts, requisite job qualifications, social protection and many other areas. In fact, mobile workers (and inward investors) have to become versed in the specifics of each national labour market within the EU in which they operate and adapt to them. Steady but slow progress has been made to ensure that mobile workers are not at a disadvantage to host-country nationals in the social

18 For example, when the Commission successfully argued that a working week in excess of 48 hours was a health and safety matter (1993), a UK Conservative Government launched a challenge to the European Court of Justice arguing that the regulation of working time was an issue of labour market flexibility, for domestic policy alone to determine and, therefore, ought not be subject to Qualified Majority Voting. The ECJ (1996) rejected these grounds, though conceded that EU law could not require that the minimum weekly rest period should in principle include Sunday.

19 Improvement in particular of the working environment to protect workers' health and safety; working conditions; social security and social protection of workers; protection of workers where their employment contract is terminated; the information and consultation of workers; representation and collective defence of the interests of workers and employers; conditions of employment for third-country nationals legally residing in Union territory; the integration of persons excluded from the labour market; equality between men and women with regard to labour market opportunities and treatment at work; the combating of social exclusion; the modernisation of social protection systems.

insurance entitlements they accumulate (including their pension entitlements), the social protection they enjoy as workers, the qualifications required of them for given jobs, etc. The core objective being pursued, however, remains not the creation of an *EU* labour market across which workers compete on wages, but that access by workers from one MS to the labour markets of other MS should be on equal terms to their own nationals.

The Posted Workers' Directive (PWD), for example, enshrines the principle of 'host country' control over the pay and other core conditions of workers who remain contracted to an employer in another MS while carrying out work in the host country.

When first adopted in 1999, the PWD was greeted as a significant advance for 'Social Europe' and a check on the extent to which the freedom to provide services and the free movement of workers could undermine labour standards. Its objective is to facilitate the cross-border mobility of workers for assignments in another Member State and to ensure that such mobility is *not* motivated by the ability to exploit wage differences, even in the short-term. It seeks to do this by increasing the transparency of the legal obligations of employers contracting for work in another Member State and of the legal entitlements of the employees they bring with them. It specifies a cluster or nucleus of employment conditions where 'host country' norms and regulations must be honoured, *and* how and where such national norms and regulations are to be found. In doing the latter, however, some national labour markets (such as Sweden's) that functioned relatively smoothly - largely on the basis of voluntary collective agreements at the local level, and without a large recourse to national-level legislation or universally applicable collective agreements - have been deemed by the ECJ to be insufficiently transparent and, thus, in effect, creating obstacles to the cross-border provision of services (the Laval case, 2007).[20]

In other instances also, Court rulings since 2004 (not necessarily addressing situations arising from the activities of companies or workers from the NMS, e.g., the Luxembourg ruling of June 2009) have shaken the confidence of some of the proponents of 'Social Europe' in the OMS that an EU of 27 can avoid competition in wages and working conditions to the detriment of current employees in the OMS. The gap in living standards which the Internal Market now embraces – with, for example, minimum wages, *after* adjustment for differences in purchasing power, ranging from under €270 a month in Bulgaria and Romania to over €1100 in Luxembourg, the Netherlands, Belgium, France, the UK and Ireland (data for January 2009 in *Eurostat, 29/2009*) – and the demonstrated willingness of large numbers of nationals from the NMS to seek work in the OMS have, some believe, shifted the onus of proof onto proving that wage competition is not occurring rather than establishing that it has. There is less trust than before that the balance is right between the ability of European 'hard law' to drive negative integration in pursuit of the four freedoms, the ability of 'soft law' such as OMC to promote positive integration (such as raising skill levels and productivity in national labour

20 In the Laval case (2007), the ECJ ruled that a Swedish trade union had acted unlawfully in taking strike action to force an Estonian construction firm carrying out construction work in Sweden to honour the terms of a local collective agreement. It ruled that Sweden's national context made it excessively difficult for a foreign undertaking to determine the pay obligations with which it was to comply, and that the local collective agreement which the union wanted the Estonian firm to honour included issues outside the nucleus of employment conditions to which the PWD applied. In a parallel case (Rüffert), the ECJ ruled that the German State of Lower Saxony improperly sought to sanction a firm for not obliging a Polish firm it had subcontracted to pay minimum rates above the national rate as a Public Contracts Law in Lower Saxony required. The Court ruled that this was to go beyond the PWD.

markets where they are low) and the ability of national legislation and institutions to protect high labour market standards where they exist.[21]

The possible incentives created by the Fifth Enlargement for employers and individual workers to have greater recourse to previously existing channels of indirect wage competition need to be acknowledged. The scale of subcontracting by companies in the OMS of companies from the NMS, the numbers of workers being 'posted', the scale and reach of agency workforces, the increasing number of mobile self-employed and the extent to which some of them may – in effect – be working as employees, etc., are just some of the channels which need to be monitored and where appropriate new measures – at the domestic policy level and/or and at the EU level – may need to be developed. But the Fifth Enlargement's contribution to reinvigorating channels of indirect wage competition should not be exaggerated. For example, while Poland was the country from which the single largest number of workers were posted in 2006, the next six countries posting the most workers were EU 15 Member States (Germany accounted for only a marginally smaller number than Poland); in most EU 15 Member States, posted workers from elsewhere in the EU 15 figure more prominently than posted workers from the NMS (European Commission, 2008: 121).[22]

6.3.5 Enlargement, Welfare States and Social Inclusion

There is an extensive international literature on the consequences of migration for welfare states (e.g., Brücker *et al.*, 2002). It points to some core reasons as to why migrants may differ systematically from comparable natives (those with similar socio-economic characteristics) in their utilisation of social welfare (income support and services). For example, migrants may be disproportionately employed in jobs that are cyclically sensitive and/or where abrupt termination of employment is likely; while the first migrants to arrive may concentrate on finding and holding employment, family reunification may bring further arrivals who are less likely to participate in the workforce; discrimination by employers may disadvantage migrants in their job-seeking; migrants may struggle with language difficulties and lack important local labour market knowledge; a significant proportion of migrants may have suffered psychological trauma in the process of migrating; the clustering of migrants through which they provide each other with greater support in an unfamiliar and sometimes hostile environment may serve to further distance them from the host society and slow their integration.

Despite the number and plausibility of these reasons as to why migrants might have greater recourse to income transfers and social services than comparable natives, the empirical evidence that they, in fact, do is mixed, and does not confirm the view that migration leads to a drain on the welfare states. This evidence is mainly from the US and from studies of non-EEA migrants in the EU. In the specific case of East-West migration from the new EU Member States, however, analysis of

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21 Some mistrust can be disproportionately directed to the EU rather than national level. For example, the mix of national governments on the European Council that revised the Lisbon Strategy in 2004 and initially endorsed the 'country of origin' principle in the first (Bolkestein) draft Services Directive was quite different in character to the mix that had spoken through the Council that first launched the Lisbon Strategy in 2000. In like manner, the ECJ has received new lawyers from different backgrounds each time new states acceded. This has led to concerns - in smaller, affluent MS - that its recent rulings reflect less sympathy for the idiosyncratic industrial relations and social welfare regimes (Døvlik and Visser, 2009) and for national diversity in general (Hemmerijk, 2009).

22 The data show Ireland as receiving an estimated 4,000 posted workers in 2006 (half from the EU 10 and half from the EU 15) and posting 3,000 workers of its own.

welfare dependency remains limited, for the simple reasons that it is a recent event and because transitional arrangements restricting welfare access were imposed in all EU15 member states in 2004, with the single exception of Sweden.

Several characteristics of the East-West labour mobility triggered by the Fifth Enlargement serve to suggest that observations and findings based on migrants in the USA or on non-EEA migrants in the EU may have limited applicability to the case of nationals of the new Member States. For example:

- The evidence is that the large majority of East-West movers have moved for work purposes and been successful in finding employment.
- In addition, East-West movers tend to be younger and to have less dependants living with them than the populations which they join.
- The potentially disproportionately large rise in unemployment among them during the current recession (as a result of being recently employed and concentrated in cyclically-sensitive sectors and almost absent from public sectors) has led to the first significant numbers of them becoming reliant on welfare in their host countries.
- East-West movers who become unemployed enjoy free re-entry to their host country's labour market which makes returning to their home country likely if they consider they have more support there.
- The EU supports labour mobility across its territory. People who move for purposes other than employment (students, retirement, etc.) are required to be self-supporting and not to constitute a charge on the state to which they move.
- The social assistance that is available independently of work and on the basis of need alone is for each MS to determine. All MSs participate through an OMC in seeking to reduce poverty and social exclusion on their territories.

In summary, in so far as East-West movers have tended to be young, well-educated, single and intent on finding and holding employment, they are more likely to be net contributors to, than net beneficiaries of, their host countries' welfare states. The taxes they pay are redistributed to the inactive such as children, the young and retired (Doyle, Hughes, & Wadensjö, 2006), more of whom are natives and not migrants. The proportion of unemployed NMS nationals in the OMS who will remain on social assistance in their host countries after their social insurance-based support is exhausted will depend on several factors other than the rules governing eligibility for assistance and its generosity. These include the expected duration of the unemployment spell where they are, the earnings prospects they face should they return home, the family and social networks available in the alternative locations, and the extent to which they have already made and acted on a decision to make the host country their home (e.g., by purchasing an apartment or house; marrying a host country national; having children in school in the host country).

The effects of East-West migration on the welfare states of *sending* countries are different. In this case, the fact that migrants from the NMS are overwhelmingly of working age, intent on working and – in many cases – leave employment in their home country that is low paying and unsatisfactory (as was the case with emigration in Ireland in a previous era, cf. NESC, 1991) contributes to raising the dependency ratio and reducing tax revenues in the countries they leave. For example, some estimates for Lithuania suggest its elderly dependency ratio could more than double by 2050 and its social security system fail entirely (Kadziauskas, 2007), while studies for Poland similarly warn about the demographic consequences of post-enlargement out-migration and its consequences for the social security system (Kupiszewski and Bijak, 2007; Kaczmarczyk and Okólski, 2008). A core variable capable of hugely mitigating these negative consequences is the extent to which the migration is temporary or permanent: 'if the current migration flows lead to efficient brain circulation, empowering people to leave inactivity, increase their human capital abroad, and then utilise it at home, current outflows of migrants from new member states may in fact lead to more stable welfare systems in the medium or long run' (Kahanec and Zimmerman, 2008: 22).

The wider impacts of enlargement on social inclusion in the new Member States are monitored (among other things) in their National Strategic Reports for Social Protection and Social Inclusion 2008-2010, which all Member States prepare by way of participation in the OMC of that name. Challenges specific to the social situations of the NMS post-enlargement emerge in their reports such as the impact on health services of emigrating professionals, of rising inflation on fixed incomes and of inward investment in property on the price of accommodation. Generalisation is difficult, however, and, as in the EU 15, the quality of domestic policy making remains the core determinant of social progress. Tentatively, one could read into the data the beginnings of their movement as a group from being characterized by *relatively* egalitarian income distributions and low poverty thresholds to higher income inequality and higher poverty thresholds (e.g., Figure 1.6, *Growing Unequal? Income Distribution and Poverty in OECD Countries*. OECD 2008).

No major difference between the NMS and OMS was noted in responses to a Eurobarometer question on the social impacts of enlargement posed in February 2009 (Eurobarometer, 2009). Asked whether the integration of Central and Eastern European countries into the European Union had lowered social standards in Europe as a whole, 44 per cent of respondents in Central and Eastern Europe and 47.5 per cent in the EU 15 disagreed, while 38 per cent and 39 per cent respectively agreed. The Member States in which a majority of respondents agreed with the statement included Slovenia (52 per cent) and Hungary (51 per cent), on the one hand, and Greece (62 per cent) and Portugal (50 per cent), on the other. Irish respondents were the third most positive overall with only 26 per cent in agreement that enlargement had lowered social standards across the EU and 69 per cent disagreeing.[23]

6.3.6 Challenges at the EU level

Significant challenges continue to attend how the EU at large, and the NMS and OMS respectively, will adapt over the long-term as a result of the recent enlargement.

The global financial and economic crisis that broke in 2008 has added further complexities as it has impacted differently on individual states and revealed their very different capabilities and levels of resources for confronting the toll being taken by the crisis on the stability of banking systems, flows of credit, public finance positions, levels

23 Eurobarometer (2009), Views on European Union Enlargement. Analytical Report.

of employment, levels of household wealth and social cohesion. The prospect has even arisen that fresh push factors could arise fuelling renewed East-West migration from those NMS that fail to respond effectively to the several dimensions of their current crises.

Even without the disturbing impact of the current crisis on some of the NMS, the pace of convergence of the NMS with the levels of productivity and living standards of the OMS is a significant uncertainty. The longer wide gaps remain, the longer push factors will fuel migration and the more initial intentions to work temporarily in another MS may turn into decisions to remain abroad indefinitely (thus denying the sending countries the opportunity to benefit from the enriched human capital of their returning workers). The pace of convergence of NMS with the economic performance and achievements of the OMS depends, in part, on the scale and successful utilisation of their Structural and Cohesion Fund receipts. In the latest Financial Perspective, covering the period 2007-2013, these amount to about 3% of their annual GDP (though very much smaller as proportions of the GDP of the donor MS). Partly guided by Ireland's widely acknowledged success in leveraging Structural Fund receipts during its period of rapid catch-up (net EU receipts peaked at just over 6 per cent of Irish GDP in 1991), Cohesion Policy in the NMS currently focuses on fostering their local growth potential, prioritising such areas as research and innovation, ICT, transport infrastructure, the business environment and human capital. It also seeks to strengthen stable, participatory, transparent and accountable institutions in the NMS in the management of public funds. As the Commission study notes, 'the extent to which the new Member States utilise the leverage potential of EU transfers in order to move onto a higher growth path in the long run will depend on their absorption capacity and, in particular, on the quality of their domestic policy environment' (European Commission, 2009a:21).

The pace of convergence of the NMS with the OMS also depends on the success of the former in leveraging their lower living standards and wages to boost the exports of goods and services. This requires that wages rise in the NMS but as productivity pulls them up and without endangering their competitiveness. Otherwise, wage increases driven, for example, by comparison with prevailing EU 15 levels or shortages of skilled labour, will restrict their economic development and significantly reduce the range and scale of their internationally trading businesses (such as happened in the former East Germany after unification). Ireland's experience in this regard was positive for a period. Rising productivity (powered by inward investment and rising educational levels) outpaced the increase in wages to keep industry competitive, while emigration was not on a scale sufficient to create skilled shortages and damage competitiveness. The early Irish experience may be hard to replicate in each of the NMS.

Against these two large backdrops – the damage being wrought in some of the NMS by the current global crisis and the number of years that convergence will require – specific uncertainties continue to attend the East-West migration that has already occurred. For example, we do not know how much of the migration potential of these countries has already been exhausted. Even though net flows into the EU 15 have started to decline, some studies suggest that the present stocks of NMS workers in the EU 15 amounts to about 50 per cent of the long-term potential for migration from those countries (Brücker *et al.,* [2009] cited in

Kahanec and Zimmerman, eds, 2009: 51). We do not know what proportion of those who have already moved engaged in a largely once-off decision to work in another MS for a while or constitute a new and relatively permanent stratum of mobile labour across the EU who will engage in 'circular migration' in response to relative changes in labour demand. We do not know how workers from the EU 8 who choose to stay in the labour markets of the EU 15 will fare over the long run, how quickly they will overcome any underutilisation of their human capital and experience upward mobility in their host labour market or whether difficulties will attend their long-term integration.

6.4 The Fifth Enlargement and Ireland

6.4.1 Ireland's Trade and Investment Flows

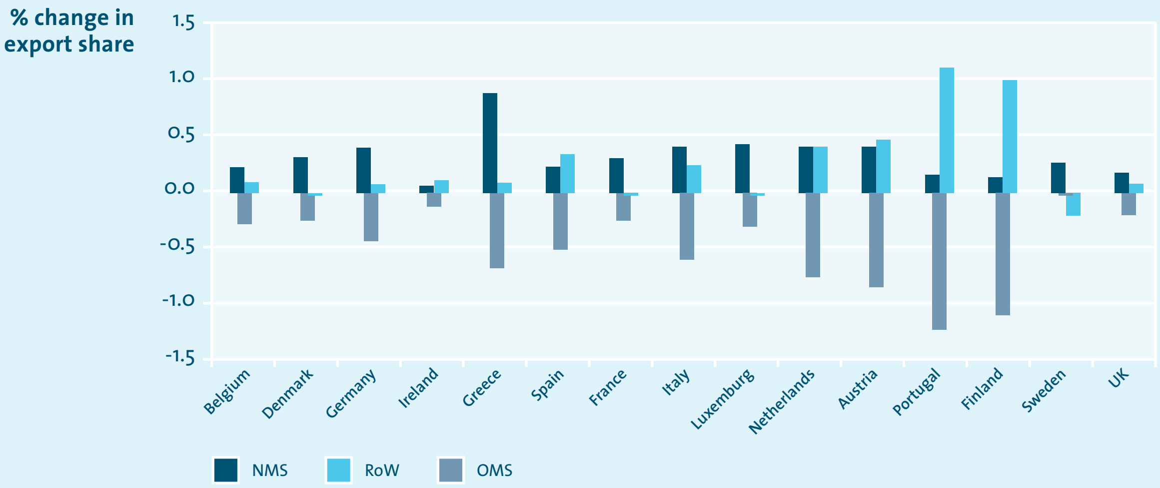
Other things being equal, the extension of the Internal Market to twelve new Member States – by adding 26 per cent to the EU's population and incorporating economies with the potential and need to grow faster than the EU 15 – suggests that trade and investment links between Ireland and the NMS would grow strongly. At the same time, the literature on the major determinants of international trade would suggest that the scale of Irish trade and investment with the NMS would remain modest. That literature finds that the size of economies and their proximities in geographical and cultural terms (the factors captured by 'gravity models') are more decisive in fostering trade between two countries than the removal of formal barriers. Ireland is one of the most distant of the EU 15 States from the NMS and, until large immigration began to alter the situation (discussed in the next sub-section), had quite tenuous historical, cultural and business ties with the NMS.

Figure 6.3 appears to confirm the significance of Ireland's geographic distance from the NMS and the small size of many of the latter economies. Ireland's exports record the least shift towards the New Member States of any EU 15 country over the period 1999-2007; the share going to the EU 10 rose the least (and the share going to the EU 15 fell the least) between 1999 and 2007.

However, an analysis of trading volumes confirms that, despite little change in the *relative* importance of export markets in the NMS, the NMS have become significantly more important trading partners. Ireland's commodity exports to the NMS in Central and Eastern Europe doubled between 1995 and 2003, and then tripled between 2004 and 2008 (Table 6.5). In the five years since Enlargement, Ireland's exports to the region have grown very much faster than exports overall. By 2008, the EU 10 accounted for over 2 per cent of Ireland's total commodity exports and had absorbed 7.4 per cent of the increase since 2003.

In 2004, the three principal markets in Central and Eastern Europe for Irish products were Poland, the Czech Republic and Hungary but the markets were small (total exports valued at €260m, €196m and €147m respectively) and exports to all countries in the region had been shrinking since 2000 (Table 6.6). After 2004, however, strong growth asserted itself and exports to the region grew at an annual rate of 22 per cent over the next five years; exports to Poland practically tripled, those to the Czech Republic grew by 70 per cent while Romania overtook Hungary as the third largest market with gross Irish commodity exports to Romania valued at €257m in 2008.

Figure 6.3 Shifts of Export Destinations from Individual Old Member States, 1997-2007



Source European Economy 1/2009: 64.

Table 6.5 Ireland's Commodity Exports, 1995-2008

	World	EU 10	United Kingdom	Germany	EU 10 as % World
Year	$m	$m	$m	$m	%
1995	43,789	407	11,140	6,329	0.93
1998	64,247	657	14,208	9,654	1.02
1999	71,227	805	15,627	8,506	1.13
2000	76,262	1,091	16,653	8,630	1.43
2001	82,973	864	19,957	10,503	1.04
2002	88,479	788	21,235	6,363	0.89
2003	93,038	866	16,836	7,708	0.93
2004	104,308	998	18,428	7,984	0.96
2005	110,003	1,135	18,856	8,234	1.03
2006	108,763	1,671	19,511	8,737	1.54
2007	122,233	2,203	22,936	9,211	1.80
2008	127,047	2,682	23,337	8,961	2.11
Growth					
1995-'03	113%	113%	51%	22%	
2003-'08	36%	210%	39%	16%	

Source UN COM-trade online.

Table 6.6 Goods Exports to the New Member States (€million)

	2000	2004	2008	Annual Percentage Change 2004-2008
Bulgaria	34.8	27.4	65.2	24.2
Cyprus	42.5	24.1	32.1	7.4
Czech Republic	346.5	196.3	332.7	14.1
Estonia	25.6	12.7	47.3	38.9
Hungary	224.2	146.9	196.6	7.6
Latvia	16.6	16.7	56.2	35.4
Lithuania	12.1	7.3	24.4	35.3
Malta	22.3	10.5	21.7	19.9
Poland	360.8	259.7	747.1	30.2
Romania	74.6	73.0	257.0	37.0
Slovakia	47.3	36.5	69.8	17.6
Slovenia	44.2	26.3	28.0	1.6
Total above	1251.6	837.4	1,878.1	22.4

Source CSO special tabulation and CSO *Trade Statistics*.

Goods exports, including manufacturing, are a crucial barometer of the Irish economy's performance and prospects. Services exports, however, have been growing faster than goods exports in recent years and have several features particularly attractive to the economy's needs: e.g., they maintain their relative prices in international trade better than manufacturing and – thus – help reverse the deterioration in Ireland's terms of trade; they are employment intensive; a wide spectrum of subsectors have a potential to export services; and they can be regionally dispersed (NESC, 2008; Forfás, 2008). The availability and quality of data on international trade in services, however, still lags that on trade in goods and the latter is, correspondingly, more extensively analysed. Nevertheless, Eurostat data on international trade in services are available from 2004 onwards.

Between 2004 and 2008, Ireland's total services exports grew by over 60 per cent (Table 6.7). Those going outside the EU 27 grew faster than those being sold within it, by 78 per cent as against 56 per cent. Exports to the euro area grew in line with the overall growth of services exports but those going to the UK registered slower growth of under 40 per cent. By 2007 (latest available figures), the NMS accounted for only 2.6 per cent of Ireland's services exports but they had nearly tripled in value since 2004 when their share of total exports had been only 1.4 per cent.

Table 6.7 Ireland's Services Exports (€m) by Broad Area, 2004-2008

	2004	2005	2006	2007	2008	Growth '04 to '07
	€m	€m	€m	€m	€m	%
Intra-EU 27	28,882	32,862	3,5251	43,911	45,096	56
...of which						
NMS	597	1,006	1,450	1,761	..	195
Euro Area	16,003	18,140	19,256	2,4181	25,695	61
UK	11,058	12,257	12,853	15,758	15,311	38
Extra-EU27	13,542	15,353	21,819	24,048	24,110	78
Total	42,424	42,819	57,069	67,960	69,203	63
Intra-EU as % of Total	68	77	62	65	65	
NMS as % of Total	1.4	2.3	2.5	2.6		

Notes 1. NMS of 10 only (BG and RO not included).
2. Euro Area of 12 only (less CY, MT, SI and SK to avoid double counting).

Source Eurostat (online data base).

Some perspective on how unusual or satisfactory this pace of development of Irish service exports to the NMS since Enlargement is may be gleaned from a comparison with the other OMS. It was the experience of most of them also that extra-EU services exports grew faster than intra-EU exports over this period. By 2008, in fact, the share of Ireland's services exports that were intra-EU, at 35 per cent, was close to the EU average (Eurostat, 2009). A more focused comparison with the services-intensive Dutch economy, however, suggests that Ireland may still have significant further scope to expand exports to the NMS. The Dutch services economy relies more on global markets than its Irish counterpart (41 per cent of its services exports are extra-EU) yet 3.8 per cent of its overall services exports go to the NMS as against Ireland's 2.6 per cent (Table 6.7).

Tables 6.7 and 6.8 together suggest that the Netherlands and Ireland each experienced the NMS after Enlargement as a particularly buoyant market for their services exports and grew exports to the region three times faster than their services exports overall. While the growth in Irish services exports to the NMS was more than double that of the Netherlands, the proportionate significance of markets in the NMS to Dutch service exporters is half as great again as for Irish exporters.

Foreign direct investment

Finally, some data are available on foreign direct investment flows from Ireland to the NMS. Though they are sparse and cover only the five years, 2003-2008, they merit attention because of the potential that enlargement was considered to offer companies in Ireland to relocate operations to the NMS either to serve markets

Table 6.8 Netherlands' Service Exports (€m) by Broad Area, 2004-2008

	2004 €m	2005 €m	2006 €m	2007 €m	2008 €m	Growth '04 to '08 %
EU 27 39,752	40,802	45,739	48,132	50,919	28	
...of which NMS	1,656	2,281	2,562	3,138	–	89
Total (world)	68,262	73,998	77,020	81,534	85,935	26
Intra-EU as % of Total	58	55	59	59	59	
NMS as % of Total	2.4	3.1	3.3	3.8	–	

Source Eurostat (online data base).

there or to serve third country markets from there. Table 6.9 confirms that that ODI from Ireland to the NMS has become a feature since 2004 but that it remains a very small part of the overall direct investment flows in and out of the Irish economy. A net outflow to the NMS 10 has consistently occurred since 2003 but its scale is insignificant compared to the substantial net inflows from the EU 15 and the magnitude of the net flows (more often in but sometimes out) between Ireland and the USA.

The re-routing of some former inward investment away from Ireland towards the EU 10 can, in significant instances, have been expected to have occurred anyway, and in all probability gone outside the EU in the absence of enlargement. A significant part of the ODI by indigenous companies in the EU 10 has been of the sort termed 'market seeking' and was, therefore, not alternative to an investment in Ireland. Generally, the continuing strong growth of the Irish economy to the end of 2007 belied any fears that enlargement would damage inward investment, employment growth, etc.

Table 6.9 Net flows of Direct Investment, Ireland, 2000-2008 (€m)

Partner	2000	2001	2002	2003	2004	2005	2006	2007	2008
World	5024	4543	8999	4917	14552	11509	12215	15178	9030 (p)
...of which									
EU 15	-23	3466	(c)	3816	8737	(c)	6370	6689	(n.a.)
NMS			(c)	-20	-171	(c)	-221	-93	(n.a.)
USA		1371	425	-580	1456	-3402	4161	4439	1321 (p)

Source Eurostat Online Database (code: bop_fdi_main)
(c) confidential
(n.a.) not available.

6.4.2 Intra-EU Labour Mobility and Ireland

The scale of migration from the NMS has been by far the most significant consequence of the 2004 enlargement for Ireland. It was not anticipated by the Commission or within Ireland that Ireland would prove to be 'by far the largest receiving country for nationals from the 2004-accession countries relative to its population size' (D'Auria *et al.*, 2008). Prior to enlargement, Germany and Austria were widely expected to be the preferred destinations but, in the event, they attracted significantly less between them than the smaller, more distant and less historically linked Irish economy (Table 6.10). The projected inflow to Ireland was to be 'negligible' (Kvist, 2004) or quantified at around one tenth of what subsequently transpired (Doyle, *et al.,* 2006:5). In effect, though the Irish economy accounted for only 1.5 per cent of the combined GDP of the EU 15 in 2004, Ireland absorbed 16 per cent of all the EU 10 nationals who moved to the EU 15 to work after2004, including 33 per cent of all Lithuanians, 17 per cent of all Poles and 11 per cent of all Slovaks (European Commission, 2009e: 131).[24]

Expressed in proportionate terms, the remarkable nature of Ireland's experience may be seen ever more clearly. The average EU 15 experience was that the East-West movement of NMS nationals occasioned an average annual rate of growth of 0.10 per cent in the population of working-age over the period 2004-2007. In Ireland, it occasioned an average annual growth rate of 1.4 per cent, more than four times the rate of the second most impacted country, the UK (0.33 per cent), and fourteen times the average experience of the EU 15. In less than five years, it is estimated that EU 10 nationals added 5.6 per cent to Ireland's population of working age, as against 1.3 per cent in the UK and 0.4 per cent in the EU 15 as a whole (Table 6.10).[25]

It is also noteworthy that, in most EU15 Member States, migration from countries *outside* the EU after 2004 continued to substantially exceed the numbers arriving from the EU10 Member States (Figure 6.4).

Even in the UK, where migration from the EU 8 was also on a large scale, migration from outside the EU 27 remained the dominant component. The Irish experience is unusual in this respect also that, uniquely in the EU, some 60 per cent of its overall migration was composed of nationals from the NMS. To a significant extent, enlargement enabled Ireland to replace the largely employer-driven work permit system of the time with intra-EU labour mobility. Much of the large reduction in work permits issued or renewed after 2004 was due to the 'reclassification' of Eastern European nationals, but that is not without importance – working in Ireland as EU nationals rather than on work permits increased their flexibility and protection within the Irish labour market.[26]

24 EU 15 nationals themselves exhibit mobility within the EU. Ireland was also the third most popular destination for UK movers, absorbing 18 per cent of those who moved between 2004 and 2007.

25 Because of its very much larger economy, the UK absorbed over one-half of all EU 10 movers

26 The number of new work permits issued reached a low of 8,166 in 2005 but increased thereafter driven by those being issued to Indian nationals.

Table 6.10 Changes in EU Migration Flows following the 2004 Enlargement

Immigration Impact on Receiving (EU15) Member States

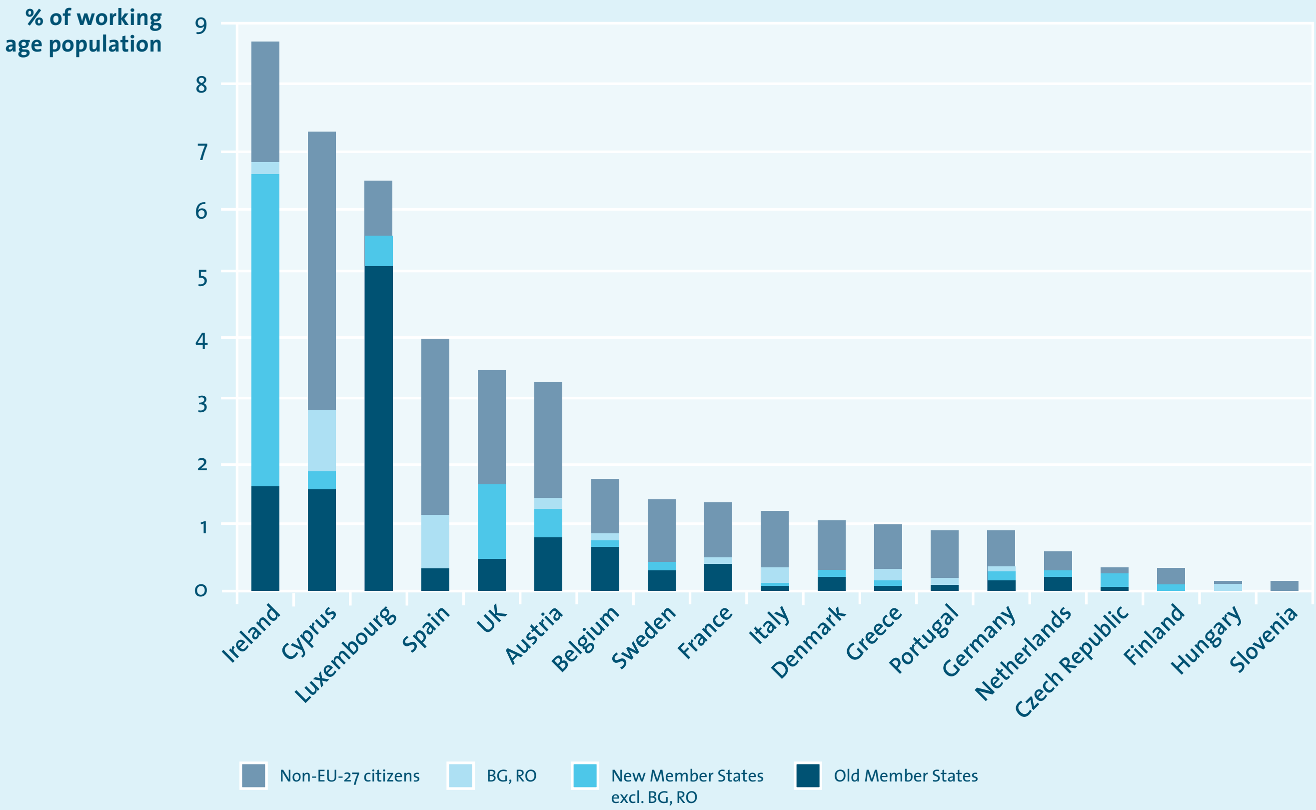
Countries	Change in number of EU10 citizens resident in individual EU15 countries (2004-2007)		
	000's	% of Working Age Population of individual EU15 countries*	Annual Average Impact on Working Age Population (%)
Belgium	20	0.29	0.07
Denmark	3	0.08	0.02
Germany	96	0.18	0.04
Ireland	162	5.56	1.39
Greece	7	0.09	0.02
Spain	67	0.22	0.06
France	5	0.01	0.00
Italy	32	0.08	0.02
Luxembourg	na	na	na
Netherlands	17	0.15	0.04
Austria	26	0.46	0.12
Portugal	na	na	na
Finland	6	0.17	0.04
Sweden	12	0.20	0.05
UK	532	1.32	0.33
Total (EU15)	**991****	**0.37**	**0.10**

Emigration Impact on Sending (EU10) Member States

Countries	Change in number of EU10 citizens emigrating to EU15 countries (2004-2007)		
	000's	% of Working Age Population of individual EU10 countries*	Annual Average Impact on Working Age Population (%)
Czech Republic	44	0.60	0.15
Estonia	14	1.49	0.37
Cyprus	No change***		
Latvia	62	3.95	0.99
Lithuania	121	5.22	1.30
Hungary	31	0.44	0.11
Malta	No change***		
Poland	627	2.32	0.58
Slovenia	1	0.08	0.02
Slovakia	92	2.36	0.59
Total (EU10)	**991******	**1.93**	**0.48**

Source D'Auria *et al* (2008: Table 1).

Figure 6.4 Recent Intra and Extra -EU Movers as Proportions of the Resident Working-age Population



Source European Economy 1/2009.

By mid-2007, 8 per cent of all jobs in the Irish economy were held by EU 10 nationals, and they had filled 56 per cent of the additional 245,000 jobs created over the period 2004-2007 (Table 6.11). By sector of the economy, they accounted for 21 per cent of all employment in 'Hotels and Restaurants', 13 per cent in 'Construction', 11 per cent in 'Production Industries' and 10 per cent in 'Wholesale and Retail Trade', while they were virtually absent in 'Public Administration and Defence' and 'Education' (Table 6.12).

There are several reasons *why* so many EU 10 nationals chose Ireland as their preferred EU 15 destination in the aftermath of enlargement. Ireland was one of only three OMS not to adopt transitional arrangements in 2004 and this was a contributing factor, but not dominant. The adoption of TAs by such countries as Germany with which, for example, Poles and Baltic nationals had close historical and cultural ties, undoubtedly diverted some movers to Ireland. There is evidence, however, that those more likely to be diverted in this way were skilled and that, by not adopting TAs at a time when the majority of EU 15 countries did, Ireland may have received a higher quality of EU 10 inflow. Germany, for example, experienced an increased inflow from the NMS despite its introduction of TAs but there is evidence that the proportion who were self-employed was higher and the skill composition lower than the inflow it had received from the EU 10 prior to 2004 (Brenke *et al.*, 2009). Self-employment, in fact, appears to have been used as a means to circumvent TAs in Germany.

The high degree of certainty of finding jobs in the rapidly growing Irish economy appears to have been the paramount factor accounting for the scale of East-West migration to Ireland (e.g., Galgóczi *et al.*, 2009). From the late 1990s until 2008, employment growth in Ireland was significantly faster than elsewhere in the EU 15 and the unemployment rate one of the lowest. That jobs in Ireland paid high levels of nominal earnings relative to the home countries (nominal as well as real earnings affect migration incentives when a significant part of the income earned

Table 6.11 Percentage of Total Employment held by Nationals of Other Countries, by Economic Sector, 2004 and 2007

	All Nationals of Other Countries		New EU Nationals only	
Sector	**2004** %	**2007** %	**2004** %	**2007** %
Agriculture, forestry & fishing	2.9	6.2	1.3	3.2
Production Industries (inc. Manufacturing)	7.7	17.7	2.1	11.0
Construction	6.9	17.2	2.6	12.6
Wholesale & retail trade	5.8	17.3	1.5	10.0
Hotels & restaurants	18.4	37.3	5.1	20.7
Transport, storage & communications	5.3	13.2	0.7	6.4
Financial & other business services	6.7	15.5	0.7	5.9
Public administration & defence	1.3	2.0	*	*
Education	4.7	6.7	*	0.7
Health	6.9	14.4	0.4	2.3
Other Services	6.5	15.7	0.9	5.5
Total	6.7	15.6	1.5	7.8

Source CSO, *Quarterly National Household Survey.*

Table 6.12 Numbers Employed, 2004 and 2007, and Changes: by Sector and Nationality

	Total Employment	Employment Changes 2004-2007				Total Employment
	2004	Irish Nationals	New EU Nationals	All Other Nationals	Total Change	2007
Sector	000s	000s	000s	000s	000s	000s
Agriculture, forestry & fishing	112.5	+2.0	+2.3	+1.8	6.2	118.7
Production Industries (inc. Manufacturing)	301.0	-38.6	+25.6	+2.7	-10.3	290.7
Construction	227.5	+19.2	+29.1	+3.2	51.5	279.0
Wholesale & retail trade	265.4	+7.7	+27.1	+11.4	46.2	311.6
Hotels & restaurants	112.7	-9.0	+21.7	+6.9	19.6	132.3
Transport, storage & communications	115.7	-4.8	+6.9	+3.0	5.1	120.8
Financial & other business services	247.7	+19.9	+15.7	+13.8	49.4	297.1
Public administration & defence	94.4	+9.7	*	+0.9	10.6	105.0
Education	118.4	+17.0	*	+3.7	20.7	139.1
Health	182.4	+19.6	+4.3	+15.0	38.9	221.3
Other Services	116.3	-4.8	+5.7	+6.0	7.0	123.3
Total	**1894.2**	**+37.9**	**+138.4**	**+68.4**	**244.7**	**2,138.9**

Source CSO, *Quarterly National Household Survey*.

in the host country is consumed in the sending country) was also significant – a non-negligible proportion of those who moved left employment in their home countries in order to earn more (which was a characteristic of Irish emigration also [NESC, 1991]). Sweden, however, is a country with high entry-level earnings and it adopted neither TAs nor new restrictions in accessing welfare, but received only small inflows (Gerdes and Wadensjö, 2009); this seems to confirm the primacy of the role of strong labour demand in the Irish case. Further factors specific to Ireland may have played a support role, e.g., the English language, cheap air transport, the profile given Ireland's success inside the EU by media in the Accession States, and a generally pervasive sense that Ireland – its people and bureaucracies (central and local government) – were accommodating and welcoming.

The characteristics of East-West migration to Ireland up to 2008

The large collapse in employment and sharp escalation in unemployment that gathered pace during 2008 are impacting strongly on EU 10 nationals in Ireland, reducing the inflow and causing some return migration and onward movement to third countries. The scale of the attrition and whether significant differences attach to those who leave and those who stay are still difficult to discern (discussed below). The core characteristics of East-West movers to Ireland up to the peak year of 2007 had become quite clearly established.

They were largely concentrated in the 15-39 age group and were disproportionately single (i.e., arrived without dependants).

They have a good level of education. Compared to their Irish counterparts, a higher proportion had completed the full cycle of secondary education, while they were just as likely to have participated in some form of third level education (Table 6.13). However, East-West movers were the least likely among migrant groups in Ireland to have a third level diploma or degree: 'collectively immigrants in Ireland are a remarkably educated group' (Barrett and Duffy, 2008).

Table 6.13 Educational Distribution of Immigrants to Ireland (2005)

Highest Level of Educational Attainment	Native	NMS	EU13	UK	All Immigrants
	%	%	%	%	%
No formal/ Primary only	10.5	6.4	1.1	2.4	4.0
Lower Secondary	16.7	9.3	2.2	18.3	8.4
Upper Secondary	29.0	37.8	22.4	19.6	26.8
Post Leaving	12.0	14.6	8.2	11.4	10.4
Third Level (diploma, etc.)	11.8	12.6	14.2	15.1	13.6
Third Level (degree or above)	19.9	19.2	51.9	33.3	36.8

Source QNHS, Q 2 2005 (Barrett and Duffy, 2008).

They have a higher level of labour market participation and a higher employment rate than Irish nationals. For example, in 2006, their labour force participation rate was 90% compared with 62% of Irish nationals, and less than 1,000 were on the unemployment register (Doyle *et al.*, 2006). Into 2009 (first quarter), however, recession had taken its toll but their participation rate still remained well above that of Irish nationals (84% compared to 60%).[27]

27 The high proportion with a completed secondary education as their highest educational attainment may contribute to these high participation rates, by showing particularly flexibility and willingness to work in entry-level jobs (as was observed of Irish Leaving Certificate holders in the US in the late 1980s).

They are employed more in some sectors of the economy than others (Tables 6.11 and 6.12) and, generally, in lower grade occupations than their educational levels would suggest.

Their earnings levels place them, as a group, firmly in the lower half of the earnings distribution. Overall, the median hourly earnings of EU 10 nationals in 2006 were two thirds of the national median (ESO, 2007). This reflected in part that two sectors which they entered in particularly large numbers are relatively low paying ('Hotels and Restaurants'; 'Wholesale and Retail trade'). In a number of empirical analyses on Irish migration, the ESRI estimates a pay gap for EU-10 migrants ranging from 18 to 45 per cent. It is suggested this initial wage disadvantage is experienced because they lack 'location specific human capital, language skills (being) one such example' (Barrett & McCarthy, 2007). Indeed, this failure of well educated EU 10 immigrants 'to fully capture returns to (their) human capital' is considered to make their impact on the Irish labour market more akin to a 'lower skill impact' than a 'high-skill impact' (Barrett, 2009:158).

From the start, elements of 'circular migration' (the same people arriving, leaving and returning again) and temporary migration (people arriving for a once-off stay of short or medium duration) were mixed in to the large inflow. This was a feature of post enlargement mobility in other countries also; for example, data for the UK suggest that around half of the EU-8 citizens who came to work there since 2004 may have already left the country by 2008 (European Commission, 2008). Circular and temporary migration help explain why the number of PPSNs issued to EU 10 nationals was consistently larger than estimates of the numbers at work or resident in Ireland at any one time.

While proportions of the inflow were circular and short-term, another group of migrants – their size difficult to determine – showed evidence of revising upwards their intended length of stay in Ireland by, for example, being joined by family members, enrolling their children in school, purchasing an apartment or house, etc.

The impacts of East-West migration on Ireland

While East-West migration to Ireland was very much higher than anticipated, it is remarkable that, while the economy remained strong and had a high labour demand, the scale of intra-EU labour mobility into Ireland was not particularly problematic.

Aggregate-level data

Until the 2008 recession broke, and declining domestic and export demand pulled down employment, the evolution of employment and earnings in aggregate had not substantiated understandable concerns that the scale of labour inflow from the EU10 was beyond the economy's capacity to absorb.

As noted, there was evidence that EU 10 nationals were replacing Irish workers in some sectors of the economy (Tables 6.11 and 6.12) but, until the end of 2007 at least, the replaced Irish workers were more evidently moving into other jobs than being displaced. In four sectors of the economy, employment levels of Irish nationals rose by more than those of EU 10 nationals (principally in education, health and financial and other business services). In three other sectors, employment increased for both

EU 10 and Irish nationals, though more for the first than for the second (most notably in the wholesale and retail trade but also in construction). In the four remaining sectors, growth in the number of EU 10 nationals in employment was associated with a decline in the employment of Irish nationals, principally in manufacturing. However, the standardised unemployment rate remained steady at around 4.5 per cent between the years 2002 to 2007 inclusive, and only began a sharp upward climb with the collapse of the housing bubble and the onset of recession in 2008.

Doyle *at al* (2006) examined earnings growth pre- and post-enlargement. They found average hourly earnings of employees grew less in the five quarters after accession (by 5.7 per cent) than in the five quarters pre-enlargement (growth of by 8.8 per cent p.a.). However, they pointed out there was previous experience of such a slowdown and that other factors might also be influencing. On a sectoral basis, positive earnings growth continued post-enlargement in two sectors that received particularly large inflows of EU 10 workers, the construction industry and 'wholesale and retail trade' (op. cit.). In a comparative EU context, earnings growth in Ireland remained among the highest in the euro area in the immediate post-enlargement era; the average annual growth in compensation per employee was over 5 per cent in nominal terms over the period 2002-2007, and almost 3 per cent in real terms (adjusted by the GDP inflator) (*European Economy* 5/2008: Graphs 73 and 75).

Theory

This evidence, at first appearance, that a workforce can increase by as much as 6 per cent over four years through migration and yet experience neither a notable fall in earnings nor rise in unemployment is surprising. It is partly explained by the strength of aggregate labour demand in Ireland at a time when major reserves of labour became available more easily than before. It is, also, to some extent, anticipated in the literature modeling the effects of immigration on a host country's labour market (Kahanec *et al.*, 2009; Chiswick *et al.*, 1992). It points to the pivotal issue of whether migrants are complementary to the native workers or substitutes for them and, hence, to the skills composition of the migrant inflow.[28]

If migrants act as substitutes for native workers, because their skills and experience are similar, native workers may lose out in a competition for jobs and receive lower wages and/or experience higher unemployment (e.g., Commander, Hietmueller, & Tyson, 2006). However, if migrant workers act as a complement to the native work force, these effects can be lessened or even reversed. Skilled immigration, by adding to the supply of skilled workers, can, in a first round of effects, exert a downward pressure on the wages of high-skilled native labour and increase the demand for low-skilled native labour (for whom the demand is complementary with the level of employment of high-skilled workers), pulling up the latter's wages and/or employment. However, the dynamic effects of the increased supply of

28 It is important to note that migrants' skills refer not just to the educational attainment, qualifications and experience they bring with them but to the transferability of these characteristics to the host country labour market and their ability and freedom to use their human capital in it (Kahanec and Zimmermnn, 2009).

skilled workers can overwhelm its first round negative effects on the skilled native workforce (Bonin *et al.*, 2008; Doyle *et al.*, 2006). The competitiveness of exporting sectors may be improved leading to higher output and increased employment. The new diversity created by the skilled migrants may make it easier to attract inward investment in services and high-tech manufacturing. Skilled migrants may stimulate international trade with their home countries and be disproportionately likely to generate new start-ups. The induced higher employment level of low skilled workers, in turn, helps to increase demand for high skilled workers. All these factors may offset the original wage decline of this higher skilled group.

The impact of low skilled immigration is modelled similarly but the conditions under which dynamic effects overcome first round dampening effects on the wages and/ or employment levels of low skilled native workers are more onerous. Where wages of the low skilled are lowered in response to unemployment, an increase in the level of low-skill employment can result which, in turn, increases the demand, and thus wages, for higher skilled labour. A recovery to wage growth for the low skilled must await the downstream impact of the rising level of high skilled employment. There is the additional complication that low skilled inflows are more likely to result in migrants holding vulnerable employments in large numbers, making them likely to experience the attractions and hazards (e.g., benefit withdrawal traps) of host country welfare states sooner than their high skilled counterparts.

It is clear that the extent to which migration is driven by demand or supply impacts on the degree to which migrant labour might be a substitute or complement to native labour. Demand-driven migration tends to be complementary, particularly where a work permit system demands that host country employers demonstrate a lack of available native workers. Supply-driven migration, on the other hand, brings both substitutes and complements into the host country labour force.

Modeling

D'Auria *et al.,* (2008) have simulated the effects of the East-West migration that actually occurred for each Member State applying the same model to all. A core assumption behind their simulation is that the skill distribution of arriving migrants was similar to that of the local population. Not surprisingly, given the exceptional scale of EU 10 migration to Ireland, they find the economic effects have been correspondingly greater in Ireland than elsewhere. Over the period 2004-2007, their results suggest that Irish GDP was more than 4 per cent larger, the average standard of living slightly lower (down 1.33 per cent) and the price level almost 5 per cent lower (Table 6.14.) These estimates are four times greater than for the second most affected country, the UK.

In the case of Ireland, a number of ESRI studies have considered the impact of migration on wages and employment. Barrett *et al.,* (2006) use data from 2003 and model the impact of immigration of different skill compositions on the wage and employment levels using a structural model. If the inflow of the immigrants who arrived between 1993 and 2003 (a net inflow of approximately 72,000) is assumed to have been 85 per cent high skilled (in the positions they occupied in the Irish economy and not just on basis of their characteristics), their simulation suggests the average wage of skilled workers is lower by around 6 per cent over the long

Table 6.14 Medium- to Long-Run Country Specific Effects Based on the Change in the Number of EU10 Citizens Resident in Individual EU15 countries over the period 2004-2007

	GDP	GDP per capita	Price level
Receiving Countries			
Belgium	0.22	-0.07	-0.24
Denmark	0.06	-0.02	-0.07
Germany	0.14	-0.04	-0.15
Ireland	4.23	-1.33	-4.67
Greece	0.07	-0.02	-0.08
Spain	0.17	-0.05	-0.18
France	0.01	-0.002	-0.01
Italy	0.06	-0.02	-0.07
Luxemburg	n.a.	n.a.	n.a.
Netherlands	0.11	-0.04	-0.13
Austria	0.35	-0.11	-0.39
Portugal	n.a.	n.a.	n.a.
Finland	0.13	-0.04	-0.14
Sweden	0.15	-0.05	-0.17
UK	1.00	-0.32	-1.11

Source D'Auria *et al* (2008). QUEST simulation

Notes The core assumption behind this simulation is that there is no change in skill distributions between migrants and the local population.

run and their employment level higher by about 2.7 per cent. By contrast, there is no downward pressure on the average wage of the low skilled (though 15 per cent of the inflow was assumed to be low skilled) while their employment level also is some 2.4 per cent higher[29]. The impact of the high skilled inflow in improving competitiveness and raising output was the primary mechanism through which these long run impacts materialised.

The authors acknowledge, however, that a significant 'occupational gap' characterises EU10 nationals in the Irish economy and that many take jobs below those appropriate to their skill levels (as discussed above, because they lack local labour market knowledge, have still to acquire mastery of English, encounter employers who discount their educational qualifications, etc.). They describe the simulation above, therefore, as their upper bound estimates and consider the lower bound estimates to be those which

29 *Op. cit.*, Table 7

Table 6.15 Inferred Impact of 180,000 EU 10 Migrants on Irish Macroeconomic Variables

	% change
Average wage	-7.8
Total employment	4.4
GNP	5.9
GNP per worker	1.7

Source Barrett (2009).

the model provides when the migrant inflow is assumed equal in skills to the native Irish workforce (under this assumption, therefore, the migrant inflow is assumed to be two thirds skilled and one third low skilled. The relatively high educational attainment of the inflow is discounted on the basis of the observed occupational gap). In this scenario, the average wage of high skilled workers is around 4 per cent lower and their employment level about 2 per higher over the long-run, while low skilled workers see virtually no change in their average wage and a 2 per cent increase in employment.[30]

In later work, Barrett (2009) rescales the 2006 study to 'infer' the impact of the significantly higher level of migration that occurred up to 2008 and estimates the impact of the stock of immigrants then in the labour force (180,000). As the rate of unemployment remained low into 2008, the scenario of most interest is where the model assumes that the wage level was the central adjustment variable.

The results (Table 6.15)show that average wages were lower by 7.8 per cent than they would have been in the absence of migration, employment 4.4 per cent higher, GNP 4.4 per cent higher and GNP per worker 1.7 per cent higher. It is the actual mechanisms that may be underlying what can only be suggestive findings which are of most importance. Barrett reflects in particular that, in the absence of the migrant inflow, wages would have risen, competitiveness would have been eroded, and GNP and employment would have been smaller. Migration may, in effect, have restrained the deterioration of competitiveness for a number of years. A second mechanism is suggested by the fact that, while an extra 180,000 workers adds 8 per cent to the workforce, employment rises by only 4.4 per cent in the model (and unemployment is assumed steady). It is possible and plausible that the fall in wages led to more Irish people withdrawing from the workforce.

With the hindsight that is plentiful after the collapse of Ireland's property market and the onset of the global financial and economic crisis in 2008, the principal 'cost' of the labour inflow on the scale that Ireland experienced may now be considered to be that it contributed to keeping economic growth too high for too long. Combined with the ease that the euro brought to importing capital, high immigration fed the perception

30 *Op. cit.*,Table 8. A third scenario makes the extreme assumption that 85 per cent of the inflow is unskilled (reversing the first scenario). This is the only one which reports unambiguously bad results for the low skilled who either face a rise of 4 per cent in their unemployment rate (assuming wage rates are nor reduced) or a fall in their average wage of 3.7 per cent (if wages are allowed fall to market clearing rates).

that the economy's potential growth path was higher than, in fact, was the case. At the same time, however, it must be acknowledged that recourse might have been had, in the absence of enlargement, to substantial migration from the same and other countries anyway. Concerns that the economy was overheating in the years 2004-2007 had simply not convinced Ireland's authorities and social partners enough to adopt and support deliberate decisions to slow growth. A greater reliance on work permits in the absence of enlargement would, then, have had more migrants working under restricted conditions and a lower status, while illegal entry and stays in Ireland might also have increased. In this scenario, a major benefit of enlargement was to ensure that a large proportion of the migrants brought in to Ireland's booming economy had the status and benefits of EU citizens.

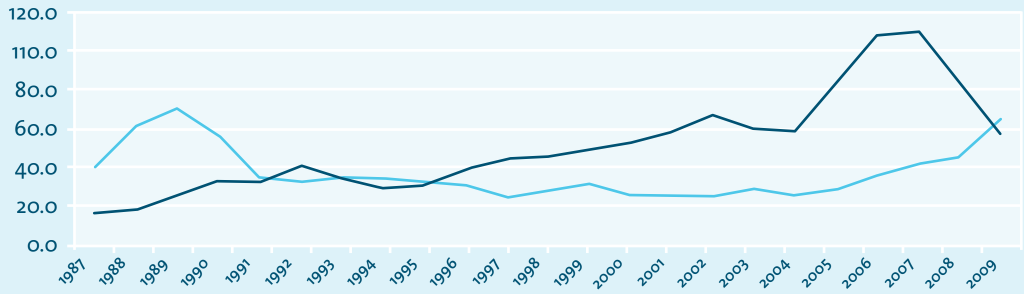
Notwithstanding this, the scale of immigration after 2004 moved rapidly to become 'probably the most significant and keenly contested issue in Irish industrial relations' (Roche, 2007: 74). Multiple concerns were expressed about downward pressure on wage levels and employment conditions, flagrant breaches of health and safety conditions, and the strategic use of redundancy and outsourcing to displace Irish workers (the 'Irish Ferries on dry land' scenario). A much wider interest has, been taken in Ireland, since 2004, in the significance of recent ECJ rulings and in the revised European Services Directive. With the creation of NERA and the passage of significant new labour market regulation (Mulvey, 2006), it is clear that previous limitations on the capacity of Ireland's labour market authorities to enforce existing standards have begun to be eased. It is the stimulus which enlargement has given to these types of development that illustrate, for Ireland, how the 2004 enlargement can hasten the pace of structural reforms that are required anyway to meet the challenges of globalisation (Commission Commission, 2009b).

By contrast, it can be argued that the ready availability of workers from elsewhere in the EU eased the pressures to implement desirable reforms in Ireland's welfare state and ALMPs. Over the eight-year period, 2000-2007, the percentage of the working age population in receipt of social welfare did not come down; it marginally increased from 14.5 per cent to 15.6 per cent (Grubb, 2009) though total employment in the economy increased by 26 per cent and the strength of labour demand was pulling in workers from across the new member states to meet labour shortages at every skill level. The stubbornly high level of welfare dependency among people of working age was rarely focussed as a major challenge to Ireland's categorical social welfare payments, practices of targeting, procedures for integrating usage of services with welfare payments, public employment service structures, and locally-based social inclusion strategies.

The impact of recession on East-West migration to Ireland

The large majority of workers from the new Member States in Ireland took employment after 2004 in construction and services sectors supplying the domestic market (Table 6.12). They have, accordingly, been disproportionately impacted by the collapse in construction and in consumer spending that gathered pace in 2008. Over the twelve-month period, April-June 2008 to April-June 2009, their numbers in employment fell by 25 per cent, more than four times the fall in employment of

Figure 6.5 Annual Immigration and Emigration ('000s), 1987 -2009



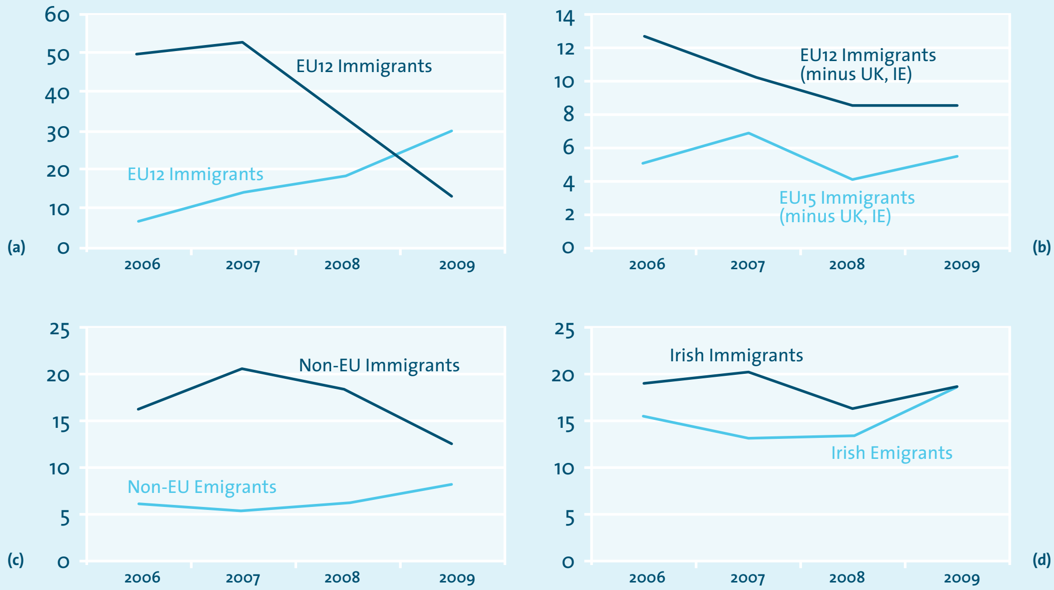
Irish nationals which was 6 per cent (Q2 QNHS). The numbers of unemployed NMS nationals, at the same time, rose more rapidly than the numbers of unemployed nationals by 140 per cent as against 113 per cent over the twelve months and, by November 2009, they accounted for 18.6 per cent of the Live Register (as against an estimated 15 per cent of the labour force).[31] This rise in unemployment is still less than the scale of the drop in their employment would suggest and is due to the element of return migration which the depth of the recession in Ireland has triggered among NMS nationals.

Labour migrants are known to be 'very responsive to economic cycles', in particular where mobility restrictions do not exist (Kahanec *et al.*, 2009). As such it might be expected, where migration had been determined by strong labour demand and economic circumstances deteriorate, that many former migrants might move on to more attractive destinations. Migration to Ireland peaked in 2007 and dropped sharply in 2008 and 2009 (Figure 6.5). As the Figure also shows, emigration, the absolute levels of which had trended upwards since 2004, accelerated sharply in 2008 and is estimated to have been larger than immigration in 2009.

The CSO's annual release, *Population and Migration Estimates*, provides estimates of the levels of immigration and emigration to and from Ireland by nationality. As Figure 6.6 makes clear, flows of EU 12 nationals have been affected most by recession, with the inflow falling from some 50,000 in 2006 to around 12,000 in 2009 and the outflow rising from under 10,000 to 30,000 (quadrant [a]). By contrast, immigration from elsewhere in the EU (outside of the Common Travel Area) and from outside the EU has fallen more slowly and emigration on the part of the same nationals risen more slowly (quadrants [b] and [c]). Emigration of Irish nationals, on the other hand, appears to be rising as fast as that of EU 12 nationals since 2008, though there is also evidence of an increased return flow of former Irish emigrants (quadrant [d]). It is likely that some Irish people losing their jobs overseas are making the same assessment as some EU 12 nationals becoming unemployed in Ireland, i.e., that surviving a period of unemployment will be easier in their home country.

31 CSO (2009), *Live Register. Additional Tables.* 8 December 2009.

Figure 6.6 Estimated Immigration and Emigration by Nationality, 2006-2009: '000s



Source Population and Migration Estimates, various years (CSO).

6.5 Further Enlargements of the Union

The Fifth Enlargement of the European Union went ahead primarily to strengthen democracy and the rule of law in Central and Eastern Europe and to guarantee peace on its Eastern frontiers. Significant economic uncertainties attended this enlargement but, five years later, it was clear that substantial economic benefits had accrued to both old and new Member States, while the political objectives were convincingly met.

There is a considerable waiting list of countries which now wish to join the EU. Croatia, Turkey and Macedonia have been officially recognised as 'candidate countries' while full membership has been promised to other countries in the Western Balkans (i.e., to Serbia, Montenegro, Albania, Bosnia-Herzogovina and Kosovo when its status has been finally decided). In the east, Ukraine and Moldova openly aspire to the idea of eventual membership, while Belarus, Georgia and Armenia are considered by some to be long-term prospects. Finally, the dramatic impact of the global financial crisis of 2008 brought Iceland to make its application.[32]

For most if not all of these countries the principal attractions of EU membership include the prospect of lasting peace with neighbours, the consolidation of respect for law, the enjoyment of responsive and effective democratic government internally, and enduring economic prosperity. Their pursuit of membership is a confirmation that 'enlargement is one of the most effective foreign policy instruments of the EU' and that 'the accession process gives strong encouragement to political and economic reform in the enlargement countries and reinforces peace and stability in Europe' (European Commission 2009b).

32 The three most recent applications for membership to the EU have been received from Montenegro (December 2008), Albania (April 2009) and Iceland (July 2009). Accession negotiations with Croatia are nearing the final phase. Accession negotiations with Turkey have reached a more demanding stage requiring a new impetus for reform. The former Yugoslav Republic of Macedonia has made significant progress in meeting key challenges. The Commission is preparing an opinion on the application for membership from Montenegro. It is also preparing an opinion on the application of Iceland. It stands ready to prepare an opinion on the application from Albania, once invited to do so by Council.

However, the admission of so many countries—several of them with still bitter border disputes, some facing significant internal challenges to law and order, most of them small in size (the seven aspirants from the Western Balkans have a combined population of 24 million) and all of them (save Iceland) contributing to an eastward in the EU's centre of gravity—raises profound questions about the nature of the EU, how it is to function effectively and how its constituent national populations relate to it. Of all the countries in the queue, the prospect of Turkish membership – because of its size, Moslem culture, history and borders to the East – accelerates the need for this questioning.

These issues cannot be explored here but it is clear that Ireland must play its full part in helping the EU to fulfill an historic mission towards countries that are still far from enjoying the stability and standards now associated with EU membership and enjoyed by Ireland.

In June 2006, the European Commission was asked by the European Council to evaluate the 'absorption capacity' of the Union in relation to future enlargement. The Council contained several members not at all enthusiastic about the prospect (France, for example, has gone so far as to require referenda to be held before accession treaties can be ratified). A renewed consensus on enlargement was, nevertheless, agreed by the December 2006 European Council as the way forward. The new policy is based on the principles of consolidation of commitments, fair and rigorous conditionality and good communication with the public, combined with enhancing the EU's capacity to integrate new members. Experience with the fifth enlargement and the 2006 consensus have made the 'rule of law' in candidate states, including as it does the fight against corruption and organized crime, a stronger priority. But the 2006 consensus was that it was in the EU's interest to keep up the momentum of the enlargement process.

Nevertheless, it must be recognized that public opinion in the Old Member States has become less confident about future enlargement. For example, in the EU 15, 52 per cent of responses were *not* in favour of 'further enlargement to include other countries in future years' and 38 per cent were in favour, in clear contrast to respondents in the new Member States where a large majority were in favour (64 per cent) and only 21 per cent against. Respondents in Ireland were slightly more positive towards further enlargement than the EU 15 as a whole but opinion seemed evenly divided (42 per cent were in favour and 40 per cent against.[33] Overall, for the first time since 2001, public opinion in the EU as a whole is more against than for further enlargement.

It is difficult to say with complete certainty why this decline in support for enlargement has taken place. The far distance of many of the countries aspiring to membership from most of the older Member States and the uncertain external and internal peace that several of the former enjoy undoubtedly contribute to unease in both elites and public opinion within the OMS. It also seems that some people equate further EU enlargement with further immigration and that they fear further changes in their way of life that this would cause. Some also view enlargement as part of a globalisation, which is perceived as destroying jobs, creating high levels of unemployment and reducing wage. And then there are the deeper questions as to how such an enlarged Union could continue to function effectively, and how the respective interests of large and small states would continue to be balanced. There are clear guidelines as to how enlargement should proceed if the interests of existing Member States and the acute needs of aspirant countries are to be met. It is an open-ended and transparent process in which Ireland should aspire to play a full role.

33 *EUROBAROMETER 71 (2009), Public opinion in the European Union. Fieldwork: June-July 2009.*

Appendices

Table 6A.1 Break down of Manufacturing Exports by Technology Intensity

	Low-technology industries (LTI)			Medium-low-technology industries (MLT)			Medium-high-technology industries (MHT)			High-technology industries (HT)			ICT industries (ICT) (part of HT)		
% of total	**1999**	**2004**	**2006**	**1999**	**2004**	**2006**	**1999**	**2004**	**2006**	**1999**	**2004**	**2006**	**1999**	**2004**	**2006**
NML 31	28	21	21	20	22	37	38	42	11	13	14	11	13	14	
OMS	22	21	18	17	16	19	43	46	46	18	18	16	13	12	12
HU	22	19	11	11	11	16	42	41	45	25	29	28	26	29	28
PL	37	32	26	28	27	27	29	35	41	6	6	7	6	7	7
RO	55	54	39	22	18	21	20	22	36	3	5	5	2	6	5

Source European Economy 1/2009: Table III.1.6.

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