Molsberger, Josef; Kotios, Angelos

Working Paper
The single European market of 1992 within the GATT of the nineties

Tübinger Diskussionsbeiträge, No. 7

Provided in Cooperation with:
University of Tübingen, School of Business and Economics

Suggested Citation: Molsberger, Josef; Kotios, Angelos (1990) : The single European market of 1992 within the GATT of the nineties, Tübinger Diskussionsbeiträge, No. 7, Eberhard Karls Universität Tübingen, Wirtschaftswissenschaftliche Fakultät, Tübingen

This Version is available at:
http://hdl.handle.net/10419/104915

Terms of use:
Documents in EconStor may be saved and copied for your personal and scholarly purposes.

You are not to copy documents for public or commercial purposes, to exhibit the documents publicly, to make them publicly available on the internet, or to distribute or otherwise use the documents in public.

If the documents have been made available under an Open Content Licence (especially Creative Commons Licences), you may exercise further usage rights as specified in the indicated licence.
The Single European Market of 1992 within
the GATT of the Nineties

Josef Molsberger und Angelos Kotios

Tübinger Diskussionsbeiträge
The Single European Market of 1992 within the GATT of the Nineties

Josef Molsberger und Angelos Kotios


Diskussionsbeitrag Nr. 7
August 1990

Wirtschaftswissenschaftliches Seminar
Mohlstraße 36, D-7400 Tübingen
Josef Molsberger and Angelos Kotios

The Single European Market of 1992 within the GATT of the Nineties

1. Introduction

When the European Economic Community was founded, in 1958, concern over its impact on world trade flows and on the multilateral trade system was widespread. Actually, for a number of years, the Community proved to be rather open to Third Countries's trade - with the exception of agriculture. The internal liberalization - abolishment of tariffs and quotas - was accompanied by a considerable lowering of the Common External Tariff, in the Kennedy Round of the GATT. It is true that this tariff round was initiated by the U.S., but the EC did accept the challenge and played its role in the worldwide liberalization process of the 1960s. If the European Common Market caused trade diversion at all, it was certainly a minor problem.

The picture has changed since the beginning of the 1970s. The macroeconomic and structural problems that were to be faced after the first oil-price shock of 1973 altered the trade policy attitude of the EC member states and, consequently, the nature of the European trade policy (Wolf, 1983, p. 191 ss.; Patterson, 1983, p. 223 ss.; Hailbronner/ Bierwagen, 1989, p. 385 ss.). Since about the mid-1970s the EC became more power-conscious and more eurocentric. The regional differentiation of the Common Trade Policy, already initiated during the 1960s, was further developed. Numerous preferential treaties created a hierarchical structure of the EC's external trade relations. As of to-day, MFN tariffs are applicable to imports from only 7 Western industrialized countries and - only recently - from a few state trading countries. This policy of regional discrimination is a clear deviation from the liberal principles of non-discrimination and MFN treatment among GATT partners. It has introduced an element of politicization
into the international trade relations. There are more instances of discrimination and politization in the EC trade policy: For sectoral protectionism the Community has increasingly applied selective, discriminatory instruments that are not conforming at least to the spirit of the GATT obligations. NTBs of this kind protect sensitive sectors such as textiles and apparel, steel, shipbuilding, aircraft construction, electronics, automobiles and machine tools.

It is interesting to note that the increasing external protectionism ran parallel with a retardation, or even a setback, of the internal integration process in the EC that characterized the period between the beginning of the 1970s and the middle of the 1980s. Many of the above-mentioned protectionist measures were taken not by the Community but by individual member states. They were backed by intra-Community protectionism. Thus the national protectionism affected not only Third Countries but also the other EC members.

The period of stalemated in the internal integration process definitely came to an end when the EC Commission published, in 1985, its programme for Completing the Internal Market. It put on the agenda the elimination of remaining non-tariff barriers to intra-Community trade. After the dismantling of tariffs and quotas in the early years of the Community this is the second great motion towards internal liberalization. And this new initiative of the Commission has in fact set free forces that are comparable to the initial integrative à la an after the foundation of the Community.

Will the setting-up of the "Internal" (or "Single") European Market also have liberalizing effects upon world trade that would be comparable to the experience of the 1960s? Or will it spur tendencies to build a "fortress", or at least a "reservation Europe"? How will the EC after 1992 act within the multilateral trading system? Will the GATT system be strengthened or weakened by the establishment of the Single European Market?
2. **Interdependencies between the Single-Market Programme and the EC's External Trade Relations**

The aim of the EC Commission's Single-Market programme is to complete the European integration by creating, within the Community, a large market without internal border lines which is comparable to the conditions of a national market. To reach this objective the EC applies a double strategy. It combines measures of "negative integration" - the dismantling of national barriers to intra-Community trade - with "positive integration" steps - the formulation of common policies (Kotios/Molsberger, 1989).

The "negative integration" approach aims at fully guaranteeing the "four freedoms" of the EEC Treaty by eliminating non-tariff obstacles that impair these freedoms. Physical, technical and fiscal barriers to intra-Community trade are to be abolished so that free movement of goods, services, capital, and persons is possible. The *White Paper* of the EC Commission (1985) lists numerous measures of "negative integration" (the number has meanwhile increased to 282). They include prohibition of certain practices, harmonization of minimum standards, and mutual recognition of national regulations and standards. It is expected that this programme will abolish discrimination on grounds of nationality, intensify Community-wide competition, and allow greater economies of scale.

The "positive integration" measures refer to common policies, and to harmonization or co-ordination of policies. They include common policies in the areas of anti-trust, research and development, social cohesion, and the coordination of macro-economic policies and of national subsidization policies. The Commission's *White Paper* paid less attention to measures of positive integration, but they were included in the Single European Act of 1987. The majority of the member states sees also the realization of the Economic and Monetary Union (EMU) as a necessary condition for a complete internal market integration.

The basic philosophy of the Internal Market programme is one of classical liberalism: to open up markets in order to increase competition, enforce higher efficiency of production, and better serve the consumers. This is nothing else but the philosophy underlying the argument for international free trade - with the difference that the Internal Market
programme is concerned only with free trade within the Community borders. It is an open question whether the same argument should - and will - also be applied to EC trade with third countries (Scharrer, 1986; Koopmann, 1989b).

The EC Commission has not been very explicit about the external dimension of the Single Market. Among the motives for the new integration concept of the EC are certainly considerations as to the international competitiveness of European firms and the competition between the EC and the U.S. and Japan (Bangemann, 1989). But the Single Market programme itself is oriented only towards the internal problems. The White Paper of 1985 and the Single European Act of 1987 lack concrete statements on the external dimension of 1992. The latest report on the implementation of the Single Market programme gives not more than a vague assertion that the EC will be a "partner" to Third Countries (EC Commission, 1990, p. 6, para. 19). This is also the promise of the commission's 1988 declaration of intents concerning the external dimension of the Single Market (EC Bulletin, 10-1988, p. 10-13).

Whatever the final outcome will be, there are interdependencies between the completion of the internal market and its external dimension. On the one hand, the Single Market strategy will induce changes in the external trade regime of the EC. National protectionism of member states against third country imports or different import quotas for the member states will no longer be effective after the border controls within the Common Market are abolished. The consequences for the third countries' trade will depend on the details of the Community's external trade regime. On the other hand, the success of the Single Market strategy depends also upon the external trade regime (Fieleke, 1989, p. 15; Grimm et al., 1989, p. 26). More external protectionism means less competition in the Internal Market; this again entails a less efficient allocation of resources, slower technological progress and lower growth in the Community. If the hitherto existing discriminatory import regimes are kept it will be difficult to dismantle border controls within the Community (Kotios/Molsberger, 1989, p. 7-9).

At the present date it is not possible to assess definitely the external effects of the Single Market programme. The realization of the
programme itself is yet partly uncertain; the balance between protectionist and liberal tendencies within the Community is not yet decided; and the possibilities of third countries – particularly the U.S. and developing countries – to press for a liberal external trade regime of the Community cannot be judged definitely. The following arguments on the external perspectives of the Single Market – risks and opportunities for the EC's external trade relations – are therefore partly speculative and conditional.

3. **Risks of the Single Market for the EC's Trade Relations with Third Countries**

It is undeniable that the completion of the European Single Market implies risks for traders and investors of third countries. Outside the EC, especially in the U.S., both businesses and government officials have been worried by these risks. Fear of a "Fortress Europe" – a Single Market secluded from the outside – is still widespread. Statements of EC officials to the contrary (EC Bulletin, 10-1988, p. 10 ss.; Henderson, 1989, p. 10–13) have been cold comfort. The main risks can be grouped under the following four headings.

a) **Increasing Discrimination by a Stronger Community Preference?**

A dismantling of non-tariff barriers within the EC will automatically increase the Community preference, that is: increase the discrimination of imports from third countries. Other things being equal – in particular if the foreign trade regime of the EC is not changed – this will increase the danger of trade diversion. For example, intra-Community liberalization in the fields of services, government procurement, and technical barriers to trade are not applicable to suppliers from third countries (Koopmann, 1989a, p. 424 ss.). There is no obligation under international law to extend these liberalizations to foreign firms. The EC has repeatedly stated that this will be possible only on the basis of reciprocity (EC Bulletin, 10-1988, para. 1.2.5 ss.; Henderson, 1989, p. 10–12). It is thus up to the EC's part-
ner countries to develop appropriate strategies.

The EC's new policy in the field of standardization will also increase the Community preference (Hufbauer, 1990, p. 54). The harmonization of minimum standards, the introduction of new standards systems, and the provision of greater transparency will benefit EC firms in first instance (Maier/Walter, 1988). The same holds true for the new policy of mutual recognition of national test and certification procedures (Fieleke, 1989, p. 16; McAllister, 1989, p. 21; Schlecht, 1988, p. 7). Neither the GATT Codes nor other international treaties obligle the EC to apply its new standardization policies to firms from third countries.

Investors from third countries have also to face discrimination in the EC. Community treatment for products of third-country investors - e.g. Japanese cars produced in the EC - is only granted in case of a rather high local content of the value added. These restrictions do not apply to EC firms (Koopmann, 1989a, p. 429 s.).

b) Increasing Protectionism through Unification of National Trade Barriers?

In spite of Article 113 of the EEC Treaty some competences in trade policy are still left with individual member states. They administer single quota restrictions for imports, and export restraining agreements with third countries. In addition, the common trade policy is often split up into special arrangements for individual member countries, e.g. differentiated import quotas or tariff quotas or import measures limited to one or several member states (EC Commission, 1985, para. 397; Molsberger, 1989, p. 10 s.).

All these measures of 'regional protectionism' risk to become ineffective through 'triangular imports' via other member states. In the past this has been excluded by intra-Community protectionist action under Article 115 of the EEC Treaty - with or without prior consent of the Commission (Molsberger, 1989, p. 16 ss.). When under the Single Market programme the internal border controls are abolished another solution has to be found. On principle three options are possible:
(1) All protectionist measures of individual member states could be eliminated, without compensation through Community-wide protectionism. This solution has been proposed e.g. by the German Federal Government. But it appears to be hardly realistic, given serious structural problems in sensible sectors (e.g. automobiles) of several member states (Koopmann, 1989a, p. 415; DIW, 1988, p. 449 s.). At best some national quota restrictions on imports from East European countries could be eliminated as a consequence of the treaties that were recently signed. If the textiles and clothing sector is integrated into GATT, as aimed at in the Uruguay Round, national quantitative restrictions in these fields could also be phased out.

(2) For a transitional period the EC member states could be allowed to keep old, and even to introduce new, protectionist measures against imports from third countries; but protectionist measures at the internal borders would be excluded. Under these conditions national import restrictions at the external border would give some protection (Schlecht, 1988, p. 7); but they would be only temporarily effective, because in the longer run imports would take their way via other member states. This option would be a second best solution. It would at least allow a competition of national trade-policy systems and would prevent conflicts between the Community and its trade partners (Kotios/Molsberger, 1989, p. 13).

(3) Community measures could be substituted for national protectionist measures. Regarding several sensitive goods the Commission does not exclude this solution, provided that it would not increase the level of protection in the Community (EC Bulletin, 10-1988, para. 1.2.8). However, since this transformation of single member states' measures into Common protectionist action would extend the protectionism to the Community as a whole, an absolute increase of the level of protection appears to be unavoidable. Such a Community-wide sharing of national protectionist measures is opposed by the more liberal EC members. The German Federal Government, e.g., has rejected outright any 'harmonization' on an average level of protectionism (Jahreswirtschaftsbericht 1989, para. 42). It is an open question, however, whether the liberal position will prevail in the decision-making processes of the EC.
c) **Increasing Demand for Community Protectionism?**

The completion of the Single Market will certainly spur competition within the EC. This will increase adjustment needs and problems in several member countries. It is to be expected that the 'losers' or 'potential losers' will exert pressure on their national governments to be compensated at least by protection from third-country competition. Isolated national protectionism will be ever more difficult within the Single Market. This situation implies the danger that the national governments in question will either increase subsidization of national industries or transmit the protectionist pressure into the EC Council. Both options would bring about an increase of protectionist elements in the European trade policy (DIW, 1988, p. 450 s.; McAllister, 1989, p. 19). This is the nucleus of the 'Fortress Europe' argument.

In addition, the elimination of intra-EC trade borders may result in balance-of-payments deficits of countries with a large share of less competitive industries. If the EMU precludes exchange-rate changes as well as exchange control and intra-Community protectionism, there could be pressure to cure the balance-of-payments problems by external protectionism (Grimm et al., 1989, p. 25; Franzmeyer, 1987, p. 269).

d) **Greater Bargaining Power of the EC and Specific Reciprocity?**

A success of the Single Market programme will probably strengthen the EC's bargaining position in international trade diplomacy; the greater market will be more attractive for third-country exporters, and the EC institutions will dispose of extended competences. This situation does not necessarily result in an abuse of the greater bargaining power of the EC. But experience shows that risks for third countries are involved: the EC has not always refrained from employing its bargaining power to reach selective protectionist objectives. This explains certain fears that the Single Market would encourage similar actions of the Community (Grimm et al., 1989, p. 24 s.; DIW, 1988, p. 450 s.).
Special concern has been expressed as to the reciprocity approach that the EC will practise in the future. EC representatives have been using vague notions like 'global reciprocity', 'equality of advantages', 'equal conditions of market access' (Maier/Walter, 1988; Koopmann, 1989a, p. 427; Henderson, 1989, p. 11). The danger is seen that the EC would use a narrowly defined reciprocity approach that would compare market shares in single sectors or industries and thus end up in bilateral bargaining – which is always detrimental to small and powerless trade partners.

4. Opportunities of the Single Market for a Liberal Trade Regime of the EC

The European Single Market does not only hold risks for international trade. It also provides opportunities for firms from third countries and for a liberalization of the EC trade policy. These opportunities are to be seen against the risks. But at the present date it is not yet possible to draw a balance of both tendencies.

a) Increasing Imports through Higher Growth?

It is to be expected that the realization of the Single Market will spur competition, innovations and growth in the European Community. Higher growth and, consequently, higher incomes in the EC can be assumed to stimulate imports from third countries. At least this holds true for products that have a positive income elasticity of demand and that are not subject to quantitative import restrictions – provided that the external trade regime of the Community stays unchanged.

On principle there are good reasons to expect these positive opportunities for increased imports, but the effect should not be overstated. The estimates of increased growth rates are partly over-optimistic (Cecchini, 1988, p. 134; Emerson et al., 1988, p. 193 ss.; Henderson, 1989, p. 3-5). Henderson is certainly right when he argues that "... there is little reason to think that the increment to growth deriving from the Single Market would in itself do a great deal to improve the prospects of the other twelve OECD countries" (1989, p. 4).
b) Better Market Access for Third-Country Suppliers?

The elimination of intra-EC border controls and NTBs will also facilitate the distribution of imported goods (Schlecht, 1988, p. 5 s.). Products that have been imported into one EC country can be sold without restraints into other member states. As a consequence, foreign suppliers could optimize their distribution systems and lower distribution costs. Foreign investors, too, could optimize their production location within the EC and realize economies of scale (Krenzler, 1988, p. 243). Harmonization or mutual recognition of technical standards and regulations facilitates production conditions of foreign producers, too, whether they produce inside or outside the Community. They are no longer forced to offer up to twelve product variants (Balz, 1989, p. 473 s.; Koopmann, 1989a, p. 424).

c) Greater Flexibility and Readiness for Adjustment in the Single Market?

The Single Market programme aims at abolishing internal barriers to intra-Community trade and competition. Its realization will, therefore, eliminate artificial restraints of the readiness for adjustment and impediments to economic flexibility. Greater flexibility and readiness for adjustment would be a precondition for a liberal external trade regime of the EC. For open borders of the EC would increase adjustment needs. Thus, the completion of the Single Market, the readiness for adjustment and an open external trade regime are interdependent.

The readiness for adjustment would further be enhanced by favourable economic conditions within the Community. There are good reasons to expect higher growth and employment in the EC and improved competitiveness of European firms as a consequence of the market-oriented programme for 1992. Thus, there could be less pressure to use protectionist measures for objectives of internal economic policies. The demand for protectionism could decrease (McAllister, 1989, p. 18; Langer, 1989, p. 447 s.; Fieleke, 1989, p. 13 s.).
d) **Liberalization of the EC's Trade Policy in Response to Third Countries' Actions?**

As in the past, a successful integration of the European internal market could be imitated by other groups of countries. The outcome would then be a world economy comprising several free-trade communities, e.g. Europe, North America, Pacific Asia. Some observers see this as a chance for strengthening the liberal multilateralism (Preeg, 1989, p. 5). But this of course presupposes that the trade blocks do not fall in protectionist isolation. If this condition is given, the other trade blocks could induce the EC - via reciprocity deals - to liberalize its foreign trade regime.

Even under the status quo it is probable that trade partners will negotiate for better access to the European market - in the multilateral setting of the Uruguay Round and bilaterally. The EFTA countries, e.g., are developing strategies to participate in the advantages of the Single Market (Langer, 1989, p. 443 ss.). The East European countries have expressed their intention to enter into closer relations with the EC, and the Community has reacted by offering association treaties (Bolz, 1989, p. 490). Developing and newly industrialized countries so far have hardly been able to articulate their fears and wishes as to the external effects of the Single Market (Fasbender/Menck, 1989, p. 521).


Pressure and negotiations will be necessary to induce the EC to liberalize market access. The Commission is reluctant to extend the benefits of the internal liberalization "automatically and unilaterally" to third countries. It has announced to be ready for negotiations on a reciprocity basis only (EC Bulletin, 10-1988, para. 1.2.6 and 1.2.7).
5. **The Single Market and the EC's Position in the Uruguay Round and Afterwards**

For years the EC has been preoccupied by the Internal Market programme, and this preoccupation will last for the near future. EC officials tend to play down the external dimension of 1992. Negotiations, even discussions, on the accession of EFTA countries to the Community have been deliberately postponed. Only the revolutionary developments in Central and Eastern Europe have led the EC to exceptionally consider its external trade relations with these countries that have started political and economic reforms. Association of at least some of them may be agreed upon even before the completion of the Single Market. But apart from this, the Internal Market has absolute priority on the EC agenda.

This political preoccupation of the EC - the concentration on the internal problems - has created almost as much concern in third countries as the factual discrimination that is expected from the Single Market. The question is whether the EC, until the completion of the Single Market and afterwards, will loose interest in worldwide, multilateral liberalization and will lack a co-operative attitude in the GATT Uruguay Round.

Such an - only - inward-looking policy of the Community would be of crucial importance for the multilateral system. For the EC, as the world's biggest exporter and importer, has not only a decisive factual influence upon world trade flows. Together with the U.S., the Community is also one of the dominant actors in the GATT system. These dominant actors share a common responsibility for the functioning and the development of the multilateral trade system (Pelkmans, 1986, p. 83 ss.). The final outcome of the Uruguay Round and the structure of the Post-Uruguay GATT depend to a great deal upon the attitude of the EC.

The EC's position during the Uruguay Round so far does not show direct connections between the Single Market programme and the multilateral negotiations. The defensive attitude of the Community as to agricultural trade, safeguards, 'internal' subsidies and anti-dumping measures differs hardly from its position in past multilateral negotiations. The same can be said of the EC's offensive attitude as to tariff reductions,
trade-related aspects of intellectual property rights or trade in tropical products. The EC policy in these fields seems to be independent of the Single Market programme. Its determinant factors probably are different and not directly related to 1992: difficult adjustment problems in certain sectors, prevailing protectionist ideology in some member states, and protectionist pressure by certain interest groups.

The Single Market programme has probably influenced the EC's emphasis on reciprocity and on graduation of newly industrialized countries. The reluctance to liberalize unilaterally may be proof of the fact that the EC officials are increasingly aware of the importance of the European Market. This is certainly true of the services area where the Community insists on equivalent conditions of access to third countries's markets.

The EC's proposal to gradually liberalize trade in textiles and clothing and to integrate this sector into GATT fits into the Single Market programme since it would eliminate the disintegrating effects of Article 115 actions. Whether there is also a formal connection between internal and external strategy cannot be decided from outside.

At the present date it is not possible to make a definitive statement on the external effects of the Single Market programme and on the EC's trade diplomacy of the future. It is still an open question whether the liberal, multilateral tendencies among the EC member countries or the protectionist, centrist attitudes will prevail. If it is allowed to base a prognosis on past experience, neither a strict seclusion nor a generous opening of the Single Market is to be expected. Only a compromise as a result of package deals in the Council seems to be probable. The EC's trade policy shows constant features. Apparently the Single Market programme did not change dramatically these constants. This may partly be due to the inherent weaknesses of decision making in matters of trade policy and the precarious balance of liberal and interventionist tendencies within the EC (Molsberger, 1989). It does not mean, however, that this relative immobility of the EC trade policy should not cause concern: already the present trade regime of the Community comprises problematic bilateralist and selective measures (Henderson, 1989, p. 16).
On the other hand, the European Community is not at all the only sinner in a world of multilateral angels. What the EC has ventured in its Internal Market programme - a complete opening of all markets to foreign competition, if only of other member states - is without precedent. If the EC - contrary to the fears of a 'Fortress Europe' - offered the extension of Internal Market privileges to other GATT members on a multilateral and reciprocal basis - which one of the GATT states would really be willing to share this adventure?
References


Kotios, Angelos, and Josef Molsberger, "Progress and Problems in the Process of European Integration: The Last Eighteen Months in German Perspective", Paper prepared for the Symposium of the Confederation of European Economic Associations on European Economic Integration, Vienna,


Ludlow, Peter W., "Future of the International Trading System", Economic Impact, 1990/1, p. 4-10.


