

**FAMILIARITY BREEDS CONTEMPT: STRATEGIES OF ECONOMIC  
REFORM AND POPULAR ATTITUDES TOWARD EUROPEAN  
INTEGRATION IN LITHUANIA AND ESTONIA**

A Dissertation

Presented to the Faculty of the Graduate School

of Cornell University

in Partial Fulfillment of the Requirements for the Degree of

Doctor of Philosophy

by

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May 2010

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In referenda held in 2003, more than ninety percent of Lithuanians supported joining the European Union (EU), while fewer than two-thirds of Estonians did so. Why? The small existing literature on cross-national differences in EU support has focused on political and cultural variables, such as party competition and the history of independent statehood. Using survey data and content analysis of newspapers, however, I show that Lithuanians and Estonians had different economic expectations about the EU. Most Lithuanians hoped that joining the EU would help Lithuania to catch up with the West by increasing foreign investment and trade. By contrast, many Estonians worried that the accession would make their country dependent on the West by driving domestic producers bankrupt and allowing foreigners to buy up local economic resources.

Based on statistical data and press reports, I argue that these expectations reflected the two countries' strategies of economic reform. Lithuania sold state-owned enterprises (SOEs) to their managers, imposed moderate tariffs on imports, and continued to trade heavily with Russia. This strategy slowed down the development of services and modern industry. By contrast, Estonia sold SOEs to foreign investors, abolished all tariffs, and reoriented its trade rapidly to the West. This approach hurt agriculture and traditional industry. As a result, both Lithuanians and Estonians were unhappy about their country's economic situation. However, Lithuanians saw European integration as a solution to their country's problems, while Estonians considered it a cause thereof. I conclude by showing that my theory "travels" to Slovakia and the Czech Republic.

## BIOGRAPHICAL SKETCH

Aleksander Lust grew up in Tartu, Estonia. A *magna cum laude* graduate of Middlebury College with Highest Honors in political science, he studied German politics and history at the Free University of Berlin as a fellow of the *Studienstiftung des Abgeordnetenhauses von Berlin*. He received his Ph.D. in government from Cornell University in 2010.

Alex has presented papers at the annual meetings of the American Political Science Association and the American Association for the Advancement of Slavic Studies. He has published articles in *East European Politics and Societies* and *Problems of Post-Communism* and reviewed books for *Comparative Political Studies* and *Political Geography*.

A founding member of the Estonian Social Democratic Party, Alex believes that the world would be a better place if more social scientists participated in politics and more politicians studied social science. In his spare time, he runs and practices Tae Kwon Do.

To the memory of my grandmother, Olga Lust

## ACKNOWLEDGMENTS

In writing this dissertation, I have incurred many debts, professional and personal. Valerie Bunce was an excellent chair: firm in her expectations but tolerant of approaches different from her own. She also shared with me her broad knowledge of post-Communist politics and helped me to see how my argument “travels.” I started my research under the guidance of Jonas Pontusson, now at Princeton University. His work on the similarities and differences between capitalist economies has strongly influenced my thinking about political economy. Sidney Tarrow introduced me to the large literature on popular attitudes toward European integration in Western Europe and encouraged me to combine qualitative and quantitative analysis.

Matthew Evangelista brought an international relations perspective to a comparative project. He also helped me to clarify the logic of my argument and to think about alternative hypotheses. Isaac Kramnick, a political theorist, was an incisive outside reader. His suggestions about organization and style have improved this manuscript greatly. Jeremy Rabkin, a specialist in American politics, encouraged me to pursue my interest in East European Euroskepticism long before it became fashionable. Now at George Mason University, he remains of model of intellectual integrity and courage. Tina Slater, our department’s graduate field assistant, helped me to navigate the thesis submission process with skill and good cheer. She deserves a raise.

To persist in their solitary pursuits, scholars depend on the support of their family. My wife and fellow political scientist, Zhang Wu, was my closest companion in graduate school. When the going got tough, she cooked me Hunanese dishes and sang Chinese folk songs. My sister Kersti Lust helped me to stay in touch with my native Estonia. A historian, she reminded me that Estonians never liked their foreign rulers. My parents, Anu and Karl Lust, made sure that I got a good education despite the family’s straightened economic circumstances. They also taught me to stand up against social

injustice, Communist or capitalist. My grandmother Olga Lust encouraged me to learn foreign languages, which made this project possible. A medical doctor, she was a professional with a conscience. I dedicate the dissertation to her memory.

## TABLE OF CONTENTS

<b>Biographical Sketch .....</b>	<b>iii</b>
<b>Dedication .....</b>	<b>iv</b>
<b>Acknowledgments .....</b>	<b>vi</b>
<b>List of Tables .....</b>	<b>viii</b>
<b>Motto.. .....</b>	<b>.ix</b>
<b>Chapter 1: Introduction: Bringing the Economy Back In .....</b>	<b>1</b>
<b>Chapter 2: Development or Dependency? Content Analysis of Lithuanian and Estonian Newspapers.....</b>	<b>26</b>
<b>Chapter 3: For Richer or Poorer? Macro-Level Analysis of Survey Data.....</b>	<b>44</b>
<b>Chapter 4: Calculation, Community, or Cues? Micro-Level Analysis of Survey Data.... ..</b>	<b>60</b>
<b>Chapter 5: Insiders or Outsiders? Strategies of Economic Reform in Lithuania and Estonia .....</b>	<b>84</b>
<b>Chapter 6: Conclusion: First Causes, Second Cases .....</b>	<b>111</b>
<b>Bibliography .....</b>	<b>136</b>



## LIST OF TABLES

<b>Table 1.1: In or Out? Support for Joining the European Union (EU) in Eastern Europe in 2003.....</b>	<b>2</b>
<b>Table 1.2: Spot the Difference: Lithuania and Estonia in 2003.....</b>	<b>17</b>
<b>Table 1.3: Enthusiasts and Skeptics: Political Parties and the EU in Lithuania and Estonia in 2003-2004.....</b>	<b>21</b>
<b>Table 2.1: Meet the Press: Lithuanian and Estonian Newspapers in 2003 .....</b>	<b>29</b>
<b>Table 2.2: Stairway to Heaven or Road to Hell? Lithuanian and Estonian Attitudes toward the EU in 2003 .....</b>	<b>31</b>
<b>Table 3.1: Awareness of and Interest in European Issues in 1992 .....</b>	<b>46</b>
<b>Table 3.2: Support for European Integration in 1992 and 2003 .....</b>	<b>47</b>
<b>Table 3.3: Perceived Advantages of EU Membership in 1992.....</b>	<b>48</b>
<b>Table 3.4: Perceived Disadvantages of EU Membership in 1992 .....</b>	<b>49</b>
<b>Table 3.5: Perceived Winners and Losers of EU Accession in 1992 .....</b>	<b>50</b>
<b>Table 3.6: Knowledge about the EU in 2003 .....</b>	<b>51</b>
<b>Table 3.7: The Expected Impact of EU Membership in 2003.....</b>	<b>52</b>
<b>Table 3.8: The Meaning of EU Citizenship in 2003 .....</b>	<b>53</b>
<b>Table 3.9: What Kind of Europe? Images of the EU in 2003 .....</b>	<b>54</b>
<b>Table 3.10: Fears about the EU in 2003.....</b>	<b>55</b>
<b>Table 3.11: Perceived Winners and Losers of EU Accession in 2003 .....</b>	<b>58</b>
<b>Table 4.1: Scales and Categories: Description of Variables .....</b>	<b>73</b>
<b>Table 4.2: Cognition or Calculation? Regression Results.....</b>	<b>77</b>
<b>Table 4.3: Similar Structure, Different Attitudes: Distribution of Variables.....</b>	<b>79</b>
<b>Table 5.1: Ties That Bind: Foreign Investment and Trade in Lithuania and Estonia in 2003 .....</b>	<b>90</b>
<b>Table 5.2: Muddling Through: Output and Employment in Lithuania and Estonia in 1990 and 2003.....</b>	<b>92</b>
<b>Table 5.3: Old and New: Manufacturing Output and Employment in Lithuania and Estonia in 1994 and 2003 .....</b>	<b>93</b>
<b>Table 5.4: Well Served: The Service Sector in Lithuania and Estonia in 2001 .....</b>	<b>94</b>
<b>Table 6.1: How Similar? Lithuanian and Estonian Economies in 1989 .....</b>	<b>118</b>
<b>Table 6.2: Asset or Liability? Lithuanian and Estonian Industry in 1989.....</b>	<b>119</b>
<b>Table 6.3: Similar Speed, Different Direction: Foreign Investment and Trade in Slovakia and the Czech Republic in 2003.....</b>	<b>129</b>

The pessimist says, “Things are awful. They cannot possibly get any worse.”

The optimist says, “Oh yes, they can!”

Soviet joke

## CHAPTER 1

### INTRODUCTION: BRINGING THE ECONOMY BACK IN

#### Introduction

In December 2002, the European Council invited eight post-Communist countries—the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Slovakia and Slovenia—to join the European Union (EU) in 2004 and placed two more countries—Bulgaria and Romania—on the waiting list. In many ways, this seemed like a dream come true for Eastern Europe. Many candidate countries had close historical and cultural ties with Germany, Austria, or the Nordic countries. Joining the EU would allow them to “return to Europe.” After World War II, they had been occupied or otherwise dominated by the Soviet Union. The EU would protect their independence from Russia. During the democratic revolutions of 1989-1991, they had overthrown corrupt Communist dictatorships. The EU would show them on how to build democratic and trustworthy states. Finally, they were much poorer than Western Europe. The EU would help them to catch up by giving them economic aid and opening its markets to their products.

Over the next few months—from March to September 2003—the prospective members held referenda on whether or not they should join the EU. These were widely regarded as a formality: the EU and the applicant country governments signed the accession treaties in April 2003, when only Slovenia had voted. However, the results of the referenda showed that popular support for EU membership varied significantly across Eastern Europe (see Column A of Table 1). In some countries—Slovenia, Slovakia and Lithuania—the overwhelming majority of voters (90-94%) supported EU membership. In other countries, however, a significant minority of the electorate—16% in Hungary, 23-24% in Poland and the Czech Republic, and 32-33% in Latvia and Estonia—opposed the accession. Bulgaria and Romania joined the EU in 2007 without holding a

referendum. However, opinion polls showed that voters in these two countries supported the EU at least as strongly as their counterparts in Slovakia, Slovenia and Lithuania (see Column B of Table 1.1).

**Table 1.1: In or Out? Support for Joining the European Union (EU), 2003**

	A) Referendum		B) Survey*	
	For (%)	Against (%)	For (%)	Against (%)
Bulgaria	-	-	74	4
Czech Republic	77	23	58	18
Estonia	67	33	41	31
Hungary	84	16	71	11
Latvia	67	32	49	27
Lithuania	91	9	75	12
Poland	77	23	70	14
Romania	-	-	83	2
Slovakia	94	6	70	10
Slovenia	90	10	79	10

\* The remaining voters were unsure or said that they would not vote.

Sources: Nugent (2004), 278-279 (Column A) and Candidate Countries Eurobarometer 2003.2 (May 2003), [http://ec.europa.eu/public\\_opinion/cceb.en.htm](http://ec.europa.eu/public_opinion/cceb.en.htm) (Column B).

What explains cross-national differences in EU support in Eastern Europe? As comparativists are wont to do, the existing literature focuses on political and cultural variables (Pontusson 1995). Some scholars argue that countries with a short history of independent statehood are less supportive of the EU than long-established nation-states because they attach higher value to political sovereignty. Others suggest that ethnically divided societies oppose European integration because ethnic majorities worry that the EU will force them to make concessions to the minorities or because ethnic minorities co-blame the EU for their low status. Still others find that democratization, elite divisions, and the presence of significant anti-EU parties encourage popular opposition to the EU. In democratic countries, people can agitate against EU membership without fearing arrest. Elite divisions indicate that it is socially acceptable to be a Euroskeptic. Powerful Euroskeptic parties will mobilize their supporters to vote against the EU.

*This dissertation will develop an alternative, economic explanation of cross-national differences in EU support by comparing the Baltic states of Lithuania and Estonia. I will argue that the two countries pursued different strategies of economic reform. Lithuania followed an insider-oriented strategy. It maintained state ownership of infrastructure and sold other state-owned enterprises (SOEs) to their Soviet-era managers. It imposed moderate tariffs on imports and continued to trade heavily with Russia. By contrast, Estonia adopted an outsider-oriented strategy. It sold SOEs, including infrastructure enterprises, to foreign investors. It abolished all import tariffs and re-oriented its trade rapidly from Russia to the West. Neither strategy worked well, however. The Lithuanian strategy slowed down the development of services and “new” industry. The Estonian strategy led to a decline of agriculture and “old” industry. Neither approach could prevent the decline of infrastructure. As a result, both Lithuanians and Estonians were dissatisfied with their (country’s) economic situation. However, Lithuanians saw European integration as a solution to their (country’s) problems, while Estonians considered it a cause of theirs.*

This introductory chapter is organized as follows. The next section will review the existing literature on cross-national variation in EU support in Western and Eastern Europe. (The literature on the West is relevant because much of the scholarship on the East is based on it.) The following section will summarize my argument. The conclusion will outline the rest of the dissertation.

## **Go West, Young Man: Literature Review**

### **Identity Crisis**

Since the 1980s, Eurobarometer surveys have found that some countries (e.g., Greece, Portugal, Spain, Italy and Germany) are more supportive of the EU others (e.g., Britain, Sweden, Denmark, Finland and Austria) (Jolly 2007, chap. 6).<sup>1</sup> To explain this pattern, Eichenberg and Dalton (1993) suggest that small states, such as Belgium and the Netherlands, are more open to outside political and cultural influences than large countries, such as Britain and France. Gabel and Palmer (1995) and Gabel (1998 a, b) contend that countries that suffered heavy casualties in World War II (Germany, Italy and France) are more anxious to avoid another military conflict than those that suffered little (the Nordics). Kalthenthaler and Anderson (2001) argue that countries with a long history of independent statehood (Britain and France) are more reluctant to give up power to supra-national institutions than countries that only became independent in the nineteenth and twentieth centuries (Ireland and Greece). Finally, Vössing (2005) claims that some countries (Germany) have a more open national identity than others (Britain).

There are also two qualitative studies that explore cross-national differences in EU support. Diez Medrano (2003, chap. 2-3, 5-8) argues that country-specific historical experiences explain why Spain and Germany support European integration, while Britain opposes it. Germany has a guilty conscience because it started two world wars. Moreover, after World War II, West German leaders realized that other European countries would not allow Germany to become reunified unless it was firmly anchored in European institutions. Spain experienced economic and political decline from the seventeenth century to the 1970s. From the richest country in Europe, it became one of the poorest. Its political development was marked by authoritarian rule, frequent coups,

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<sup>1</sup> Of course, attitudes toward the EU have also changed over time. For example, Belgium and the Netherlands used to be strongly pro-European, but have now moved to(wards) the Euroskeptic camp.

and a civil war. As a result, Spain sees EU membership as a way of developing its economy and democratizing its politics. Unlike Germany and Spain, Britain has traditionally focused on maintaining its colonial empire and tried to stay aloof from European conflicts. More recently, it has cultivated a special relationship with the US.<sup>2</sup>

Gstöhl (2002, chap. 1, 2, 7) compares popular attitudes toward the EU in three traditionally Euroskeptic countries: Sweden, Switzerland, and Norway. Specifically, she wants to explain why Sweden joined the EU in the 1990s, while Switzerland pursued partial integration (e.g., through economic agreements) and Norway stayed out. She argues that Swedish national identity was based on a neutral foreign policy and an economic model of centralized collective bargaining and high social spending. Once the Cold War ended and the Swedish economic model disintegrated, Sweden joined the EU in order to improve its access to EU markets. Switzerland wants to keep both its neutral foreign policy and its federal, direct-democratic political system. However, because of its role as one of Europe's banking centers, it is interested in closer economic ties with the EU. Finally, Norway sees European integration as a threat to economic prosperity and political sovereignty. Unlike Sweden and Switzerland, it has a long history of foreign rule—by Danes, Swedes and Germans—which it is anxious not to repeat. It also has large stocks of oil and fish, which it is unwilling to share with other countries.<sup>3</sup>

How well do these findings from Western Europe hold up in Eastern Europe? Like Gabel (1998 a, b) and Gabel and Palmer (1995), Allam and Goerres (2008) find that there is a strong correlation between World War II deaths and support for European integration: the more casualties a country suffered, the more likely it is to support adopting the common European currency, the euro. They argue that the euro symbolizes peace and security in Europe. This makes it attractive to countries that want to avoid

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<sup>2</sup> Eichenberg and Dalton (1993) make the same argument about the origins of British Euroskepticism.

<sup>3</sup> Gstöhl (2002, chap. 7) also notes that Norway depends less on EU markets than either Sweden or Switzerland.

conflict with their neighbors. Like Eichenberg and Dalton (1993), they also find that small states are more supportive of the euro than large ones. Small countries feel vulnerable to political pressure from big states. Relative to their population, they are also over-represented in EU institutions, especially the European Parliament. As a result, they support policies that strengthen the EU at the expense of national governments.

Other cultural and historical findings from Western Europe, however, have been reversed in Eastern Europe. In contrast to Anderson and Kaltenthaler (2001), Grabbe and Hughes (1998, chap. 6), Grabbe (2003), Ozolina (2003) and Mikkel and Pridham (2004) find that opposition to the EU is stronger in countries with a short history of independent statehood, such as the Czech and Slovak republics and the Baltic states. For centuries, these countries were dominated by foreign powers: Austria, Germany, Sweden, Poland, and Russia. Now they want to enjoy their hard-won sovereignty instead of being bossed around by the EU. Pettai (2005) and Vetik, Nimmerfelt and Taru (2006) argue that Estonian and Latvian Euroskepticism stems from their cultural peripherality. Colonized by German crusaders in the thirteenth century, Estonians and Latvians did not develop a national consciousness until the nineteenth century. By contrast, Lithuania was an independent grand duchy ruled by an indigenous nobility until it merged with Poland in the sixteenth century. As a result, Estonians and Latvians define their national identity in opposition to Europe, while Lithuanians consider themselves part of Europe.

Students of Baltic politics, home to the largest ethnic minorities in Eastern Europe, have explored the role of ethnicity in shaping popular attitudes toward the EU. Evans and Lipsmeyer (2001), Ozolina (2003), Mikkel and Pridham (2004), and Pettai (2005) argue that Estonia and Latvia are less supportive of the EU than Lithuania because they experienced a larger influx of Russian migrants during the Soviet rule. After the breakup of the Soviet Union, Estonia and Latvia passed strict citizenship laws to minimize Russian political influence. By contrast, Lithuania gave citizenship to all Russians who wanted it because there were so few of them. Now Estonians and Latvians



worry that the EU will force them to change their citizenship policies, while Lithuanians know that their laws easily pass EU muster. By contrast, Whitefield, Rohrschneider and Alisauskiene (2006) assert that it is the Estonian and Latvian Russians who oppose EU membership. The EU pays lip service to the idea of equal rights, but accepts the Baltic view that Russians are migrants who must apply for citizenship. As a result, the Russians look to the Russian state for help.

### **Trust Me**

There is an interesting debate among West Europeanists on how the quality of political institutions affects support for European integration. In a quantitative study, Delhey (2007) finds that citizens of more democratic countries—measured in terms of respect for political and civil liberties—trust other EU member states more than people living in less democratic societies. He argues that participation in democratic politics makes people more tolerant and confident of their ability to influence the government. These attitudes, in turn, are conducive to international cooperation. In his qualitative comparison of Britain, Germany and Spain, however, Diez Medrano (2003, chap. 5-8) comes to the opposite conclusion: it is the lack of democracy at home that makes people support European integration. Spaniards and Germans support the EU because they see it as a guarantor of post-war democratic reforms. Britons oppose the EU because they consider it a threat to representative government.

On a related note, Delhey (2007) finds that corruption decreases people's trust in other European countries. As with democracy, he argues that people's attitudes toward international politics reflect their experience with domestic politics: if the politicians they know are corrupt, they will expect the same of all politicians. By contrast, Sánchez-Cuenca (2000) finds that corruption increases support for European integration. He reasons as follows. European integration requires countries to give up part of their national sovereignty. For example, the EU, rather than national governments, will be in

charge of issuing currency, distributing agricultural subsidies, and admitting immigrants. The costs of giving up sovereignty are high in countries where politicians and civil servants act in the public interest (little corruption) and low in countries where officials pursue their private interests (a lot of corruption). This explains why south European countries (Spain, Portugal and Greece) are most supportive of the EU and the Nordic countries and Britain least so, while continental Europe falls in between.

The most robust political finding about Western Europe, however, is that political elites shape popular attitudes toward the EU. The elites in question are political parties. If most parties support European integration, so do most voters; if not, then not. There are two causal mechanisms at work: party identification and the political opportunity structure. Many voters know and care little about the EU. When they have to vote on issues like EU membership, the common currency, or the EU constitution, they follow cues from the party they vote for in national elections (Wessels 1995; Anderson 1998; Van Kersbergen 2000; Steenbergen and Scott 2004). More subtly, elite disunity encourages people to vote against European integration regardless of their party affiliation. Euroskeptic parties make available negative information about the EU that pro-EU elites prefer to gloss over. By speaking out against the EU, they also puncture the illusion that “everybody” supports the EU. This encourages EU opponents to turn out and vote (Ray 2003, 2004; Steenbergen and Scott 2004; Hooghe and Marks 2005).

Moving on to Eastern Europe, most scholars come down on the side of Diez Medrano in the debate over whether democracy increases or decreases support for the EU. Christin (2004), Vachudova (2005, chap. 6, 8) and Rohrscheider and Whitefield (2004, 2006) find that there is a negative correlation between democratization and support for EU membership.<sup>4</sup> According to Christin (2004) and Vachudova (2005), citizens of less democratic countries (the Balkans and Slovakia) believe that joining the

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<sup>4</sup> Rohrscheider and Whitefield (2004) also find that democracy encourages opposition to *foreign ownership*.

EU would strengthen democratic political institutions at home, while people living in more democratic countries (Central Europe and the Baltic states) feel that they do not need outside aid. Rohrschneider and Whitefield (2004, 2006) argue that democracy allows political entrepreneurs to mobilize opposition to the EU and encourages public debate about the advantages and disadvantages of Western integration. By contrast, undemocratic governments intimidate EU opponents and discourage public debate.

Rohrschneider and Whitefield's (2004, 2006) point about public debate brings us to elite unity argument. Szczerbiak and Taggart (2004 a, b) argue that the outcomes of the EU accession referenda in Eastern Europe depended on underlying public support for the EU (which they do not explain) and party positions on EU membership. In Slovakia, Hungary, Slovenia and Lithuania, all major political parties supported the accession, which marginalized Euroskeptic ideas in the public discourse and discouraged anti-EU voters from participating in the referendum. In the Czech Republic, Poland, Estonia and Latvia, however, significant parties opposed EU membership, which gave credibility to Euroskeptic ideas and encouraged anti-EU voters to turn out and vote.<sup>5</sup> Similarly, Kopecký and Učen (2003) and Kopecký and van Holsteyn (2006) maintain that the Slovaks strongly supported the accession because all major political parties—including the populist Movement for Democratic Slovakia—called on their supporters to do so. By contrast, many Czechs opposed the EU because the Czech conservatives criticized EU regulatory policies as socialist (although they supported the accession in principle), while the Communists opposed the EU as a Trojan horse of multinational capital.

### **The Wealth of Nations**

There is a sizable literature on the economic determinants of cross-national differences in support for European integration in *Western* Europe. Until recently, much

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<sup>5</sup> In an earlier paper, however, Taggart and Szczerbiak (2003) find that there is no correlation between popular and party-based Euroskepticism.

of this research focused on *quantitative differences* in the countries' macro-economic performance in terms of growth, employment, and inflation. In a classic study, Eichenberg and Dalton (1993) show that *support for EU membership is stronger in rich countries than in poor countries and in times of economic growth than during recessions*. Their argument is straightforward. From the founding of the European Coal and Steel Community in 1952 to the signing of the Maastricht treaty in 1992, European elites have promoted European integration as a way of boosting economic growth. A common market will allow countries to specialize in areas where they have a comparative advantage. A common currency will reduce interest rates and stabilize prices. As a result, European voters hold the EU responsible for domestic economic conditions.

Anderson and Kaltenthaler (1996) find that there is a strong correlation between EU support and unemployment and inflation: when unemployment and inflation go up, support for the EU goes down. Similarly, countries that joined the EU during the stagflation of the 1970s (Britain, Ireland and Denmark) are less pro-European than countries that joined in the 1950s, when unemployment and inflation were low (France, Germany, Italy, Belgium and the Netherlands). Eichenberg and Dalton (2007), however, find that inflation affects EU support, but unemployment does not. They reason as follows. The EU has a common monetary policy (the European Monetary Union), but no comparable fiscal union. Moreover, even EU fiscal policies—tariffs, agricultural subsidies, and value-added taxes—have a direct effect on prices, but only an indirect impact on employment. As a result, voters blame the EU for inflation, but not unemployment.<sup>6</sup>

*Other scholars, however, have reached the opposite conclusion: it is economic failure, not success, that creates support for the EU. Voters support European integration if they think that their own government is doing a bad job managing the economy and*

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<sup>6</sup> However, they find that the correlation between EU inflation and EU support has become weaker since the 1990s.

that the EU would do better. Thus, Duch and Taylor (1997) find that citizens of poor countries (e.g., Ireland) are more likely to consider EU membership a good thing than voters in rich countries (e.g., the Nordics). Mattli (1999, chap. 1, 3-4) argues that countries apply for EU membership after their growth rate has been below the EU average for a few years. This, he says, explains why the UK, Ireland and Denmark applied to join the EU in the late 1960s, while Finland and Sweden did so in the early 1990s. Gärtner (1997) and Kaltenthaler and Anderson (2001) find that support for the euro is stronger in countries with a history of loose fiscal and monetary policy and high unemployment and inflation (Greece, Portugal, Spain and Italy) than in countries that have successfully pursued tight economic policies (the UK and the Nordics).

On the whole, then, *the findings about the relationship between economic success and support for European integration are contradictory and depend heavily on the time period and countries analyzed.* This may explain why some scholars of West European politics have recently turned their attention to *international economic relations and qualitative differences between European economies.* Kaltenthaler and Anderson (2001), Brinegar, Jolly and Kitschelt (2004), Brinegar and Jolly (2005), and Eichenberg and Dalton (2007) find that countries that are net recipients of money from the EU budget—via agricultural subsidies and funds for infrastructure development—are more supportive of European integration than countries that are net contributors. Clearly, the former benefit from EU membership, while the latter would be better off on their own. By and large, this is a north-south divide: the poorer, agricultural economies of the south (Spain, Portugal and Greece) are more supportive of the EU than the rich, industrialized and service-oriented economies in the north (Britain and the Nordics).

Eichenberg and Dalton (1993 and 2007), Kaltenthaler and Anderson (2001), Brinegar, Jolly and Kitschelt (2004), and Brinegar and Jolly (2005) find that countries that trade more actively with other countries and/or conduct most of their trade with other EU nations (e.g., Germany, France, Belgium and the Netherlands) are more supportive of

the EU than countries that trade less actively and/or conduct a lot of their trade with non-EU countries (e.g., Britain and Ireland).<sup>7</sup> Ingebritsen (2000, chap. 1-2, 6) replicates this finding in her study of Nordic countries: Finland and Sweden, which trade mostly with the EU, are more pro-European (or less Euroskeptic) than Norway and Iceland, which trade mostly with the US and the UK.<sup>8</sup> Two explanations are offered for these findings. First, trade increases the economic and political power of export-oriented industries, which will lobby the government to pursue policies (such as EU accession) that will improve their access to foreign markets. Second, trade makes people more familiar with other countries and, hence, reduces their fears and prejudices about foreigners.

Finally, some researchers have argued that “varieties of capitalism” (Hall and Soskice 2001) explain cross-national differences in EU support. Brinegar, Jolly and Kitschelt (2004) find that voters in countries with centralized wage bargaining (Austria and the Nordic countries) are less supportive of the EU than voters in countries with decentralized bargaining (the rest of the EU, except Britain which is both decentralized and anti-EU).<sup>9</sup> They reason as follows. Under centralized bargaining, unions have an incentive to moderate their wage demands in exchange for full employment. National central banks reward such restraint by increasing money supply. Under decentralized bargaining, unions have an incentive to bargain for as high wages as possible. National central banks penalize such excess by cutting money supply. With the introduction of the euro, however, this system of rewards and punishments breaks down. Unions in decentralized countries will still bargain for large wage increases, which will increase prices in both decentralized and centralized countries. In response, the European Central Bank will cut money supply, which will increase unemployment in all countries.

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<sup>7</sup> However, Eichenberg and Dalton (2007) find that this relationship only holds until 1991.

<sup>8</sup> Ingebritsen (1998, chap. 6) also argues that Norway and Iceland have large fishing industries that would lose government subsidies and be required to adopt stricter environmental regulations in the EU.

<sup>9</sup> They leave out Ireland, Spain, Portugal and Greece whose wage-bargaining systems are still in flux.

Other analysts have argued that cross-national differences in EU support reflect quantitative or qualitative differences between welfare states. Ray (2004) finds that voters in countries with high levels of social spending (northern Europe) worry that European integration will lead to loss of social benefits, while voters in low-spending countries (southern Europe) do not. Following Esping-Andersen (1990, chap. 1), Brinegar, Jolly and Kitschelt (2004) distinguish between social democratic (universal coverage and high benefits), conservative (broad coverage and medium benefits), and liberal (restricted coverage and low benefits) welfare states.<sup>10</sup> They find that opposition to the EU is strongest in social democratic welfare states (the Nordic countries), where voters have the most to lose from the convergence of social policy toward the EU mean.

This logic, of course, would imply that voters in liberal welfare states would support the EU most strongly because they would have the most to gain from a common European social policy. However, this is not the case: voters in liberal Britain and Ireland are less supportive of the EU than voters in conservative continental Europe (e.g., Germany, France and Italy). Brinegar and Jolly (2005) argue that this is because people are risk-averse: they are afraid that changes to the current system, whatever it is, will create problems. For example, imposing the conservative welfare state on liberal economies might initially lead to higher unemployment and inflation. As a result, popular support for the EU is strongest in countries with the dominant—i.e., the conservative—welfare model because they would have to make the least changes if the EU adopted a common social policy.

Unlike with Western Europe, *the literature on the economic determinants of cross-national differences in EU support in Eastern Europe is very small, consisting of four studies.*<sup>11</sup> Like the older literature on Western Europe, three of the four papers focus

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<sup>10</sup> For a recent discussion of European welfare states, see Pontusson (2005), chap. 2, 8.

<sup>11</sup> As I will discuss in chapter 4, there is a sizable literature on the economic determinants of *individual-level variance* in support for European integration. For example, Tucker, Pacek and Berinsky (2002) and Tverdova and Anderson (2004) find that subjective winners of economic reforms (people who believe that

on the relationship between macro-economic outcomes and EU support. *Caplanova, Orviska and Hudson (2004) find that support the EU is strongest in countries whose GDP has grown the most during the transition to capitalism, while opposition to the EU is strongest in countries whose GDP has grown the least.* They make the following argument. East European countries have made a transition from socialism to capitalism. This transition has involved economic integration with the West through foreign investment and trade. As a result, East Europeans view EU accession as a continuation (or completion) of the post-Communist transition.

*By contrast, Christin (2005) finds that support for the EU is strongest in countries that are doing poorly economically (have high growth and low inflation), while opposition to the EU is strongest in countries that are doing well (have low growth and high inflation).* He argues that voters support or oppose the EU depending on whether they think that their country is economically self-sufficient or not. In high-growth, low-inflation countries, people believe that their country can succeed without EU help. In low-growth, high-inflation countries, however, people believe that their country needs to join the EU in order to stabilize its economy and receive EU aid. In an unpublished paper, Herzog and Tucker (2008) conclude that both Caplanova et al and Christin are right: while growth increases support for the EU, inflation reduces it, as does unemployment. However, all relationships are relatively weak. Finally, in another unpublished paper, Allam and Goerres (2008) argue that small countries are more supportive of the euro than big countries because they suffer more from price fluctuations in international markets and, hence, would benefit from a fixed exchange rate.

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their financial situation is improving and/or support the market economy) are more supportive of the EU than subjective losers (those who believe that their financial situation is worsening and/or oppose the market economy). However, they do not explore the implications of their argument for *cross-national variance* in EU support. That's unfortunate because the their data show that (a) the relationship between perceived financial situation and EU support does not hold in Poland and Slovakia (Tucker, Pacek and Berinsky, 562) and that (b) compared with Latvia, support for the EU is significantly stronger in Bulgaria and Slovakia and weaker in Estonia, even controlling for attitudes toward the market (Tverdova and Anderson, 200, 204).



## **Familiarity Breeds Contempt: My Argument in Brief**

To test the existing explanations of cross-national differences in EU support, and to develop my own, I will compare two “most similar systems” (Bunce 1999, chap. 1; Przeworski and Teune 1970, chap. 1-2; Tarrow 2010): the Baltic states of Lithuania and Estonia. As Table 1.2 shows, both are small countries in the northeastern periphery of Europe (for inspiration, see Lim 2007, 37). Both have a short history of political independence in the modern era, although Lithuania was an independent grand duchy in the Middle Ages. Both suffered large population losses during World War II through Soviet deportations of the former elites to Siberia, Nazi massacres of Jews and Communists, and the conscription of soldiers to Soviet and German armies. Under the Soviet rule of 1944-1991, both countries (but Estonia more so than Lithuania) experienced a large influx of Russian migrants, who settled in self-contained communities and whom the locals saw as a threat to their language and culture (Kiaupa et al 2002, chap. V, VI; Misiunas and Taagepera 1993, chap. 2-3; Lieven 1993, chap. 3-4).

Since the collapse of Communism, Lithuania and Estonia have built reasonably liberal, democratic, and effective states. People can express their opinions, join political groups, and participate in demonstrations without fearing arrest. Both countries hold regular elections, which governments often lose ([www.freedomhouse.org](http://www.freedomhouse.org)). The one blemish on Estonia’s record is that many of its ethnic Russian residents lack citizenship, largely because they have failed to pass the (rather tough) language and civics test.<sup>12</sup> However, under EU pressure, Estonia has granted citizenship to all children born in Estonia since the breakup of the Soviet Union (Pettai 2003; Budryte 2005, chap. 3). Both countries have relatively high levels of administrative corruption: to “get things done,” individuals and firms often bribe government officials. However, because of frequent turnover in government, systemic corruption is low: it is hard to purchase favorable

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<sup>12</sup> However, both countries passed strict language laws that require civil servants to speak the titular language.

legislation (Karklins 2005, chap. 3; World Bank 2000, chap. 1; [www.transparency.org](http://www.transparency.org)).

Economically, however, both countries have struggled since breakup of the Soviet Union. In the first half of the 1990s, their real GDP declined by more than a third while employment fell by a quarter as central planning collapsed. Since then, they have experienced some economic growth as they have “built capitalism” (Aslund 2002). However, at the time of the EU referendum in 2003, Lithuania’s per capita GDP was a still smaller than it had been in 1990, while Estonia’s was slightly bigger. Both countries also employed about 20% fewer people than they did under Communism, a change that was only partly reflected in the official unemployment rates of 10-12% (OECD 2000, chap. I; OECD 2003, chap. I, II; <http://publications.worldbank/WDI/>). Finally, both countries have adopted “liberal” welfare systems characterized by limited coverage and low social spending (Bohle and Greskovits 2008; <http://epp.eurostat.ec.europa.eu>). As a result, Estonia and, to a lesser extent, Lithuania have experienced a large increase in income inequality (Milanovic 1998, chap. 4; <http://publications.worldbank/WDI/>).

For all these similarities, however, Lithuanians and Estonians have very different views on European integration: a large majority of Lithuanians supported joining the EU, while a significant minority of Estonians opposed the accession. To explain why, I will use a “mixed” research design (Putnam 1993, chap. 1; Tarrow 1995). I will begin by conducting a qualitative content analysis of interviews with voters in Lithuanian and Estonian newspapers. *I will show that most Lithuanians hoped that joining the EU would help Lithuania develop economically by increasing foreign investment and trade and making Lithuania eligible for EU subsidies. By contrast, many Estonians worried that the accession would make Estonia dependent on the West by driving domestic producers bankrupt and allowing foreigners to buy up local resources.* I will also show that most Lithuanians saw European integration as an alternative to the economic policies pursued by their government, while most Estonians saw it as a continuation of such policies.

**Table 1.2: Spot the Difference: Lithuania and Estonia in 2003 (unless otherwise noted)**

Variable	Lithuania	Estonia	Similar or Different?
<b>EU support (effect)</b>	High: 91% in referendum; 73% in Eurobarometer survey	Low: 66% in referendum; 41% in Eurobarometer survey	<b>Different</b>
<b>Economic strategy in 1992-2003 (cause)</b>	Insider-oriented: manager-owners; moderate tariffs; trade with Russia	Outsider-oriented: foreign owners; no tariffs; trade with the EU	<b>Different</b>
<b>Structure of economy (link)</b>	Large agriculture and “old” industry; small service sector and “new” industry	Small agriculture and “old” industry; large service sector and “new” industry	<b>Different</b>
Size (population and territory)	Small: 3.6 million people; 65,000 km <sup>2</sup>	Small: 1.4 million people; 45,000 km <sup>2</sup>	Similar
Distance of capital from Brussels	Far: 1470 km; but close to Warsaw (393 km)	Far: 1601 km; but close to Helsinki (83 km) and Stockholm (378 km)	Similar
History of independent statehood	Short in the modern era: 1920-1940; but independent grand duchy in 1236?-1569	Short: 1920-1940 only; German colonization beginning in 1208	Different
Deaths during World War II	High (9%): Soviet deportations; Nazi Holocaust; guerrilla war	High (8%): Soviet deportations; Nazi and Soviet conscription; bombings	Similar
Size and treatment of Slavic minority	Medium size: 17%; OK treatment: full citizenship, but strict language law	Large size: 32%; Bad treatment: limits on both citizenship and language	Different
Political rights (a) and civil liberties (b)	Free: Freedom House scores of 1(a) and 2 (b) on 1-7 scale	Free: Freedom House score of 1 (a) and 2 (b) on 1-7 scale	Similar
Corruption	Moderate: Transparency International score of 5.5 on 1-10 scale	Moderate: Transparency International score of 4.7 on 1-10 scale	Similar
Support for Euroskeptic parties	Low: 18% for Liberal Democrats and Agrarians in 2004 election	High: 38% for Center Party and People’s Union in 2003 election	Different
Economic performance in 1990-2003	Bad: per capita GDP down from \$12,566 to \$12,000; unemployment up from n/a to 12%	Semi-bad: per capita GDP up from \$10,194 to \$13,906; unemployment up from 1% to 10%	Similar
Social performance in 1988-2003	Bad: Gini index of income inequality up from 0.22 to 0.32	Very bad: Gini index up from 0.23 to 0.37	Similar
Welfare state	Liberal: limited coverage and low spending (15% of GDP)	Liberal: limited coverage and low spending (14% of GDP)	Similar

*Sources:* Table 1.1; Statistics Lithuania, [www.std.lt](http://www.std.lt); Statistical Office of Estonia, [www.stat.ee](http://www.stat.ee); Nordregio 2000, 64-65; [www.geobytes.com](http://www.geobytes.com); Kiaupa et al 2002, S. II-V; Misiunas and Taagepera 1993, 356; [www.freedomhouse.org](http://www.freedomhouse.org); [www.transparency.org](http://www.transparency.org); Central Electoral Committee of Lithuania, [www.vrk.lt](http://www.vrk.lt); National Election Commission of Estonia, [www.vvk.ee](http://www.vvk.ee); <http://publications.worldbank/WDI/>; <http://epp.eurostat.ec.europa.eu>.

I will then test these hypotheses with data from the Candidate Countries Eurobarometer, the most comprehensive survey of public opinion on European integration. I will show that most Lithuanians believed that joining the EU would increase economic growth, reduce unemployment, and improve the standard of living for ordinary people. By contrast, most Estonians felt that the accession would increase prices and unemployment and make life more difficult for vulnerable groups like the elderly, farmers, small businessmen, and the unemployed. I will also show that most Lithuanians supported EU membership regardless of how they were doing economically and what they thought of their current economic situation. In Estonia, by contrast, the rich and people who were happy with their economic situation supported EU accession, while the poor and the unhappy opposed it.

To explain the results, I will compare the economic development of Lithuania and Estonia since the breakup of the Soviet Union (for inspiration, see George and Bennet 2005, chap. 1, 9). Using secondary literature and statistical data from the European Bank for Reconstruction and Development, I will show that Lithuania and Estonia pursued different strategies of economic reform. *Lithuania followed an insider-oriented strategy.* It maintained state ownership of basic infrastructure (e.g., railways and power plants) and sold non-infrastructure enterprises to their Soviet-era managers. It imposed moderate tariffs on imports, particularly of agricultural goods, and continued to trade heavily with Russia. *By contrast, Estonia adopted an outsider-oriented strategy.* It sold large state-owned firms, including infrastructure enterprises, to Nordic and American investors. It abolished all import tariffs and reoriented its trade rapidly from Russia to the West. *This explains why Lithuanians saw EU accession as an alternative to current economic policies, while Estonians considered it a continuation of such policies.*

Based on newspaper accounts and statistical data from the World Bank and the Vienna Institute for International Economic Studies, however, I will argue that *neither strategy worked very well.* The Lithuanian strategy slowed down the development of

services—especially complex services like finance and communications—and “new” industry (e.g., electronics), which lacked access to Western capital and technology. It also failed to stop the decline of infrastructure (e.g., railways) since the state did not have money for capital investments. The Estonian strategy hurt agriculture and “old” industry (e.g., food processing), which did not receive enough FDI to compensate for the loss of government subsidies and whose exports were subject to high tariffs in both Eastern and Western markets. It also led to a rapid decline of infrastructure, whose foreign owners used their monopoly power to increase prices and cut services while renegeing on their investment promises. *This explains why both Lithuanians and Estonians were dissatisfied with their country’s economic situation.*

I will also test the two most compelling alternative hypotheses to my economic theory. *The first one posits that Estonians are more Euroskeptic than Lithuanians because they have a) a shorter history of independent statehood and b) a larger Russian minority* (Vetik, Nimmerfelt and Taru 2006; Pettai 2005; Mikkel and Pridham 2005; Evans and Lipsmeyer 2001). Lithuania was an independent state from the thirteenth to the sixteenth century, when it was incorporated into Poland and, later, Russia. Estonia was colonized by the German crusaders in the thirteenth century. Until the Russian revolution of 1917, the Germans constituted the ruling class in Estonia, regardless of which power—the Teutonic Order, Sweden, or Russia—claimed sovereignty over its territory. Estonia also experienced a larger inflow of Slavic (mostly Russian) migrants under the Soviet rule: the Slavs make up 17% of the population in Lithuania, but 32% in Estonia. Since they came in large numbers, many Estonian Russians lived in closed ethnic enclaves and never learned the local language. As a result, Estonians are more touchy about their political independence and cultural identity than Lithuanians.

Using content analysis and survey data, I will show that there is some evidence for the nationalism hypothesis. Compared with Lithuanians, Estonians were less likely to believe that their country was historically part of Europe and more likely to worry that

they would lose their political independence and cultural identity in the EU. *However, at the individual level, there was no consistent relationship between nationalist values and EU support in either country.* Thus, people who identified themselves with their nation (rather than Europe) opposed EU membership, but people who were proud of their nation supported the accession. *Moreover, at the aggregate level, opposition to the EU in Estonia (but not in Lithuania) increased significantly in 1992-2003—something that would be difficult to explain in terms of national identity alone.* Instead, it seems that Estonians' negative experience with foreign investment and trade made them worry about losing their sovereignty and identity, while Lithuanians' lack of foreign experience quieted such concerns.

*Another serious causal rival to my theory would focus on political factors, namely a) party preferences (Mažylis and Unikaitė 2004; Mikkel and Pridham 2004; Duvold and Jurkynas 2006; Sikk 2006) and b) the political opportunity structure (Szszerbiak and Taggart 2004 a, b; Mikkel and Kasekamp 2005).* In Lithuania, all major parties, including the governing post-Communist Social Democrats, supported EU membership as a way of modernizing the Lithuanian economy and increasing living standards. Foreign investment and aid would improve Lithuanian infrastructure and create new, high-paying jobs. Better access to EU markets would allow Lithuanian farmers to compete with European producers on equal terms. By contrast, the largest party in Estonia, the left-populist Centrists, opposed EU accession on current terms because it would hurt domestic producers and the poor. EU sanitary and quality standards would drive farmers and small businesses bankrupt. EU-mandated environmental surcharges and consumption taxes would increase the price of food, gasoline, and electricity, not to mention alcohol and cigarettes.

I will demonstrate that there is some support for both hypotheses. At the aggregate level, Euroskeptic parties clearly enjoyed more popular support (measured by their vote share in the most recent general election) in Estonia than in Lithuania (see

Table 1.3). At the individual level, party preferences influenced voters' attitudes toward the EU in Estonia, but not in Lithuania. However, Estonians who did not have a party preference also tended to oppose EU membership. This suggests that political opportunities had stronger impact on EU support than party preferences per se (for the difference between the two, see Tarrow 1998, chap. 5). By joining the other parties in advocating EU membership, Lithuanian Social Democrats helped to create the impression that "everybody" supported the EU. By criticizing the terms of the accession, Estonian Centrists broke the "spiral of silence" and encouraged latent Euroskeptics—their own supporters and people who did not have a party preference—to vote against the EU (Noelle-Neumann 1991, chap. 1, 3, 17, 26).

**Table 1.3: Enthusiasts and Skeptics: Political Parties and the EU in Lithuania and Estonia in 2003-2004**

Party	Lithuania		Party	Estonia	
	EU (1-20)*	Vote (%)**		EU (1-20)*	Vote (%)**
Labor Party <sup>a</sup>	-	28			
Liberal Democrats	14	11	Center Party	10	25
Agrarians	11	7	People's Union	14	13
Social Democrats	17	21			
Social Liberals <sup>b</sup>	16	-	Moderates	19	7
Liberal/Center Union	19	9	Reform Party	17	18
Homeland Union	19	15	Fatherland	17	7
			Res Publica	19	25

\* Position on a scale from 1 (opposes joining the EU) to 20 (supports joining the EU).

\*\* Share of the vote in the most recent (2003 or 2004) general election.

<sup>a</sup> New party.

<sup>b</sup> Joint list with Social Democrats.

Sources: Expert survey by Benoit and Laver (2006), [http://www.tcd.ie/Political\\_Science/ppmd](http://www.tcd.ie/Political_Science/ppmd); Central Electoral Committee of Lithuania, [www.vrk.lt](http://www.vrk.lt); National Election Committee of Estonia, [www.vvk.ee](http://www.vvk.ee).

*However, I will argue that (lack of) elite conflict over EU accession itself was, in part, a product of the strategies of economic reform. In the 1990s, Lithuania's post-Communists advocated "national capitalism," including voucher-based privatization and protectionist trade policies. In the 2000s, however, they came to support European*

integration because their financial backers among the insider-owners wanted to have better access to European markets, while their working-class and rural voters felt that insider-oriented reforms had only benefited the former Communist nomenklatura. The Centrists followed a different trajectory. Heirs to the anti-Communist (but vaguely social democratic) Popular Front, they did not have a clear position on the EU (or anything else) in the 1990s. In the 2000s, however, they adopted Euroskeptic themes to appeal to domestic capitalists, who wanted to do business with Russia, and workers, farmers and pensioners, who blamed foreigners for the hardships they had endured.

### **The Road to the Referendum: Chapter Outline**

Chapter 2 will use content analysis of a) interviews with voters and b) letters to the editor in Lithuanian and Estonian newspapers to develop hypotheses about why most Lithuanians supported joining the EU, while many Estonians did not. I will show that most Lithuanians believed that joining the EU would help their country to catch up with the West by making it eligible for EU subsidies and encouraging foreign investment and trade. They also hoped to take advantage of the accession individually by working and studying abroad. In any case, they argued, life was so bad that it could not possibly get worse. By contrast, many Estonian respondents worried that joining the EU would make their country dependent on the West by driving domestic producers out of business and allowing foreigners to buy up local resources. They also believed that they would be personally worse off in the EU because prices would increase and jobs would disappear. Asked to explain why they thought so, they said that all previous economic reforms had made their life worse.

Chapter 3 will test the hypotheses developed in Chapter 2 with survey data from the Candidate Countries Eurobarometer (CCEB). I will show that both at the beginning and the end of the EU accession process, Lithuanians and Estonians thought of the EU mainly in economic terms. In 1992, both Lithuanians and Estonians strongly supported



EU membership so that their countries could get EU aid and gain access to European markets. They were less interested in the political benefits of the accession, such as help with building democracy and protecting peace and security in Europe. In 2003, most Lithuanians still supported joining the EU, in part because they believed that Lithuania was historically part of Europe, but mostly because they hoped that it would improve their standard of living. By contrast, over a third of Estonian voters now opposed EU membership because they worried that it would undermine their political independence and cultural identity and, above all, increase prices, destroy jobs, and hurt farmers, pensioners, and other vulnerable groups.

Chapter 4 will use the 2003 CCEB to explore the micro-foundations of these macro-level differences. I will show that, in both countries, people who trusted the government were more supportive of EU membership than those who did not. Clearly, EU referenda were, to some extent, votes of (non-) confidence in the political elites. However, the differences between the two countries were at least as important as the similarities. Knowledge about the EU increased support for the EU in Lithuania, but not in Estonia, perhaps because Lithuania negotiated a more favorable accession treaty. Party preferences affected EU support in Estonia, where the largest party opposed the accession on current terms, but not in Lithuania, where all major parties supported EU membership. Finally, the strongest predictors of EU support in Estonia were income and satisfaction with one's economic situation, neither of which had any impact on EU support in Lithuania. Clearly, Estonians saw EU accession as a continuation of current economic policies, while Lithuanians did not.

Chapter 5 will compare Lithuanian and Estonian strategies of economic reforms to explain why most Lithuanians supported EU membership, while many Estonians (particularly the poor and the disgruntled) opposed it. Lithuania followed an insider-oriented strategy. It maintained state ownership of basic infrastructure (e.g., railways) and sold other state-owned enterprises (SOEs) to their Soviet-era managers. It imposed

moderate tariffs on imports and continued to trade heavily with Russia. Estonia pursued an outsider-oriented strategy. It sold SOEs, including infrastructure enterprises, to foreign investors. It abolished all import tariffs and quickly reoriented its trade from Russia to the EU. Neither strategy worked particularly well. The Lithuanian strategy slowed down the development of services and “new” industry (e.g., electronics). The Estonian strategy led to a rapid decline of agriculture and “old” industry (e.g., food processing). Neither strategy could prevent the decline of infrastructure (e.g., railways). As a result, both Lithuanians and Estonians were unhappy about their country’s economic situation, but Lithuanians saw European integration as a solution to their country’s problems, while Estonians considered it the cause of theirs.

Chapter 6 will summarize the main findings of the dissertation and explore two more issues. First, I will explain why Lithuania and Estonia adopted different strategies of economic reform. The immediate explanation is simple. In Lithuania, the post-Communist Democratic Labor Party, with close personal and financial ties with Soviet-era managers, won the first independence-era parliamentary election. In Estonia, the conservative Fatherland, backed by the German Christian Democrats, Estonian émigrés, and export-import businesses, emerged victorious. However, I will argue that Lithuania and Estonia would have probably pursued different economic policies regardless of which party came to power. Historically, Lithuania’s best friend—and worst enemy—had been Poland, another poor East European country. Estonia had close ties with Germany, Sweden and Finland, rich West European nations. As a result, Estonia could expect to receive more Western investment than Lithuania. The two countries also had different economic structures. Lithuania had a larger agriculture and heavy industry. Estonia had a bigger service sector and light industry. Therefore, Estonia could more easily withstand the loss of the Russian market and raw materials.

Second, using the example of the former Czechoslovakia, I will show that my argument “travels” to Central Europe (see Bunce 1999, chap. 1, 6 for a similar move).

Like Lithuania, Slovakia pursued an insider-oriented strategy of reforms. It sold SOEs to their managers and provided cheap loans to firms undergoing privatization. It imposed high tariffs on Western imports and continued to trade heavily with Russia and Eastern Europe. This policy slowed down the development of skill-intensive services and “new” industry (e.g., cars), which lacked access to Western capital, technology, and markets. In the EU accession referendum, 94% of Slovaks supported EU membership, more than in any other Central European country. By contrast, the Czech Republic pursued an outsider-oriented strategy similar to Estonia’s. It sold large SOEs to Western (mostly German) capitalists and provided subsidies to foreign “greenfield” investors. It exempted most EU goods from import tariffs and reoriented its exports to the EU. These policies undermined agriculture and “old” industry (e.g., steel and mining), which received little foreign investment and were subject to EU tariffs. In the EU referendum, only 76% of Czechs supported the accession, less than in any other Central European country.

## **CHAPTER 2**

### **DEVELOPMENT OR DEPENDENCY? CONTENT ANALYSIS OF LITHUANIAN AND ESTONIAN NEWSPAPERS**

#### **Introduction**

Why did Lithuanians strongly support EU membership, while Estonians came close to rejecting the accession? To answer this question, scholars have focused on history and culture. Grabbe and Hughes (1998, chap. 6), Grabbe (2003), Ozolina (2003), and Mikkel and Pridham (2004) argue that Estonian and Latvian Euroskepticism reflects their short history of independent statehood. Lithuania was an independent grand duchy in the Middle Ages. By contrast, Estonia and Latvia only became independent states after World War I. As a result, Estonians and Latvians are more suspicious of all kinds of unions than Lithuanians. Pettai (2005) and Vetik, Nimmerfelt and Taru (2006) claim that Estonians and Latvians have a less secure national identity than Lithuanians. Medieval Lithuania was ruled by an indigenous aristocracy. Estonia and Latvia were colonized by German crusaders and only developed a national consciousness in the nineteenth century. As a result, Estonians resent the Europeans, while Lithuanians consider themselves their equals.

Analysts have also debated the role of ethnicity in shaping popular attitudes toward the EU in the Baltics. Evans and Lipsmeyer (2001), Ozolina (2003), and Pettai (2005) argue that Estonia and Latvia experienced a larger influx of Russian migrants during the Soviet rule than Lithuania. After the breakup of the Soviet Union, they adopted a strict citizenship law in order to limit Russian political influence. By contrast, Lithuania gave citizenship to all Russians who wanted it. Now Estonians are worried that the EU will force them to change their citizenship laws, while Lithuanians are confident that their policies will pass EU muster. However, Whitefield, Rohrshneider and Alisauskiene (2006) maintain that it is the ethnic Russians who oppose EU membership

in the Baltics. The EU agrees with the Balts that the Baltic Russians are migrants who must learn the local language and apply for citizenship. It also put pressure on Russia to withdraw its troops from the Baltics. Estonia and Latvia are more Euroskeptical than Lithuania simply because they have more Russians.

*Using qualitative content analysis of Lithuanian and Estonian newspapers, however, this chapter shows that Lithuanians and Estonians also had different economic expectations about the EU. Most Lithuanians hoped that joining the EU would help their country to develop economically by making it eligible for EU subsidies and encouraging foreign investment and trade. They also planned to take advantage of the accession individually by working, studying and/or permanently settling in the West. By contrast, many Estonians worried the accession would make Estonia dependent on the West by driving domestic producers out of business and allowing rich foreigners to buy up Estonian economic resources. They also thought that they would be personally worse off in the EU because prices would increase and jobs would disappear.*

The rest of the chapter is structured as follows. The next section will discuss the methodology of content analysis. The following section will compare popular attitudes toward the EU in Lithuania and Estonia using CA of Lithuanian and Estonian newspapers. The conclusion will sum up my findings.

### **(Dis)content Analysis: Turning Words Into Numbers (and Back)**

To analyze popular attitudes towards European integration in Estonia, I used ethnographic content analysis (ECA) of Lithuanian and Estonian newspapers. ECA has a lot in common with its better-known cousin, quantitative content analysis (QCA). Both reduce the content of a text to a set of categories (e.g., themes) through systematic coding. Both then compare the frequencies of these categories to assess their importance (Neuendorf 2002, chap. 1, 3; Weber 1990, chap. 1-2). However, EQA differs from QCA

in two ways. First, QCA uses theoretically predetermined categories to analyze data. By contrast, EQA approaches data with certain theoretical expectations (for example, I expected economic issues to be more important for Baltic voters than previous research had suggested), but allows the categories to emerge out of the data. Second, QCA typically uses “manifest coding,” which means that the coder counts specific words or phrases in the text. By contrast, EQA involves “latent coding,” whereby the coder looks for ideas and concepts underlying particular verbal expressions (Altheide 1987; Altheide 1996, chap. 1-4, 6). This makes EQA a better tool for generating new hypotheses.

Ms. Ieva Šriupšaitė, a graduate student in the Department of Communications at the Vytautas Magnus University in Kaunas, conducted the CA of Lithuanian newspapers. I analyzed Estonian papers. Our sample included a) the English-language weekly *Baltic Times*; b) the national quality dailies; c) the national tabloids; d) the national weeklies; e) the rural newspaper; f) the main Russian-language newspapers; and g) the main newspaper in each region (county) of Lithuania and Estonia. (For a brief description of the papers, see Table 2.1).<sup>13</sup> We analyzed all issues of these newspapers from the month of the EU referendum (May 2003 in Lithuania and September 2003 in Estonia). Our sample included 1) letters to the editor and 2) articles that *directly quoted voters*, including a) “question of the day” interviews with “(wo)men in the street” before the referendum; b) investigative reports on attitudes toward the EU in particular regions; and c) “exit” interviews with voters on the referendum day. We excluded 1) opinion pieces and 2) longer interviews with elites, such as politicians, businessmen, and academics.

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<sup>13</sup> Aukše Balcytienė, “Lithuanian Media – A Question of Change,” in *Baltic Media in Transition*, ed. Peeter Vihalemm (Tartu: Tartu University Press, 2002), 103-134; Aukše Balcytienė and Rūta Marcinkevičienė, “Lithuania: Print is Dead... Long Live Print,” in *Print and Online Newspapers in Europe: A Comparative Analysis of 16 countries*, ed. Richard van der Wulff and Edmund Lauf (Amsterdam: Het Spinhuis, 2005), 187-200; Halliki Harro-Loit, “Estonia: Examining Newspaper Change,” in *Print and Online Newspapers in Europe*, ed. van der Wulff and Lauf, 105-116; and Kertu Saks, “From Soviet to Market-Oriented: Organisational and Product Changes in Estonian Newspapers, 1988-2001,” in *Baltic Media in Transition*, ed. Vihalemm, 187-206.

**Table 2.1: Meet the Press: Lithuanian and Estonian Newspapers in 2003**

Lithuania		Estonia	
Title	Description	Title	Description
<b>A) Baltic and National Papers</b>		<b>A) Baltic and National Papers</b>	
<i>Baltic Times</i>	Weekly	<i>Baltic Times</i>	Weekly
<i>Kauno diena</i>	Daily	<i>Eesti Päevaleht</i>	Daily
<i>Lietuvos rytas</i>	Daily	<i>Postimees</i>	Daily
<i>Lietuvos žinios</i>	Daily	<i>SL Õhtuleht</i>	Daily tabloid
<i>Obzor</i>	Russian weekly	<i>Estoniia</i>	Russian daily
<i>Respublika</i>	Bilingual daily	<i>Molodezh Estonii</i>	Russian daily
<i>Vakaro žinios</i>	Daily tabloid	<i>Maaleht</i>	Rural weekly
<i>Valstiečių laikraštis</i>	Rural semiweekly		
<i>Veidas</i>	Weekly		
<b>B) Regional papers</b>		<b>B) Regional papers</b>	
<i>Alytaus naujienos</i>	Daily	<i>Hiiu Leht</i>	Semiweekly
<i>Kalvotoji Žemaitija</i>	3 x per week	<i>Järva Teataja</i>	Daily
<i>Klaipėda</i>	Daily	<i>Koit</i>	3 x per week
<i>Panevėžio rytas</i>	3 x per week	<i>Lääne Elu</i>	3 x per week
<i>Šiaulių kraštas</i>	Daily	<i>Meie Maa</i>	Daily
<i>Suvalkietis</i>	3 x per week	<i>Pärnu Postimees</i>	Daily
<i>Tauragės kurjeris</i>	Daily	<i>Sakala</i>	Daily
<i>Utenis</i>	3 x per week	<i>Severnoe Poberezhe</i>	Russian daily
		<i>Valgamaalane</i>	Daily
		<i>Virumaa Teataja</i>	Daily
		<i>Vooremaa</i>	3 x per week
		<i>Võrumaa Teataja</i>	3 x per week

*Note:* The Lithuanian weekly *Ekstra*, the Estonian weekly *Eesti Ekspress* and the Estonian regional paper *Raplamaa* had no articles that met our selection criteria.

Our unit of coding was a theme: some positive or negative aspect of EU membership. The themes were developed by a) inspecting the various reasons people gave for their vote choice and b) grouping them together under a common denominator. (For examples, see the next two paragraphs.) Some people gave more than one reason for why they supported or opposed the EU, although few respondents mentioned more than two or three reasons. These were all coded separately, provided that they fell under separate themes. Some people were not sure how they would vote because they liked some things about the EU and disliked others. The issues they mentioned were also coded separately. Naturally, people brought up various reasons—economic, political, and cultural—to explain why they supported or opposed the EU. In this chapter,

however, I will concentrate on economic issues because they a) have been largely ignored in the existing literature and b) made up about two thirds of all references to the EU in Lithuania and about 60% in Estonia.

In explaining why they supported or opposed the EU, most people focused on *what* they thought the consequences of joining the EU would be. EU supporters believed that the accession would increase economic growth, while EU opponents believed that it would destabilize the economy (*Growth v. Instability*). EU supporters thought that the EU would provide subsidies to farmers, while EU opponents thought that it would impose unreasonable regulations on farmers (*Subsidies v. Regulations*). EU supporters argued that the accession would create jobs and increase wages, while EU opponents argued that it would destroy jobs and increase prices (*Higher Living Standard v. Lower Living Standard*). Finally, EU supporters hoped to work and study abroad, while EU opponents worried that foreigners would drive domestic producers bankrupt and buy up local economic resources (*Opportunities in the West v. Exploitation by the West*). As Table 2.2 shows, most Lithuanians believed that joining the EU would help their country develop economically, while many Estonians feared that it would impoverish their country and make it dependent on the West.

However, some respondents also explained *why* they believed that EU membership would make life better or worse. Some EU supporters said that joining the EU would allow their country to continue its successful economic policies, such as privatization and free trade, while some EU opponents said that the accession threatened their country's achievements, such as rapid economic growth (*Continuation of Success v. Threat to Success*). For the most part, however, *both* EU supporters and opponents were unhappy about their country's current economic situation, especially widespread poverty and unemployment. However, EU supporters (most Lithuanians) hoped that EU accession would solve these problems, while EU opponents (many Estonians) feared that it would make them worse (*Remedy to Failure v. Continuation of Failure.*)



**Table 2.2: Stairway to Heaven or Road to Hell? Lithuanian and Estonian Attitudes toward the EU in 2003**

Positive Themes	Number of references		Negative Themes	Number of references	
	Lithuania	Estonia		Lithuania	Estonia
<b>A) WHAT?</b>			<b>A) WHAT?</b>		
Growth	31	30	Instability	6	25
Subsides	14	17	Regulations	5	24
Higher Standard of Living	25	23	Lower Standard of Living	8	33
Opportunities in the West	26	17	Exploitation by the West	7	29
<b>B) WHY?</b>			<b>B) WHY?</b>		
Continuation of Success	3	8	Threat to Success	1	6
Remedy to Failure	19	9	Continuation of Failure	11	19

*Source:* Content analysis of Lithuanian and Estonian newspapers in Table 2.1 from May (Lithuania) and September (Estonia) 2003.

## **Lithuania: The EU as Development**

### **Lithuania needs to catch up and the straightest way to success is the EU**

Most Lithuanians hoped that joining the EU would help their country to develop economically by encouraging foreign investment and trade.

Lithuania needs to catch up, and the straightest way to success is the EU. Frontiers will open, financial help will come, and the number of investors will increase.

The EU is progress. Lithuanian businessmen will be able to sell their goods in other countries more easily; it will be easier for people to move around; maybe there will be more work for young people.

But wouldn't EU membership would subject Lithuania to more intense foreign competition? Many people said that they welcomed competition because it would force Lithuanian producers to become more efficient and allow Lithuanian workers to show how diligent they were.

After we join the EU, we will be forced to compete with other countries. This will help our country to make progress: Lithuania will no longer be a secluded province of Europe. That's why it is a good idea to vote 'yes' in the referendum.

I would like as many people as possible to vote for the EU. Lithuanians are very diligent. This quality will be appreciated in EU member states and will become the basis for the prosperity of our country.

By contrast, staying outside the EU would lead to an economic catastrophe. Lithuania was too small to survive on its own. The only alternative to EU accession was to become like Belarus—an isolated and impoverished country in the Russian periphery.

I am just afraid what will happen if we vote 'no.' If we don't become part of Europe, what other model do we have? Belarus? Kaliningrad? People there have absolutely no hope at all. As difficult as things are here now, joining the EU will give us some sort of hope.

There is no question about how to vote—I will vote for the EU. I cannot even imagine where we would find ourselves if we stayed outside Europe. Could we be alone? Like Switzerland? But are we such a strong and powerful country? Alone by ourselves we would not have any chance. Could we live closed like Belarus? Neither a person nor a country can close themselves off.

## **For Lithuanian farmers EU help is like a life-buoy**

Besides foreign investment and trade, Lithuanian EU supporters argued, another big advantage of EU membership was that it would make Lithuania eligible for EU aid. In particular, Lithuanian farmers would begin to receive EU subsidies, which would increase their pitifully low incomes and allow them to compete on equal footing with West European agribusinesses.

The situation of farmers cannot become worse - only better. In EU countries agriculture is subsidized and Lithuania is not rich enough to be able to subsidize its own farmers sufficiently. For Lithuanian farmers EU help is like a life buoy.

Joining the EU will enable our farmers to get the support that farmers in European countries are getting. I will vote for EU membership, and I invite all rural people to do so. I think that after we join the EU, much fairer relations [between Lithuania and Europe] will develop and support for farmers will be real, not declarative.

More broadly, EU subsidies would help rural areas to develop. Towns and villages could build new roads; farms and food processing plants could purchase new equipment. Computers and internet would connect rural Lithuania to the wider world.

[O]ur villages and agriculture will definitely have to be modernized. Over the next few years, a lot of EU resources will be allocated for that. There will be money to renovate buildings, equip factories, buy machinery, support young farmers, improve roads, plant forests, energize rural communities, etc. These projects will be funded from 60% [of the total cost] to 100%. If these funds are used as intended, maybe our villages will recover.

Computers, e-mail, internet are still just a dream for most villagers. I hope that after Lithuania becomes a member of the EU, all these twenty-first century information technologies will be available even in the remotest corners of the countryside and allow everybody to communicate with the rest of the world.

Some Lithuanians even worried that EU support for farmers would be so generous that they would stop working hard. Instead of relying on EU aid, they argued, people should take advantage of the economic opportunities created by EU accession.

It's important to know some language of the EU and not to be lazy waiting for someone to put a plate full of offers in front of your nose.

With financial support and subsidies, farmers were encouraged to approve of EU accession. I and all other students who voted affirmatively in the referendum expect from Europe not subsidies or pity, but opportunities to live differently.

### **I hope for a different, easier life, better salaries for everybody**

Whether they placed their hopes in subsidies or the free market, however, most Lithuanians believed that EU membership would improve their standard of living.

Economic growth and closer ties with foreign countries would create new jobs.

It is a good day for Lithuania. When we join the EU, the economy will get better and people will have more jobs. Maybe then young people will have a reason to stay here instead of going abroad.

I think that after we join the EU, my services as a translator will be also needed in Lithuania. I heard that the demand for such specialists would constantly increase.

Growing competition for workers would put pressure on domestic capitalists to raise wages.

I hope for a different, easier life, better salaries for everybody. It will be easier to go and work abroad, and when there are fewer good workers left, businessmen will have to increase salaries.

I will vote for the EU because I hope that after Lithuania becomes a member of the EU there will be more jobs and salaries will increase—people will be richer.

Wage increases, in turn, would boost tax revenues and allow the government to spend more on social programs, such as pensions.

Isolation has never brought use to anyone. After we join the EU, better conditions for business will be established. Production will expand. Even ordinary people will begin to live better because more taxes will be levied. These [taxes] will also be used to improve social conditions.

Maybe then our pensions will increase slightly and [natural] gas will become cheaper because now I spend all my money on medicines and heating.

## **The freedom of migration: isn't that what the Lithuanians want?**

Finally, many Lithuanians hoped that joining the EU would make it easier for them to travel, study, work and/or settle permanently in Western Europe. People could travel in Europe without the hassle and humiliation of passport controls and customs inspections.

A young and energetic person with plenty of unrealized ideas will definitely say 'yes': 'yes'—to united Europe, 'yes'—to open borders, 'yes'—to the whole world under my feet.

Don't Lithuanian citizens want millions of euros to flow into Lithuania, don't we want to travel in Europe like normal people and not like second-class aborigines? ... Do we really want to go through customs procedures that degrade our dignity, to be denied treatment at Western hospitals, to stand in lines in front of embassies, to drive old cars and to buy clothes for our children from second-hand stores? Awful.

Young people could study abroad to broaden their horizons and learn new skills:

Borders with European countries will open; there will be more opportunities to study and work in foreign countries.

It will be easier for young people to study abroad, to improve themselves, to experience a new culture, to broaden their understanding, and to come back to Lithuania with more knowledge.

It would also become easier for Lithuanians to work abroad. Work visas would no longer be required of Lithuanian citizens. Lithuanians who work in Europe illegally would receive legal status.

I clearly understand the advantages of Lithuanian membership in the EU. Lithuanians in Ireland will feel it the next day. They will no longer need work permits and even those who are working here illegally will become legal workers at once. The Lithuanian driver's license will also become valid immediately.

I voted 'for' [the EU] because I hope to find a job in Europe. I would like to go to Denmark for at least a month; I could pick strawberries there. But farmers there do not want us because they have to do additional paperwork for workers from non-EU countries. From now on everything will be better.

Finally, EU membership would allow Lithuanians to settle permanently in Europe where the standard of living would remain higher than in Lithuania for a long time.

The freedom of migration allows us to choose the best place to live and work. Isn't that what Lithuanians want?

I am happy in advance for our young people who will now have totally different opportunities to choose a European country where they would like to live and work. It is still impossible to have a European standard of living in our country, and I do not believe that this will become possible any time soon.

### **How long can we be beggars?**

Thus far, I have focused on *what* the Lithuanian Euro-enthusiasts expected from the EU, from financial aid to the opportunity to work abroad. However, the CA also offers some insights into *why* most Lithuanians held positive views about the EU. Some (very few) people said that joining the EU would continue the policies that had already made life better for ordinary Lithuanians.

I gladly voted for EU membership. I trust European states and I am very happy that Lithuania will become part of united Europe. And my children, young farmers, believe in their future. They live on the land and are satisfied; we have enough of everything thus far.

I decided to vote 'for' [the EU] a long time ago. People in Lithuania already have a good standard of living, but I hope that there will be more order. I do not know any Russian woman who will vote 'against.'

However, most Lithuanians said that they supported the EU because *life could not get any worse*. Unemployment was high; pensions were low; there was no money for nice things in life; young people were leaving the country.

I will vote like everyone else—for Europe. How long can we be beggars? I believe that life will get better in Europe. It cannot get worse than it is now: the youth is running away from Lithuania, there is no work, and how do the pensioners live? The referendum is our hope for a better life.

It is a matter of material things—I want to travel, to go to Egypt, Turkey. But as it is now, after I pay my rent and utilities and buy some food, I do not even have extra money left to go to a café and buy a coffee. A person needs some of the nice things in life, too.

Some Lithuanians specifically blamed Lithuania's problems on their corrupt government and exploitative capitalists.

I support joining the EU because I know that it cannot get any worse than it was under the rule of Russians and [the post-Communist prime minister Algirdas] Brazauskas. Now there is no truth, no justice, no order left in Lithuania. I hope that my son and my grandchildren will live in a different Lithuania.

When Lithuania joins the EU, borders will open and those who are exploiting cheap labor, or illegally exporting workers to Western countries, will lose their earnings. Besides, employers will have to raise wages, at least for the most professional workers. Otherwise they will go where they can get better paid.

The EU offered Lithuania a way out of its economic difficulties. People could earn a decent living and the quality of life would improve.

I will vote 'for' [the EU]. My motive is simple: I am young, I need to create a family and bear children. I believe that my family will be better off with the EU than without. It cannot get any worse than it is now and I believe that it will get better. If you do not believe in anything, maybe you should go to Ireland to clean fish? I do not want to do that. I want to live in my country and to work normally.

Let us not be afraid of the current EU states because life cannot get any worse. I hope that in a few years we can see smiles more often in the streets of Lithuanian towns. And maybe someday Paul McCartney himself will come and sing his joyful protest ballad, 'Let's give Ireland to the Irish.'

## **Estonia: The EU as Dependency**

### **Why do we need another transition period, new instability?**

If Lithuanians looked forward to the economic changes that EU membership might bring, Estonians said that they were tired of changes. After more than ten years of strenuous economic reforms, they felt, Estonia had achieved a modicum of stability.

Joining the EU would upset this.

Let everything stay as it is. There have been so many changes recently that we would now like to have some peace.

Things have just got settled; we have been working our way towards stability for twelve years. Why do we need another transition period, new instability?

More concretely, many Estonians argued that their country was economically unprepared for EU accession. The Estonian economy was too weak to withstand European competition. Estonian consumers would not be able to afford European prices.

We are not developed enough to join the EU. Let's wait a little and then compete like equals with Germany and other countries.

I am against EU accession. I think that the Estonian economy is not yet ready for it—in the sense that we have a very weak economy, but the EU has high prices.

Finally, some people argued that Estonia should follow the example of Nordic countries that had gotten rich without joining the EU or adopting the euro.

Why are they dragging us to the EU? And why isn't prosperous Norway joining? Where are the economic calculations showing that I will be better off there? There are no such calculations, only talk.

Against, against. And why did the Swedes say 'no' to the euro? Because it is not good.

### **If we cannot fish all year around, we will die of hunger**

Many Estonians feared that EU regulations would drive Estonian farmers out of business. The EU would regulate every aspect of agricultural production, from raising animals to baking bread.

On average, every day some official will come by to check up on me. These guys are such a pain. They say that chickens and cows cannot be [kept] together [in the same shed]. Damn it, this is disrespect for our culture.

You are not allowed to use a wood basin to make bread, even though dough mixed in a steel basin does not taste the same.

Fishermen, too, would be hurt by EU regulations. The fishing season would be shortened and limits would be imposed on how much fish can be caught.

The EU built us a school that cost two million [Estonian crowns], but it also limits fishing and comes up with requirements that we cannot fulfill. If we cannot fish all year around, we will die of hunger.



I think that people worry the most about the future of fishing—that the EU will impose strict quotas on fishing and that people will have nothing to live on.

Finally, EU sanitary standards would bankrupt small businesses. For example, stores and restaurants in the countryside would be required to install expensive new equipment or closed down.

They say that there are laws in the EU about how many sinks a store must have. And ventilation and stuff. And how many times you must write down the temperature in the refrigerators. And all kinds of controls and stuff.

Take, for example, the standards for school cafeteria. I have nothing against them being renovated, but if some kids will not be able to eat because rural schools must have their food prepared elsewhere, then this makes no sense.

### **Pensioners and the unemployed will have to eat porridge for a long time**

If Lithuanians believed that joining the EU would raise the standard of living for most people, Estonians thought that ordinary people would be worse off in the EU.

Unemployment would increase. Foreign investors would rather move production to Russia than raise wages for Estonian workers. Family farms and small businesses would go bankrupt because of EU regulations.

And these foreign firms that employ many people now—many of them will immediately go bankrupt in the union. They are simply so greedy that they would rather let their businesses go under and set up shop in Russia than increase wages here.

Like many people in rural areas, I am afraid of losing my job. Without a job, there is no income. What are people going to live on? Small barns will be closed down.

However, the biggest fear about EU accession in Estonia was that it would increase prices. The EU would impose tariffs on imports from non-EU countries and increase consumption taxes. This would increase the price of food, alcohol, gasoline and other basic necessities.

I would not change course. You won't be able to get a bottle [of beer] for less than a euro? Where will I get this money from?

Some people say that food prices will increase by half, others that they will go up 2.5 times. One man said that the price of gasoline will increase 1.8 times. Everything will become more expensive. My pockets will be emptier and my life more difficult.

Inevitably, price increases would hit low-income groups (e.g., pensioners, the unemployed, and people who earn the minimum wage) the hardest.

A big disadvantage of joining the EU is that prices will rise faster than wages and pensions. ... The pensioner or the unemployed who could occasionally afford sausage before the accession will have to eat porridge for a long time after the accession.

(Buys socks.) I can afford to buy one pair for myself. I think that we, poor people, who barely make the minimum wage, will not gain anything from it. They say that everything will become more expensive.

### **Blacks and others will come in and privatize everything**

Most important, however, many Estonians believed that EU membership would subject their country to Western exploitation. Competition from European agribusinesses would drive Estonian farmers bankrupt.

Everything will become more expensive and stores will only sell European goods. We work our asses off here, but who is going to buy our potatoes and onions now?

When the borders open up, foreign foodstuffs will take over the market. All that remains in Estonia is the income tax on wage laborers. The big shots of the republic said before the referendum that the EU promoted local and national agriculture. But this does not exist in Estonia!

Foreign capitalists would buy up Estonian economic resources. This included both the remaining SOEs, such as the power plants, and natural resources, such as Lake Peipsi, the main source of livelihood for the fishermen living on its coast.

Blacks and others will come in and privatize everything—factories and stuff. Power plants and stuff.

To tell you the truth, we are a very much afraid of the future. One source of income for us is the lake; if some rich uncle comes and buys it up, we will lose our livelihood. Most of our men earn their living by fishing and of course we are all dependent on it.

Poor foreigners (“blacks,” “Turks”) would migrate to Estonia and take away jobs from local workers.

When we join the EU, blacks will move in. Why do we need them? Our own people do not have enough work.

Estonians are quite attached to their own country. I do not think that our people would like to work and live in Turkey, for example, but people from there might want to come and live here.

Finally, EU membership would cost Estonia more money than it would receive in return. Whatever subsidies it might receive in the first few years after the accession, it would have to pay them back once other, even poorer countries joined the EU.

It’s very simple: I do not like it. They will take away money from the Republic of Estonia and that’s all there is to it. (Who will take away money?) The EU! (And we will have nothing left?) Nothing! What has agriculture got?

Those who support the EU say nice things, but all these subsidies promised to farmers are temporary. At some point we will have to start paying them back, perhaps when other countries will join the EU in a few years. Then it’s Estonia’s turn to start supporting others.

### **Life is hard and will get harder in the EU**

In explaining why they expected bad things from the EU, some Estonian Euroskeptics argued that Estonia did not need to join the EU because life had already gotten better since the breakup of the Soviet Union. Joining the EU, they believed, might hurt Estonia’s hard-won economic success.

We have a future without the EU: our life has already gotten better.

Yes, I will vote, but I will vote ‘against’ [EU membership]. I do not see any point in this accession. We have lived normally until now and we will continue to do so. There is no point in going there.

Most Estonian Euroskeptics, however, believed that *life had gotten worse* during the transition to capitalism. It was hard to find a job. Pensions and social benefits were unacceptably low.

In the Soviet era, I worked at a factory. Now I do not know what to do. I get 240 kroon a month [in disability benefits]. What can I get for that money?

I will vote against [the EU]. Let them put things in order at home and then we can vote for it. The pension systems do not function as they should. Damn it! I worked in a steel-casting plant for forty-one years and earned decent money. Now I must cut bread with a string.

Some people specifically blamed Estonia's economic problems on the Western-oriented privatization and trade policies that successive Estonian governments had pursued since the breakup of the Soviet Union.

They [the government] have made a lot of mistakes already. Take, for example, the privatization of the railway and the monopolization of electric power. That's why I think that many people will not vote because they no longer believe in anything.

The path chosen by Estonian politicians could be briefly characterized as the shortest path to the destruction of the people. This includes the sale of strategic enterprises belonging to the state and the unlimited inflow of foreign capital. The deliberate worsening of economic ties with some of our neighbor states should also be mentioned. I mean our eastern neighbor, among others.

Joining the EU, the Euroskeptics felt, would make existing economic problems worse.

Life is hard and will get harder in the EU.

Everybody makes a decision based on their own level of development and experience. We live badly under this government and we will live even worse under the next. Actually, life is not that hard for retired people, who at least get a stable pension, but the young unemployed get no help whatsoever.

## **Conclusion**

The existing literature has used political and cultural variables to explain why most Lithuanians supported joining the EU, while many Estonians did not. However, my CA of newspapers showed that Lithuanians and Estonians were also concerned about the

economic consequences of EU accession. *Most Lithuanians believed that EU membership would help their country develop economically.* Western companies would invest more in Lithuania, while Lithuanian firms would gain a better access to the EU market. The EU would also provide subsidies to the vulnerable sectors of the Lithuanian economy, such as agriculture. Together, economic growth and EU aid would reduce unemployment and increase wages. This, in turn, would allow the government to collect more money in taxes and to increase social benefits. Many Lithuanians also hoped that EU accession would allow them to better their lot individually by making it easier to work, study and settle in Western Europe. *In explaining why they expected the EU to make their life better, Lithuanians typically said that life was so bad (as indicated by widespread unemployment and poverty) that it could not get any worse.*

By contrast, *many Estonians believed that EU membership would impoverish their country and make it economically dependent on the West.* Joining the EU would upset the fragile economic stability Estonia had achieved after more than a decade of strenuous economic reforms. EU subsidies would be accompanied by stringent sanitary and environmental regulations, which would drive farmers, fishermen and small businessmen bankrupt. EU-imposed consumption taxes and tariffs on non-EU imports would increase prices (e.g., of food and gasoline), which would make life harder for the poor. Most important, EU accession would subject Estonia to Western economic exploitation. Rich foreigners would buy up Estonian infrastructure and natural resources; poor foreigners would take away jobs from Estonian workers; Estonia would have to pay more towards the EU budget than it would get in return. *In explaining why they thought that EU membership would have such dire consequences, many Estonian Euroskeptics argued that prior Western-oriented economic reforms (e.g., free trade and the sale of SOEs to foreign investors) had destroyed Estonian industry and agriculture and reduced the quality of basic infrastructure (e.g., railways and power plants).*

## CHAPTER 3

### FOR RICHER OR POORER? MACRO-LEVEL ANALYSIS OF SURVEY DATA

#### Introduction

The previous chapter used content analysis (CA) of letters to the editor and interviews with voters in Lithuanian and Estonian newspapers to develop hypotheses about the origins of Lithuanian Euroenthusiasm and Estonian Euroskepticism. I found that Lithuanians and Estonians had different economic expectations about the EU. Most Lithuanians believed that EU membership would help their country to catch up with the West by making it eligible for EU subsidies and encouraging foreign investment and trade. They also hoped to improve their lot individually by working or studying abroad. By contrast, many Estonians felt that joining the EU would make Estonia dependent on the West by driving domestic producers bankrupt and allowing foreigners to buy up local resources. They also worried that their standard of living would decline because unemployment and prices would increase.

This chapter will test this hypothesis with survey data from the Central and Eastern Eurobarometer (CEEB) and its successor, the Candidate Countries Eurobarometer (CCEB), the main sources on public opinion on EU enlargement in Eastern Europe. Compared with CA, survey research has two advantages for the purpose of *testing* hypotheses. First, survey data are more *representative* than data collected through CA. The voters whose responses I CA'd may or may not have been typical of Lithuanian and Estonian voters. The sampling methods used in survey research help to make sure that the results accurately describe the entire population (Fowler 2002, chap. 3). Second, surveys are more *structured* than CA. People quoted in the last chapter gave all kinds of reasons for why they (dis)liked the EU. It was not easy to categorize their responses and to tell which categories were more important than others. Survey research

deals with this problem by asking all respondents the same questions and making them choose their answers from a closed list of alternatives (Fowler 1995, chap. 3-4).

Survey data also provide two practical advantages for my project. First, they allow me to compare the *relative importance of economic and non-economic concerns* for Baltic voters. Because of time and financial limits, I could only conduct a CA of people's economic expectations about the EU. The surveys I will use—the 1992 CEEB and the 2003 CCEB—dealt with political and cultural issues as well. Second, surveys enable me to *trace changes in Baltic attitudes over time*. Both CEEB and CCEB asked respondents how much they knew about the EU, whether they supported EU membership, what (dis)disadvantages the accession would have, and which social groups would benefit from it. The two time points I chose mark the beginning and the end of the Baltic states' accession to the EU. In 1992, Lithuania and Estonia held referenda on their new constitutions and their first post-Communist elections. In 2003, the two countries held referenda on EU membership, in preparation for joining the EU a year later.

I will show that in 1992, most Lithuanians and Estonians (80-90%) supported EU membership because they believed that it would promote trade with the West, increase Western financial aid, help to create a free market economy, and, ultimately, improve the standard of living for most people. By contrast, they were uninterested in the political and security benefits of accession, such as help with building democracy and protecting peace in Europe. In 2003, two-thirds of Lithuanians still supported EU membership, in part because they believed that Lithuania was historically part of Europe, but mostly because they hoped that the accession would make it easier for them to work abroad and/or increase their incomes if they stayed at home. By contrast, fewer than half of Estonians now supported the accession because they thought that it would undermine their political independence and cultural identity and, above all, cost too much money, increase unemployment, and make life more difficult for farmers, pensioners and other vulnerable groups.

## 1992: “Permissive Consensus”

Scholars have used the term “permissive consensus”—a combination of lack of knowledge and interest with a high level of support—to describe West European attitudes toward the EU in the 1960s and 1970s (Lindberg and Scheingold 1970, chap. 1; Jolly 2007, chap. 6). This term also accurately describes Baltic attitudes toward European integration in 1992. The respondents were first asked whether they a) had heard of and b) were interested in various European institutions. As Table 3.1 shows, most people (about 80%) had heard of the EU. However, only 20-30% of the respondents had heard of “Europe Agreements” for closer economic, political and cultural ties with the EU. Slightly more people (30-40%) had heard of PHARE (the EU’s main aid program for Eastern Europe) and European trade issues. A similar picture obtains when we look at people’s interest in European issues. Between a quarter and third of the respondents were interested in the EU and the “Europe Agreement,” while about 40% were interested in PHARE and trade, indicating that the Balts already saw the EU as an economic project.

**Table 3.1: Awareness of and Interest in European Issues in 1992 (%)\***

	<b>Heard?</b>	<b>Interested?</b>
<b>European Union</b>		
Lithuania	77	26
Estonia	81	30
<b>Europe Agreement</b>		
Lithuania	21	30
Estonia	33	34
<b>PHARE<sup>a</sup></b>		
Lithuania	32	41
Estonia	38	37
<b>EU trade issues</b>		
Lithuania	40	44
Estonia	41	39

\* Only positive responses included.

<sup>a</sup> Poland-Hungary: Aid for the Restructuring of Economies.

*Source:* Own calculations from Central and Eastern Eurobarometer 1992 (CCEB 1992).



While they knew and cared little about the EU, however, the Balts generally supported European integration. As Table 3.2 indicates, one half of Lithuanians and a third of Estonians had a positive image of the aims and activities of the EU. This may not sound like a ringing endorsement until we note that only 1-2% of the respondents had a negative image of the EU. (The remaining voters had a neutral image.) About 80% of the Balts thought that their country should conclude a “Europe Agreement” with the EU, while only 2-5% felt that it should not do so. This is remarkable because, as we saw in the previous paragraph, only 20-30% of the people had *heard* of such agreements. Finally, between 80-90% of the voters supported joining the EU as a full member in the future, while only 4-5% opposed this idea.

**Table 3.2: Support for European Integration in 1992 and 2003 (%)\***

	YES		MAYBE		NO	
	1992	2003	1992	2003	1992	2003
<b>Positive Image of EU?</b>						
Lithuania	47	57	31	26	1	11
Estonia	33	28	37	45	2	22
<b>EU Membership a Good Thing?</b>						
Lithuania	-	65	-	23	-	9
Estonia	-	31	-	42	-	17
<b>Support Europe Agreement?</b>						
Estonia	76	-	-	-	2	-
Lithuania	80	-	-	-	5	-
<b>Support EU Membership?</b>						
Lithuania	88	70	-	-	4	12
Estonia	80	40	-	-	5	31

\*DON'T KNOWs not reported.

Source: Own calculations from CEEB 1992 and Candidate Countries Eurobarometer April 2003 (CCEB 2003.2).

Why did most Balts support European integration? The answer is that they believed that they personally and their country at large would benefit economically from closer ties with the EU. The respondents were asked what they thought the main advantages of EU membership would be (see Table 3.3). In both countries, the most popular choice (mentioned by 30-40% of the people) was the improvement of living

standards. This was followed by increased trade and financial aid (about 20% of the sample). Another 15% or so thought that EU membership would help to create a free market economy, facilitate European economic cooperation, and remove restrictions on travel to Western countries. By contrast, very few people in either country were interested in the political or cultural aspects of EU membership. Thus, fewer than 10% of the respondents thought that the advantages of EU accession included political cooperation with European countries, Western help with the development of democracy, or greater peace and stability within Europe. (However, 12% of Estonians thought that joining the EU would improve national defense and security.)

**Table 3.3: Perceived Advantages of EU Membership in 1992 (%)**

	Lithuania	Estonia
1. Improve living standards	39	31
2. Improve trade	20	20
3. Financial and economic aid	20	16
4. More European economic cooperation	16	16
5. No travel restrictions	16	8
6. Help create free market economy	15	15
7. Shortages will disappear	11	6
8. Help democracy	7	7
9. More European political cooperation	6	7
10. Improve security and defense	6	12
11. Peace and stability within Europe	3	5
13. NONE	2	2
14. DON'T KNOW	18	21

*Source:* Own calculations from CEEB 1992.

The respondents were also asked what they thought the main disadvantages of EU membership would be. As Table 3.4 illustrates, *most people—about 60% in both countries—could not think of any disadvantages of the accession*: some 20% thought that there were no disadvantages and about 40% said that they did not know if there were any disadvantages. However, 12-16% of Estonians thought joining the EU would subject their country to Western political and economic domination, respectively. In Lithuania,

the biggest fears were unemployment and emigration (10%), followed by foreign economic domination and the loss of cultural identity (9%). On the whole, however, a) there was broad but shallow support for joining the EU in both countries b) based on vague expectations of economic gain but c) to some extent tempered by fear of Western economic, political and cultural domination.

**Table 3.4: Perceived Disadvantages of EU Membership in 1992 (%)**

	Lithuania	Estonia
1. Unemployment	10	8
2. Emigration	10	3
3. Economic domination	9	16
4. Loss of cultural identity	9	4
5. Foreigners will come and buy up the country	8	8
6. Increase in crime	5	3
7. Political domination	4	12
8. Economic inequality	4	3
9. Fall in living standards	2	2
10. Loss of political sovereignty	2	1
12. NONE	21	21
13. DON'T KNOW	39	40

*Source:* Own calculations from CEEB 1992.

Partly contradicting this conclusion are data reported in Table 3.5, which suggest that the Balts already believed that some people would gain more from joining the EU than others. Both Lithuanians and Estonians thought that high-status groups in the private sector (businessmen) were more likely to benefit from closer ties with the EU than low-status groups (manual workers and low-income groups) and the public sector (state-owned enterprises and civil servants). Further, Estonians were already somewhat less hopeful about the EU than Lithuanians: they were up to ten percentage points less likely to believe that any given group would benefit from the accession. However, among the top expected beneficiaries of EU membership in both countries were the state-run health care and education systems, presumably because people hoped that the EU would help to finance them. Moreover, both Lithuanians and Estonians believed that

most groups would be better off in the EU: when we subtract expected losses from expected gains, we get a positive balance for all groups in both countries.

**Table 3.5: Perceived Winners and Losers of EU Accession in 1992 (%)\***

	Lithuania			Estonia		
	+	-	=	+	-	=
Health care system	72	7	65	67	3	64
Private business	72	11	61	65	7	58
Education system	66	6	60	42	4	38
Farmers	57	23	34	45	20	25
State-owned enterprises	51	28	23	41	21	20
Manual workers	45	25	20	32	20	12
Civil servants	38	27	11	30	20	10
Low-income groups	31	33	-2	26	21	5

*Source:* Own calculations from CEEB 1992.

### **2003: “Constraining Dissensus”**

Fast forward to 2003, when Lithuania and Estonia received invitations to join the EU and held referenda on whether they should do so. As Table 3.6 indicates, the Balts remained ignorant about EU history and institutions. For example, fewer than a third of the respondents knew when the EU was established (after World War II), how members of the European Parliament were elected (directly by EU citizens), and whether there were borders between EU countries (yes, although the question is ambiguous). However, the Balts had become quite knowledgeable about EU symbols, membership and location. Thus, 83% of Lithuanians and 81% of Estonians recognized the EU flag (blue with yellow stars). A solid 65% of Lithuanians and 73% of Estonians knew that the EU consisted of fifteen member states. Finally, 55% of Lithuanians and 69% of Estonians knew that EU headquarters were located in Brussels, Strasbourg and Luxembourg, up from 15% and 27%, respectively, in 1992. (This was the only factual question asked in 1992.)

**Table 3.6: Knowledge about the EU in 2003 (%)\***

	<b>RIGHT ANSWER</b>	<b>WRONG ANSWER</b>
<b>1. The EU is made of fifteen member states (true)</b>		
Lithuania	65	9
Estonia	73	6
<b>2. The EU is headquartered in Brussels, Strasbourg and Luxembourg (true)<sup>a</sup></b>		
Lithuania	55 (15)	12 (12)
Estonia	69 (27)	6 (13)
<b>3. The EU was created after World War I, in the late 1910s and early 1920s (false)</b>		
Lithuania	19	28
Estonia	27	25
<b>4. The European flag is blue with yellow stars (true)</b>		
Lithuania	83	2
Estonia	81	2
<b>5. There are fifteen stars on the European flag (false)</b>		
Lithuania	23	45
Estonia	8	64
<b>6. The EU has its own anthem (true)</b>		
Lithuania	31	17
Estonia	18	34
<b>7. The members of the European Parliament are directly elected by citizens (true)</b>		
Estonia	23	22
Lithuania	29	19
<b>8. There is a president of the EU directly elected by all citizens (false)</b>		
Lithuania	33	18
Estonia	38	14
<b>9. There are no borders between the countries of the European Union (false)</b>		
Lithuania	15	15
Estonia	32	44

\* DON'T KNOWs not reported.

<sup>a</sup> 1992 data in brackets.

Source: Own calculations from CCEB 2003.2.

However, while knowledge about the EU had increased, support for EU membership had decreased (go back to Table 3.2). In Lithuania, the decline was relatively modest. Thus, 70% of Lithuanians planned vote for EU membership, down from 87% in 1992, while 12% planned to vote against the accession, up from 5%. A majority of 57% of Lithuanians now had a positive image of the EU, up from 43% in 1992, while 12% had a negative image, up from 1%. Further, 60% of Lithuanians thought that EU membership would be a good thing, while 10% thought that it would be

a bad thing. In Estonia, however, the “permissive consensus” of 1992 had given way to a “constraining dissensus” (Hooghe and Marks 2008). Only 40% of Estonians supported EU membership, down from 80%, while 31% opposed it, up from 5%. While a third of Estonians still had a positive image of the EU, 25% now had a negative image, up from 5% in 1992. Finally, only 40% of Estonians believed that joining the EU would be a good thing, while 20% believed that it would be a bad thing.

The still strong if diminished support for the EU in Lithuania and the widespread opposition to the union in Estonia were rooted in very different expectations about the impact of EU membership on a) the respondents personally and b) the country at large. As Table 3.7 shows, *69% of Lithuanians but only 42% of Estonians thought that their country would benefit from EU joining the EU. Even more dramatically, 54% of Lithuanians but only 28% of Estonians believed that they would personally benefit from EU accession.*

**Table 3.7: The Expected Impact of EU Membership in 2003 (%)\***

	YES	NO
<b>... Country will benefit</b>		
Lithuania	69	14
Estonia	42	33
<b>... Will personally benefit</b>		
Lithuania	54	17
Estonia	28	33

\*DON'T KNOWs not reported.

Source: Own calculations from CCEB 2003.2.

This, of course, raises the question of *what kinds of benefits and costs people* expected EU membership to entail. The reader will recall that, in 1992, most Estonians and Lithuanians hoped that EU accession would improve their standard of living by increasing trade with and aid from the West. Unfortunately, the 2003 survey did not specifically ask about the advantages of EU accession, so a direct comparison is not possible. However, the respondents were asked about the meaning of EU citizenship. As

Table 3.8 makes clear, *both Lithuanians and Estonians were mainly interested in the economic rights associated with EU membership*, such as the right to work, study, travel, or settle permanently in the EU. By contrast, people were largely indifferent to the political rights they would acquire as EU citizens, such as the right to vote in European and local elections. On both economic and political issues, however, Estonians were about twenty percentage points less likely than Lithuanians to associate EU citizenship with any rights.

**Table 3.8: The Meaning of EU Citizenship in 2003 (%)\***

	<b>Lithuania</b>	<b>Estonia</b>
1. The right to work in any EU country	80	61
2. Being able to study in any EU country	75	54
3. The right to move permanently to any EU country	66	51
4. Access to social welfare in any EU country	55	41
5. The right to vote in local elections in any EU country	33	11
6. The right to vote in national elections in any EU country	30	10
7. The right to vote in European elections in any EU country	30	11

\*Only positive responses reported.

Source: Own calculations from CCEB 2003.2.

Another question asked voters to agree or disagree with a number of statements about the EU. As Table 3.9 illustrates, most Lithuanians and Estonians thought that their leaders were doing what was necessary to join the EU, although they doubted that their country had much to offer the EU or would have much say in European affairs. There was also broad agreement that enlarging the EU would protect peace and security in Europe and make Europe culturally richer and politically more important. *However, Lithuanians and Estonians disagreed on a) how “European” their country was and b) whether their country would benefit from EU membership economically.* Thus, 59% of Lithuanians but 48% of Estonians believed that their country’s membership in the EU was historically and geographically justified. As many as 66% of Lithuanians but only 54% of Estonians thought that being a member of the EU would help their country’s economy. Most dramatically, 61% of Lithuanians but only 38% of Estonians believed

that joining the EU would lead to higher quality of life, while only 18% of Lithuanians but 42% of Estonians worried that EU accession would increase unemployment.

**Table 3.9: What Kind of Europe? Images of the EU in 2003 (%)\***

	Lithuania		Estonia	
	YES	NO	YES	NO
1. [The country] has a lot to offer the EU	33	46	19	65
2. The more countries there will be in the EU, the more peace and security will be guaranteed in Europe	68	16	62	21
3. With the enlargement, [the country] would be able to have its voice heard more strongly in Europe	53	20	51	31
4. [The country's] leaders are doing what is needed to become a member of the EU	72	9	80	7
5. The more there will be countries in the EU, the more important it will be in the world	64	13	69	12
6. With more member countries, Europe will be culturally richer	58	17	52	27
7. [The country's] membership of the EU is historically and geographically natural, justified	59	13	48	26
8. Being a member of the EU would help [the country's] economy	66	15	54	26
9. [The country's] membership of the EU would lead to a higher quality of life	61	14	38	36
10. With the enlargement, there would be more unemployment in [the country]	19	49	42	41

\*DON'T KNOWs not reported.

Source: Own calculations from CCEB 2003.2.

The survey also asked people what their biggest fears about the EU were. As Table 3.10 shows, both Lithuanians (54%) and Estonians (67%) were most afraid of increasing crime and drug trafficking. It is difficult for me to interpret this because I did not CA non-economic fears about the EU, nor has this issue received much attention in the literature.<sup>14</sup> However, the Balts may have worried that joining the EU would make their countries a more attractive route for drug trafficking from Russia to Europe. Lithuanian and Estonian guards on the Russian border typically turn a blind eye to the

<sup>14</sup> Of course, Inglehart (1977, chap. 12; 1990, chap. 2, 4) argues that concerns over physical safety and economic security both reflect broader “materialist” values.



drug trade, either because they have been bribed or because they are afraid of getting killed. With EU accession, Baltic drug couriers could travel to Europe without a visa and with minimal customs inspections. The Balts may have also thought that the EU was “soft on crime.” In the 1990s, Lithuania and Estonia abolished the death penalty in order to qualify for membership in the Council of Europe, a non-EU institution often confused with the European Council. In the early 2000s, the EU required Lithuania and Estonia to build new prisons that would meet EU guidelines for the humane treatment of inmates.

**Table 3.10: Fears about the EU in 2003 (%)\***

	<b>Lithuania</b>	<b>Estonia</b>
1. An increase in drug trafficking and organized crime	54	67
2. More difficulties for our farmers	46	54
3. Joining the EU will cost our country too much money	44	57
2. More difficulties for our farmers	46	54
4. Our language being used less and less	33	53
5. The end of litas or kroon (national currency)	34	52
6. A loss of power for smaller members	24	52
7. The transfer of jobs to countries with lower production costs	33	44
8. The loss of our identity and culture	20	42
9. The loss of social benefits	16	26
10. Richer countries paying more than others	17	20

\*Only positive responses reported.

Source: Own calculations from CCEB 2003.2.

However, Estonians were more worried than Lithuanians about the consequences of EU accession for their political independence and cultural identity. Thus, only 33% of Lithuanians but 53% of Estonians thought that their language would be used less after the accession; 24% of Lithuanians but 52% of Estonians—that small countries would lose power in the EU; and 20% of Lithuanians but 42% of Estonians—that they would lose their culture and identity in the EU. These results provide some support for the historical and cultural interpretations of Baltic attitudes to the EU proposed by Pettai (2005) and Vetik, Nimmerfelt and Taru (2006). For example, Estonians may place higher value on political independence than Lithuanians because they have almost no tradition of independent statehood. Similarly, Estonians may be more attached to their national

culture because the line between elite (German or Polish) and peasant culture was traditionally sharper in Estonia than in Lithuania.

However, the data also support the main results of my content analysis, namely that *a) economic concerns were at least as important for Lithuanian and Estonian voters as political and cultural issues and that b) Estonians were more worried about the negative economic consequences of the accession than Lithuanians.* Above all, 46% of Lithuanians but 54% of Estonians believed that the accession would create problems for farmers; 44% of Lithuanians but 57% of Estonians—that joining the EU would cost too much money; and 34% of Lithuanians but 52% of Estonians—that the EU would do away with their national currency. Less commonly, 33% of Lithuanians but 44% of Estonians thought that the accession would lead to the transfer of jobs to other countries; 16% of Lithuanians but 26% of Estonians—that EU membership would reduce social benefits; and 17% of Lithuanians but 20% of Estonians—that it was unfair that rich countries paid more toward the EU budget than others.

The CA conducted in the previous chapter helps us to make sense of these fears. EU production quotas would fix Estonian agricultural output at the level of the late 1990s, the trough of the post-Communist agricultural depression, while EU regulations would require farmers to build separate sheds for different animals and to buy expensive new equipment. EU-imposed tariffs and indirect taxes would increase the price of basic necessities like food, gasoline, and electricity. Workers would respond to the rising cost of living by demanding higher wages. As a result, domestic firms would go out of business, while foreign companies would relocate their production to Russia, where there are fewer regulations. This, in turn, would reduce tax revenues and force the government to cut social benefits. After ruining the domestic economy, the Estonian government would replace the kroon with the euro, confiscating people's savings in the process. At the same time, the EU would rig its accounting rules so that Estonia would pay more toward the EU budget than it would receive in return.

Like the 1992 CEEB, the 2003 CCEB asked respondents which social groups were most likely to benefit from EU membership and which ones were most likely to lose. As Table 3.11 indicates, both Lithuanians and Estonians expected a) big businesses, politicians, and civil servants; b) urban residents, professionals, and people who speak foreign languages; and c) children and young people to be the main beneficiaries of the accession. The groups seen as least likely to benefit included a) farmers and small businessmen; b) rural residents, the unemployed, and people who do not speak foreign languages; and c) middle-aged and elderly people and pensioners. In this sense, public opinion had changed little from 1992, when most Balts thought that private businesses were more likely to gain from EU membership than state-owned enterprises, manual workers, and low-income groups (go back to Table 3.5).

**Table 3.11: Perceived Winners and Losers of EU Accession in 2003 (%)\***

	Lithuania			Estonia		
	+	-	=	+	-	=
1. Young people	82	3	79	66	3	63
2. People who speak foreign languages	79	2	77	82	0	82
3. Large businesses	75	2	73	69	2	67
4. Politicians	75	3	72	83	1	82
5. Professionals	63	4	59	61	2	59
6. Children	59	4	55	44	6	38
7. Civil servants	45	5	40	62	4	58
8. Inhabitants of capital city	37	7	30	29	7	22
18. The unemployed	41	16	25	22	33	-11
20. Small and medium-sized businesses	37	18	19	12	30	-18
19. Middle-aged people	28	16	12	12	28	-16
21. Farmers	35	25	10	18	38	-20
22. Pensioners	22	22	0	16	37	-21
23. Inhabitants of rural areas	27	29	-2	14	44	-30
24. Elderly people	20	24	-4	11	41	-30
25. People who don't speak foreign languages	15	34	-19	4	60	-56

\*DON'T KNOWs not reported.

Source: Own calculations from CEEB 2003.2.

However, a clear difference a) from 1992 and b) between the two countries emerges when we calculate the expected *net* effect of EU accession on various groups—i.e., when we subtract the percentage of respondents who expected a particular group to lose from the accession from the percentage of people who expected that group to win. *Lithuanians still believed that, on balance, most groups would benefit from the accession.* The only exceptions were people who do not speak foreign languages and, by a small margin, rural people and the elderly. *By contrast, Estonians now expected people without marketable resources to lose from the accession.* In ascending order, the net benefit scores were -19% for Lithuania (-56% for Estonia) for people who do not speak foreign languages; -4% (-30%) for the elderly; -2% (-30%) for the inhabitants of rural areas; 0% (-21%) for pensioners; +12% (-20%) for farmers; +12% (-16%) for middle-aged people; +19% (-18%) for small businesses; and +25% (-11%) for the unemployed.

## **Conclusion**

This chapter set out to do two things: a) to compare the relative importance of economic and non-economic concerns about the EU for Baltic voters and b) to explore changes in Lithuanian and Estonian attitudes toward the EU over time. The main results of my analysis can be summarized as follows. *In 1992, the overwhelming majority of Lithuanian and Estonian voters (80-90%) supported EU membership.* They did so mostly for economic reasons. *They hoped that joining the EU would improve trade with West European countries, increase foreign aid, help to create a free market economy, and, in the end, raise most people's standard of living.* They also believed that all social groups—from public sector workers to private sector owners—would benefit from EU membership. By contrast, both Lithuanians and Estonians were indifferent to the potential political benefits of EU accession, such as help with building democracy and protecting peace and security in Europe. Few people thought that joining the EU would

have any negative consequences, although some Estonians worried that it would subject their country to foreign political and economic domination.

*By 2003, however, Lithuanian and Estonian attitudes toward the EU had diverged considerably. About two thirds of Lithuanians still supported EU membership. They believed that Lithuania was geographically and historically part of Europe. They also hoped that joining the EU would make it easier for Lithuanians to work abroad and increase incomes for those who stayed at home. By contrast, Estonian support for the EU had dropped to below half of the electorate. This was in part because Estonians worried that joining the EU would undermine their political independence and cultural identity. More importantly, however, Estonians believed that joining the EU would cost too much money, create difficulties for farmers, and increase unemployment. They also thought that the accession would benefit people with marketable economic resources (young people, urban residents, large businessmen, and professionals) and hurt those who lacked such resources (old people, rural residents, small businessmen, and the unemployed).*

**CHAPTER 4**  
**CALCULATION, COMMUNITY, OR CUES? MICRO-LEVEL ANALYSIS OF**  
**SURVEY DATA<sup>15</sup>**

**Introduction**

Thus far, this dissertation has explored cross-national differences in EU support at the *aggregate* level. Using content analysis of Lithuanian and Estonian newspapers and macro-level analysis of survey data, I have shown that both Lithuanians and Estonians thought of the EU mainly in economic terms, but that Lithuanians had more optimistic economic expectations about the EU than Estonians. However, I have not yet considered the *micro-foundations* of these differences. Which social groups (e.g., in terms of sex, ethnicity, income, and education) were more likely to support EU membership in Lithuania and Estonia? What attitudes (and aptitudes)—“cognitive mobilization,” post-materialism, nationalism, trust in government, or satisfaction with one’s economic situation—distinguished EU supporters from EU opponents? Finally, was the relationship between social structure and attitudes and EU support the same in Lithuania and Estonia? For example, did the same groups (e.g., the rich and people who are satisfied with their economic situation) support the EU in the two countries?

In this chapter, I will show that there were both similarities and differences in the social basis of EU support in Lithuania and Estonia. In both countries, people who trusted the government were more likely to support EU membership than those who did not. Clearly, the EU referenda were, to some extent, votes of (non-)confidence in political leaders. Other similarities were negative, however. Post-materialist values, which are a strong predictor of EU support in Western Europe, had no impact on EU

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<sup>15</sup> With apologies to Hooghe and Marks (2005).

support in either country because almost all Lithuanians and Estonians turned out to be materialists. More surprisingly, nationalism—a variable favored by students of East European politics—either increased or decreased EU support depending on how it was operationalized, presumably because Baltic nationalists disagreed among themselves on whether the EU was good or bad for the nation.

However, the differences in the structural and attitudinal basis of EU support in the two countries were at least as important as the similarities. Party preferences affected EU support in Estonia, where the largest party opposed the accession on current terms, but not in Lithuania, where almost all parties supported EU membership. “Cognitive mobilization” (operationalized as knowledge about the EU) increased support for the EU in Lithuania but not in Estonia, perhaps because Lithuania negotiated a more favorable accession treaty than Estonia. Finally, the strongest predictors of EU support in Estonia were income, education, and satisfaction with one’s economic situation, none of which had any influence at all on EU support in Lithuania. Clearly, as my CA suggested, Estonians saw EU accession as a continuation of current economic policies, while Lithuanians did not.

The chapter is organized as follows. The next section will review the literature on individual-level determinants of EU support in a) Western and b) Eastern Europe. The following section will test the existing theories with survey data from Lithuania and Estonia. The conclusion will sum up my findings. Throughout the chapter, I will pay particular attention to two questions. First, *how well do theories developed in the West European context work in Eastern Europe?* Second, *do the same theories explain EU support in Lithuania and Estonia?*

## **Literature and Hypotheses**

### **Community: Cognitive Mobilization, Post-Materialism, and Nationalism**

Systematic research on popular attitudes toward European integration goes back to the work of Ronald Inglehart in the 1970s. Inglehart (1970; 1977, chap 12) argues that public support for European depends of two factors: a) “cognitive mobilization” (CM) and b) post-materialist values. An individual is cognitively mobilized (CMd) if she has a good understanding of political issues. She is also eager to express her opinions about politics and to persuade others, for example in discussions with family and friends. Inglehart argues that CM increases support for European integration in two ways. First, CMd individuals are more likely to seek out information about the EU, which, in turn, will make European institutions look more familiar and less threatening. Second, they have broader horizons: they are more likely to place their personal concerns in a national and global context.<sup>16</sup> Most researchers have found strong support for the CM hypothesis in both Western and Eastern Europe (Jansson 1991; Duchesne and Frogner 1995; Anderson and Reichert 1996; Cichowski 2000).

However, Inglehart (1977, chap. 12; 1990, chap. 2, 4) also argues that CM is a necessary but not sufficient condition for EU support. It also matters what kinds of values people hold. Inglehart argues that since the 1960s, Western societies have experienced a gradual shift from materialist to post-materialist (PM) values. Materialists are concerned about economic and physical security. They give priority to issues like fighting crime, maintaining high rates of economic growth, and stabilizing prices. By contrast, post-materialists (PMs) care about self-expression, political participation, and the quality of life. They think that it is important to protect the freedom of speech, to

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<sup>16</sup> Of course, an obvious criticism of the CM hypothesis would be that CM is simply a funny way of describing socio-economic status: after all, upper-status people are generally more articulate and more interested in politics than their lower-status peers. This problem is particularly acute when education is used as a measure of CM, as in Inglehart (1970) and Cichowski (2000).



give people more say in government, and to take good care of our environment. Inglehart argues that PMs are more likely to support European integration than materialists. They are less preoccupied with making money, which leaves them more time for political and intellectual pursuits. They are also more open to new things, including new political arrangements, such as the EU.

Tests of the PM hypothesis have produced contradictory results, however. Inglehart and Reif (1991) find that PMs are significantly more supportive of the EU than materialists. However, Jansson (1991) and Duchesne and Frognier (1995) find that, once we control for cognitive mobilization, the relationship between post-materialist values and EU support becomes weaker or disappears entirely. They suggest that some materialists support European integration as a way of increasing economic efficiency, while some PMs oppose it as a bureaucratic monster. Anderson and Reichert (1996) find that PMs support the EU in northern Europe, but oppose it southern Europe. They argue that voters in rich countries associate European integration with non-economic values like peace and environmental protection, while voters in poor countries see the EU as an engine of economic development.

More recently, scholars exploring popular attitudes toward the EU have turned their attention to another set of values: nationalism. They argue that the EU has undergone significant changes in the past two decades. It used to be a customs union, concerned about bringing down tariff barriers between European countries. Nowadays, however, it increasingly impinges on the sovereignty of its member states in areas far removed from trade policy. For example, the EU now has a central bank and a common currency, the euro. The highest judicial body in the EU is the European Court of Justice, which promotes the rights of minorities against the claims of the nation-states. With the adoption of the Schengen visa regime, EU countries are also moving towards a common immigration policy. Many people believe that these changes are undermining their

country's political independence and cultural identity. They express their frustration by voting against the expansion of EU powers and the admission of new members.

In general, scholars working on Western Europe have found strong support for the nationalism hypothesis. Carey (2002) and Risse (2002) find that, compared to EU supporters, EU opponents are more likely to be proud of their country, to think of themselves as citizens of their country rather than Europeans, and to worry that their language and culture will disappear in the EU. McLaren (2002) and De Vreese and Boomgarden (2005) claim that anti-EU voters are distinguished by their hostility to immigrants: for example, they believe that immigrants take away jobs from local workers, abuse the welfare system, create trouble in schools, and follow offensive religious practices. Sciarini and Listhaug (1997) argue that Swiss and Norwegian voters rejected EU membership in the 1994 referenda because they worried that it would compromise their national sovereignty and weaken democratic institutions. Christin and Trechsler (2002) find that Swiss Euroskeptics believe that joining the EU would undermine their country's traditions of direct democracy and neutral foreign policy.

*Scholars working on Eastern Europe, however, have disagreed on whether nationalism increases or decreases support for European integration.* On the one hand, Grabbe and Hughes (1998, chap. 6), Grabbe (2003) and Ozolina (2003) argue that opposition to the EU is strongest in countries that have the shortest tradition of independent statehood, such as the former Czechoslovakia and the Baltic states. Having just escaped from one union, why should they rush to join another? Pettai (2005) and Vetik, Nimmerfelt and Taru (2006) maintain that Estonian and Latvian Euroskepticism reflects their cultural peripherality. Both countries were colonized by Germans in the thirteenth century. As a result, opposition to Europe (Germany) became the cornerstone of their cultural identity during the "national awakenings" of the nineteenth century. Concretely, Vetik et al show that Estonian Euroskeptics believe that Estonia should

follow its own path of economic development and disregard EU rules if they hurt Estonian interests.<sup>17</sup>

By contrast, Whitefield, Rohrscheider and Alisauskiene (2006) contend that, at least in the Baltic countries, nationalism *strengthens* support for EU membership because the alien and hostile “other” for Baltic nationalists is not Europe, but Russia. Russia occupied the Baltic states during World War II. In the ensuing decades, it redrew their borders, suppressed their cultures, and encouraged the in-migration of Slavic workers. Although it grudgingly recognized Baltic independence in 1991, it did not remove its troops until 1994. It has refused to ratify border treaties with Latvia and Estonia and continues to meddle in their affairs under the pretext of protecting minority rights. As a result, many Balts believe that EU membership will serve as a “soft” security guarantee against Russia. (Conversely, many Slavs worry that joining the EU will reduce Russian influence in their country.) To support their argument, Whitefield and his collaborators show that ethnic Balts and voters who feel proud of their nationality are more likely to support EU accession than ethnic Slavs and voters who lack national pride.

### **Cues: Party Preferences and Trust in Government**

Another popular explanation for public support for European integration focuses on political factors, such as party preferences and trust in government. Scholars working in this tradition assume that voters know little about the EU. For example, Anderson (1998) finds that two thirds of EU citizens are poorly informed about EU history and institutions. This is a product of rational ignorance: most voters lack the time and motivation to learn more about a seemingly distant and bureaucratic organization. How, then, do people make decisions when they are asked to vote on issues like EU expansion

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<sup>17</sup> This, of course, raises the question of whether Vetik and his collaborators actually measure *economic*, rather than *cultural*, nationalism. Clearly, following one’s own path of economic development is an economic issue. EU rules, too, are controversial largely because they hurt farmers, fishermen, and small businessmen.

or closer integration? Anderson argues that voters know a lot about domestic politics: they prefer one party to others; they trust the government or not. When voting on European issues, they transfer their attitudes toward domestic politics to the EU.

But what kinds of domestic political cues have the most influence on people's attitudes to the EU? Some researchers argue that voters "follow the party line": they adopt the position of the party that is closest to them on domestic issues (Van Kersbergen 2000). Inglehart and Reif (1991) and Wessels (1995) find that political conflict over European integration overlaps with the left-right cleavage: supporters of liberal and conservative parties are more supportive of the EU than socialist, Communist and Green voters. Anderson (1998) finds that supporters of mainstream parties favor European integration, while voters of anti-establishment parties—the Communists and the far right—oppose it. This is particularly true in countries where anti-establishment parties have made opposition to the EU an important part of their platform (e.g., Austria, France and Denmark).

Studies of East European politics have generally confirmed the idea that a) parties differ in their views of European integration and that b) party preferences influence popular attitudes toward the EU. Kopecký and Mudde (2002) and Beichelt (2004) argue that nationalist and unreformed Communist parties oppose EU membership, while other parties support it. Cichowski (2000) and Anderson and Tverdova (2004) show that voters of pro-EU parties are more supportive of the EU than voters of anti-EU parties. Sikk and Ehin (2005) and Sikk (2005) find that supporters of Estonia's left-populist Center Party were more likely to vote against EU membership than supporters of other parliamentary parties. Reversing the causal arrow, Whitefield, Rohrschneider and Alisauskiene (2006) argue that EU supporters in the Baltic countries vote for liberal and conservative parties, while EU opponents vote for social democratic, populist, and ethnic (Russian) parties.

Other scholars have argued, however, that voters may not know or care where parties stand on EU issues. In Western Europe, many parties are internally divided on

European integration. In Eastern Europe, party identification is weak. However, we can reasonably make two assumptions. First, most voters know whether they are satisfied or dissatisfied with the performance of the government. For example, they either approve or do not approve of how the government handles the economy, crime, or some other issue that is important for them. Second, voters believe that European integration is the government's project. In candidate countries, governments negotiate with the European Commission about the terms of the accession. In EU member states, governments formulate (through their participation in the European Council) and implement EU policies. As a result, voters who are satisfied with the government's job performance will support European integration, while people who are dissatisfied will oppose it.

Concretely, Franklin, Marsh and Welzien (1994) and Franklin, van der Eijk and Marsh (1995) claim that the Danish voters initially rejected the 1992 Maastricht treaty, which established the European economic and monetary union, because they wanted to punish their government for poor economic management. They find that there was no significant decline in Danish popular support for European integration before the referenda. However, many voters were deeply unhappy about rising unemployment and other economic woes.<sup>18</sup> The "Franklin thesis" has found an enthusiastic following in Estonia, a would-be Nordic country. Ehin (2001), Vetik (2003) and Sikk and Ehin (2005) argue that most Estonians believed that they—and their country at large—would benefit membership. However, many people still voted against the EU because they did not trust the politicians who were in charge of the accession negotiations.

However, in Western Europe, the Franklin thesis has recently received a drubbing from Sánchez-Cuenza (2000), who finds that trust in government *reduces* support for the EU once we control for trust in European institutions. He argues that European

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<sup>18</sup> However, Svensson (2002) argues that Danish voters opposed the Maastricht treaty and subsequent measures to "deepen" European integration on policy grounds. In particular, most Danes opposed a common EU social policy, the single European currency, and the leveling of economic differences between EU member states.

integration presents European citizens with a choice between national sovereignty and supranational governance. For example, should the national governments or the EU be in charge of monetary, agricultural, and immigration policy? Voters who trust their government want to preserve as much national sovereignty as possible, while voters who mistrust the government prefer to be ruled from Brussels. At the aggregate level, this translates into a north-south divide in EU support: north Europeans trust their government and mistrust the EU; south Europeans mistrust their government and trust the EU.

### **Calculation: Economic Resources and Perceptions**

The third major family of theories about the sources of popular attitudes toward the EU focuses on economic factors. Gabel and Palmer (1995), Gabel and Whitten (1997) and Gabel (1998 a, chap. 2-4; 1998 b) argue that voters support or oppose European integration based on economic cost-benefit calculations. The EU is, above all, a common market for goods, labor, and capital. EU states have abolished tariffs on each other's products and reduced non-tariff barriers, such as subsidies and preferential tax treatment. They also recognize each other's diplomas and have banned nationality-based discrimination in hiring, except in the public sector. Finally, they have removed controls on the movement of capital, including both direct and portfolio investment.

These policies, Gabel and others argue, benefit individuals who possess marketable resources (white-collar jobs, higher education, and a lot of money) and hurt those who do not. Free trade lowers the price of manufactured goods. This benefits white-collar workers, who buy manufactured goods, but hurts blue-collar workers, who produce them. Free movement of labor increases competition for jobs. This benefits educated workers, who can move wherever they can make the most money, but hurts uneducated workers, who may lose their jobs. Free movement of capital puts pressure on governments to cut taxes and spending. This benefits the rich, who pay more in taxes than they get back in transfers, but hurts the poor, who depend on social welfare

programs to survive. As a result, white-collar workers, the educated and the rich support European integration, while blue-collar workers, the uneducated and the poor oppose it.

Gabel's theory has received strong support from most scholars who have tested it with West European data (Anderson and Reichert 1996; Anderson 1998; McLaren 2002). However, in a recent paper Brinegar and Jolly (2005) argue that the strength of relationship between skills (education) and EU support depends on a country's level of economic development (the average level of education). While educated people are generally more supportive of the EU than their uneducated compatriots, this is more true in the developed (well-educated) countries of northern Europe than the less-developed (poorly educated) countries of southern Europe. Developed countries have a surplus of highly-educated people who would benefit from the opportunity to work for foreign companies or to seek employment abroad. By contrast, less-developed countries have few educated people, whose scarcity value and, hence, incomes would decline if the domestic labor market were opened to foreign competition.<sup>19</sup>

In the same vein, Ray (2003, 2004) and Brinegar, Jolly and Kitschelt (2004) argue that the relationship between economic values (self-identified leftism and support for the expansion of the welfare state) and EU support depends on the welfare state type. They find that leftist/pro-welfare people support the EU in liberal welfare states (Britain), oppose it in Social Democratic welfare states (Scandinavia), and are equally likely to support and oppose it in Christian Democratic welfare states (continental Europe).<sup>20</sup> They explain this pattern as follows. Most EU countries have Christian Democratic welfare states, so European integration is likely to lead to the convergence of social policy along Christian Democratic lines. This is good news for the pro-welfare people in

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<sup>19</sup> The reader will recognize that this is the logic of the Heckscher-Ohlin theory explaining why capitalists support free trade in capital-rich countries, but oppose it in capital-poor countries (Carbaugh 2004, chap. 4).

<sup>20</sup> For the typology of welfare states, see Esping-Andersen (1990, chap. 1). For a recent discussion, see Pontusson (2005), chap. 2, 8.

liberal countries, where social spending would increase and benefits would become more equal and more broadly available, but scares the leftists in Social Democratic countries, where spending and coverage would shrink and benefits would become less equal.

To what extent do either economic a) resources or b) attitudes explain individual-level variance in EU support in Eastern Europe? *Tucker, Pacek and Berinsky (2002) and Herzog and Tucker (2008) argue that East Europeans support or oppose EU membership based on whether they consider themselves winners or losers of the transition to capitalism.* Their argument proceeds in two steps. First, European countries have made a transition from socialism to capitalism. It is too early to tell which social groups (for example, in terms of education and occupation) have benefited from, or been hurt by, the transition since East European economies continue to evolve. *However, the transition has clearly created subjective winners and losers.* Winners believe that their economic situation is improving and support the market economy. Losers think that their economic situation is worsening and oppose the market.

Second, Tucker et al argue that *East Europeans view EU accession as a guarantee that their governments will continue economic reforms.* They do not explain why, but it is not difficult to think of possible reasons. At the Copenhagen summit in 1992, the EU adopted criteria that countries need to meet to qualify for EU membership. These included “the existence of a functioning market economy as well as the capacity to cope with competitive pressure and market forces within the Union” (European Council 1993, 13).<sup>21</sup> In 1997, the EU decided to start accession negotiations with some East European applicant countries (the Czech Republic, Estonia, Hungary, Poland, and Slovenia), but not (yet) with others (Bulgaria, Latvia, Lithuania, Romania, Slovakia). All countries in the first group met the economic criterion for membership; except Slovakia, none of the countries in the second group did (European Commission 1997, 1-57). Over

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<sup>21</sup> The other criteria were political (democracy and human rights) and administrative (ability to implement the EU law).



the next few years, the EU instructed the laggards to privatize the remaining SOEs, eliminate price controls and subsidies, open energy and agriculture to foreign competition, and reduce government spending (European Commission 2003, 1-45).

The evidence for the “winners and losers” hypothesis is quite strong (Anderson and Tverdova 2004; Caplanova, Orviska and Hudson 2004; Rohrschneider and Whitefield 2004; Jacobs and Pollack 2006; Whitefield, Rohrschneider and Alisauskiene 2006). But do economic values and perceptions have the same impact on EU support in all countries? And if not, why not? These are the questions that intrigue Christin (2004). Like much of the existing literature, Christin finds that economically contented and pro-market voters are more supportive of the EU than their discontented and anti-market peers. However, he also finds that this relationship is stronger in countries that have high economic growth and low inflation than in countries that have low growth and high inflation. He interprets this result as follows. In countries that are doing well, the losers of reforms feel that they can vent their anger on the EU without hurting their country’s long-term economic prospects. In countries that are doing poorly, however, most people support EU membership as the only way of preventing economic collapse.

*While most scholars agree that subjective economic well-being affects support for EU membership, however, they disagree over whether objective socio-economic status does so.* On the one hand, Cichowski (2000), Tucker, Pacek and Berinsky (2002), Anderson and Tverdova (2004), Jacobs and Pollack (2006), Herzog and Tucker (2008), Ehin (2001), Sikk and Ehin (2005), and Vetik, Nimmerfelt and Taru (2006) find that, controlling for attitudes, occupation, education and income have no impact on EU support. On the other hand, Caplanova, Orviska and Hudson (2004), Doyle and Firdmuc (2006), Whitefield, Rohrschneider and Alisauskiene (2006), and Allam and Goerres (2008) find that, as Gabel predicts, white-collar workers, college graduates, and the rich are more supportive of EU accession than blue-collar workers, primary school graduates,

and the poor. None of these scholars, however, consider the possibility that economic resources might be a better predictor of EU support in some countries than in others.

### **Data and Analysis**

To test these hypotheses, I used the Candidate Countries Eurobarometer (CCEB) from May 2003, the most comprehensive such survey ever and the last one conducted before Lithuania and Estonia held referenda on EU accession in May and September, respectively. Following Brinegar, Jolly and Kitschelt (2004), Brinegar and Jolly (2005) and Ray (2004), I specified the dependent variable—EU support—as a combination of a) the general perception of the EU and b) the intended vote in the referendum. (See Table 4.1 for a brief description of the variables.) The general perception of the EU could be good (3), neither good nor bad (2), or bad (1). The vote intention also falls into three categories: for (3), do not know or would not vote (2), or against (1). The two individual variables were correlated at 0.73 in Lithuania and 0.77 in Estonia. The combined variable (a scale from 2 to 6) is a more nuanced measure of EU support than either variable on its own because it has *both an attitudinal (perception) and a behavioral (vote intention) component*. It also has a more normal distribution, which facilitates regression analysis (Dielman 1996, chap. 4-5; Foster, Barkus and Yavorsky 2006, chap. 3).

The independent variables are the variables highlighted in the existing literature on EU support in Western and Eastern Europe: cognitive mobilization, post-materialism, nationalism, party preferences, trust in government, availability of economic resources, and subjective economic well-being. Some variables were fairly easy to operationalize. Following Gabel (1998 a, chap. 3-4; 1998 b) and (Doyle and Firdmuc 2006), I operationalized economic resources by income (a scale from 1 to 10), education (a dummy variable with four categories based on the age when the respondent stopped studying: 16 or before, 19 or before, after 19, or still studying), and occupation (a dummy variable with three categories: white-collar, blue-collar, or not working). Party

preferences are a dummy variable with three categories: pro-EU parties, anti-EU parties, and no party preference (Anderson 1998; Anderson and Tverdova 2004).<sup>22</sup> Trust in government is a dummy variable with two values: trust or not (Franklin and collaborators 1994, 1995; Ehin 2001). The demographic control variables are sex, ethnicity (Baltic or Slavic), age, and type of community (urban or rural).

**Table 4.1: Scales and Categories: Description of Variables**

<b>Variable</b>	<b>Description</b>
<b>A) ATTITUDES AND APTITUDES</b>	
EU support	Scale from 2 (no support for the EU) to 6 (full support)
Cognitive mobilization	Scale from 0 (no knowledge of the EU) to 9 (perfect knowledge)
National pride	Scale from 1 (not at all proud of the nation) to 4 (very proud)
National identity	Scale from 1 (identifies with Europe only) to 4 (nation only)
Pro-EU party <sup>a</sup>	Categorical: yes=1; no=0
Anti-EU party <sup>a</sup>	Categorical: yes=1; no=0
Trust government	Categorical: yes=1, no=0
Life got better <sup>b</sup>	Categorical: yes=1; no=0
Life got worse <sup>b</sup>	Categorical: yes=1; no=0
<b>B) SOCIO-ECONOMIC STATUS</b>	
Sex	Categorical: male=1; female=0
Age	Scale in years
Ethnicity	Categorical: Balt=1; Slav=0
Income	Treated as scale from 1 (lowest 10%) to 10 (highest 10%)
Up to 16 <sup>c</sup>	Categorical: yes=1; no=0 (stopped studying at age 16 or earlier)
20 or above <sup>c</sup>	Categorical: yes=1; no=0 (stopped studying at age 20 or later)
Still studying <sup>c</sup>	Categorical: yes=1; no=0
Blue-collar <sup>d</sup>	Categorical: yes=1; no=0
White-collar <sup>d</sup>	Categorical: yes=1; no=0
Rural <sup>e</sup>	Categorical: yes=1; no=0

<sup>a</sup> “Do not know” or “would not vote” are the reference category.

<sup>b</sup> “Life has stayed about the same” is the reference category.

<sup>c</sup> Stopped studying at age 17-19 is the reference category.

<sup>d</sup> Not working is the reference category.

<sup>e</sup> Urban is the reference category.

*Source:* CCEB 2003.2 (May 2003).

<sup>22</sup> No significant party in either country opposed EU membership *in principle*. Some parties, however, criticized *the terms and timing of the accession*. These included the right-populist Liberal Democratic Party and the Union of Peasants and New Democracy in Lithuania and the left-populist Center Party and the agrarian People’s Union in Estonia. I classified these parties as “anti-EU” and all other parties as “pro-EU.” See Duvold and Jurkynas (2006), 107-127 and Sikk (2006), 41-63.

Cognitive and cultural variables turned out to be more difficult to operationalize, however. The CCEB does not include Inglehart's four-item index of post-materialism (PM). As a substitute, I considered using a question that asked voters to choose two most important issues facing the country from a list that included the environment. However, only 1% of voters in Lithuania and Estonia considered the environment an important issue and they were neither more nor less likely to support the EU than the remaining 99% of voters. This could either mean that a) concern for the environment is not a valid measure of PM that b) M/PM divide is not an important cleavage in the Baltics. Therefore, I decided to leave PM out of the analysis.<sup>23</sup> To operationalize cognitive mobilization (CM), Inglehart (1977, chap. 12; 1990, chap. 10) creates an index that combines a) the frequency of discussing politics with others, b) the frequency of persuading others, and c) objective knowledge of the EU. However, knowledge about the EU turned out to be much more strongly correlated with EU support than either persuading others or discussing politics.<sup>24</sup> To give Inglehart the benefit of the doubt, I operationalized CM as knowledge, on a scale from 0 to 9.<sup>25</sup>

As discussed above, the literature on Eastern Europe has generally used either national pride or national (as opposed to European) identity to operationalize nationalism (Vetik, Nimmerfelt and Taru 2006 v. Whitefield, Rohrschneider and Alisauskiene 2006). However, it is not obvious why one would be a better measure of nationalism than the other. Following Carey (2002), I then considered operationalizing nationalism as a combination of national pride and national identity. However, pre-regression correlation

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<sup>23</sup> Including concern for the environment in the regression would not affect the regression results.

<sup>24</sup> Knowledge was correlated with EU support at 0.29 in Lithuania and 0.16 in Estonia. Persuading others was correlated with EU support at 0.1 in Lithuania and 0.13 in Estonia. Discussing politics was correlated with EU support at 0.08 in Lithuania and uncorrelated in Estonia.

<sup>25</sup> Aside from these practical considerations, I would argue that only knowledge about the EU directly measures "cognitive mobilization," while the frequency of discussing politics and persuading other people measure other things, such as interest in politics and strength of personality.

analysis showed that the two variables were unrelated in Lithuania and only moderately correlated in Estonia.<sup>26</sup> Moreover, *they had the opposite impact on EU support: in both countries, people who were proud to be part of their nation strongly supported the EU, while people who identified with the nation strongly opposed it.*<sup>27</sup> As a result, I decided to a) to break nationalism into two variables, national pride and national identity, both measured on a scale of 1-4, and b) to include both of them in the regression.

Finally, I broke with Tucker, Pacek and Berinsky (2002) and the scholars who have followed them in defining the “subjective” winners and losers of market reforms because I think that their definition is misleading. Tucker, Pacek and Berinsky create an index of winners and losers by combining two variables: a) perceived changes in one’s situation over the previous five years and b) expected changes in the next five years. *However, only the first variable (changes in the previous five years) deals with one’s past experience with economic reforms, which is what we normally understand by being a winner or a loser.* By contrast, the second variable (changes in the next five years) involves expectations about the future and, if anything, distinguishes between optimists and pessimists, which is a different issue. *Therefore, I used only the first variable to define winners and losers: winners think that their personal situation has gotten better, while losers think that it has gotten worse.* (The largest group—stayed about the same—is the reference category in the three-way dummy variable.)<sup>28</sup>

The results of the regression analysis are presented in Table 4.2. Variables are marked with one, two or three asterisks depending on whether they were significant at the

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<sup>26</sup> The correlation coefficient was 0.16 in Estonia.

<sup>27</sup> The correlation between national pride and EU support was 0.35 in Lithuania and 0.27 in Estonia. The correlation between national identity and EU support was –0.29 in Lithuania and –0.27 in Estonia.

<sup>28</sup> The question (Q2 in the May 2003 CCEB) reads as follows: “If you compare your present personal situation with five years ago, would you say it has improved, stayed about the same, or got worse?” I realize that this question does not specifically address economic changes, but I assume that one’s “present personal situation” has a significant economic component. Unfortunately, the survey does not have any questions about economic values.

10%, 5%, or 1% level. I also estimate the substantive significance of the statistically significant variables by calculating how much the dependent variable (EU support) would change if we changed the value of the independent variable from its minimum to its maximum level. For dummy variables (education, occupation, trust in government, party preferences, and subjective economic well-being), the substantive effect equals the regression coefficient. For continuous variables (income, national pride, national identity, and CM), the substantive effect is calculated by multiplying the coefficient by the range of the variable, i.e., the minimum value subtracted from the maximum.

Beginning with cognitive and cultural factors, Lithuanians who knew a lot about the EU were up to 73% more supportive of the EU than those who knew little. By contrast, CM had no impact on EU support in Estonia. The most likely explanation for this is that Lithuania negotiated a more favorable accession treaty than Estonia. Thus, it was given a transition period for introducing EU sanitary and quality standards for farms, food-processing plants, and small businesses. It also got bigger production quotas—and, hence, subsidies—for agriculture. Finally, it received more financial aid for restructuring the energy sector, especially the Ignalina nuclear power plant. Altogether, Lithuania received 643 euros of EU aid per capita in 2004-2006, while Estonia received 602 euros.<sup>29</sup> As a result, knowledge should increase support for the EU in Lithuania, but not necessarily in Estonia, a possibility that Cichowski (2000) overlooks.

*By contrast, nationalism turned out to be useless as a predictor of EU support in both countries: people who identified with the nation opposed EU membership, while people who were proud of their nationality supported it.* Presumably Baltic nationalists disagreed on what the EU membership would mean for the nation. Would it subordinate Lithuania and Estonia to their Polish and German masters of old or protect their newly-gained independence from Russia? Would it undermine their unique Baltic or Finno-

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<sup>29</sup> The calculations are based on Zeff (2004), 176, 280. See also Auštrevičius (2007), 225-258 and Streimann (2007), 157-187.

Ugric culture or reinforce their European (non-Slavic) cultural identity? Would it allow them to keep their strict language and citizenship laws or force them to liberalize these policies? *This would explain why prior researchers have come to different conclusions about the relationship between Baltic nationalism and EU support, depending on whether they have operationalized nationalism as national identity (Vetik, Nimmerfelt and Taru 2006) or national pride (Whitefield, Rohrschneider and Alisauskiene 2006).*

**Table 4.2: Cognition or Calculation? Regression Results**

Independent Variables	Unstandardized Coefficient (Standard Error)		Substantive Significance	
	Lithuania	Estonia	Lithuania	Estonia
<b>A) ATTITUDES AND APTITUDES</b>				
Cognitive mobilization	0.08 (0.02)***	0.01 (0.03)	64%	-
National pride	0.31 (0.05)***	0.29 (0.07)***	93%	87%
National identity	-0.41 (0.06)***	-0.37 (0.07)***	-123%	-111%
Pro-EU party <sup>a</sup>	-0.12 (0.09)	0.24 (0.14)*	-	24%
Anti-EU party <sup>a</sup>	0.01 (0.14)	-0.02 (0.14)	-	-
Trust the government	0.25 (0.09)***	0.38 (0.11)***	25%	38%
Personal situation got better <sup>b</sup>	0.07 (0.1)	0.08 (0.13)	-	-
Personal situation got worse <sup>b</sup>	0.03 (0.1)	-0.69 (0.13)***	-	-69%
<b>B) SOCIO-ECONOMIC STATUS</b>				
Sex	-0.29 (0.08)***	0.06 (0.11)	-29%	-
Age	0.00 (0.00)	0.00 (0.00)	-	-
Ethnicity	-0.6 (0.19)***	0.03 (0.14)	-60%	-
Income	-0.01 (0.02)	0.07 (0.03)**	-	63%
Up to 16 <sup>c</sup>	-0.12 (0.13)	0.12 (0.15)	-	-
20 or above <sup>c</sup>	0.03 (0.1)	0.02 (0.14)	-	-
Still studying <sup>c</sup>	0.03 (0.17)	0.55 (0.24)**	-	55%
Blue-collar <sup>d</sup>	0.08 (0.11)	-0.03 (0.15)	-	-
White-collar <sup>d</sup>	0.11 (0.12)	0.14 (0.17)	-	-
Rural <sup>e</sup>	-0.12 (0.09)	-0.02 (0.13)	-	-
	<b>R<sup>2</sup> = 24%</b>	<b>R<sup>2</sup> = 26%</b>	<b>N = 615</b>	<b>N = 630</b>

*Note:* I rounded up all coefficients and standard errors to the nearest percentage point.

\* Coefficient is significant at the 10% level ( $p \leq 0.10$ ).

\*\* Coefficient is significant at the 5% level ( $p \leq 0.05$ ).

\*\*\* Coefficient is significant at the 1% level ( $p \leq 0.01$ ).

<sup>a</sup> “Do not know” or “would not vote” are the reference category.

<sup>b</sup> “Life has stayed about the same” is the reference category.

<sup>c</sup> Stopped studying at age 17-19 is the reference category.

<sup>d</sup> Nor working is the reference category.

<sup>e</sup> Urban is the reference category.

*Source:* CCEB 2003.2 (May 2003).

Moving on to politics, *Lithuanians and Estonians who trusted the government were more likely to support the EU than those who did not*, as Franklin et al (1994, 1995) and Ehin (2001) predict. This makes sense because the governments dominated the accession process in both countries. They negotiated the EU accession agreements with minimal consultation with the parliament or interest groups (e.g., business and labor) (Raik 2004; Sissenich 2007, chap. 7). They also ran active pro-EU “information” campaigns, arguing that EU accession would increase economic growth and allow the state to spend more money on social programs (Auštrevičius 2005; Past and Palk 2005). However, the relationship between trust and EU support was stronger in Estonia (37%) than in Lithuania (25%), although more Estonians (54%) than Lithuanians (32%) trusted the government (see Table 4.3). As I will argue in the next chapter, this may reflect the fact that Lithuania pursued an insider-oriented strategy of economic reform, while Estonia followed an outsider-oriented strategy.

*Party preferences, on the other hand, affected EU support in Estonia*, where voters of pro-EU parties were 24% more like to support EU membership than people who did not have a party preference, *but not in Lithuania*. This is what we would expect. In Lithuania, all major parties, including the governing post-Communist Social Democrats, supported EU membership as a way of modernizing the Lithuanian economy and increasing living standards (Mažylis and Unikaitė 2004; Auštrevičius 2005; Duvold and Jurkynas 2006). Foreign investment and EU financial aid would improve Lithuanian infrastructure and create new, high-paying jobs. Better access to EU markets would allow Lithuanian farmers to compete with European producers. By contrast, the largest party in Estonia, the left-populist Centrists, opposed EU accession on current terms because it would hurt domestic producers and the poor (Savisaar 1999, Part III; Mikkel and Kasekamp 2005; Sikk 2006). EU sanitary standards and environmental regulations would bankrupt Estonian farmers, small businessmen, and the oil-shale-based energy industry. EU-imposed tariffs and indirect taxes would increase prices.



**Table 4.3: Similar Structure, Different Attitudes: The Distribution of Variables**

<b>Variable</b>	<b>Lithuania</b>	<b>Estonia</b>
<b>A) ATTITUDES AND APTITUDES</b>		
Support the EU (5-6)*	76	45
Undecided/Indifferent (4)*	11	20
Oppose the EU (2-3)*	13	35
Knows little about the EU (0-4)*	64	63
Knows a lot about the EU (5-9)*	36	37
Proud of nation (3-4)*	63	62
Not proud of nation (1-2)*	37	38
Identifies mainly with nation (3-4)*	86	83
Identifies mainly with Europe (1-2)*	14	17
Would vote for pro-EU party	38	30
Would vote for anti-EU party	9	35
Does not know or would not vote	53	35
Trusts government	32	54
Does not trust government	68	46
Personal situation got better	25	31
Personal situation stayed about the same	39	41
Personal situation got worse	36	28
<b>B) SOCIO-ECONOMIC STATUS</b>		
Male	47	45
Female	53	55
Young (15-29)*	26	26
Middle-aged (30-59)*	50	48
Old (60 and above)*	24	26
Balt	93	72
Slav	7	28
Poor (1-3)*	40	33
Middle-income (4-7)*	51	54
Rich (8-10)*	9	13
Stopped studying at age 16	22	21
Stopped studying at age 17-19	31	40
Stopped studying at age 20 or above	30	26
Still studying	15	13
Blue-collar	18	20
White-collar	26	32
Not working	56	47
Rural	30	32
Urban	70	68

\*The numbers in the brackets refer to the collapsed values of the continuous variables.

Source: CCEB 2003.2 (May 2003).

Interestingly, however, *Estonians who did not have a party preference were as likely to oppose the EU as those who supported anti-EU parties.* This suggests that while some Euroskeptics took their cues from anti-EU parties, as Cichowski (2000) and Anderson and Tverdova (2004) argue, others responded to a favorable political opportunity structure created by elite conflict over European integration (Tarrow 1998, chap. 5). By criticizing the terms of the accession, the Centrists gave Euroskeptics intellectual ammunition. Estonia's accession treaty with the EU consisted of 4,900 pages of dense, bureaucratic text.<sup>30</sup> The Centrists took the parts that hurt Estonian interests (e.g., energy, agriculture, and indirect taxes) and popularized them. The Centrists also helped to increase the social prestige of Euroskepticism. At first, public opposition to the EU was limited to the extra-parliamentary Independence and Labor parties, which most people either a) had not heard of or b) considered extremist. The Centrists showed that “reasonable” people could have doubts about the EU (Noelle-Neumann 1991, chap. 17).

How much did economic resources perceptions influence EU support in Lithuania and Estonia? In Lithuania, men were 29% more likely to vote for the EU than women, while ethnic Lithuanians were 60% more supportive of the accession than ethnic Slavs. On balance, men and Lithuanians probably stood to benefit more—or lose less—from EU accession than women and Slavs. For example, men could go and work on Europe's farms and construction sites, while women would have to stay at home and take care of children. Ethnic Lithuanians could visit their relatives in Europe and America, while ethnic Slavs would be cut off from their families in the former Soviet Union. However, none of the most direct indicators of socio-economic status—e.g., income and education—had any impact on EU support in Lithuania. By contrast, the Estonian case clearly supports Gabel's (1998 a, chap. 2; b) argument that economically competitive

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<sup>30</sup> The accompanying *acquis communautaire*—the EU law—was about 80,000 pages long. See Anna Grzymala-Busse and Abby Innes, “Great Expectations: The EU and Domestic Political Competition in East Central Europe,” *East European Politics and Societies*, 17, no. 3 (2003): 65.

individuals are more supportive of the EU than their non-competitive peers. Thus, the rich were 69% more likely to support EU membership than the poor, while students were 55% more likely to do so than non-students.

This brings us to the most interesting result of my analysis, which concerns the relationship between subjective (economic) well-being and EU support. In Lithuania, perceived (economic) changes in the previous five years had no impact on EU support.<sup>31</sup> In Estonia, by contrast, people who felt that their (economic) situation had worsened were 69% less likely to support EU accession than those who felt that their (economic) situation had stayed the same. This is *not* because Estonians are a particularly discontented bunch: fewer Estonians (28%) than Lithuanians (36%) believed that their situation had worsened, while more Estonians (31%) than Lithuanians (25%) believed that their situation had improved. *Rather, the difference between Estonia and Lithuania is that unhappy Estonians blamed the EU for their misery, while unhappy Lithuanians did not*, a possibility that the existing literature ignores (Tucker, Pacek and Berinsky 2002; Herzog and Tucker 2008; but see Christin 2004 for a different contextual argument).

## **Conclusion**

This chapter has considered three sets of theories explaining why some people in Eastern (and Western) Europe are more supportive of European integration than others: cultural and cognitive, political, and economic. The cognitive approach asserts that voters support European integration if they are “cognitively mobilized”: the more people know about the EU, the less likely they are to have irrational fears about joining the union. Cultural theories contend that opposition to the EU is stronger among voters who hold nationalist and materialist values because they see European integration as a threat

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<sup>31</sup> The reader is entitled to ask whether the results would be any different if I used Tucker, Pacek and Berinsky’s (2002) index of winners and losers, which combines past and future (expected) economic changes. The answer is that this variable would still have a much weaker, albeit statistically significant, effect on EU support in Lithuania than in Estonia.

to their country's political sovereignty, national identity, and traditional values. Political explanations hold that voters are more likely to support EU accession if they trust the politicians who conduct the accession negotiations. They also maintain that voters look to their favorite political party for cues on what to make of the EU.

Finally, economic theories argue that voters support the EU depending on either their a) objective socio-economic status or b) subjective economic well-being. Scholars working on Western Europe have argued that economically competitive individuals (the rich, the educated, and white-collar workers) are more supportive of European integration than non-competitive individuals (the poor, the uneducated, and blue-collar workers) because they are more likely to benefit from increased mobility of labor and capital. Students of East European politics have suggested that the "winners" of the transition to capitalism (people who believe that their economic situation is improving and who support the market economy) are more likely to support joining the EU than the "losers" (people who think that their economic situation is worsening and who oppose the market) because they see EU accession as a continuation of market-oriented economic reforms.

How well did these different theories work in Lithuania and Estonia? Cultural theories did poorly. Post-materialist values did not have any influence on EU support because almost all Lithuanians and Estonians turned out to be materialists (at least if concern for the environment is a valid measure of post-materialism.) Surprisingly, nationalism was equally useless as a predictor of EU support because nationalist voters disagreed on whether the EU was good or bad for the nation. Political theories fared better. In both countries, people who trusted the government were more supportive of the EU than those who did not, presumably because governments dominated the EU accession process. In Estonia, voters of pro-EU parties were more likely to support EU membership than voters of anti-EU parties and people who did not have a party preference. However, this relationship did not hold in Lithuania where all major parties supported EU accession.

The most important and original contribution of this chapter, however, has been to show that *the relationship between cognitive and economic variables and EU support depended on national context. Knowledge about the EU increased support for EU membership in Lithuania, but not in Estonia. Objective lack of economic resources (at least as defined by Gabel 1998 a, b) and subjective economic discontent reduced EU support in Estonia, but not in Lithuania.* These findings are consistent with some recent comparative studies on EU support in Western Europe, which argue that socio-economic status and support for economic redistribution more strongly in some countries than others (Brinegar, Jolly and Kitschelt 2004; Ray 2003, 2004; Brinegar and Jolly 2005). However, they challenge much of the existing literature on Eastern Europe, which has sought to establish universal causal patterns. The next chapter will explain why national context matters, and how.

## **CHAPTER 5**

### **INSIDERS OR OUTSIDERS? STRATEGIES OF ECONOMIC REFORM IN LITHUANIA AND ESTONIA**

#### **Introduction**

This dissertation has compared Lithuanian and Estonian attitudes toward the EU using CA of newspapers and statistical analysis of survey data. Two main results have emerged from my analysis. First, at the time of the EU referendum, many Lithuanians and Estonians felt that their (country's) economic situation had worsened during the transition to capitalism. Full employment had given way to high unemployment. Real incomes had dropped. Basic infrastructure (e.g., railways and power plants) was falling apart. Second, Lithuanians and Estonians had different economic expectations about the EU. Most Lithuanians believed that joining the EU would solve their (country's) economic problems by encouraging foreign investment and trade and allowing Lithuanians to work abroad. By contrast, many Estonians believed that joining the EU would make their (country's) economic problems worse by driving domestic producers bankrupt and allowing foreigners to take control of Estonian local resources.

Why did Lithuanians and Estonians have such different economic expectations about the EU even though they were both unhappy about their (country's) current economic situation? The existing literature on cross-national differences in EU support is not very helpful in answering this question because it has paid more attention to politics and culture than economics. The (very) few economically-minded works have focused on quantitative and macro-economic differences in the candidate countries' economic performance—and produced contradictory results. Some authors have found that countries that are doing well economically (e.g., in terms of growth) are more supportive of the EU than countries that are doing badly, while others have come to the opposite conclusion. In this chapter, however, I will argue that we need to analyze the qualitative

and micro-economic differences between East European economies to explain why some countries strongly supported EU membership, while others came close to rejecting the accession.

*Using statistical data, newspaper accounts, and secondary literature, I will show that Lithuania and Estonia pursued different strategies of economic reform.<sup>32</sup> Lithuania followed an insider-oriented strategy. It maintained public ownership of basic infrastructure (e.g., railways and power plants) and sold other state-owned enterprises (SOEs) to their Soviet-era managers. It imposed moderate tariffs on imports, especially of agricultural products, and continued to trade heavily with Russia until the 1998 financial crisis. By contrast, Estonia followed an outsider-oriented strategy. It sold SOEs, including infrastructure enterprises, to foreign investors, especially Swedes, Finns, and Americans. It abolished all import tariffs and rapidly reoriented its trade from Russia to the EU. This explains why Lithuanians saw EU accession as an alternative to their country's current economic policies, while Estonians saw the accession as a continuation of such policies.*

*Neither strategy worked particularly well, however. The Lithuanian strategy helped to protect output and employment in agriculture and "old" industries (e.g., food processing and oil refining), which had been equipped with the latest Soviet technology and which benefited from continued access to the Russian market. However, it slowed down the development of services and "new" industry (e.g., electronics), where the existing equipment was obsolete. The Estonian strategy led to the growth of the services and "new" industry, which received a lot of foreign direct investment (FDI) and could export their products to the West duty-free. However, it harmed agriculture and "old"*

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<sup>32</sup> For a similar argument, see Béla Greskovits and Dorothee Bohle, "Development Paths on Europe's Periphery: Hungary's and Poland's Return to Europe Compared," *Polish Sociological Review* 1, 33 (2001): 3-27, who compare the "foreign-led" transition in Hungary with the "state-led transition" in Poland. See also Lawrence P. King, "Postcommunist Divergence: A Comparative Analysis of the Transition to Capitalism in Poland and Russia," *Studies in Comparative International Development* 37, 3 (Fall 2002), 3-34 and who compares "capitalism from without" in Poland with "capitalism from above" in Russia.

industry (e.g., food processing), which received little FDI and were subject to high tariffs in both Eastern and Western markets. Neither strategy could prevent the decline of infrastructure, although the Lithuanian strategy slowed it down while the Estonian strategy sped it up. *As a result, both Lithuanians and Estonians were dissatisfied with their (country's) economic situation.*

The rest of the chapter is structured as follows. The next section will analyze Lithuania's insider-oriented reforms and their sectoral consequences. The following section will discuss Estonia's outsider-oriented strategy. The conclusion will conclude.

### **Lithuania: Insider-Oriented Reforms**

Lithuania pursued an insider-oriented strategy of transition to capitalism. In the 1992 general election, the post-Communist Democratic Labor Party won a landslide victory by promising to manage the transition to the market economy more competently and compassionately than their conservative opponents. A key element of their reform program was voucher privatization. All residents of Lithuania received vouchers based on their age: older people got more vouchers. The vouchers could be used to buy apartments, land, and—through investment funds set up by enterprise employees—shares in enterprises undergoing privatization.<sup>33</sup> Enterprises where voucher privatization was impracticable—the Ignalina nuclear power plant, the Mažeikiu Nafta oil company, Lithuanian Gas, Lithuanian Railways, Lithuanian Airlines, the ports, the major banks, and Lithuanian Telecom—were excluded from privatization until 2000.<sup>34</sup>

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<sup>33</sup> More controversially, they could also be sold for cash.

<sup>34</sup> OECD, *The Baltic States: A Regional Economic Assessment* (Paris: OECD, 2000), 30-32; V. Stanley Vardys and Judith B. Sedaitis, *Lithuania: The Rebel Nation* (Boulder, CO: Westview Press, 1997), 197-201; Thomas Lane, *Lithuania: Stepping Westward* (London and New York: Routledge, 2002), 140-143, 174-179; Albertas Šimėnas, "Formation of the Market Economy in Lithuania," in *Lithuanian Economic Reforms: Practice and Perspectives*, ed. Antanas Buračas, Dean M. Larson and Joseph P. Kairys (Vilnius: Margi Raštai, 1997), 17-62; Andres Aslund, *Building Capitalism: The Transformation of the Former Soviet Bloc* (Cambridge and New York: Cambridge University Press, 2002), 272-274; Ian Jeffries, *The Countries of the Former Soviet Union at the Turn of the Twenty-first Century: The Baltic and European States in Transition* (London and New York: Routledge, 2004), 245-255.



In principle, foreigners were encouraged to participate in the privatization process: some firms (e.g., the Lietuva hotel in Vilnius, the Kaunas Confectionary, and Klaipėda Tobacco) were even set aside for hard-currency sales to the highest bidder. In practice, however, foreign investors encountered numerous legal and bureaucratic obstacles. In 1992-1994, three ministries were in charge of privatization: finance, economics, and a branch ministry (e.g., industry or commerce). This slowed down privatization because potential investors had to get three different permissions. Equally important, the Lithuanian constitution of 1992 prohibited foreigners from buying land. The constitution was amended in 1996 to allow foreign investors to purchase non-agricultural land accompanying real estate, but they still had to apply for permission from the local (county) government to do so.<sup>35</sup>

The privatization process was insider-oriented in another way as well: there were significant advantages for enterprise employees. Workers and managers could purchase up to 50% of the shares in the firm where they worked at a special low rate before the bidding was opened to the general public. The post-Communist government argued that this was the fairest method of privatization because it would turn workers, whose hard work had built up the enterprises, into owners. In practice, however, the preference for insiders meant that most SOEs became the private property of enterprise managers, the main financial backers of the post-Communists. Managers dominated the investment funds that company employees set up to purchase enterprises from the state. Managers also bought up vouchers from impoverished workers—both at their own plant and at other SOEs—at a fraction of their nominal value.<sup>36</sup>

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<sup>35</sup> Lane, *Lithuania*, 177-179; Albertas Šimėnas, “Lithuania’s Economy During the Period of Reforms,” in *Lithuanian Economic Reforms*, ed. Buračas, Larson and Kairys, 63-74; Valdas Samonis, “Economic Reforms in the Baltics: The Case of Lithuania,” in *Privatization in Central and Eastern Europe: Perspectives and Approaches*, ed. Demetrius S. Iatridis and June Gary Hopps (Westport and London: Praeger, 1998), 73-84.

<sup>36</sup> OECD, *The Baltic States*, 30-32; Samonis, “Economic Reforms,” 73-84; Šimėnas, “Lithuania’s Economy,” 63-74; Jeffries, *Countries of the Former Soviet Union*, 245-255.

The post-Communist government also pursued a modest industrial policy to help Lithuanian producers survive the transition from socialism to capitalism. It tried to restructure enterprises slated for privatization by changing their profile, breaking them into smaller units, or establishing “daughter companies.” It also wrote off their tax arrears and, in some cases, lent them money at below-market interest rates. Finally, it passed a bankruptcy law that made it difficult for banks to take delinquent firms to court and gave regional authorities the right to “review” (i.e., stop) bankruptcy proceedings against large employers. The government also subsidized Lithuanian farmers. It set a target price for most agricultural products and purchased the “surplus” production from the farmers at that price. It also provided export subsidies to the most competitive branches of Lithuanian agriculture, dairy farming and livestock breeding.<sup>37</sup>

Lithuanian trade policy under the post-Communists was moderately protectionist and oriented towards Russia. While the average mean tariff was low (3% in the 1997), tariffs on agricultural goods were as high as 50-90%. Lithuania also imposed quantitative restrictions on agricultural imports in areas where Lithuanian producers were not competitive (e.g., cereals). Until the 1998 financial crisis, Lithuania continued to trade heavily with Russia. This was, in part, because the Russian market remained open to Lithuania: in 1993, Russia and Lithuania granted each other most-favored-nation status. However, the nomenklatura owners of Lithuanian firms also preferred to sell their goods in Russia where they had prior contacts and which they considered a less demanding market. Lithuania’s approach to Western trade was cautious: its 1995 association agreement with the EU provided for a six-year transition period to free trade.<sup>38</sup>

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<sup>37</sup> OECD, *The Baltic States*, 122-129; Sandrine Cazes and Alena Nesperova, *Labor Markets in Transition: Balancing Flexibility and Security in Central and Eastern Europe* (Geneva: ILO, 2003), 41-42; Samonis, “Economic Reforms,” 73-84; Šimėnas, “Lithuania’s Economy,” 63-74; Živilė Šatūnienė, “Political Economy of Lithuania’s Membership in the Common Agricultural Policy (CAP),” *Lithuanian Political Science Yearbook* 1, no. 1 (2000): 240-263.

<sup>38</sup> World Bank Tariff database, <http://sitesources.worldbank.org/INTRES/Resources/469232-1107449512766/tar.2007.xls>; OECD, *The Baltic States*, 40-48, 191-192; Piritta Sorsa, “Lithuania: Trade Issues in Transition,” in *Trade in the New Independent States*, ed. Constantine Michalopoulos and David G.

In the 1996 general election, the conservative Homeland Union and the clerical Christian Democratic Union defeated the Laborites by promising to fight corruption, put an end to “nomenklatura privatization,” and reorient Lithuanian trade to the West. True to its election promises, the new government adopted more outsider-oriented economic policies. The constitution was changed to allow foreign citizens to buy non-agricultural land. Many remaining SOEs—mostly banks and semi-infrastructure firms like the Lithuanian Telecom, Lithuanian Shipping, and Lithuanian Gas—were sold to foreign—mostly Nordic and German—investors. (However, one third of Lithuanian Gas was sold to its main supplier, the Russian Gazprom.) The country’s largest firm, the Mažeikiu Nafta oil refinery, was sold to an American company. A new bankruptcy law was passed that made it easier for creditors and suppliers to take delinquent firms to court.<sup>39</sup>

However, the conservative government did not go all the way in liberalizing and Westernizing Lithuanian economic policy. The most important infrastructure enterprises—the power plants and the railways—remained public property, although the conservatives considered privatizing the railway. Several banks, too, stayed in state hands, including the Savings Bank, Lithuania’s largest financial institution, and the Agricultural Bank, the main creditor of the country’s farm industry. The new bankruptcy law notwithstanding, the government rarely started bankruptcy proceedings against firms that owed the state back taxes. Although foreign investors were allowed to buy land

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Tarr (Washington, DC: The World Bank, 1994), 157-70; Niina Pautola-Mol, “Preferential Trade Agreements: Specific Aspects of EU-Baltic Trade Integration,” in *The Road to the European Union, Volume 2: Estonia, Latvia and Lithuania*, ed. Vello Pettai and Jan Zielonka (Manchester and New York: Manchester University Press, 2003), 243-246; Ramūnas Vilpišauskas, “Regional Integration in Europe: Analysing Intra-Baltic Economic Cooperation in the Context of European Integration,” in *Road to the European Union*, ed. Pettai and Zielonka, 163-204; Ramūnas Vilpišauskas and Guoda Stepanovičienė, “The Baltic States: The Economic Dimension,” in *Winners and Losers of EU Integration: Policy Issues for Central and Eastern Europe*, ed. Helena Tang (Washington, DC: The World Bank, 2000), 58-60; Raul Mälik, “Trade Patterns: The Baltic States and the Baltic Rim,” *The Baltic Review* 22 (2003), 14-17.

<sup>39</sup> OECD, *Baltic States*, 122-129; Lane, *Lithuania*, 145-149, 180-187; Edward B. Jakubauskas, “The Lithuanian Economy on the Threshold of the New Millennium,” *Journal of Baltic Studies* 31, no. 2 (Summer 2000): 127-130; Tõnis Arnover, “Erastamine toob Leetu raha,” *Äripäev*, 4 June 1999; Tõnis Arnover, “Leedu võtab pikki samme,” *Äripäev*, 2 April 2002.

accompanying real estate, the ban foreign ownership of agricultural land remained in place. While industrial subsidies were cut, agricultural subsidies were increased. Lithuania also maintained tariffs on Western agricultural imports since Western countries declined to remove theirs. As a result, as Table 5.1 indicates, Lithuania received little FDI and continued to trade heavily with Russia.<sup>40</sup>

**Table 5.1: Ties That Bind: Foreign Investment and Trade in Lithuania and Estonia in 2003**

	Lithuania	Estonia
Private sector share in GDP (%)	75	80
Foreign direct investment per capita, 1989-2003 (\$)	1067	2402
Share of trade in GDP (%)	93	119
Share of trade with non-transition countries (%)	64	72

*Source:* EBRD, *Transition Report 2004* (London: EBRD, 2004), 45, 124 and 151.

In the 2000 election, an alliance of post-Communists and “historic” Social Democrats won a plurality of the vote by accusing the conservatives of selling off “strategic enterprises” to unscrupulous foreigners. After a year of parliamentary infighting, the Social Democrats formed a coalition with the centrist Social Liberals. For the most part, the new government continued the conservative policy of privatizing SOEs through direct sales to foreign investors. Thus, it sold the Savings Bank to the Swedish Swedbank and the Agricultural Bank to the German Norddeutsche Landesbank. However, unlike the conservatives, it was willing to approve the resale of privatized SOEs to Russian investors. For example, it allowed Russia’s Konversbank to purchase Snoras Bankas from its Luxembourg-based owners and encouraged Williams to sell Mažeikiu Nafta to its main supplier of crude oil, the Russian Yukos. It also sold the

<sup>40</sup> OECD, *The Baltic States*, 122-129; Pautola-Mol, “Preferential Trade Agreements,” 243-246; Šatūnienė, “Political Economy,” 240-263; Vilpišauskas, “Regional Integration,” 163-204; Eugenijus Maldeikis and Gediminas Rainys, “Estonia, Latvia, Lithuania: The Way to Europe,” in *Transformations of Post-Communist States*, ed. Wojciech Kostecki, Katarzyna Zukrowska and Bogdan J. Góralczyk (New York: St. Martin’s, 2000), 142-147; Tõnis Arnover, “Leedu surutud seisus,” *Äripäev*, 28 May 1999; Argo Kүүnemäe, “Leedus kolmas valitsus poole aasta jooksul,” *Äripäev*, 11 November 1999; “Lithuania Must Decide on Selling the Land to Foreigners,” *Baltic Review* 21 (2002): 33.

national airline to a consortium consisting of domestic construction and electronics firms and a Turkish travel agency.<sup>41</sup>

As Table 5.2 shows, Lithuania's insider-oriented strategy was not particularly successful in promoting growth and protecting jobs. Lithuania's per capita GDP was smaller in 2003 (\$12,000) than it had been in 1990 (\$12,566), while unemployment had increased from essentially zero to 12%. However, these aggregate figures conceal significant differences between sectors. Lithuanian agriculture did quite well in terms of employment: relative employment in agriculture remained constant at 18-19% in 1990-2003. Import tariffs protected Lithuanian farmers against larger and more efficient Western agribusinesses. Continued access to the Russian market allowed farmers to export goods that the small domestic market could not absorb. However, agricultural output declined from 17-27% of the GDP in 1990-1991 to 6% in 2003.<sup>42</sup> Many farmers could no longer afford to purchase agricultural inputs (e.g., gasoline, machinery, and fertilizers), whose price shot up to world market levels. Farm exports to Russia fell significantly after the 1998 Russian financial crisis when Russia devalued its currency.<sup>43</sup>

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<sup>41</sup> Rokas M. Tracevskis, "Election Campaign Reaches Its Peak," *Baltic Times*, 5 October 2000; "Williams Out, Yukos Taking Over," *Baltic Times*, 22 August, 2002; Steven Paulikas, "Russia Enters Lithuanian Banking Market," 25 March, 2003; "Sale of Lithuanian Airlines Approved by Authorities," *Baltic Times*, 6 July 2005; Jeffries, *Countries of the Former Soviet Union*, 230-237, 245-255.

<sup>42</sup> Why did Lithuanian agricultural (as well as industrial and service) output fluctuate so much in 1990-1991? The most likely explanation is that a) real output did not change much, but b) prices did since this was a time of price liberalization.

<sup>43</sup> OECD, *Baltic States*, 48-56, 215-230; OECD, *Labor Market and Social Policies*, 18-20, 35, 39; Cazes and Nesporova, *Labor Markets in Transition*, 8-16, 32-37, 41-43; Ilkka Alanen, "Annex Tables and Figures," in *Mapping the Rural Problem in the Baltic Countryside: Transition Processes in the Rural Areas of Estonia, Latvia and Lithuania*, ed. Ilkka Alanen (Aldershot, UK and Burlington, VT: Ashgate, 2004), 274, 276-277; Donatas Stanikunas, Irena Krisciukaitiene and Romualdas Zemeckis, "Trends in Development in Lithuanian Agricultural Policy," in *Mapping the Rural Problem*, ed. Alanen, 81-190; 195-201; Vardys and Sedaitis, *Lithuania*, 202-203; Lane, *Lithuania*, 192-193; Nordic Center for Spatial Development (Nordregio), *Regions of the Baltic States* (Stockholm: Nordregio, 2000), 236-239, 248-251, 260-263; Jeffries, *Countries of the Former Soviet Union*, 259-261.

**Table 5.2: Muddling Through: Output and Employment in Lithuania and Estonia in 1990-2003**

	Lithuania		Estonia	
	1990	2003	1990	2003
<b>A) Output</b>				
GDP per capita at PPP (2005\$)	12,566	12,000	10,194	13,906
Composition of GDP (%) (1991 data in brackets)				
...Agriculture	27 (17)	6	17 (18)	4
...Industry	31 (51)	32	50 (40)	29
...Services	42 (33)	62	34 (42)	68
<b>B) Employment</b>				
Unemployment rate (%)	-	12	1	10
Structure of employment (%)				
...Agriculture	19	18	21	6
...Industry	41	28	37	32
...Services	39	54	42	61

*Source:* The World Bank, *World Development Indicators Online*, <http://publications.worldbank/WDI/>.

Lithuanian industry did poorly in terms of both output, which declined from 31-50% of the GDP to 32%, and employment, which dropped from 40-41% to 28% of the workforce (see Table 5.2). However, as Table 5.3 shows, the decline was not uniform. Output and employment remained at Soviet-era levels (relative to total output and employment) in food processing, textiles, and oil refining. Fitted out with the latest Soviet technology in the 1980s, these industries had a small quality gap with the West and benefited from continued access to the Russian. By contrast, output and employment declined in the technologically most advanced sectors of Lithuanian industry, such as machinery and electronics. With a few exceptions (e.g., the refrigerator maker Snaiğė), these industries had a large quality gap with the West. As a result, they rapidly lost their market share in Russia (and Lithuania itself) when Western products became available.<sup>44</sup>

<sup>44</sup> OECD, *The Baltic States*, 254; OECD, *Labor Market and Social Policies*, 18-20, 39; Cazes and Nesporova, *Labor Markets in Transition*, 8-16, 32-37, 41-43; Vardys and Sedaitis, *Lithuania*, 64-68, 202-203; Gediminas Rainys, "Industrial Restructuring: Analysis by Branch and Case Studies," in *Lithuanian Economic Reforms*, ed. Buračas, Larson, and Kairys, 101-14; Nordregio, *Regions of the Baltic States*, 252-259, 264-267; Jeffries, *Countries of the Former Soviet Union*, 261-262.

**Table 5.3: Old and New: Manufacturing Output and Employment in Lithuania and Estonia in 1994-2003 (% of total)**

	Lithuania		Estonia	
	1994	2003	1994	2003
<b>A) Output</b>				
Food products, beverages and tobacco	31	21	36	18
Textiles and textile products	12	13	9	11
Leather and leather products	1	1	2	1
Wood and wood products	3	7	5	16
Pulp, paper, publishing and printing	4	5	6	8
Petroleum products	25	19	0	0
Chemical products and fibers	3	5	8	5
Rubber and plastic products	1	5	2	4
Other non-metallic mineral products	4	3	6	5
Fabricated metal products	2	3	5	10
Machinery and equipment n.e.s.*	5	3	2	3
Electrical and optical equipment	6	9	6	8
Transport equipment	1	2	5	5
Manufacturing n.e.s.*	3	5	7	9
<b>B) Employment</b>				
Food products, beverages and tobacco	19	20	21	15
Textiles and textile products	22	23	20	19
Leather and leather products	3	1	3	2
Wood and wood products	6	11	8	14
Pulp, paper, publishing and printing	3	5	5	6
Petroleum products	1	2	0	0
Chemical products and fibers	3	2	6	2
Rubber and plastic products	1	3	1	3
Other non-metallic mineral products	8	4	5	4
Fabricated metal products	4	5	5	8
Machinery and equipment n.e.s.*	10	4	6	4
Electrical and optical equipment	13	8	7	8
Transport equipment	4	3	5	4
Manufacturing n.e.s.*	5	9	9	12

\*Not elsewhere specified.

Source: Wiener Institut für Internationale Wirtschaftsvergleiche (by request).

Unlike industry, Lithuania’s service sector experienced significant development during the transition to capitalism: as Table 5.3 shows, the proportion of the workforce employed in services increased from 39-42% to 54% in 1990-2003, while the share of services in the GDP grew from 33-42% to 62%. However, it would be a mistake to view this as evidence of the rapid modernization of the Lithuanian economy. As Table 5.4 makes clear, output and employment increased the most in relatively simple services, such as trade, where local entrepreneurs could earn a quick return on small amounts of capital. For example, Lithuania’s largest private employer at the time of the EU referendum was the domestically-owned VP Market retail chain. By contrast, output and employment grew more slowly in complex services, such as finance and transportation and communications, which required large investments in technology and skills.<sup>45</sup>

**Table 5.4: Well Served: The Service Sector in Lithuania and Estonia in 2001 (% of total)**

Type of Service	Gross Value Added		Employment	
	Lithuania	Estonia	Lithuania	Estonia
Wholesale and retail trade	26	22	28	24
Hotels and restaurants	2	2	3	5
Real estate, renting, and business	14	17	7	11
Transport and communications	21	25	10	15
Financial intermediation	4	7	2	2
Other services*	32	27	50	42

\*Health care, education, social services, and public administration.

Source: Own calculations from OECD, *Promoting Trade in Services: The Experience of the Baltic States* (Paris: OECD, 2004), 17.

As discussed above, an important element of Lithuania’s insider-oriented reform strategy was state ownership of “strategic” enterprises, such as power plants and railways. At the time of the EU referendum, about 70% of Lithuania’s electricity was

<sup>45</sup> OECD, *Labor Market and Social Policies*, 35; Cazes and Nesporova, *Labor Markets in Transition*, 8-16, 32-37, 41-43; Jakubauskas, “The Lithuanian Economy,” 127-130; “Leedu 50 suurima käibega ettevõtet aastal 2002” and “Kiire majanduskasv kajastub Leedu ettevõtete tulemustes,” *Äripäev* 24 November 2003; “Lithuanian Banking: Phoenix Rising, Slowly,” *Baltic Times*, 24 May 2000; Steven Paulikas, “Hotel Boom Puts Vilnius on Business Map,” *Baltic Times*, 6 February 2003; “VP Market to Open Household Appliance Chain,” *Baltic Times*, 3 June 2004.



produced at the state-owned Ignalina nuclear power plant (INPP) in southeastern Lithuania. To protect the competitiveness of Lithuanian firms and to prevent social unrest, the Lithuanian government kept the price of electricity low (at about the cost of production). It also forbade the plant to cut off non-paying customers. Some liberal economists argued that INPP should be allowed to operate like a normal, profit-oriented enterprise. However, nobody suggested privatizing the plant because it had a monopoly position in the Lithuanian market. Moreover, only the state had the qualified personnel (Russian-trained nuclear engineers and technicians) to operate the plant.<sup>46</sup>

However, INPP became the most contentious issue in Lithuania's accession negotiations with the EU in 2000-2003. The EU considered the plant unsafe and required Lithuania to close it down as a precondition for membership. Some analysts predicted that this would lead to widespread social protest. For two reasons, however, it did not. First, the Lithuanian public was divided on whether INPP should be kept open or not. On the one hand, INPP produced the bulk of Lithuania's electricity and did so very cheaply. On the other hand, however, it was an RBMK facility—the same type that exploded at Chernobyl in 1986—prone to technical problems.<sup>47</sup> Second, it seemed that Lithuania could afford to close INPP. The EU allowed Lithuania to shut it down gradually, the first reactor in 2004 and the second in 2009. This gave Lithuania time to modernize its existing gas-fueled power plants and to build new ones. The EU also agreed to pay part of the cost of closing INPP, such as storing the nuclear waste and finding new jobs for the plants workers. In this context, EU demands did not seem unreasonable.<sup>48</sup>

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<sup>46</sup> "Energy Restructuring OK'd Despite Ignalina Deadlock," *Baltic Times*, 15 November, 2001; "Ignalina Posts 2001 Loss," *Baltic Times*, 9 May 2002; "Electricity Output, Exports Soaring," *Baltic Times*, 10 April 2003.

<sup>47</sup> Meter J. Mladineo, "A Chasm Widens at Ignalina," *Baltic Times*, 18 March 1999; Edvinas Butkus and Peter J. Mladineo, "Industrialists: Ignalina Must Stay," *Baltic Times*, 9 December 1999; Daniel Silva, "Ignalina Shuts Down Again," *Baltic Times*, 3 December 1998; Daniel Silva, "Shutdowns Rose at Ignalina Last Year," *Baltic Times*, 25 February 1999.

<sup>48</sup> "Fund for Ignalina Closure Launched," *Baltic Times*, 12 April 2001; "EU Agrees on Ignalina Funding," *Baltic Times*, 13 June 2002; "Brazauskas to Talk Ignalina in Brussels," *Baltic Times*, 24 October 2002; "15

Lithuania also inherited from the Soviet Union a well-developed railway system, which handled the bulk of passenger and freight transportation within Lithuania and between Lithuania and other Soviet republics. After the breakup of the Soviet Union, the number of passengers traveling by railway fell as many people bought used Western cars or switched to buses. Hence, passenger rail service started losing money. Freight transportation—especially the transit of Russian raw materials to Europe—should have been quite profitable given Lithuania’s favorable geographical location between Russia, Poland, and Germany. However, as with electricity, the state kept freight tariffs low and used the (small) profits from freight traffic to subsidize passenger transportation. As a result, the railway could not afford to rebuild the track or buy new rolling stock.<sup>49</sup>

To deal with these problems, the conservative government of 1996-2000 considered a) splitting the railway into a track arm and a passenger arm and b) privatizing both of them, preferably to Western investors. However, the Social Democrat-led government of 2001-2004 scrapped these plans. On balance, this was probably the right decision. Combining passenger and cargo services allowed the state to continue to provide passenger transportation in rural areas where roads are bad or non-existent. Low prices helped Lithuania to increase its share in the transit of Russian raw materials to Europe even though Lithuanian ports were not originally designed for this purpose. After Lithuania joined the EU, state ownership made the Lithuanian railway eligible for EU structural funds since the EU only subsidizes railroads where the state is the majority owner. As a result, the Lithuanian railway is in relatively good shape.<sup>50</sup>

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Projects Approved for Ignalina Shutdown,” *Baltic Times*, 15 July 2004; “Ignalina Atomic Plant Shuts Down First Reactor,” *Baltic Times*, 22 December 2004.

<sup>49</sup> Peter L. Mladineo, “Railway to Get Massive Overhaul,” *Baltic Times*, 25 November 1999; Baltic News Service (BNS), “Railways Cutting Passenger Services,” *Baltic Times*, 22 March 2001.

<sup>50</sup> BNS, “Latvian, Lithuanian Rail Freight Volumes Up, Estonian Railways Lags,” *Baltic Times*, 11 December 2003; “Lithuanian Railways to Boost Locomotive Fleet,” *Baltic Times*, 17 June 2004; Talis Saule Archdeacon, “Train Travel: Turning Passenger Rail Service Around,” *Baltic Times*, 30 January 2008.

The one exception to Lithuania's policy of not privatizing basic infrastructure was the Mažeikiu Nafta (MN) oil company. It includes an oil export terminal, an oil pipeline, and, most importantly, the largest oil refinery in the Baltic states in the town of Mažeikiai in western Lithuania. Fitted out with the latest Soviet technology in the 1980s, it was Lithuania's largest enterprise under Communism. It purchased cheap crude oil from Russia and turned it into various oil products—gasoline, diesel, kerosene and jet fuel—which it sold back to Russia at a handsome profit. After the Soviet Union disintegrated, MN fell onto hard times. The price of Russian oil increased, while Russian demand for refined oil products declined. At the same time, Western markets remained closed to MN, whose products did not meet EU environmental standards and whose managers lacked connections in the West. As a result, MN began losing money.<sup>51</sup>

The conservative government of 1996-2000 decided that the only way to solve MN's problems was to find it a Western partner. In 1999, it sold 33% of the stake in MN and the management rights to the Oklahoma-based Williams International. It was not clear why this particular "strategic investor" was chosen because no open bid was held. The sale price was a low \$150 million for a company that produced 6% of Lithuania's GDP. However, Williams promised to replace the Soviet-era equipment with American technology and to reorient MN's exports to Western Europe. These hopes were soon disappointed. In 1999-2002, Williams invested \$58 million in MN, mostly to repair existing facilities. At the same time, it borrowed \$288 million from the state to cover MN's continuing losses caused by irregular oil supplies from Russia, weak sales in Russia and Europe, and the high salaries of American executives.<sup>52</sup>

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<sup>51</sup> Kristina Kalašinskaitė and Manuela Tvaronavičienė, "Case Study of Controversial Privatization: Lithuanian Experience," *Studia Universitatis Babeş-Boylai-Studia Europea* 50, no. 1 (2005), 233-246; Irma Pauskevičiute and Michael Roe, "The Politics of Oil in Lithuania: Strategies After Transition," *Energy Policy* 29 (2001), 383-397; Matej Vipotnik, "The Good, the Bad and the Ugly," *Financial Times*, 25 November 1998; "Lithuania's Oil Problems Get Slippery," *Baltic Times*, 27 May 1999.

<sup>52</sup> Jeffries, *Countries of the Former Soviet Union*, 250-251; Matej Vipotnik, "Lithuania to Sell Stake in Refinery," *Financial Times*, 2 September 1999; Anthony Robinson, "US Investor Picks an Apposite Approach: Adding Value to the Production Chain Will Be Welcomed by Regional Oil Companies, Aware

The privatization of MN led to an anti-Western backlash. After the parliament approved the contract with Williams, thousands of people gathered in front of the parliament to protest against the sell-off of the Lithuanian economy to greedy foreigners. Public support for EU membership dropped below 50%, the lowest ever.<sup>53</sup> However, in 2002, Williams resold its stake in MN to Yukos, its largest supplier of crude oil, which also purchased another 27% of the shares from the state, for a total of \$235 million. Like Williams, Yukos invested little in new technology and made no headway in the European market. It also failed to pay back the loans that MN had received from the state under Williams' stewardship, although the Social Democrat-led government cut the interest rate from the standard 10% to 7%. Finally, it ran into trouble with the Russian government, which threatened to seize its assets in lieu of unpaid taxes. As a result, people's anger over the poor performance of MN turned from the Americans to the Russians and support for Western integration rebounded.<sup>54</sup>

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of the Need to Raise Efficiency," *Financial Times*, 19 May 2000; Anthony Robinson, "Mažeikiu Refinery Supply Agreed," *Financial Times*, 22 May 2000; Tõnis Arover, "Mažeikiu Nafta," *Äripäev*, 2 June 2000; "Yukos Signs Supply Deal with Mažeikiu," *The Baltic Times*, 18 April 2002; "Williams Out, Yukos Taking Over," *Baltic Times*, 22 August, 2002; "Mažeikiu Takes a Breather," *Baltic Times*, 3 April 2003; "Ghost of Mazeikiu Sell-Off Continues to Haunt Politicians," *Baltic Times*, 27 May 2004.

<sup>53</sup> Liudas Mažylis and Ingrida Unikaitė, "Euro-Referenda: Lithuania's Case," in *Central Europe Beyond Double Enlargement*, ed. Algimantas Jankauskas, Ramūnas Vilpišauskas and Inga Vinogradnaitė (Vilnius: Vilnius University Press, 2004), 47-48; Vijai Maheshwari, "Lithuania Signs Sell-Off Deal Despite Protests," *Financial Times*, 30 October 1999; Rokas M. Tracevskis, "Lithuania Remains a Pro-Western Country," *Baltic Times*, 27 January 2000; Vijai Maheshwari, "Secrets of Post-Soviet Bloc PR: Management Cultural Communication," *Financial Times*, 15 February 2000.

<sup>54</sup> Jack Andrews, "Russia Oil Group Gains Refinery in Lithuania," *Financial Times*, 21 August 2002; "Williams Out, Yukos Taking Over," *Baltic Times* 22 August, 2002; "Yukos Increasing Oil Deliveries, Manager Presence at Mažeikai," *Baltic Times*, 31 October 2002; "Mažeikiu Nafta Sees Profits Again," *Baltic Times*, 13 March 2003; "State Gives Investor Huge Break," *Baltic Times*, 10 July 2003; "Mažeikiu Refinery to Stay in Yukos' Control," *Baltic Times* 5 February 2004; "State Adopts Wait-and-See Approach to Yukos," *Baltic Times* 15 July 2004; Stefan Wagstyl and Jan Cienski, "Baltic Lesson for EU in Dealing with a Resurgent Russia: Cooperation with Moscow is Not Easy," *Financial Times*, 24 November 2006.

## **Estonia: Outsider-Oriented Reforms**

Unlike Lithuania, Estonia pursued an outsider-oriented strategy of reforms from the start. The winner in the 1992 parliamentary election was the conservative Fatherland, which promised to “clean the house” and reorient the Estonian economy to the West. The conservatives adopted international tenders as the main method of privatizing large SOEs.<sup>55</sup> The government advertised forthcoming sales of SOEs in domestic and international newspapers (e.g., *Frankfurter Allgemeine Zeitung*, the *Financial Times*, and the *Wall Street Journal*). Interested investors submitted confidential bids to the Estonian Privatization Agency, modeled after the German Treuhandanstalt. After preliminary negotiations with the tenderers, the government selected the best bid. There were almost no advantages for insiders or restrictions for foreigners in the process. No shares were set aside for managers and workers. Domestic buyers had to pay in cash, just like foreign investors, although they were allowed to pay in installments.<sup>56</sup>

In general, the conservative government tried to choose investors that would be a good match for the enterprises being privatized. For example, price was not the only factor in choosing the best bid: prior experience in the industry and willingness to meet investment and employment targets were equally important. This could be seen as industrial policy of sorts. However, the government did not pursue the more traditional industrial policies followed by the Lithuanian government. Thus, it made no attempt to restructure enterprises before selling them off. With the exception of one large textile

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<sup>55</sup> A variety of methods, including auctions for cash, voucher privatization, and management buyouts, were used to privatize small enterprises. Vouchers could also be used to buy land and apartments and minority shares in large SOEs.

<sup>56</sup> OECD, *The Baltic States*, 30-32, 122-132; Mart Laar, *Estonia: The Little Country That Could* (Suffolk: St. Edmundsbury Press, 2002), 253-271; Erik Terk, *Privatisation in Estonia: Ideas, Processes, Results* (Tallinn: Estonian Institute for Future Studies, 2000), 7-18, 120-138, 143-156; David J. Smith, *Estonia: Independence and European Integration* (London and New York: Routledge, 2001), 126-133; Clemens Buchen, “Estonia and Slovenia as Antipodes,” in *Varieties of Capitalism in Post-Communist Countries*, ed. David Lane and Martin Myant (Basingstoke and London: Palgrave Macmillan, 2007), 65-89; Aslund, *Building Capitalism*, 270-272; Jeffries, *Countries of the Former Soviet Union*, 166-175.

plant in the Russian-dominated northeast, it abolished all industrial subsidies, including tax rebates. Finally, it passed a strict bankruptcy law that made it easy for the state and the banks to take delinquent firms to court and to seize their assets.<sup>57</sup>

The conservative government also welcomed foreign “greenfield” investors. Estonian law allowed foreign investors to do everything local firms could do. For example, foreigners could buy non-agricultural land and invest in all sectors of the economy. The government also concluded investment protection treaties with the EU, the Nordic countries, and the US. Under these treaties, foreign companies could repatriate profits and pay the same (low) taxes as domestic firms. Disputes between the Estonian state and foreign firms were to be settled by international arbitration courts. Finally, the government advertised Estonia as pro-business country. It summarized its economic philosophy as “Give us trade, not aid.” With funding from the World Bank, it paid *Newsweek* to publish a special supplement on “The Little Country That Could.” As Table 5.1 illustrates, these efforts paid off: in 1989-2003, Estonia attracted about twice as much FDI per capita as Lithuania.<sup>58</sup>

Finally, Estonia followed a more liberal and Western-oriented trade policy than Lithuania. In 1993, it abolished all import tariffs and quotas, a policy that it reaffirmed in its 1994 trade agreement and 1995 association agreement with the EU. The EU agreed to free trade in principle, but imposed tariffs on Estonian agricultural products, which remained in place until 2004. Until 1998, the EU also maintained quotas on Estonian goods in “sensitive” industrial sectors, such as textiles and chemicals. Despite EU

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<sup>57</sup> OECD, *The Baltic States*, 30-32, 122-132; Laar, *Estonia*, 179-197; Terk, *Privatisation in Estonia*, 7-18, 120-138.

<sup>58</sup> Aslund, *Building Capitalism*, 434-437; Laar, *Estonia*, 244-250; Zenons Norkus, “Why Did Estonia Perform Best? The North-South Gap in the Post-Socialist Economic Transition of the Baltic States,” *Journal of Baltic Studies*, 33, no. 1 (2007: 36-37); Jeffries, *Countries of the Former Soviet Union*, 175; Matej Vipotnik, “Baltic Countries,” *Financial Times*, 8 May 1998; Aivar Hundimägi, “Hiinlased tahtsid RETi tehases toota telereid,” Eda-Liis Kann, “Välisfirmad kompenseerivad majanduslangust” and Kristjan Tamla, “Majandus 1993 – esimene täisaasta oma rahaga,” all in *Äripäev*, 29 January 2003.

protectionism, however, Estonia rapidly reoriented its trade from Russia to the West. This was partly a matter of necessity: in 1994, Russia imposed punitive tariffs (double the most-favored-nation rate) on Estonian goods. However, Western owners of Estonian firms also preferred to sell their goods in the more stable and (for them) familiar European markets. These developments are reflected in Table 5.1: in 2003, Estonia traded more actively with Western countries than Lithuania.<sup>59</sup>

In the 1995 general election, Estonians voted the conservatives out of office in favor of two centrist parties representing the interests of former mid-level nomenklatura: the urban Coalition Party (CP) and the Country People's Party (CPP). The new government tweaked with Estonia's outsider-oriented policies. Thus, domestic investors could use vouchers to buy up to 50% of stake in SOEs. Farmers received modest export subsidies. However, there was no fundamental change in economic strategy. Sales for cash to foreign capitalists remained the preferred method of privatizing large SOEs. For example, Estonian Telecom was sold to the Finnish and Swedish consortium TeliaSonera, Estonian Shipping to a Norwegian and American consortium called ESCO Holdings, and Estonian Air to Scandinavian Airlines. Estonia's trade policy also remained the most liberal in Europe: the urban CP vetoed the rural CPU's proposal to re-introduce import tariffs.<sup>60</sup>

The 1999 general election produced contradictory results. On the one hand, it marked the electoral breakthrough—from about 10% in the previous elections to about

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<sup>59</sup> OECD, *The Baltic States*, 40-48, 191-92; OECD, *Labor Market and Social Policies*, 32-34; Laar, *Estonia*, 236-41; Magnus Feldmann and Rzeen Sally, "From the Soviet Union to the European Union: Estonian Trade Policy, 1991-2000," *World Economy*, 25, no. 1 (January 2002): 83-87; Janno Reiljan and Kristina Toming, "Key Socio-Economic Problems of the European Union's Eastern Enlargement Seen from an Estonian Perspective," in *Driven to Change: The European Union's Enlargement Viewed from the East*, ed. Antoaneta L. Dimitrova (Manchester and New York: Manchester University Press, 2004), 78-84, 88-93; Smith, *Estonia*, 121-122; Aslund, *Building Capitalism*, 171-182.

<sup>60</sup> Laar, *Estonia*, 319-341; Terk, *Privatization in Estonia*, 155-162; Smith, 93-101; Jeffries, *Countries of the Former Soviet Union*, 137-140, 170-171; Väinu Rozental, "Erastamise lõpp jättis mõru maigu," *Äripäev* 4 August 2003; "Valitsus kinkis Telekomis ära," *Äripäev* 29 January 2008; and Martin Hanson, "Merelaevanduse erastamisega sai riik 200 miljoniga mööda pükse," *Äripäev* 22 June 2006.

25% in this and the following elections—of the left-populist Center Party, which promised to keep “strategic enterprises” under state control and to protect domestic producers from unfair foreign competition. However, the three parties that formed the new government—the conservative Fatherland Alliance, the liberal Reform Party, and the nominally social-democratic Moderates—blamed the CP/CPP for stalling economic reforms. In 2000-2002, the new government privatized—or attempted to privatize—Estonia’s basic infrastructure. It broke the national railway into an infrastructure arm and a passenger carrier and sold them to American and British investors. It also signed a preliminary contract for the sale of the power plants to the US firm NRG Energy.<sup>61</sup>

What results? As Table 5.2 shows, Estonia’s per capita GDP increased from \$10,194 to \$13,906 in 1990-2003, while unemployment increased from 1% to 10%. The biggest beneficiary of Estonia’s outsider-oriented strategy was the service sector: the share of services in the GDP increased from 34-42% in 1990-91 to 68% in 2003, while the proportion of workers employed in services grew from 42% to 61%.<sup>62</sup> Services grew faster than other sectors because they the bulk of the FDI in Estonia. At the time of the EU referendum, Swedes and Finns owned the Tallinn stock exchange and most Estonian banks, phone companies, department stores, and supermarkets. Americans, Dutch, Germans, Norwegians and Danes owned the railway infrastructure, the oil transit firms, the (natural) gas distribution network, the shipping company, the national airline, and the largest private security firm. Finally, foreign tourists made up the bulk of the clientele of Estonian hotels and spas, many of which were also owned by Western companies.<sup>63</sup>

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<sup>61</sup> Laar, *Estonia*, 353-360; Edgar Savisaar, *Usun Eestisse* (Tallinn: TEA, 1999), 134-142, 164-193; Smith, *Estonia*, 105-106; Jeffries, *Countries of the Former Soviet Union*, 142-159, 171-74.

<sup>62</sup> As with Lithuania, it is likely that the changes in the composition of the GDP in 1990-91 reflected changes in relative prices.

<sup>63</sup> OECD, *Labor Market and Social Policies*, 35; Smith, *Estonia*, 122-123; Nordregio, *Regions of the Baltic States*, 68-73, 102-105, 110-113; “Välisraha teab teed Eestisse,” *Äripäev*, 3 October 2002; Inno Tähismaa, “Välisinvesteeringud: hea aeg on alles ees” and “Eesti välisinvesteeringuid juhivad pangandus ja Rootsi,” *Äripäev*, 27 November 2002; Kairi Kurm, “Estonia Offering Competitive Edge,” *Baltic Times*, 16 January 2003; “Välisraha Eestis 133 miljardi eest,” *Äripäev*, 26 June 2003.



As Table 5.2 indicates, Estonian industry did not do as well as services: in 1990-2003, industrial output declined from 40-50% to 29% of the GDP while industrial employment fell from 37% to 32% of the workforce. Relative to industry as a whole, output and employment increased in wood-processing and electrical and optical equipment (see Table 5.3). These industries used local energy and/or raw materials, received a lot of FDI, and could export their products to the EU duty-free. Textiles and clothing occupy a middle position: they used imported cotton but local electricity and were subject to EU quotas but not tariffs. This allowed them to attract some FDI. Finally, production and employment fell in food processing, chemicals, and machinery and equipment. These industries depended heavily on imported Russian energy and raw materials (chemicals and machine-building), were subject to high EU tariffs (food processing), and received little FDI (all of the above).<sup>64</sup>

If the performance of Estonian industry was uneven, Estonian agriculture largely collapsed during the transition to capitalism. As Table 5.2 makes clear, agricultural output declined from 17-18% of the GDP in 1990-91 to 4% in 2003, while agricultural employment fell from 19-21% of the workforce to 6%. This was partly due to “objective” factors. The price of agricultural inputs (oil, machinery, and fertilizers) increased much faster than the price of agricultural products. Russia, traditionally the most important market for Estonian foodstuffs, imposed punitive tariffs on Estonian exports. However, Estonia’s free trade policy also contributed to the decline of Estonian agriculture. On the one hand, Estonian farmers and food processors faced tough

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<sup>64</sup> OECD, *The Baltic States*, 252; OECD, *Labor Market and Social Policies*, 2003, 36; Marek Tiits, Rainer Kattel and Tarmo Kalvet, *Made in Estonia* (Tartu: Institute of Baltic Studies, 2005), chap. 3 and 74-85; Garri Raagmaa, Mihkel Laan and Antti Raamat, “Transformation of Estonia’s Industrial Structure: Continued De-Industrialisation or Interlude in Re-Industrialisation,” *Baltic Review* 22 (2003): 8-12; Per Högselius, *The Dynamics of Innovation in Eastern Europe: Lessons from Estonia* (Cheltenham, UK: and Northampton, MA: Edward Elgar, 2005), 96-102, 152-162; Vaikko Maripuu, “Kas rünnakrühm eksporditööstus on väsinud?” *Äripäev*, 27 November 2002; Merike Riipinen, “Elektri- ja optikaseadmete tootmine veab tööstust kiiremale arengule,” *Äripäev*, 15 August 2005; Siim Sultson, “Tekstiilitööstus kui Eesti tööstuse teerajaja,” *Äripäev*, 15 November 2006; Madli Kents, “Tööstuse parimad päevad lahkusid koos NSVLiga,” *Äripäev*, 31 August 2005; Sten Grundig, “Volta läbi saja aasta,” *Äripäev*, 31 August 2005.

competition from EU-subsidized European agribusinesses at home because Estonia had no agricultural (or any other) tariffs. On the other hand, Estonian producers found it hard to enter European markets because the EU imposed high tariffs and non-tariff barriers (e.g., quality and sanitary requirements) on Estonian agricultural goods.<sup>65</sup>

*The biggest failure of Estonia's outsider-oriented reform policies, however, was the (attempted) sale of infrastructure monopolies—railways and power plants—to Western investors in 2000-2002.*<sup>66</sup> The Estonian railway faced the same problems as its Lithuanian counterpart: unprofitable passenger service and lack of money to invest in the track and the rolling stock. In 2000, the government split the railway into a) a track and freight arm (Eesti Raudtee) and b) a passenger arm (Edelaraudtee). It sold Edelaraudtee to the British firm GB Railways, the only serious bidder in an open tender, for a modest \$600,000. For reasons that remain unclear, however, the Brits soon resold the company to two Estonian businessmen. The new owners doubled Edelaraudtee's share capital from \$6 million to \$12 million. However, they discontinued much of Estonia's passenger rail traffic as unprofitable and laid off half of the company's 800 workers.<sup>67</sup>

*The cuts in passenger rail traffic led to the first significant social protest among ethnic Estonians since the breakup of the Soviet Union.* In Tartu, the largest city in the

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<sup>65</sup> Alanen, "Annex Tables and Figures," 273, 275, 277; Janno Reiljan and Dorel Tamm, *An Analysis of an Industry's Competitiveness: The Case of the Estonian Agricultural Sector* (Tartu: Tartu University Press, 2005), chap. 3; Reiljan and Toming, "Key Socio-Economic Problems," 78-84, 88-93; Smith, *Estonia*, 136-140; Nordregio, *Regions of the Baltic States*, 82-89, 98-101, 106-109, 126-129. The rapid breakup of the collective farms also contributed to the decline of Estonian agriculture. See Ilkka Alanen, "The Transformation of the Agricultural Systems in the Baltic Countries – A Critique of the World Bank Concept," in Alanen, *Mapping the Rural Problem*, 19-44.

<sup>66</sup> For how private monopolies reduce social welfare, see Joseph E. Stiglitz, *Economics of the Public Sector*, 2<sup>nd</sup> ed. (New York and London: Norton, 1988), 71-74. For the privatization of infrastructure in Estonia, see Terk, *Privatisation in Estonia*, 173-184 and Heido Vitsur, "Privatisation of Enterprises of Infrastructure: Why Did It Misfire?," *Baltic Review*, 21 (2002), 14-17.

<sup>67</sup> Hindrek Riikoja, "Edelaraudtee müüdi GB Railwaysile," *Postimees*, 30 November 2000; "Depoo töötajad said koondamistate," *Postimees*, 16 February, 2001; Hindrek Riikoja, "Edelaraudtee pärisperemehed on Vichmann ja Ruubel," *Postimees*, 2 August 2001; Devyani Banerjee, "Rail Deal Unveils Shady Investors," *Baltic Times*, 9 August 2001; Marko Liibak, "Raudtee ja ametiühingud ei jõudnud koondatavate arvus kokkuleppele," *Postimees*, 23 December 2002.

rural southeast, the area most affected by the loss of train transportation, 4,000 people signed an open letter to the parliament and the president demanding the resignation of the government. In the small towns and villages of the southeast, hundreds of people lined the railway track with burning candles on the night when the last train made its way from Tartu to Orava on the Russian border. In the following weeks, smaller crowds gathered front of local government offices and abandoned train stations to demand the resumption of rail traffic. Popular protest had some impact: the government provided subsidies to the worst-hit municipalities to start bus service. However, people generally found buses to be inferior to trains because they were more expensive, operated at inconvenient times, and did not run when the roads were muddy or icy.<sup>68</sup>

The privatization of Eesti Raudtee turned out to be even more complicated. Unlike the rolling stock, the track is a natural monopoly: there is only one track. The track was also quite valuable economically because Russian oil companies used it to transport crude oil and bitumen to Europe. As a result, the government decided to hire a Western consulting firm to advise it during the privatization process. The European Bank for Reconstruction and Development (EBRD), the East European “window” of the World Bank, offered to pay half of the consulting fee. An international tender was held. The best bid was made by PricewaterhouseCoopers, one of the “big six” accounting firms, which offered to do the job for \$800,000. Upon the insistence of the EBRD, however, the government awarded the contract to GIBB, a small British firm with no experience in infrastructure privatization, which charged \$2.4 million for its services.<sup>69</sup>

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<sup>68</sup> Martin Pau, “Teadmatusse kaduva rongi tragöödia,” *Postimees*, 11 January 2001; Villu Päärt, “Küünlad ääristasid rongi viimset teekonda,” *Postimees*, 5 March 2001; Asta Niinemets, “Tartlased protesteerisid raudtee erastamise vastu,” *Postimees*, 28 April 2001; Asta Niinemets, “Vältimatu bussisõit sunnib paastuma,” *Postimees*, 21 March 2001; Vallo Nuust, “Vallajuhid nõuavad vanade rongipeatuste taastamist,” *Postimees*, 31 August 2001.

<sup>69</sup> Kalle Muuli, “Pärnoja laseb kaitsepolitseil oma tegevust uurida,” *Postimees*, 21 March 2001; Aleksei Gunter, “Minister Charged with Shady Privatization,” *Baltic Times*, 29 March 2001; Tiina Joosu and Mihkel Kärmas, “Miks te nii tegite, Väino Sarnet?,” *Eesti Ekspress*, 12 April 2001; “Osa majandusminister Mihkel Pärnoja pikast paturegistrist,” *Postimees*, 29 September 2001; Aivar Reinap, “Kiirustamine raudteemüügil röövis riigilt sadu miljoneid,” *Postimees*, 14 February 2003.

Things went from bad to worse with the privatization of Eesti Raudtee itself. Again, an open tender was held. Bids were submitted by Raudtee Erastamise Rahva Aktsiaselts (RER), a group of Estonian transit traders, the Baltic Rail Service (BRS), a consortium that included the Chicago-based firm Rail World and the British company Jarvis International, and Rail Estonia (RE), a consortium led by two Americans, Antonio Angotti and John Orrison. Based on GIBB's advice, the government sold 66% of the stake in Eesti Raudtee to RE, which offered to pay more than any other bidder: \$100 million. Orrison said that the money would come from a loan from Chase Manhattan and Deutsche Bank. When RE failed to pay the required \$10 million deposit, however, it emerged that Orrison had never contacted the two banks. Angotti turned out to be a common criminal: he had had been sentenced to 42 months in prison for fraud and money laundering and was wanted by the FBI for jumping bail. Shortly, both men left Estonia.<sup>70</sup>

With the would-be investors fleeing the country, the government re-sold Eesti Raudtee to BRS, the other foreign bidder, for \$60 million. In many ways, BRS was an improvement over RE. It was owned by two really-existing railway firms with some experience in operating private railways in the US, UK and New Zealand. In 2001-2005, it invested about \$200 million of its own money in the railway. In other ways, however, BRS behaved more like a rent-seeker than a "strategic" investor. It spent most of the \$200 million on purchasing used locomotives from Rail World (i.e., from itself), which turned out to be too heavy for the Soviet-made track. At the same time, it invested very little in the railway track. As a result, the condition of the track deteriorated to the point

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<sup>70</sup> Erkki Erilaid, "Erastamisnõustaja Gibb (sic) soovitab raudtee erastada Rail Estoniale," *Postimees*, 12 December 2000; Paavo Kangur, "Jürgensoni kohmakas tants köiel," *Eesti Ekspress*, 25 January 2001; "Massei-Angotti pettis välja pool miljonit dollarit," *Eesti Päevaleht*, 22 February 2001; "Businessman Connected with Rail Estonia Wanted in the U.S.," *Baltic Times*, 1 March 2001; Kalle Muuli, "Raudtee erastamist varjutab musta raha kahtlus," *Postimees*, 12 April 2001; Paavo Kangur, "Sajandi spekulatsioon," *Eesti Ekspress*, 3 May 2001; Erkki Erilaid, "Eesti Raudtee iga hinna eest erastamine muutus farsiks," *Postimees*, 31 December 2001; Peeter Ernits, "Angotti noolis raudteed siinsete prominentide toel," *Postimees*, 9 October 2002; Peeter Ernits, "Kosjasõit Eesti moodi ehk kuidas raudteele osav kosjamoor leiti ja ta selle abil mehele pandi," *Postimees*, 10 March 2003;

where, in some places, it was unsafe for trains to move faster than 25 km/h. It also laid off 2,500 of Eesti Raudtee's 4,000 workers, most of whom could not find new jobs. In 2006, the government, which now included the left-populist Center Party, bought back the railway from BRS for \$188 million, three times the original sale price.<sup>71</sup>

The government also attempted to privatize the Narva power plants, the largest infrastructure enterprise in Estonia. The plants produce about 90% of Estonia's electricity using local oil-shale. They also employ about 2,000 people and, indirectly, provide jobs for about 4,000 oil-shale miners and transportation workers. However, they are nearing the end of their useful life: without capital repairs, they will stop working by 2016. They are also Estonia's largest producer of carbon dioxide and other "greenhouse gases." In 1996, CP-led government decided to privatize the plants and started negotiations with a would-be "strategic investor," the Minnesota-based NRG Energy. The talks languished for a while because the CP's coalition partner, the rural CPP, opposed the privatization of infrastructure. In 2000, however, the new conservative-led government signed a preliminary contract with NRG. In doing so, it was advised by the British investment bank Schroders, which received \$3 million for its services.<sup>72</sup>

As with the privatization of the railway, the contract was never made public: only members of the parliament were allowed to see it. Based on information leaked to the

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<sup>71</sup> Erkki Erilaid, "USA vedurid peavad kiirust vähendama," *Postimees*, 5 August 2003; Hindrek Riikoja, "Raudteeamet nõuab investeerimist ohutusse," *Postimees*, 8 August 2003; Peeter Raidla, "Raudtee investeeringud jäävad lubatule alla," *Äripäev*, 18 August 2004; "Estonians Protest Against Railway Disturbances," *Baltic Times*, 27 October 2004; Priit Rajalo, "Raudteefirma omanik saab riigilt trahvinõude," *Postimees*, 28 December 2005; "Estonian Government Threatens to Terminate Railway Privatization," *Baltic Times*, 26 April 2006; Sulev Vedler, "Miks tahab Savisaar raudteed osta," *Eesti Ekspress*, 29 November 2006; Andrus Karnau, "Raudteeostu otsus sündis tuliste kirgedes mõllus," *Postimees* 7 December 2006; Hindrek Riikoja, "Raudteeost avab uued rahakraanid," *Postimees*, 5 January 2007.

<sup>72</sup> Terk, *Privatisation in Estonia*, 173-184; Vitsur, "Privatisation of Enterprises of Infrastructure," 14-17; Urmas Maranik, "NRG Hopes Three's a Charm: U.S. Electricity Firm Hopes for Share of Narva Plant," *Baltic Times*, 30 July 1998; "Eesti Energia Leaders Sign NRG Deal," *Baltic Times*, 31 August 2000; Aivar Reinap, "2000: suurerastamiste ja töusu aasta," *Postimees*, 29 December 2000; "NRG Advice to Cost Eesti Energia 65 Million Kroons," *Baltic Times*, 13 June 2002, and Argo Ideon, "Elektrijaamade luhtunud erastamine neelas 73 miljonit," *Postimees*, 31 January 2003.

media, however, the government sold 49% of the shares in the power plants, combined with full management rights, to NRG for \$71 million. Indirectly, the contract also gave NRG control over Estonian oil-shale mines since the power-plants own 51% of the shares in the mines. The contract required the government to buy 75% of NRG's output until 2005 and 50% until 2015. The price of electricity sold by the power plants to the state was to increase from 2.6 to up to 3.8 cents per kWh beginning in 2000, a higher rate than in Finland and Sweden. At the same time, the price of oil-shale sold by the oil-shale mines to the power plants was fixed at the current rate of \$10 per ton until 2010. For its part, NRG promised to modernize the plants, reduce carbon dioxide emissions, and to protect jobs, but made no specific commitments.<sup>73</sup>

The sale was unpopular with the public from the beginning because it would have increased the price of electricity and given a foreign company control of Estonia's power supply. The government and NRG defended the deal as a necessary step towards Estonia's membership in NATO and the EU. In 2001, however, the media reported that NRG did not plan to invest any of its own money in the plants, but wanted to use Estonian oil shale mines as collateral to borrow money from a consortium of banks led by France's Société Générale. This enraged voters who were already unhappy about how the privatization of the railway was turning out. *163,000 people—out of Estonia's total population of 1.4 million—signed a petition against the privatization of the power plants (and, somewhat belatedly, the railway).* Under popular pressure, the government canceled the sale in 2002. NRG responded by suing Estonia for breach of contract in a British arbitration court, where the case is still dragging out.<sup>74</sup>

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<sup>73</sup> Brooke Donald, "Meri Meets NRG in Minnesota to Discuss Environment," *Baltic Times*, 13 April 2000; Kairi Kurm, "American NRG Gets Clear Shot at Power Investments," *Baltic Times*, 6 July 2000. Academics of the Estonian Academy of Sciences, "Avalik kiri Eesti elektrist," *Postimees*, 14 June 2001; Aivar Reinap and Toomas Sildam, "Valitsus müüb jõujaamad rahva survest hoolimata," *Postimees*, 28 June 2001; Annely Ammas, "Valitsus viib NRG tehingu igal juhul lõpuni," *Eesti Päevaleht*, 22 August 2001; Aivar Reinap, "Narva Elektriijaamade erastamine luhtumas," *Postimees*, 20 December 2001.

<sup>74</sup> BNS, "Valitsus ei peata Narva Elektriijaamade müüki," *Postimees*, 21 August 2001; "Mart Laari poliitiline avaldus NRG istungil," *Eesti Päevaleht*, 23 August 2001; BNS, "NRG president hirmutas

## Conclusion

This chapter set out to develop an economic explanation for why Lithuanians were more supportive of EU membership than Estonians. The small existing literature on economic causes of cross-national differences in EU support in Eastern Europe has focused on macro-economic indicators like growth and unemployment. Some scholars have argued that support for the EU is stronger in countries that are doing well economically. They argue that the transition to capitalism in Eastern Europe (e.g., privatization and liberalization) has involved close economic integration with the Western Europe (e.g., through foreign investment and trade). As a result, people credit (or blame) the EU for their country's good (or bad) economic performance. Other scholars, however, argue that EU support is stronger in countries that are experiencing economic difficulties. Joining the EU, they argue, means giving up part of a nation's economic sovereignty. People are willing to do that if their country needs EU help but not if it is doing fine on its own.

However, Lithuania and Estonia pose a problem for these macro-economic explanations. Since the break-up of the Soviet Union, both countries have experienced slow growth and a large increase in unemployment, yet most Lithuanians supported EU membership, while many Estonians did not. To explain this puzzle, I decided to explore micro-economic changes in the two countries. I found that Lithuania and Estonia pursued different strategies of economic reform. Lithuania followed an insider-oriented strategy. It maintained state ownership of infrastructure (e.g., railways) and sold other SOEs to their Soviet-era managers. It imposed moderate tariffs on imports and continued to trade heavily with Russia. By contrast, Estonia adopted an outsider-oriented strategy.

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Euroliidust väljajäämisega," *Eesti Päevaleht*, 18 December 2001; Vallo Toomet and Jaanus Piirsalu, "Eesti Energia keeldus välispankade nõudmistest," *Eesti Päevaleht*, 16 November 2001; Andres Reimer, "Elektrijaamade erastamine kukkus läbi," *Äripäev*, 20 December 2002; Aivar Reinap, "Eesti loobub Narva Elektrijaamade erastamise tehingust NRGle," *Postimees*, 8 January 2002; Aleksei Gunter, "NRG Files Lawsuit Over Sell-Off," *Baltic Times*, 20 August 2002; "NRG Energy nõuab Eesti Energialt 2,4 miljardit krooni," *Eesti Päevaleht*, 23 August 2002.

It sold large SOEs, including infrastructure enterprises, to foreign investors. It abolished all import tariffs and rapidly reoriented its trade from Russia to the West. This explains why Lithuanians saw EU accession as an alternative to current economic policies, while Estonians considered it a continuation of such policies.

Neither approach worked too well, however. The Lithuania strategy helped to protect output and employment in agriculture and “old” industries (e.g., food processing, and oil refining) which had been fitted out with the latest Soviet technology and which benefited from continued access to the undemanding Russian market. However, it slowed down the development of services and “new” industry (e.g., electronics), where the quality gap with the West was too large for Russian consumers. The Estonian strategy led to a rapid development of services and “new” industry, which received the bulk of FDI in Estonia and could export their products to the West duty-free. At the same time, it hurt Estonian agriculture and “old” industry, which received little foreign investment and were subject to high tariffs in both Western and Russian markets. Neither strategy was able to prevent the decline of infrastructure (e.g., railways), although the Lithuanian approach slowed it down, while the Estonian policy sped it up. As a result, both Lithuanians and Estonians were unhappy about their country’s economic situation.



## CHAPTER 6

### CONCLUSION: FIRST CAUSES, SECOND CASES

#### Introduction

This dissertation has argued that Lithuanians and Estonians differed in their attitudes toward European integration because their governments pursued different strategies of economic reform. Lithuania sold state-owned enterprises (SOEs) to their managers, imposed moderate tariffs on imports, and continued to trade heavily with Russia (an insider-oriented strategy). Estonia sold SOEs to foreign investors, abolished all import tariffs, and reoriented its trade rapidly from Russia to the West (an outsider-oriented strategy). The Lithuanian strategy slowed down the development of services and “new” industry (e.g., electronics). The Estonian strategy led to the decline of agriculture and old industry (e.g., food processing). As a result, most Lithuanians hoped that joining the EU would help their country overcome its economic backwardness and isolation. By contrast, many Estonians thought that the accession would further impoverish their country and increase its economic dependency on the West.

This argument raises two questions. First, why did the two countries adopt different strategies of reform in the first place? *In this chapter, I will argue that the proximate cause of the choice of strategies was party politics (or, rather, party finance).* In Lithuania, the post-Communist Democratic Labor Party won the first independence-era parliamentary election. The post-Communists had close personal ties with, and received financial support from, Soviet-era managers, who wanted to become owners of their enterprises and to protect their firms from Western competition. In Estonia, the conservative Fatherland emerged victorious. The main financial support for Fatherland came from three sources: the German Christian Democratic Party, Estonian émigrés in Western Europe and North America, and state-owned enterprises engaged in export-

import trade. These groups stood to benefit from outsider-oriented policies, such as the sale of SOEs to foreign investors, the liberalization of trade with the West, and the replacement of Soviet-era officials with émigrés in the government bureaucracy.

However, I will also argue that, *for historical, cultural, and, above all, economic reasons, Lithuania and Estonia would have probably adopted different economic policies regardless of which party was in power.* For centuries, Lithuania’s best friend—and worst enemy—had been Poland, another poor East European country. By contrast, Estonia had close cultural and historical ties with Finland, Sweden and Germany, rich West European countries. Moreover, Lithuania’s economy was dominated by agriculture and heavy industry (e.g., metal-working). These sectors required large investments, depended on Soviet inputs, and were subject to EU tariffs. As a result, Lithuania was unlikely to receive much foreign investment or to be able to sell its goods in Europe. By contrast, Estonia had a large service sector (e.g., tourism) and light industry (e.g., wood processing). These sectors required small investments, used local resources, and could export their goods (services) to the EU duty-free. This made it easier for Estonia to attract foreign investment and to reorient its trade from Russia to the West.

*I will also tackle the question of whether my argument about the link between strategies of economic reform and EU support “travels” to other EU candidate countries. Using the case(s) of the former Czechoslovakia, I will argue that it does.*<sup>75</sup>

Like Lithuania, Slovakia followed an insider-oriented strategy of reform. It sold SOEs to enterprise managers, imposed high tariffs on imports, and continued to trade heavily with Russia and Eastern Europe. This strategy hindered development of new industry (e.g., motor vehicles), which lacked capital and access to rich-country markets. As a result, most Slovaks supported EU accession as a way of modernizing their country’s economy. By contrast, the Czech republic pursued an outsider-oriented strategy similar to Estonia’s.

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<sup>75</sup> Compared to Lithuania and Estonia, Slovakia and the Czech Republic are “most different systems” since they are richer and geographically and culturally closer to the Germanic and Gallic core of the EU.

It sold large SOEs to foreign (mostly German) investors, abolished tariffs on most EU imports, and reoriented its trade from Russia to the West. These policies hurt “old” industry (e.g., steel and mining) and agriculture, which received little FDI and which were subject to EU tariffs and quotas. Hence, many Czechs opposed European integration as a threat to their traditional economy.

I will proceed as follows. The next section will explain why Lithuania and Estonia pursued different strategies of reform. The following section will show that my argument “travels” to the Slovak and Czech republics. The conclusion will summarize the main findings of my dissertation.

## **I Explaining the Explanation**

### **Lithuania: Heavy Metal**

As Fish (1998) and Bunce (1999) have argued, the first post-Communist elections strongly influenced the subsequent economic and political development of East European countries. In Lithuania, the ex-Communist Democratic Labor Party won a landslide victory in the 1992 parliamentary election.<sup>76</sup> Labor’s economic program called for a gradual transition to capitalism that would maintain production and incomes, give Lithuanians control of the country’s economic assets, and ensure social justice. Strategic enterprises (power plants, railways, the Mažeikiu Nafta oil refinery) were to remain state property. Non-infrastructure SOEs were to be privatized through vouchers issued to all Lithuanian citizens based on age.<sup>77</sup> Enterprise employees were to be allowed to buy at least 50% of the shares in their own firm. Large industrial enterprises should receive

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<sup>76</sup> Besides the post-Communist Labor party, Lithuania also had a small Social Democratic party, which saw itself as a successor to the pre-war socialists. The two parties merged in 2001. The new Social Democratic Party is, nonetheless, dominated by ex-Communist politicians and businessmen.

<sup>77</sup> On this point, the Lithuanian conservatives agreed with the post-Communists. However, they argued that no preference should be given to employees since this would allow Soviet-era managers to become owners.

subsidies from the state, as should farmers. Lithuania's trade policy should protect their interests of Lithuanian producers. Lithuania should impose moderate tariffs on imports, especially of agricultural goods, and continue to trade actively with Russia and other ex-Soviet countries, where its products enjoyed a good reputation.<sup>78</sup>

These policies reflected the economic interests of Soviet-era enterprise managers, who had close personal ties with the Social Democratic party and financed its election campaign. Above all, managers wanted to become owners of their enterprises. Voucher privatization—with preferences for enterprise employees—suited this purpose quite well. Workers would have to set up investment funds to pool their vouchers. Managers would be the obvious candidates to lead these funds. Moreover, the vouchers would be tradable. This would allow managers to buy up vouchers from impoverished workers. Managers also wanted to protect their enterprises against Western competition since Lithuanian firms were generally less efficient than their Western counterparts. (Agriculture and food processing were exceptions to this rule. However, the EU subsidized its inefficient farmers and agriprocessors, which nullified whatever comparative advantage Lithuania may have had). Finally, managers wanted to continue to trade with Russia, which was the biggest market for their products and the main source of Lithuania's energy and raw materials.<sup>79</sup>

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<sup>78</sup> See, especially, Anatol Lieven, *The Baltic Revolution: Estonia, Latvia, Lithuania and the Path to Independence* (New Haven and London: Yale University Press, 1993), chap. 8-9; Niels Mygind, "A Comparative Analysis of the Economic Transition in the Baltic Countries – Barriers, Strategies, Perspectives," in *The Transition to a Market Economy: Transformation and Reform in the Baltic States*, Tarmo Haavisto, ed. (Cheltenham, UK and Brookfield, VT: Edward Elgar, 1997), 17-66; and Terry D. Clark and Robin M. Tucker, "Lithuania Beyond the Return of the Left," in Charles Bukowski and Barnabas Racz, *The Return of the Left in Post-Communist States: Current Trends and Future Prospects* (Cheltenham, UK and Northampton, MA: Edward Elgar, 1999), 35-58. See also Thomas Lane, *Lithuania: Stepping Westward* (London and New York: Routledge, 2001), Chs. 4-5; Diana Janusauskienė, "The Metamorphosis of the Communist Party of Lithuania," in *The Communist Successor Parties of Central and Eastern Europe*, ed. András Bozóki and John T. Ishiyama (Armonk and London: M.E. Sharpe, 2002), 224-239; and Terry D. Clark and Jovita Pranevičiūtė, "Perspectives on Communist Successor Parties: The Case of Lithuania," *Communist and Post-Communist Studies* 41 (2008): 443-464.

<sup>79</sup> Valdas Samonis, "Economic Reforms in the Baltics: The Case of Lithuania," in *Privatization in Central and Eastern Europe: Perspectives and Approaches*, ed. Demetrius S. Iatridis and June Gary Hopps, (Westport, CT and London: Praeger, 1998), 73-84; Eugenijus Maldeikis and Gediminas Rainys, "Estonia,

*However, this raises the question of whether Lithuania would have pursued different, more outsider-oriented policies if the conservative Homeland Union had won the founding election? The answer is, probably not—at least not to the same extent as Estonia. For one thing, Lithuania lacked an obvious patron in Western Europe.* Historically, Lithuania's paths had crossed with Germany. In the Middle Ages, the Teutonic Order made several attempts to conquer Lithuania under the pretext of christening the heathen. However, unlike the stateless Estonia, the Lithuanian grand duchy successfully resisted the invaders.<sup>80</sup> In the nineteenth century, Germany encouraged Lithuanian nationalism to weaken the Russian empire. For example, it allowed Lithuanians to smuggle nationalist literature from East Prussia to Lithuania. When Lithuania declared itself an independent state during World War I, it first elected a German prince as its grand duke, although this agreement eventually came unstuck.<sup>81</sup>

In the 1920s, however, Lithuania's relations with Germany deteriorated. Taking advantage of German weakness, Lithuania occupied the Klaipėda (Memel) territory in East Prussia, which had been part of the Lithuanian state in the Middle Ages. Germany retaliated by banning the import of Lithuania goods. In 1938, Germany re-annexed the region, cutting Lithuania off from the Baltic Sea. The German occupation of Lithuania proper during World War II was harsh. Most of Lithuania's 200,000 Jews (8% of the population) were killed. Nationalist intellectuals, officers and clergy were put in

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Latvia, Lithuania: The Way to Europe," in *Transformations of Post-Communist States*, ed. Wojciech Kostecki, Katarzyna Zukrowska and Bogdan J. Góralczyk (New York: St. Martin's, 2000), 133-150; Lieven, *The Baltic Revolution*, chap. 8-9; Lane, *Lithuania*, chap. 4-5. For an argument that workers, too, benefited from insider-oriented economic reforms, see Niels Mygind, "Privatisation and Employee Ownership: The Development in the Baltic Countries," in *Transition in the Baltic States: Micro-Level Studies*, ed. Neil Hood, Robert Kilis and Jan-Erik Vahne (New York: St. Martin's, 1997), 131-147.

<sup>80</sup> In the battle of Žalgiris (Tannenberg) in 1410, Lithuanian and Polish troops decisively defeated the Order and put an end to German expansion to the East for the next three hundred years.

<sup>81</sup> The best sources are Zigmantas Kiaupa, Ain Mäesalu, Ago Pajur and Gvido Straube, *The History of the Baltic Countries* (Tallinn: Avita, 2002), chap. II, sec. 1-2, 4; chap. IV; chap. V, sec. 1-2 and V. Stanley Vardys and Judith B. Sedaitis, *Lithuania: The Rebel Nation* (Boulder, CO: Westview, 1997), chap. 1. See also Lieven, *The Baltic Revolution*, chap. 2 and Lane, *Lithuania*, chap. 1.

concentration camps although some of them collaborated with the Germans in exterminating the Jews. As a result, Lithuania developed both Communist and nationalist anti-German guerrilla movements. When the Soviet troops entered Lithuania in 1944 and drove the Germans out of Klaipėda, some Lithuanians were, at first, glad to see them.<sup>82</sup>

Instead of Germany, Lithuania's closest friend—and enemy—has for a long time been Poland. Lithuania was baptized by Polish priests in the fourteenth century. In the sixteenth century, Lithuania and Poland formed a political and military union (Rzeczpospolita), which conquered large areas of western Russia.<sup>83</sup> The wheel of fortune turned in the eighteenth century, when Russia annexed Lithuania and eastern Poland. However, the Lithuanian nobility maintained Polish language and culture. Relations between the two peoples soured with the rise of nationalism in the nineteenth century. Lithuanian peasants refused to join the anti-Russian uprisings staged by Lithuania's Polonized nobles in 1831 and 1863. When Lithuania and Poland became independent nation-states after the Russian revolution, Poland occupied the region around the ancient Lithuanian capital, Vilnius. Lithuania got its revenge in 1939, when the Soviet Union and Germany divided up Poland and allowed Lithuania to re-occupy Vilnius.<sup>84</sup>

Under Communism, relations between Poland and Lithuania improved, at least at the elite level: both now saw Russia as their main enemy. Many Lithuanian intellectuals read the Polish press. The Lithuanian Catholic church sent its seminarians to study in Poland. Lithuanian dissidents made contact with Solidarity. However, the Poles living in

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<sup>82</sup> Kiaupa et al, *The History of the Baltic Countries*, chap. V, sec. 2-4, 6; chap. VI, sec. 2-3; Vardys and Sedaitis, *Lithuania*, chap. 2-3; Romuald Misiunas and Rein Taagepera, *The Baltic States: Years of Dependence, 1940-1990* (Berkeley and Los Angeles: University of California Press, 1993), chap. 2; Lieven, *The Baltic Revolution*, chap. 3-4; Lane, *Lithuania*, chap. 1.

<sup>83</sup> The Polish-Lithuanian state reached the peak of its power in 1610, when it seized Moscow and put a Polish prince on the Russian throne. In 1612, however, the Russians rebelled and expelled the invaders.

<sup>84</sup> Kiaupa et al, *The History of the Baltic Countries*, chap. II, sec. 1-2; chap. III, sec. 1; chap. IV; chap. V, sec. 2, 6; Vardys and Sedaitis, *Lithuania*, chap. 1-2; Misiunas and Taagepera, *The Baltic States*, chap. 1-2; Lieven, *The Baltic Revolution*, chap. 2-4; Lane, *Lithuania*, chap. 1.

Lithuania remained hostile to their host country: in 1991, most Poles voted against Lithuanian independence, while local governments in Polish-dominated municipalities supported the attempted military coup in Moscow. After the Soviet Union broke up, Poland and Lithuania signed a border and friendship treaty whereby Poland relinquished its territorial claims to Lithuania and Lithuania promised to treat the Polish minority well. However, Poland was in no position to help Lithuania economically. Like Lithuania, Poland was a poor post-Communist country in need of foreign investment. Moreover, Poland and Lithuania had similar economies, dominated by heavy industry and agriculture. As a result, they competed with each other for export markets.<sup>85</sup>

*This brings us to the most important reason for why Lithuania adopted an insider-oriented reform strategy: the economic structure of Lithuania at the time of the breakup of the Soviet Union.* Much of the existing literature argues that economic factors cannot explain why Lithuania and Estonia adopted different foreign economic policies because their economies were very similar under Communism (Lauristin and Vihalemm 1997, 2002; Mattusch 1997; Fish 1998; Andersen 1999, Parts I, III; Maldeikis and Rainys 2000; Raun 2001; Feldmann and Sally 2002; Aslund 2002, chap. 1, 3, 9; Laar 2002, chap. 2-3; Arias-King 2003; Abdelal 2005, chap. 1, 3; Norkus 2006, 2007). As Table 6.1 shows, however, Lithuania had a larger agriculture than Estonia, accounting for 27% of its GDP and 18% of its employment, compared with 20% and 13%, respectively, in Estonia. As discussed in chapter 5, the EU imposed high tariffs on East European agricultural imports and provided large export subsidies to West European farmers and agriprocessors. If its agriculture was going to survive, Lithuania had to a) impose tariffs on agricultural imports from the West and b) to continue to export its foodstuffs to Russia, where tariffs were lower and where Lithuanian products enjoyed prior name recognition.

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<sup>85</sup> Misiunas and Taagepera, *The Baltic States*, chap. 4-6, 8; Vardys and Sedaitis, *Lithuania*, chap. 3, 6-7; Lieven, *The Baltic Revolution*, chap. 8-9; and Lane, *Lithuania*, chap. 2-3.

**Table 6.1: How Similar? Lithuanian and Estonian Economies in 1989**

	Lithuania	Estonia
<b>A) GDP (%)</b>		
Agriculture and forestry	27	20
Industry	35	36
Construction	10	8
Services	28	36
<b>B) Employment (%)</b>		
Agriculture and forestry	18	13
Industry	30	32
Construction	12	10
Services	40	45

*Source:* The World Bank, *Statistical Handbook 1993: States of the Former USSR* (Washington, DC: The World Bank, 1993), 172, 182, 412, 422.

Industry accounted for about the same share of GDP (35-36%) and employment (30-32%) in Lithuania and Estonia. However, the structure of the industry differed in the two countries.<sup>86</sup> First, as Table 6.2 indicates, Lithuania had a larger metal-working and machine-building industry (25% of total industrial output) than Estonia (16%). This industry mostly produced machine tools and electric motors for the Soviet industry and military, although it also made some domestic machinery (e.g., refrigerators and TV sets).<sup>87</sup> Second, more Lithuanian than Estonian firms reported directly to the Soviet central government. Thus, all-union enterprises owned 62% of Lithuanian plant and equipment (59% in Estonia), employed 42% of its industrial labor (34%), and produced 39% of its industrial output (28%).<sup>88</sup> Finally, Lithuanian plants were somewhat bigger (840 workers on average) than Estonian factories (790 workers).<sup>89</sup>

<sup>86</sup> However, both countries had large food-processing (22-25% of output) and textile (20-22%) industries. On balance, both of these industries stood to lose from outsider-oriented economic policies. As with raw agricultural products, EU imposed high tariffs on processed foods. Textiles depended on cotton imported from Central Asia and were subject to EU quotas and monitoring.

<sup>87</sup> OECD, *The Baltic States: A Regional Economic Assessment* (Paris: OECD, 2000), chap. 1; Vardys and Sedaitis, *Lithuania*, chap. 3; and Misiunas and Taagepera, *The Baltic States*, chap. 4-6.

<sup>88</sup> Goskomstat SSSR, *Narodnoe khoziaistvo SSSR v. 1989. g. Statisticheskii ezhegodnik* (Moscow: Finansy i Statistika, 1990), 331.

<sup>89</sup> OECD, *The Baltic States*, 27.



**Table 6.2: Asset or Liability? Lithuanian and Estonian Industry in 1989 (% of industrial output)\***

	Lithuania	Estonia
Electricity and fuels	8	7
Chemicals	3	8
Machinery and metalworking	25	16
Wood-working, pulp and paper	5	10
Construction materials	5	4
Textiles, clothing, and leather	20	22
Food processing	22	25

*Source:* World Bank, *Statistical Handbook 1993: States of the Former USSR* (Washington, DC: The World Bank, 1993), 208, 448.

These figures reflected Lithuanian economic history. With the exception of food-processing, Lithuania only began to industrialize under the Soviet rule, in the 1940s and 1950s. Based on the needs on the all-Union economy, the Soviet central planners emphasized the development of heavy industry, such as metalworking and machine-building.<sup>90</sup> However, the structure of the Lithuanian industry also affected the economic policies of the post-Soviet Lithuanian government by making an outsider-oriented strategy seem risky. Foreign investors were unlikely to take much interest in Lithuania's machine-building enterprises, which needed large investments in plant and equipment, depended heavily on Russian energy (oil) and raw materials (steel), and were used to being told by Moscow what to produce and how. Moreover, even if outside investors had been found, they would have probably moved aggressively to cut production and employment, a scary prospect given the large size of Lithuanian plants.<sup>91</sup>

<sup>90</sup> Ole Norgaard, Lars Johannsen, Mette Skak and René Hange Sorensen, *The Baltic States after Independence* (Cheltenham, UK and Brookfield, VT: Edward Elgar, 1999), chap. 2; Kiaupa et al, *The History of the Baltic States*, chap. V, sec. 5; chap. VI, sec. 4; Misiunas and Taagepera, *The Baltic States*, chap. 3-6; Vardys and Sedaitis, *Lithuania*, chap. 2-3; Lane, *Lithuania*, chap. 1-2.

<sup>91</sup> For a similar argument, see Piritta Sorsa, "Lithuania: Trade Issues in Transition," in *Trade in the New Independent States*, ed. Constantine Michalopoulos and David G. Tarr (Washington, DC: The World Bank, 1994), 157-170; OECD, *The Baltic States*, chap. 1; Norgaard et al, chap. 4.

## **Estonia: Light Wood**

In Estonia, the conservative Fatherland won the most votes in the 1992 election and formed a government with two other center-right parties. Fatherland argued that Estonia needed to break the economic power of the former nomenklatura and detach its economy from Russia. SOEs were to be privatized as quickly as possible to prevent Soviet managers from turning them into their private property or stripping off their assets. The main method of privatizing large enterprises was to be the sale of firms to foreign investors for cash.<sup>92</sup> Trade was to be liberalized and rapidly reoriented from Russia to the West. All export and import licenses, quotas, and tariffs were to be abolished. Estonia was to negotiate a free trade agreement with the EU and European Free Trade Association to allow Estonian firms to enter Western markets. Finally, to ensure that this program was implemented, the state apparatus was to be purged of corrupt and incompetent Soviet-era cadres and replaced with people selected on the basis of their integrity and qualifications.<sup>93</sup>

As with Lithuanian post-Communists, these policies reflected the economic interests of Fatherland's financial backers, including the German Christian Democratic Union (CDU), Estonian émigrés in Europe and North America, and state-owned export-import businesses.<sup>94</sup> The CDU provided the money to set up a conservative think tank and encouraged various conservative groups to form a party (Fatherland). Not

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<sup>92</sup> However, land and real estate were to be returned to their former owners. Small and medium-sized enterprises and Soviet-era housing stock were to be privatized for vouchers issued to all adult citizens.

<sup>93</sup> See, especially, Mart Laar, *Estonia: The Little Country That Could* (Suffolk: St. Edmundsbury Press, 2002), chap. 6-7, 9-10; Mikk Marran and Eve Vungo, *Eesti pöördub läände: Laari valitsus* (Tallinn: Avita, 1999), chap. 2, 4; Erik Terk, *Privatisation in Estonia: Ideas, Process, Results* (Tallinn: Estonian Institute for Future Studies, 2000), chap. 2-4; and Ardo H. Hansson, "The Political Economy of Macroeconomic and Foreign Trade Policy in Estonia," in *Trade in the New Independent States*, ed. Michalopoulos and Tarr, 133-140. See also David J. Smith, *Estonia: Independence and European Integration* (London and New York: Routledge, 2001), chap. 3-4 and Lieven, *The Baltic Revolution*, chap. 8-9.

<sup>94</sup> In other words, I am arguing that *there are no rent-seeking bad guys and reformist good guys in Eastern Europe. Everybody is a rent-seeker*: the post-Communist left and the ex-dissident right; state-owned enterprises and private businesses; domestic managers and foreign investors.

coincidentally, the first head of the Estonian Privatization Agency was a German Estonian, while German businesses were the main beneficiaries of the first wave of privatization in 1992-3.<sup>95</sup> Estonian émigrés financed Fatherland's 1992 election campaign. In return, Fatherland promoted several of them to key positions in the Estonian government, including the ministers of defense, energy and finance.<sup>96</sup> State-owned export-import businesses, such as Estonian Metal Export and the Port of Tallinn, made large financial donations to Fatherland when it was in power in 1992-1995. They did so, in part, because their managers wanted to stay on the good side of the powers that be. However, they also benefited from the conservatives' economic policies, such as the abolition of export and import tariffs.<sup>97</sup>

*However, it seems likely that any Estonian government—regardless of its ideology and the interests of its financial backers—would have adopted outsider-oriented economic policies because of a) Estonia's historical and cultural ties with Germany, Sweden and Finland and b) the structure of the Estonian economy under Communism.* The Teutonic Order conquered Estonia in one of Western Europe's last crusades in the thirteenth century.<sup>98</sup> The various Estonian tribes put up a good fight—the war lasted for nineteen years—but failed to defeat the Germans because they lacked a unified state. For the next seven hundred years, the Germans constituted the land-owning ruling class in Estonia regardless of which power—the Order, Sweden or Russia—ruled the country. Estonians tilled the land as serfs or—after the Russian crown abolished serfdom in the

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<sup>95</sup> Mikk Marran and Eve Vungo, *Eesti pöördub läände: Laari valitsus* (Tallinn: Avita, 1999), chap. 2; Allan Alaküla, "Saksa raha Isamaa kassas," *SL Õhtuleht*, 22 January 2000; Terk, *Privatisation in Estonia*, chap. 4-5; Lieven, *The Baltic Revolution*, chap. 8-9.

<sup>96</sup> For émigré financial support for Fatherland, see Leena Hietanen, *Viron kylmä sota* (Helsinki: Werner Söderström, 2008), chap. 3. For Fatherland's personnel policies, see Marran and Vungo, *Eesti pöördub läände*, chap.4; Terk, *Privatisation in Estonia*, chap. 4-5; and Lieven, *The Baltic Revolution*, chap. 8-9.

<sup>97</sup> Tarmo Vahter, "Poliitilised väljapressijad," *Eesti Ekspress*, 19 October 2006.

<sup>98</sup> Denmark conquered most of northern Estonia. However, after a peasant uprising in the fourteenth century, Denmark sold its lands to the Teutonic Order.

nineteenth century—as tenant farmers and landless laborers.<sup>99</sup>

Things changed in 1918-1920, when the newly-established Estonian state fought a war of independence against Bolshevik Russia and the Baltic-German Landeswehr. During the war, the Estonian government confiscated German landed property and distributed it to Estonian peasants. The land reform issue soured political relations between Estonia and Germany in the inter-war years: Germany demanded that the nobility be compensated; Estonia refused. However, Germany remained Estonia's largest foreign investor and second-largest trading partner after Britain.<sup>100</sup> In 1941-44, Estonia was under German military occupation. The Germans murdered Estonian Jews (about 1% of the population), Communists, and left-wing intellectuals. However, except for heavy economic requisitions, they left the rest of the population largely unmolested. As a result, no significant anti-German guerrilla movement developed in Estonia. Indeed, many Estonians volunteered to serve in the German army, especially when the Soviet troops approached the Estonian border in 1944.<sup>101</sup>

Sweden conquered Estonia after the disintegration of the Teutonic order in the sixteenth century under the twin blows of the Protestant Reformation and the military successes of the Polish-Lithuanian state.<sup>102</sup> The Swedish crown imposed heavy taxes on Estonian peasants. However, it limited statute labor and allowed peasants to sue abusive

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<sup>99</sup> The best accounts are Tõnu Tannberg, Ain Mäesalu, Tõnis Lukas, Mart Laar and Ago Pajur, *History of Estonia* (Tallinn: Avita, 2002), chap. I, sec. 7-9; chap. II, sec. 12-13; Kiaupa et al, *The History of the Baltic Countries*, chap. II, sec. 1, 2, 5; and Toivo Raun, *Estonia and the Estonians* (Stanford: Hoover Institution Press, 2001), chap. 2-3. See also Rein Taagepera, *Estonia: Return to Independence* (Boulder, CO: Westview, 1993), chap. 2; Lieven, *The Baltic Revolution*, ch. 2; and Smith, *Estonia*, chap. 1-2.

<sup>100</sup> Why did Britain play such an important role in the Estonian economy in the inter-war years? For one thing, Britain was the dominant military power in the Baltic sea region until it concluded a naval agreement with Germany in 1935. The Brits also developed a taste for Estonian bacon, eggs and cheese.

<sup>101</sup> Tannberg et al, *History of Estonia*, chap. VII, sec. 38-39; chap. VIII, sec. 40, 44; chap. IX; Kiaupa et al, *The History of the Baltic Countries*, chap. V, S. 1-3, 4, 6; chap. VI, sec. 1-2; Raun, *Estonia and the Estonians*, chap. 8, 11; Taagepera, *Estonia*, chap. 3; Misiunas and Taagepera, *The Baltic States*, chap. 1-2; Lieven, *The Baltic Revolution*, chap. 3-4; Smith, *Estonia*, chap. 1-2.

<sup>102</sup> To be more exact, southern Estonia was under Polish-Lithuanian rule from the 1580s to the 1620s. However, Sweden eventually conquered the entire country.

landlords in royal courts. It also set up the first Estonian-language schools. Sweden lost Estonia to Russia in the Great Northern War in the eighteenth century. However, it reestablished relations with its former colony after the breakup of the Russian empire. In the 1920s and 1930s, Sweden became Estonia's third-largest foreign investor and trading partner after Britain and Germany. The Estonian currency (kroon) was pegged to the Swedish krona and Estonian gold reserves were deposited in the Swedish Riksbank. In 1940, Sweden was the only Western country besides Nazi Germany that recognized the Soviet occupation of Estonia and turned over Estonian assets to the Soviet government. However, in 1944, it gave refuge to tens of thousands of Estonians fleeing from the Soviet army and became the center of Estonian émigré life in Europe.<sup>103</sup>

Finland is related to Estonia by geography—Tallinn is located eighty kilometers from Helsinki across the Gulf of Finland—and language—Finnish and Estonian are mutually intelligible. As a result, Finland became Estonia's "window to the West" during the Soviet era. In 1965, Tallinn and Helsinki established a regular ferry connection, which brought thousands of Finnish tourists to Estonia. In the 1970s, Estonians developed a taste for blue jeans and American soap operas by watching Finnish television. In the 1980s, Finnish and Estonian firms established several joint ventures (e.g., in gasoline distribution and tourism). As with Germany and Sweden, Estonia's relationship with Finland need not be idealized. Many Finnish tourists came (and come) to Estonia to purchase liquor and to visit prostitutes. The joint ventures often allowed Finnish firms to get hold of Estonian state assets at bargain-basement prices. However, thanks to Estonia's prior ties with Finland, Estonian policy-makers could expect that Western capitalists would know where Estonia was on the map.<sup>104</sup>

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<sup>103</sup> Tannberg et al, *History of Estonia*, chap. IV; chap. VIII, sec. 40, 44; chap. IX; chap. X, sec. 56; Kiaupa et al, *The History of the Baltic Countries*, chap. III, sec. 1, 3; chap. V, sec. 2, 3, 5; chap. VI, sec. 1, 2, 6; Raun, *Estonia and the Estonians*, chap. 3, 8, 11; Taagepera, *Estonia*, chap. 1-2; Lieven, *The Baltic Revolution*, chap. 2-3; Smith, *Estonia*, chap. 1-2.

<sup>104</sup> For Estonia's geographic and cultural ties with Finland, see Laar, *Estonia*, chap. 3; Tannberg et al, *History of Estonia*, chap. X, sec. 51-53; Taagepera, *Estonia*, chap. 4-5; and Misiunas and Taagepera, *The*

Finally, the economic structure of Estonia under Communism favored the adoption of outsider-oriented economic reforms. As Table 6.1 makes clear, Estonia had a larger service sector (36% of output and 16% of employment) than Lithuania (28% and 14%, respectively). Services were likely to receive more foreign investment than other sectors because they promised investors quick profits and/or large rents. For example, Estonia was likely to attract tourists from the Nordic countries and Germany. This made it profitable for investors to buy Estonian hotels and spas and to open casinos and night clubs. In the same vein, Estonia inherited from the Soviet Union a well-developed transportation infrastructure, such as railways and ports. A private owner of these facilities could earn monopoly rents from the transit of Russian raw materials to Europe.

While industry made a similar share of the GDP and employment in Lithuania and Estonia in 1989, the structure of industry differed in the two countries. As Table 6.2 shows, Estonia had a larger wood-processing industry than Lithuania (9% v. 5% of industrial output), producing furniture, pulp, and paper for the Soviet market.<sup>105</sup> This reflected, in part, Estonia's earlier history of industrialization: many Estonian wood-processing plants had been established in the late nineteenth and early twentieth centuries with Russian, German, and British capital.<sup>106</sup> However, it also facilitated Estonia's transition from socialism back to capitalism. Unlike many other sectors of industry, wood-processing used cheap local raw materials and energy (timber and electricity) and

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*Baltic States*, chap. 4-5. For the economic implications of these ties, see Hansson, "The Political Economy," 133-140; Mygind, "A Comparative Analysis of the Economic Transition," 17-66; William S. Brown, "Economic Transition in Estonia," *Journal of Economic Issues* 27, no. 2 (1993): 493-503; Siim Kallas, "Estonia and the European Union," *European Business Journal* 8, 3 (1996): 13-20; R. A. Panagiotou, "Estonia's Success: Prescription or Legacy?," *Communist and Post-Communist Studies* 34 (2001): 261-77; and Hietanen, *Viron kylmä sota*, chap. 7.

<sup>105</sup> Estonia also had a larger chemical industry (8% of GDP) than Lithuania (3%). It is unclear, however, whether this was an advantage or a disadvantage. Some chemical plants used local raw materials, such as oil-shale and phosphates. Others used oil and minerals imported from Russia. The trade prospects of the chemical industry were similarly ambiguous. There were no tariffs on Estonian chemical exports to the EU. However, the EU "monitored" them.

<sup>106</sup> Tannberg et al, *History of Estonia*, chap. VI, sec. 33; chap. VIII, sec. 40, 43.

could export its goods to the EU duty-free. This made it attractive for foreign investors, especially Nordic forestry firms looking for cheap production sites close to home.<sup>107</sup>

Estonia also controlled a larger share of its industry than Lithuania. Enterprises controlled by a) the republican government alone or b) jointly by the republican and central government accounted for 41% of Estonian fixed industrial capital, 66% of its industrial workforce, and 72% of its industrial output, compared to 38%, 58% and 61%, respectively, in Lithuania.<sup>108</sup> Finally, Estonian plants were somewhat smaller than Lithuanian factories, employing 790 workers on average (840 in Lithuania).<sup>109</sup> This made Estonia's transition to capitalism easier in two ways. First, firms controlled by republican authorities had some experience in seeking out their own suppliers and customers and deciding how to combine labor and capital to reach plan targets. This increased the likelihood that they would survive without government guidance and subsidies. Moreover, if the worst came to worst and the enterprises went bankrupt, fewer people would be hurt because they employed fewer workers in the first place.<sup>110</sup>

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<sup>107</sup> For a similar argument, see Garri Raagmaa, Mihkel Laan and Antti Raamat, "Transformation of Estonia's Industrial Structure: Continued De-Industrialisation or Interlude in Re-Industrialisation?," *Baltic Review* 22 (2003): 8-12 and Norgaard et al, *The Baltic States*, chap. 2.

<sup>108</sup> Goskomstat SSSR, *Narodnoe Khoziaistvo*, 331.

<sup>109</sup> However, Estonian factories were still big by West European standards: in 1990, the average industrial plant in Western Europe employed 160 workers. See OECD, *The Baltic States*, 27. For a similar argument about Estonia, see Panagiotou, "Estonia's Success," 261-277. For a discussion of how plant size has influenced economic attitudes and voting behavior in Western Europe, see Jonas Pontusson, "Explaining the Decline of European Social Democracy: The Role of Structural Economic Change," *World Politics* 47 (July 1995): 495-533.

<sup>110</sup> For a similar argument, see John Hansen and Piritta Sorsa, "Estonia: A Shining Star from the Baltics," in *Trade in the New Independent States*, ed. Michalopoulos and Tarr, 115-132; Hanson, "The Political Economy," 133-140; Norgaard et al, *The Baltic States*, chap. 4; and Panagiotou, "Estonia's Success," 261-277.

## II Does It Travel?

### Slovakia: Inside-Out

Does the argument I have developed in this dissertation—that Lithuania and Estonia pursued different strategies of economic reforms, which, in turn, shaped their attitudes toward European integration—“travel” to other East European countries? A preliminary analysis of the economic and political development of the former Czechoslovakia suggests that it does. Like Lithuania, Slovakia was a largely agrarian economy in the inter-war years, producing foodstuffs for the Czech as well as German and Austrian markets. After 1948, the Communist government of Czechoslovakia invested heavily in developing Slovak industry, especially steel, metal-working, and machine-building, including weapons. At the same time, it provided large subsidies to Slovak agriculture, which remained the main producer of foodstuffs for the country. *As a result, Slovakia—like Lithuania—developed a dualistic economic structure, dominated by heavy industry on the one hand and agriculture on the other.*<sup>111</sup>

The structure of its economy posed a problem for Slovakia when Communism collapsed. In 1990-1992, the new, conservative-led federal government liberalized prices and trade. This hurt Slovaks more than Czechs. Heavy-industrial goods products had been overpriced under Communism. Now their price declined relative to the price of light-industrial goods and services. Agriculture had been heavily subsidized and protected. Now it had to compete with EU-subsidized European agribusinesses. The government also launched a “peace offensive” to cut weapons production and exports.<sup>112</sup>

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<sup>111</sup> Stanislav J. Kirschbaum, *A History of Slovakia: The Struggle for Survival* (New York: St. Martin's Press, 1996), chap. 8, 11; Peter A. Toma and Dušan Kováč, *Slovakia: From Samo to Dzurinda* (Stanford: Hoover Institution Press, 2001), chap. 11; Karen Henderson, *Slovakia: Escape from Invisibility* (London and New York: Routledge, 2002), chap. 4; Sharon L. Wolchik, *Czechoslovakia in Transition: Politics, Economics, and Society* (London and New York, Pinter, 1991), chap. 1, 4.

<sup>112</sup> This term was doubly ironic. It was coined by Adolf Hitler in 1933. The Czechoslovak government also announced that it wanted to join NATO.



It joined the US- and EU-led arms embargoes on the former Yugoslavia and Arab countries (e.g., Iraq, Libya, and Syria), which had been the best customers for Slovak arms. It also “converted” military plants to civilian use, which in practice meant that factories that had produced tanks and explosives started making tractors and detergent. These policies put much of the Slovak arms industry out of business.<sup>113</sup>

In the 1992 general election, unhappy Slovaks voted into power a center-left coalition led by the populist Movement for Democratic Slovakia. The populist government is most remembered for negotiating a “velvet divorce” from the Czech Republic. Equally important, however, it adopted an insider-oriented strategy of transition to capitalism to protect Slovak economic sovereignty. It maintained public ownership of “strategic” enterprises, such as mines, oil and gas pipelines, electric power plants, railways, banks, and telecommunications. It sold the remaining enterprises—first for vouchers, then for cash, but actually on credit—to “employee corporations” dominated by enterprise managers. It provided subsidies (e.g., cheap loans through state-owned banks) to both SOEs and to firms undergoing privatization. It imposed double-digit tariffs on Western imports, especially agricultural goods, but also steel and some machinery. At the same time, it concluded various trade agreements with Russia, the Czech Republic and other East European countries.<sup>114</sup>

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<sup>113</sup> Kirschbaum, *A History of Slovakia*, chap. 12; Toma and Kováč, *Slovakia*, chap. 12; Henderson, *Slovakia*, chap. 2, 4; Wolchik, *Czechoslovakia in Transition*, chap. 4; Ivan Gabal, “Czechoslovakia: The Breakup and Its Consequences,” in *Transformations of Post-Communist States*, ed. Wojciech Kostecki, Katarzyna Zukrowska and Bogdan J. Góralczyk (New York: St. Martin’s, 2000), 110-132; Hannes Hofbauer, *EU-Osterweiterung: Historische Basis – ökonomische Triebkräfte – soziale Folgen* (Vienna: Promedia, 2007), 157-59.

<sup>114</sup> Roman Frydman, Kenneth Murphy and Andrzej Rapaczynski, *Capitalism with a Comrade’s Face: Studies in the Postcommunist Transition* (Budapest: Central European University Press, 1998), chap. 3; Susan Senior-Nello, “The Economic Criteria for EU Accession: Lessons from the Czech and Slovak Republics,” in *The Road to the European Union, Volume 1: The Czech and Slovak Republics*, ed. Jacques Rupnik and Jan Zielonka (Manchester and New York: Manchester University Press, 2003), 113-137; and Hofbauer, *EU-Osterweiterung*, 165-168; World Bank database on tariffs at <http://siteresources.worldbank.org/INTRES/Resources/469232-1107449512766/tar2007.xls>; Ian Jeffries, *Eastern Europe at the Turn of the Twenty-first Century: A Guide to Economies in Transition* (London and New York: Routledge, 2002), 351-358; 365-378; Toma and Kováč, *Slovakia*, chap. 13; and Henderson, *Slovakia*, chap. 4.

The insider-oriented policies helped to slow down the decline of output and employment in agriculture, food-processing, steel, and some sectors of metal-working (e.g., metal sheets). In these sectors, government subsidies and tariffs helped struggling firms to overcome their—small—quality gap with the West and to export their goods to Russia and Eastern Europe. By contrast, *machine-building, the leading sector of the Slovak economy under Communism, largely collapsed because its goods were of such poor quality relative to Western products that even East European consumers did not want them.* Slovak service sector presents a similar pattern. Relatively simple services—e.g., commerce and tourism—grew fast since they allowed local entrepreneurs to earn quick profits. However, *more sophisticated services—e.g., finance and telecommunications—remained underdeveloped for lack of capital and technology.*<sup>115</sup>

The failure of the insider-oriented policies to modernize the Slovak economy led to the defeat of the left-populists by a conservative-led coalition in the 1998 general election. The new government gradually opened the Slovak economy to Western investment and trade. It sold several large SOEs—e.g., telecommunications and banks—to Western investors. It allowed foreigners to buy non-agricultural land and provided subsidies (e.g., tax holidays) to foreign “greenfield” investors. It cut tariffs on Western imports and encouraged Slovak firms to export their goods to the EU. However, until the EU referendum, relatively few foreign companies invested in Slovakia because they feared the revival of nationalism and populism (see Table 6.3).<sup>116</sup> Moreover, some of

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<sup>115</sup> Vilma Juričková, “Slovak Enterprises in the Transition Process to a Market Economy,” in *East European Enterprises in the Process of Transformation to a Market Economy*, ed. Miroslaw Szreder (Commack, NY: Nova Science, 1998), 71-100; Jan Firdmuc and Jarko Firdmuc, “The Slovak Republic,” in *Winners and Losers of EU Integration: Policy Issues for Central and Eastern Europe*, ed. Helena Tang (Washington, DC: The World Bank, 2000), 190-218; Martin Myant, “The Czech Republic and Slovakia,” in *The Central and East European Handbook: Prospects onto the 21<sup>st</sup> Century*, ed. Patrick Heenan and Monique Lamontage (Chicago and London: Fitzroy Dearborn, 2000), 40-55; Tamás Novák, “Sources and Uses of Energy,” *ibid.*, 129-139; Andrew H. Dawson, “Agriculture,” *ibid.*, 140-150; Tamás Novák and Czaba Novák, “The Transformation of Manufacturing,” *ibid.*, 151-160; Lukasz Konopielko, “Banking and Other Financial Services,” *ibid.*, 161-170.

<sup>116</sup> Since then, however, Slovakia has received considerable Western investment in services and the car industry. See *Economist*, “Going East,” 4 March 2004 and “A Double-Edged Sword,” 30 April, 2004.

the biggest foreign investors in the Slovak economy were Russian companies. For example, Yukos purchased the Transpetrol oil pipeline, while Gazprom bought the Slovrusgas gas distribution network. As Table 6.3 shows, Slovakia also continued to trade heavily with Russia and Eastern Europe.<sup>117</sup>

**Table 6.3: Similar Speed, Different Direction: Foreign Investment and Trade in Slovakia and the Czech Republic in 2003**

	Slovakia	Czech Republic
Private sector share in GDP (%)	80	80
Foreign direct investment per capita, 1989-2003 (\$)	1894	3710
Share of trade in GDP (%)	136	111
Share of trade with non-transition countries (%)	66	81

*Source:* EBRD, *Transition Report 2004* (London: EBRD, 2004), 45, 120-121, 176-77.

*Like in Lithuania, the weak economic presence of the West in Slovakia and the primitive structure of the Slovak economy created a pro-EU consensus among the Slovak political parties at the time of the EU referendum.* The governing conservative and liberal parties argued that Slovakia needed to join the EU to catch up with the West economically. EU accession would promote foreign investment in industries where Slovakia had a comparative advantage because of its geographical location and skilled labor force (e.g., cars and electronics). Free trade would give Slovakia access to the rich and large EU market and stimulate competition at home. More interestingly, the national-populists also supported EU accession, even though they were now in opposition. They argued that joining the EU would allow Slovak producers to compete on equal footing with West European firms. Slovak steel and metalworking firms would be able to export their goods to the EU duty-free. Slovak farmers would begin to receive

<sup>117</sup> Milada Vachudova, *Europe Undivided: Democracy, Leverage, and Integration after Communism* (Oxford and New York: Oxford University Press, 2005), chap. 7; Myant, "The Czech Republic and Slovakia," 40-55; Toma and Kováč, *Slovakia*, chap. 14; Henderson, *Slovakia*, chap. 2, 4; Hofbauer, *EU-Osterweiterung*, 169-187; Jeffries, *Eastern Europe*, 358-365, 375-379; *Economist*, "Ivan at the Pipe," 9 December 2005.

EU subsidies. As a result, 94% of Slovaks voted for EU membership in the 2003 accession referendum, more than in any other Central European candidate country.<sup>118</sup>

### **The Czech Republic: Outside-In**

The Czech Republic presents a rather different picture from its Slovak counterpart in terms of the structure of its economy under Communism, the strategy of transition, and the economic and political consequences of that strategy. Bohemia and Moravia began to industrialize already in the second half of the nineteenth century, producing glass, textiles, coal, steel, and weapons for the Austria-Hungarian empire. During and after World War I, the Czech lands developed a large machine-building industry, including electric motors and motor vehicles (cars, buses and trams). Many of these ventures were financed by German bankers and industrialists.<sup>119</sup> After 1948, the Communist government nationalized the bulk of Czech industry. However, Czech plants continued to export some of their products (especially cars) to Western Europe. The Communists also built a strong petro-chemical industry, including fuels, rubber, fertilizers, and paints. By contrast, some older industries—e.g., steel and weapons—moved to Slovakia.<sup>120</sup>

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<sup>118</sup> Petr Kopecký and Peter Učen, “Return to Europe? Patterns of Euroskepticism among the Czech and Slovak Political Parties,” in *The Road to the European Union*, ed. Rupnik and Zielonka, 164-179; Petr Kopecký and Joop van Holsteyn, “The Grass is Always Greener . . . : Mass Attitudes toward the European Union in the Czech and Slovak Republics,” in *Public Opinion, Party Competition, and the European Union in Post-Communist Europe*, ed. Robert Rohrschneider and Stephen Whitefield (New York and Basingstoke: Palgrave Macmillan, 2006), 106-129; Karen Henderson, “EU Accession and the New Slovak Consensus,” *West European Politics* 25, 4 (September 2004): 652-670; Karen Henderson, “Slovak Political Parties and the EU: From Symbolic Politics to Policies,” in *The European Union and Party Politics in Central and Eastern Europe*, ed. Paul G. Lewis and Zdenka Mansfeldová (Basingstoke and New York: Palgrave Macmillan, 2006), 149-68; *Economist*, “The Menace of Vladimir Meciar,” 24 January 2002.

<sup>119</sup> However, Czechs also developed their own capitalist class. For example, Czech businessmen owned the Zivnostenska Banka, the Škoda car factory, and the CKD tram-maker. See Mitchell Orenstein, “Václav Klaus: Revolutionary and Parliamentarian,” *East European Constitutional Review* 7, no. 3 (1998), online edition, <http://www1.law.nyu.edu/eecr/vol7num1/special/vaclavklaus.html>.

<sup>120</sup> Hugh LeCaine Agnew, *Czechs and the Lands of the Bohemian Crown* (Stanford: Hoover Institution Press, 2004), chap. 10-11, 13-14; Rick Fawn, *The Czech Republic: A Nation of Velvet* (London and New York: Routledge, 2000), chap. 1, 3; Wolchik, *Czechoslovakia in Transition*, chap. 1, 4.

In the 1992 election, a plurality of Czech voted for the conservative Civic Democratic Party and its liberal allies. The conservative-led government of 1992-1998 pursued outsider-oriented economic policies similar to Estonia's. Large, export-oriented SOEs were sold to foreign (mostly German) investors for cash. For example, Škoda Auto was sold to Volkswagen and the engineering concerns Škoda Energo and ZPA to Siemens.<sup>121</sup> The government also welcomed foreign "greenfield" investment. Foreigners were allowed to invest in all sectors of the economy and to buy non-agricultural land. They also received generous start-up subsidies and tax breaks. Finally, the government quickly liberalized foreign trade. Except for agricultural products, tariffs on EU goods were abolished. Tariffs on non-EU imports were set at single digits. *As a result, as Table 6.3 illustrates, the Czech Republic received more FDI per capita—and reoriented its trade more rapidly from Eastern to Western Europe—than Slovakia.*<sup>122</sup>

Like in Estonia, however, outsider-oriented policies worked better for some sectors of the economy than others. Output and employment increased in services, particularly finance and telecommunications, and the machine-building industry, especially motor vehicles and electronics. These sectors received the bulk of the FDI in

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<sup>121</sup> However, many medium-sized firms and large domestically-oriented firms were sold to local investors for vouchers. See Thomas D. Hopkins, "The Czech Republic's Privatization Experience," in *Privatization in Central and Eastern Europe: Perspectives and Approaches*, ed. Demetrius S. Iatridis and June Gary Hopps (Westport, CT and London: Praeger, 1998), 61-72; Mitchell Orenstein, *Out of the Red: Building Capitalism and Democracy in Post-Communist Europe* (Ann Arbor, MI: University of Michigan Press, 2001), chap. 3-4; Hilary Appel, *A New Capitalist Order: Privatization and Ideology in Russia and Eastern Europe* (Pittsburgh: University of Pittsburgh Press, 2004), chap. 2-3; Martin Myant, *The Rise and Fall of Czech Capitalism: Economic Development in the Czech Republic since 1989* (Cheltenham, UK and Northampton, MA: Edward Elgar, 2003), chap. 4, 7, 9-10; Fawn, *The Czech Republic*, chap. 3.

<sup>122</sup> The World Bank, "1988-1999 Privatization Transaction Data," [www.fdi.net/documents/WorldBank/databases/plink/soceco/1czechrepublic.htm](http://www.fdi.net/documents/WorldBank/databases/plink/soceco/1czechrepublic.htm); The World Bank, database on tariffs, <http://siteresources.worldbank.org/INTRES/Resources/469232-1107449512766/tar2007.xls>; Senior-Nello, "The Economic Criteria for EU Accession," 113-137; Martin Myant, "The Czech Republic: From 'Czech' Capitalism to 'European' Capitalism" in *Varieties of Capitalism in Post-Communist Countries*, in David Lane and Martin Myant, ed. (Basingstoke, UK and London: Palgrave Macmillan, 2007), 105-123; Myant, *The Rise and Fall of Czech Capitalism*, chap. 4, 7, 9-10; Hofbauer, *EU-Osterweiterung*, 152-164; Jeffries, *Eastern Europe*, 156-165, 179-193; Agnew, *Czechs*, chap. 15-16; *The Economist*, "Slav Motown," 4 January, 2001; Tõnis Arnover, "Kesk-Euroopa püüab investeringuid," *Äripäev*, 27 November, 2002.

the Czech republic because they offered foreign investors the opportunity to extract quasi-monopoly rents (services) or to cut labor costs (machine-building). Under the Czech Republic's association agreement with the EU, they could also export their goods (services) to Western Europe duty-free. By contrast, *output and employment declined in agriculture and food processing, fuel, chemicals, steel, and mining*. These sectors received little FDI because of their competitive structure or capital-intensive nature. Because of EU export subsidies and import tariffs, they also faced tough EU competition at home without being able to export their products to the EU.<sup>123</sup>

*The economic problems created by Western investment and trade created a political opening for anti-EU parties.* Like in Estonia, much of the opposition to the EU came from the political left—in this case, the hard-left Communist Party of Bohemia and Moravia. The Czech Communists are unusual among the former regime parties in Eastern Europe in that they have both kept the Communist name and ideology and achieved considerable electoral success (19% of the vote in the 2002 election). They called on their supporters to vote against EU accession because it would impoverish ordinary people and undermine Czech economic independence. European competition would drive Czech agriculture and traditional industry bankrupt and increase unemployment. EU-mandated indirect taxes would increase the price of food, gasoline, electricity, and other basic goods. German and Austrian companies would take control of Czech infrastructure like railways and power plants. Germans expelled from the *Sudeten* region after World War II would come and reclaim their property.<sup>124</sup>

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<sup>123</sup> Petr Pavlik, "The Czech Republic," in *Winners and Losers of EU Integration*, ed. Tang, 121-143; Myant, *The Rise and Fall of Czech Capitalism*, chap. 11-13; Myant, "The Czech Republic," 105-123; Hofbauer, *EU-Osterweiterung*, 152-164; Myant, "The Czech Republic and Slovakia," 40-55; Novák, "Sources and Uses of Energy," 129-139; Dawson, "Agriculture," 140-150; Novák and Novák, "The Transformation of Manufacturing," 151-160; and Konopielko, "Banking and Other Financial Services," 161-170; *The Economist*, "An End to Empire," 17 December 1998.

<sup>124</sup> See, especially, the Communist Party of Bohemia and Moravia, "The KSČM at the Turn of the Millennium" (1999) and "Vote Programme of KSCM in 2002," [www.kscm.cz](http://www.kscm.cz). See also Seán Hanley, "The Communist Party of Bohemia and Moravia after 1989: 'Subcultural Party' to Neocommunist Force" in *The Communist Successor Parties*, ed. Bozóki and Ishiyama, 141-165; Dan Hough and Vladimír Handl, "The

Unlike in Estonia, however, the Czech conservatives, who were left out of government after the 2002 election, also criticized certain aspects of European integration. They argued that the EU was moving from free market liberalism towards “socialism” (centralization and regulation). The Czech Republic’s accession treaty with the EU was a case in point. EU-imposed environmental, health and safety regulations would increase the cost of doing business in the Czech Republic and make Czech goods less competitive. EU-imposed tariffs would increase the prices of consumer goods. Visa regulations would bar Czechs workers from working in most EU countries—including neighboring Germany and Austria—for several years, while foreigners would be allowed to buy land in the Czech republic from the date for the accession.<sup>125</sup> The conservative criticisms reinforced the impression cultivated by the Communists that the Czechs were getting a raw deal from the EU. As a result, *only 77% of Czechs voted for EU accession in the 2003 referendum, less than in any other Central European candidate country.*<sup>126</sup>

## Conclusion

This dissertation began with a puzzle: why did most Lithuanians support EU membership, while many Estonians did not? The existing literature on cross-national

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Post-Communist Left and the European Union: The Czech Communist Party of Bohemia and Moravia (KSCM) and the German Party of Democratic Socialism (PDS),” *Communist and Post-Communist Studies* 37 (2004): 319-339; Seán Hanley, “A Nation of Skeptics? The Czech EU Accession Referendum of 13-14 June 2003,” *West European Politics* 27, 4 (2004): 691-715; Petr Kopecký, “An Awkward Newcomer: EU Enlargement and Euroskepticism in the Czech Republic,” *European Studies* 20 (2004): 225-245; Michael Baun, Jakub Dürr, Dan Marek and Pavel Šaradín, “The Europeanization of Czech Politics: The Political Parties and the EU Referendum,” *Journal of Common Market Studies* 44, 2 (2006): 249-290; Lukáš Linek and Zdenka Mansfeldová, “The Impact of the EU on the Czech Party System,” in *The European Union and Party Politics*, ed. Lewis and Mansfeldová, 20-39; Kopecký and Učen, “Return to Europe?,” 164-179; and Kopecký and van Holsteyn, “The Grass is Always Greener...,” 106-129.

<sup>125</sup> In the end, the Czech government imposed a seven-year moratorium on foreign ownership of agricultural land, as did Slovakia. See Lynn M. Tesser, “East-Central Europe’s New Security Concern: Foreign Land Ownership,” *Communist and Post-Communist Studies*, 37 (2004): 213-239

<sup>126</sup> See the secondary sources cited in the previous paragraph and, especially, *Der Spiegel*, “Wie zu Breschnews Zeiten,” 2006 (11): 126-128 and Seán Hanley, “From Neo-Liberalism to National Interests: Ideology, Strategy, and Party Development in the Euroskepticism of the Czech Right,” *East European Politics and Societies* 18, no 3 (2004): 513-548.

differences in EU support in Eastern Europe has focused on political and cultural variables, such as the history of independent statehood and the presence or absence of significant Euroskeptic parties. I have shown that there is some support for these hypotheses. Lithuanians were less worried about losing their political independence and cultural identity in the EU than Estonians. Euroskeptic parties were stronger in Estonia than in Lithuania. I have also shown, however, that *Lithuanian and Estonian voters had different economic expectations about the EU*. Most Lithuanians hoped that joining the EU would help their country develop economically by making it eligible for EU aid and increasing foreign investment and trade. Many Estonians, by contrast, worried that the accession would impoverish their country and make it dependent on the West by driving domestic producers out of business and allowing foreigners to buy up local resources.

I have argued that *these expectations reflected the strategies of economic reform adopted by Lithuania and Estonia*. Lithuania pursued an insider-oriented strategy. It maintained state ownership of basic infrastructure (e.g., railways) and sold other SOEs to their managers. It imposed moderate tariffs on imports and continued to trade heavily with Russia. By contrast, Estonia followed an outsider-oriented strategy. It sold large SOEs, including infrastructure enterprises, to foreign investors. It abolished all import tariffs and reoriented its trade rapidly from Russia to the West. Neither strategy worked particularly well, however. The Lithuanian strategy slowed down the development of services and “new” industries (e.g., electronics). The Estonian strategy undermined agriculture, “old” industries (e.g., food processing) and infrastructure (e.g., railways). As a result, both Lithuanians and Estonians were unhappy with their (country’s) economic situation. However, Lithuanians saw the European integration as a solution to their (country’s) economic problems, while Estonians considered it a cause of theirs.

This, of course, raises the question of why Lithuania and Estonia pursued different strategies of economic reform in the first place. Party politics played a role in this. For most of the 1990s and early 2000s, Lithuania was governed by the post-



Communists, whereas Estonia was ruled by the conservatives. I have also argued, however, that Lithuania and Estonia would have probably pursued different economic policies regardless of which party was in power. *For historical and cultural reasons, Lithuania lacked an obvious patron in Western Europe, while Estonia had several* (Finland, Sweden and Germany). Moreover, *under Communism, the Lithuanian economy was dominated by agriculture on the one hand and heavy industry on the other.* These sectors were unattractive to foreign investors because they required large investment in plant and technology or were subject to EU tariffs and quotas. By contrast, *Estonia had a large light industry and service sector.* These sectors were attractive to foreign investors because they required small capital investments or allowed investors to earn monopoly rents. They could export their products to the EU duty-free.

*Finally, I have argued that my argument “travels” to the former Czechoslovakia.* Like Lithuania, Slovakia inherited from the Communist system an economy dominated by agriculture and heavy industry. To protect these sectors, the left-populist government of Slovakia sold SOEs to their managers, imposed high tariffs on EU imports, and continued to trade with Russia and Eastern Europe. These policies slowed down the development of “new” industry (e.g., cars) and skill-intensive services. As a result, most Slovaks supported joining the EU as a way of modernizing their country’s economy. Like Estonia, the Czech lands had a relatively large service sector and light industry. To help these sectors develop, the conservative Czech government sold large SOEs to foreign investors, abolished tariffs on most EU imports, and reoriented the country’s exports to Western Europe. These policies led to the decline of Czech agriculture and “old” industry (e.g., steel and mining). As a result, many Czechs opposed EU accession as threat to their traditional economy. Across Eastern Europe, it seems, familiarity with the West (through investment and trade) breeds contempt (opposition to the EU).

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