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Chances for Great Britain in Europe

by George Thomson, Brussels*

There has been no shortage of argument about the likely effect on the British economy of membership of the European Community. The debate continues even now, when Britain is a fully-fledged member of the Community — reflecting hopes of advantage and fears of damage. As there are so many uncertainties about the evolution of Europe, it is at any time hard to analyse this subject exhaustively; and this is very much so now, when the Community is charting its path towards an economic and monetary, and even a political, union. This article therefore examines only the main economic forces which are likely to bear on Britain's prospects of development as a member of the Community, as well as the implications of the practical policies at present being formulated in the Community — especially in the industrial, monetary and regional fields.

"Static" and "Dynamic" Effects

At one time much was made of the beneficial effects of removing customs barriers between countries, in terms of the principle of comparative costs: the so-called "static" effects of integration. Certainly no economic assessment can lightly disregard this aspect. But the fact is that, thanks

to progress in GATT and other international fora, tariff liberalisation has by the early 1970s reached a fairly advanced stage. So, while there were still tariff barriers between Britain and the Six in certain products, on the whole they were fairly low. It would therefore be unrealistic to expect a major impact on the growth prospects of the British economy from the abolition of tariffs in the enlarged Community between 1973 and 1977.

Much more important than these "static" effects of the customs union are what have been called the "dynamic" effects. It is here that the greatest growth potential for the British economy seems to lie: in the greater economies of scale, the sharper competition and the higher investment levels that can be expected to flow from membership of the Community. It is too early to say whether these beneficial effects have yet begun, but one can assess what form they are likely to take.

Greater Economies of Scale

The advantages of greater economies of scale, in this case the opportunities provided by a continental market of some 250 mn consumers, are likely to be of major benefit to British industry, indeed during the "great debate" about British membership of the Community, British industrialists

were active in stressing this very point.

The motor manufacturing industry is an outstanding example of an industry which requires a large market to make full use of the potential economies of scale. One major British motor manufacturer has estimated that an investment expenditure of £ 50 mn is required on new models and another £ 50 mn on expansion and modernisation expenditure each year. This expenditure necessitates an annual output of some 2 mn vehicles. Clearly a market larger than the UK is required, particularly as a choice of models is important.

Membership of the Community will enable British manufacturers to share the advantages which their continental partners have enjoyed for some time — a 500 % increase in the domestic market, permitting a standardisation of car models, a rationalisation and single-unit assembly. One estimation is that these benefits will provide the British balance of trade with an additional £ 200—500 mn by the end of the transition period in 1978 from sales in the motor industry alone. The same process, of course, applies in other export-orientated industries, and although the exact economic impact is difficult to quantify, it seems that a significant increase in the British GNP

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which would not otherwise have taken place could be expected by 1978.

The other two dynamic effects – greater competition and increased investments – are much more difficult to assess. All Western European countries, including Britain and the Federal Republic of Germany, now have a mixed economy with a large public sector. Furthermore most private enterprise is represented by vast oligopolistic industrial empires, often multinational in character. Thus the realities of today have little in common with the perfectly competitive market which we know from our economic textbooks. Nor can present-day governments afford, because of social and political pressures, to adopt a "lame-duck" attitude, writing-off unprofitable industry, even if it means mass unemployment in a particular region. The real impact of what used to be called the "cold blast of competition" may therefore be doubted – it is likely to be only marginal.

The effect of a higher level of investment as a result of membership of the Community is also a somewhat subjective matter. This particular dynamic effect is related to expectations of businessmen, who feel that membership of the Community provides a better climate for investment. Taking again the British motor industry, it has been estimated that an absolute increase in investment of £ 10–20 mn will result from membership, in part no doubt a reflection of the utilisation of the larger market. A similar pattern can be expected in the component industries and while the precise relationship between economic growth and the level of investment is sometimes disputed, it is clear that the order of magnitude involved means that the likely beneficial effects of increased investment cannot be ignored.

The analysis of the possible dynamic effects provides a rela-

tively rosy picture of the implications of membership of the Community. The analysis however has to be carefully qualified. In particular the point needs to be made that the European Community is a long way from providing a fully integrated market. While basic obstacles to trade, such as tariffs and quotas, have indeed been largely abolished, many non-tariff barriers such as differentiated public purchasing policies, conflicting standards and measurements, different legal requirements and numerous other technical barriers, remain. Attempts to make use of the European market will therefore continue to face difficulties, a notable example being provided by the trade of branded pharmaceutical goods, where free movement is still hampered by the lack of mutual recognition with respect to marketing licences granted and diverse standards of qualification required for manufacture and distribution.

Elimination of Non-tariff Barriers

If the European Community is to provide the basis for a truly continental market it will have to progress from a customs union to an economic union proper, paying full attention to the requirements of industry as well as of agriculture.

The framework for progress in the elimination of non-tariff barriers was provided by the European Commission's Industrial Policy Memorandum, issued in May 1973. The memorandum seeks to promote the establishment of a European industrial base; in particular it attempts to re-launch a programme for the removal of technical barriers to trade according to a fixed timetable, to mitigate the effects of uncoordinated tendering for public contracts, to promote the establishment of competitive undertakings on a European scale by the implementation of a European Company Law, and to devote

special attention to certain industrial sectors, especially advanced technological industries such as the aerospace sector, as well as to sectors undergoing industrial decline. The ideas contained in this memorandum would, if implemented, allow not just Britain but all the member countries of the Community, to reap the full benefits of participation in the European enterprise and their adoption is clearly of the utmost importance.

Economic and Monetary Union

Another field where substantial barriers to trade remain, thereby restricting the benefits of British membership of the European Community, is in the operation of different currency areas and monetary policies within the Community, with the attendant exchange controls. Apart from increasing the difficulties of cross-border transfers, the existence of numerous monetary units creates uncertainty and risk in international trade. While currency risks can to some extent be hedged on the forward exchange market, they nevertheless present an additional expenditure and inconvenience which acts as a disincentive.

It is however not only the businessman who is hampered in his work by differing rates of exchange. The international civil servant is troubled by exactly the same headaches. Thus as the progress of European integration proceeds there will be a growing number of attempts, for example in the field of industrial policy, which has already been mentioned, to evolve a concerted action at the Community level with regard to the public sector; initiatives which will certainly be in the interest of the United Kingdom. These will all be impeded in the same way as a smooth running of the common agricultural policy is at present complicated by the constant re-adjustments and recalculations which have to be undertaken in the currency field

to maintain the common agricultural market. A common monetary unit would therefore produce a good many sighs of relief in the corridors of Whitehall and the Berlaymont in Brussels, not only in the accountants offices of the large companies.

Another consideration which arises is the urgent need to reform the international monetary system. It is unlikely that the creation of a Community currency would, on its own, introduce calm into the turbulent seas of the world currency markets. The Dollar, the Yen, not to mention the Swiss Franc and the Austrian Schilling are all too closely tied up in the oscillating waves of speculation. Any real solution clearly has to be found at the world level. However progress in the currency field at the Community level should introduce an element of stability. This stability will be all the more enhanced if the Community, through the European Monetary Cooperation Fund manages the European Monetary Union not only efficiently but imaginatively and in a progressive way, as is to be hoped, keeping in mind the needs of the rest of the world.

Mention must also be made of the barriers to trade caused by the operation of differential economic policies, especially fiscal policies. A multinational company, particularly, is obviously held back in its international dealings if the products it produces are taxed very differently in particular parts of the Community. Not only will its expenditure on the number of accountants and clerks it needs to employ increase, but, much more significant, it is likely to be hampered in the establishment of a European-wide marketing and therefore production network. It will therefore be unable to benefit fully from the economies of scale provided by a market of 250 mn people and economic growth will be accordingly slow-

er, a fact which the British entrepreneur realises as much as his continental colleague. The establishment of a real economic union, as well as a monetary one, is thus of equal importance.

Following the Paris Summit Conference of October 1972 the European Community is committed to the achievement of Economic and Monetary Union by 1980. Phase One of the progress towards monetary union is already in operation and Phase Two is due to come into being in January 1974.

The creation of an Economic and Monetary union, like the establishment of a proper industrial base, therefore, is something which could benefit the United Kingdom's economic development. However the prospect of such a Union also holds several distinct adjustment problems for the United Kingdom, which could prove to be a major impediment to effective integration, indeed may arrest it altogether unless countervailing action is taken.

Monetary Regional Problems

A risk that needs guarding against is that monetary integration will create a fundamental disequilibrium on a regional basis, instead of the traditional balance of payments problems experienced between countries. This is a danger which is especially acute for countries like Britain, Ireland and Italy, and it appears to be no coincidence that it was these three countries, all of which have had long-standing internal regional problems, which were unable to join the Community's joint float in March 1973. Thus if the relative costs position of some countries diverges from that of other member states, it would, in a common currency area, no longer be possible to use general price level adjustments through an employment of the exchange rate mechanism in order to correct the resulting imbalance.

If it is assumed that external receipts are kept in balance by adjustments of the common currency, then individual member countries must record their overall surpluses or deficits with their partners. A country in deficit can therefore only correct its deficit by a reduction in expenditure, and by creating unemployment. Clearly these are actions which would generate strong social and political pressures, causing great tensions in the country concerned.

Doubts in Short-term Measures

Furthermore, it is very doubtful if short-term policy measures as provided by traditional deflationary action would really solve the fundamental economic problems. Thus in Britain one of the basic economic problems has been the high rate of inflation, a rate which has until recently been above that of most other European countries and one which has persistently withstood deflationary measures taken to combat it by the government. This level of inflation is the result of a complex of historical, geographical, social and political forces.

Translated into economic terms, these considerations mean that if the Community with Britain as a member develops a common monetary system without adequate economic and common structural policies Britain may, in the absence of offsetting measures, be put in a situation of absolute disadvantage and therefore be vexed by major economic difficulties.

In this context the additional dimension of capital outflows from the less-prosperous regions needs to be considered. In the medium-to-long-term, however, it appears that the actual level of economic activity, rather than the level of interest rates, is the most important consideration. Thus, in the absence of positive Community action to the contrary investments would be placed in the

most prosperous, expanding regions, and not in those undergoing decline and really in need of them. The progress towards monetary union will clearly facilitate a greater mobility of capital and this means that there could be a serious danger to countries like the United Kingdom, which, unable to devalue their currency, were undergoing a period of severe restraint. The need for offsetting measures to prevent such detrimental developments therefore becomes apparent and the establishment of a regional policy, linked to the progress towards monetary union, becomes an essential prerequisite for such a union: it can be said that monetary union and regional policy are like Siamese twins — the one cannot do without the other!

A Common Regional Policy

The case for a common regional policy by the Community is certainly a powerful one; as far as Britain is concerned it is an irresistible one if the adjustment problems resulting from membership of the Community and the latter's progress towards monetary union are to be overcome. It is apparent that rapid advance towards such a union would be arrested if national economies had not undergone the transformations required to avoid excessive regional divergencies between the economies of the member states. The reduction, by the appropriate means, of regional imbalances is therefore a factor for accelerating those economic changes upon which the strength of monetary union will depend when it comes to abandoning recourse to parity changes as a way of restoring a fundamental balance. No member state can be expected to support the economic and monetary disciplines of such a union without the Community solidarity involved in the effective employment of a common regional policy; equally, member states must be prepared to accept the disci-

pline of economic and monetary union as a condition of this Community support.

The guidelines for a future common regional policy were provided by the Commission in a report on the regional problems in the enlarged Community, issued at the same time as the industrial policy memorandum.

The Regional Policy Report proposed the establishment of two basic instruments — a Regional Development Fund and a Committee for Regional Policy. The concept of the Fund dates back to the Paris Summit Conference, which made a fundamental decision in principle to launch an effective European regional policy and to make the Fund operational by January 1, 1974, thus recognising the essential link between regional policy and economic and monetary union, the latter being due to enter into its second phase concurrently. The Committee for Regional Policy will at the same time seek to coordinate national regional policies and to find ways of complementing them at the Community level.

It is important that the European regional policy should be seen as complementing, not substituting, efforts at the local and national levels. The resources at present being spent by member states on regional policy have at best prevented the gap between the regions from growing. Economic and monetary union could, unless there is a deliberate attempt to prevent this, widen the gap. It follows that if there is to be a fair share in the prosperity generated by membership of the new Europe, then the total resources devoted to regional policy, both Community resources and national resources must increase absolutely.

Conclusions

The present paper has attempted to indicate some of the economic opportunities open to

the United Kingdom as a result of its membership of the European Community, as well as outlining some of the fundamental problems which could arise. On the whole, a medium-to-long-term perspective has been adopted. There remain, of course, considerable short-term problems, regarding the adopting of CAP food price levels, the adherence to Community steel prices and the like. While not wanting to belittle the difficulties in respect of these sectors, it is nonetheless true to say that these problems are essentially of a temporary nature, especially if, as was pledged by the Commission following the 1973 CAP price level agreements, the agricultural policy is given a fundamental reappraisal, to see how it can be improved in its mechanisms and workings.

The real challenges — both in terms of opportunities and dangers — to the United Kingdom therefore present themselves in the longer term. To reap the full benefits of economic integration an effective industrial policy must be created to remove remaining non-tariff barriers to trade. Similarly the real benefits of monetary union cannot be realised unless a dynamic regional policy is established in order to overcome the difficult adjustment problems which are likely to arise. Other new policies are also required — social policies, energy policies, environmental policies. All these policies in turn have major political, not only economic, implications; they unequivocally point in the direction of a democratic, electorally responsible European executive, a development which is clearly necessary if the economic responsibilities are to be effectively met at the European level. Only if these challenges are faced up to by the member states of the Community will the real opportunities and benefits of the European Union be shared equally by all the peoples of the Community.