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Wilhelm Nölling*

The Impact of 1992 on European Integration and Relations with the United States

The end of 1992 has of late become quite a significant date in Europe. By this time the so-called Single European Market is to be created. The date and the topic are producing intensive debates all over the world. The purpose of this article is to describe certain trends which go along with the process of approaching 1992 and which could have significant implications for the development of the world economy. What intentions do the Europeans have? Where do the risks and conflicts lie? What should be done in order to achieve a harmonious development in the relations between the USA and Europe?

The proposed Single European Market represents an enormously important economic and political challenge, one which is attracting attention throughout the world. For instance, the Deputy US-Secretary of the Treasury Peter McPherson, in a speech given to the Institute for International Economics in Washington a few months ago, pronounced the following warning: "The creation of a single market that reserves 'Europe for Europeans' would be bad for Europe, for the United States, and for the multilateral economic system."

The German Foreign Minister Hans-Dietrich Genscher recently put forward the other side of the case: "When we tear down the barriers within the EC, we shall not erect higher barriers to the outside world – on the contrary. An internal market does not mean more protectionism spread over a larger area, but greater scope for development with more openness to the outside."

In Europe there is widespread agreement in the assessment of the problems facing the world economy. Unemployment in Europe is high and shows hardly any prospect of improving. Economic growth has been disappointingly slow, but some market improvement can be recorded for 1988. Only inflation appears to be under control. It is to be feared that Europe will lose its competitiveness in certain areas vis-à-vis Japan, the United States, and some developing countries as well. Not only the developing countries but also their trading partners are suffering as a result of the intractable Third

World debt problems and the stagnation that they cause. For years there has been concern about the ability of the USA to cope with its twin deficits, and about the consequences for the world economy of a continuation of present policies or of a decisive change in direction.

What opportunities are open to Europe in overcoming the problems of slow growth and unemployment sometimes referred to as "Eurosclerosis"? In my view, two complementary approaches must be developed. Firstly, active growth and employment policies must be adopted which strengthen both supply and demand. Secondly, the idea of a single market must be supported with the aim of revitalizing Europe and by that way helping to reduce the global trade and current account imbalances.

In keeping with its topic, this article concentrates on the second one, i.e. on the intentions and problems associated with the single market. As Herr Genscher said recently: "In the European Community a process of virtually inconceivable dynamism is taking place – this process is now irreversible. The Single European Market will be an engine for growth in the world economy and above all in the whole of Europe. The development of the European Community is an expression of the desire of the European democracies to assert themselves." And the German Vice-President of the EC Commission, Karl-Heinz Narjes, has described the European Internal Market as the greatest deregulation project in recent economic history.

With the introduction of the Single European Act on 1st July, 1987, the EC member states committed themselves to the creation of a European Internal Market by 1992. The term internal market is used to describe the

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Community as an economic region without internal frontiers in which the free movement of goods, services, persons and capital has at last been realized. A broader definition has also been under discussion – in other words, a European economic region which also includes the EFTA countries Switzerland, Austria, Finland, Norway, Sweden and Iceland.

Concrete discussions about the internal market project go back to 1982. A major stimulus was the “White Paper” put out by the EC Commission in 1985. This “White Paper” is remarkable for two reasons: Firstly, it describes Europe’s enormous deficiencies in terms of integration, and contains a precise timetable of all the measures necessary between now and 1992 in order to realize the single market. (This timetable by the way accounts for no fewer than 6 pages!) Secondly, the White Paper devotes only one single sentence to implications of the single market for the Community’s policies of trade with non-member countries. It reads: “In addition, the Community’s trading identity must be strengthened, so that other trading partners will not be offered the benefits from the enlarged Community market without themselves being forced to make concessions.”

Still a Long Way to Go

It may seem surprising that the Europeans have only recently resolved to create a Single European Market. Last year, after all, the Community proudly celebrated the 30th anniversary of the Treaty of Rome – which marks its foundation – and the “four freedoms” enshrined therein – the free movement of goods, services, people and capital within the Community.

It is for quite a number of reasons that Europe has not succeeded in achieving full integration so far. However, significant moves have been made. For instance, customs duties between the EC member states were abolished 18 months ahead of schedule. Quantitative trade restrictions have been significantly reduced, and a common external tariff has been in force since 1st July,

1968. Mention must also be made of the Community’s common agricultural policy, even though it is still beset with serious problems. But there is still a long way to go before a single market is created. In the White Paper referred to above, the EC Commission listed 286 individual measures necessary in order to realize the Single European Market by the end of 1992. These measures fall into five different categories:

- the abolition of border controls within the EC,
- the removal of technical restrictions and other non-tariff barriers,
- the harmonization of fiscal divergencies,
- the liberalization of public procurement,
- and the necessary deregulation of the financial sector.

The EC Commission has so far put forward some 210 proposals, 80 of which have already been adopted by the Council of Ministers. Following approval by the Council – if necessary, this can in most cases be done on the basis of a majority vote – directives must be transformed into national law. This democratic process takes time, and not least for this reason it will not be easy to meet the deadline in 1992.

A Heterogeneous Set of Countries

Sometimes one loses sight of the fact that Europe is still a heterogeneous set of countries with different cultures, languages and religions, different levels of prosperity and economic development, and different economic structures. The member states also differ radically from each other in terms of social welfare legislation.

For example, worker participation arrangements vary from country to country, as does the legislation governing unfair dismissal, industrial health and safety, health insurance, and pensions. There is general agreement that the high level of social welfare enjoyed

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by West Germany cannot serve as a standard for the other member states in the Community. It is unclear whether welfare standards should – or can – be harmonized at a medium level, thus ensuring equal competition. The German Trade Union Federation (DGB) has made its position on this issue very clear. In the words of its chairman, the trade unions must take every step to ensure that “the internal market does not pave the way for social dumping”. Some harmonization of labour and social welfare legislation will be one of the most difficult tasks in the realization of the single market.

It must also be borne in mind that over the centuries highly differentiated national markets have developed, each with its own tastes and consumer preferences. The complete liberalization of these markets, the harmonization of indirect taxes – absolutely essential according to Commission President Delors – plus a wide range of other necessary measures will cut deeply into national sovereignty and are bound to meet with stiff opposition. Nevertheless, the chances are still good that most of the internal market will be realized by the end of 1992. “Project 1992” has already gathered considerable momentum and Europe’s politicians, businessmen and consumers place great hopes and expectations in the single market.

Economic Benefits of the Single Market

A European internal market with 320 million inhabitants will enable the Community to unleash new market forces and competitive strengths, thus preparing the way for increased growth. In terms of the number of consumers, Europe would be by far the largest single economic region in the industrialized world, well ahead of the United States (230 million inhabitants) and Japan (120 million). Because of the elimination of internal border formalities and the creation of larger markets considerable economies of scale will be gained in the production and distribution of goods and services. The benefits of this will be lower consumer prices, a higher standard of living, and a greater demand potential.

A great many private companies are already preparing for the changes in the individual goods and services markets which will be brought about by market integration. Competition for favourable starting positions has already begun. We can now observe an increase in cross-border takeovers, investments and joint ventures. The business community is focusing more and more attention on the chances and risks of this particular undertaking.

How great will the economic benefits of the Single Market be? The so-called Cecchini report

commissioned by the EC comes to the conclusion that, after a transitional period of about 6 years, the EC-GDP would be 4.5 to 7 percentage points above the level without the realization of the internal market. Between 1.8 and 5 million additional jobs would be created, while the rate of price increases would be roughly 6 percentage points lower. Even if these figures represent the upper limits of what seems possible, the internal market will most likely stimulate economic growth remarkably. At the same time there is widespread anxiety about being unprepared and about the frictions the single market is bound to create. Structural upheavals are to be expected in many sectors of the European economy. In order to keep developments under control there would therefore seem to be a strong case for an active structural policy embedded in an environment of a steady and reliable expansion of world trade. Without such political efforts the concept of an internal market might soon encounter serious difficulties.

EC – US Relations

As regards the various issues affecting relations between the planned European Internal Market and the United States, Europeans are well aware that the economic links between Europe and the USA are of enormous importance for both sides. In terms of combined bilateral trade volume, the EC is the USA’s most important trading partner, ahead of both Canada and Japan. In 1987, the combined total of imports and exports amounted to 145 billion US dollars. Since 1975, the European Community’s share of total US imports rose from 17.3 to 20 %. Over the same period the EC’s share of American exports also increased – from 21.4 to 24 %. It is true that the bulk of the Community’s trade is conducted within its own boundaries.

Between 1960 and 1987 the proportion of intra-Community trade climbed from 25 % to 59 %. Nevertheless, exports to the USA are important and have increased considerably. Between 1975 and 1987 the share of total EC exports accounted for by the USA rose from 5.3 to 8.7 %. The USA is still the Community’s most important external trading partner. It should be recognized, however, that – related to total trading volume – the EC is more important for the USA than the USA is for the EC.

It should also be recognized that other factors play a role in the formulation of a common EC trade policy – for example, the EC’s relations with EFTA, the Eastern bloc and Japan. Let us concentrate, however, on the EC’s trade relations with the USA and some of the related problems. There can be no denying that the general

climate has worsened noticeably. The EC in general and West Germany in particular have been at the receiving end of American criticism and demands that European markets should be stimulated and opened up. Trade disputes have become more frequent and more intense. The list of controversial issues is long. First and foremost there is the all-important question of agriculture. US exports of agricultural products to the European Community fell substantially. Other major issues are the subsidies for the European Airbus, the telecommunications sector, as well as the entire field of high technology. To what extent will the Single European Market place *additional strain* on trade relations between the United States and the European Community? How far has the debate progressed, and what answers must be given in the interests of fruitful co-operation? Where do the problems lie and what standpoint should one adopt?

New Opportunities for American Companies

First of all, Americans should recognize that the realization of the Single Market will open up new opportunities for American companies. As from 1993 these companies will have to deal with just one single market – instead of 12 individual markets, each one with its own regulations, technical standards, administrative procedures and barriers to market access. The markets will not only be larger, but also more clearly structured. Product planning and market strategies will operate more effectively. In 1987 exports accounted for only 9.5% of America's GNP. The corresponding figure for West Germany is 31.5%, for Japan 12.7% and for the Netherlands almost 52%. America should do all it can to use the enlarged European market in order to decrease its balance of payments deficit and to eliminate the existing imbalances.

It should be remembered that a great many foreign companies – including major US corporations such as IBM, General Motors, Ford, AT & T, plus many US banks – already have a strong foothold in the European market, either in the form of branches and subsidiaries or else in the form of collaborative ventures with European firms. These companies have high hopes and expectations of the single market. And rightly so. There is no reason to delay investment decisions for Europe at present because of uncertainty with regard to European trade policies. On the contrary – there is every reason to expect that such decisions will be far-sighted and such investments will be rewarding in the long run.

Of course, American exporters will have access to new opportunities only if European markets remain

open to products from non-EC countries. What developments can be expected here? Will we end up with the much-feared "Fortress Europe"? The Single Market will depend on the existence of a common trade policy towards third countries. Since 1969, responsibility for foreign trade policy has resided with the Community. In accordance with Article 113 of the EEC Treaty "... common commercial policy shall be based on uniform principles, particularly in regard to changes in tariff rates, the conclusion of tariff and trade agreements, the achievement of uniformity in measures of liberalization, export policy and measures to protect trade such as those to be taken in case of dumping or subsidies".

So far almost all of the Community's moves towards the realization of a single market have been directed inwards. As mentioned above, the relevant policy document contains only one sentence about foreign trade relations. Astonishingly enough, the shape of the EC's external relations after 1992 only became a topic of discussion a few months ago. The Commission has appointed a working party to develop a joint Community position on trade policy. At the present stage it is only possible to describe a few problem areas and alternative solutions.

Blank Spots in EC Trade Policy

To start with, the joint trade policy of the EC as proposed in the EEC Treaty still has numerous blank spots. For example, there are still a host of bilateral trade restrictions in force between EC member states and third countries (either individually or collectively agreed upon).

The automobile industry is a case in point. France, Italy, Spain, Great Britain and Portugal all impose restrictions of varying degrees on car imports from outside the EC. In Italy, for example, Japanese imports may account for only 1% of all new-car registrations in any one year. In France the corresponding import quota is 3%, and in the United Kingdom 11%. West Germany imposes no restrictions whatsoever on car imports from non-EC countries. However, Germany has for many years benefitted indirectly from the large, protected markets in France, Italy and the UK. By exporting to these countries, German car manufacturers have been able to offset some of the sales lost to Japanese imports on the home market.

Bilateral import restrictions cannot possibly be maintained within the framework of a Single European Market. Import quotas depend for their effectiveness on internal border controls. These, however, will be abolished as from the end of 1992. For this reason

regional import quotas must either be done away with altogether, or else replaced by Community-wide arrangements. West Germany's position is clear – it is *against* European isolationism and *for* open markets worldwide. However, this view is not shared throughout Europe. Some member states, faced with increased competition and under pressure to adapt to a Europe without internal frontiers, want only a partial opening of the Internal Market to the rest of the world.

No-one can absolutely rule out that, after 1992, temporary import protection measures will be introduced at a Community level for individual products. This would be the case if, for example, individual member states suffer particular economic difficulties as a result of the complete liberalization – both internally and externally – of European markets. Such import restrictions would e.g. have a direct effect on German-American trade relations, as West Germany would then be forced to adhere to a more protectionist stance than at present. In addition, there could be a shift in trade flows between EC countries and non-EC trading partners in the event that access to national markets of member states is affected by the imposition of Community-wide import regulations.

Community import quotas should, however, if at all only be a transitional solution, strictly limited in terms of time. In order to avoid the widespread tendency of self-perpetuation, the exact period of application must be laid down in advance. To this end the Community should carry out detailed talks with its major external trading partners – best of all during the current round of GATT negotiations.

The 8th round of GATT talks (the so-called “Uruguay round”) is in progress at present. In addition to liberalization and cuts in customs duties, a major topic is the development of a common, balanced approach towards solving the fundamental problems of world trade and the world economy. The most important issues are the liberalization of trade in services; intellectual property rights; agriculture; safeguard clauses; as well as the general functioning of GATT itself and its arbitration procedures. So far, the emphasis has been on the identification of trade problems. But now the most difficult phase of the 8th GATT round is about to begin. An interim progress report is due to be given in Montreal in December. The results are informally said to be disappointing. A greater willingness for dialogue and compromise will be essential if the GATT talks are to make significant progress. And with regard to the development of the external trade policy of the EC it should be closely interlocked with progress in the GATT talks.

Reciprocity versus National Treatment

There has been growing dispute between the US government and the European Community about external aspects of the Single Market. The already mentioned Peter McPherson and the American Ambassador to West Germany, Richard Burt, have recently warned the Europeans against closing off their markets and against making access to their markets depend on the fulfilment of *reciprocal* demands. This means, for example, that American companies would be permitted to carry out only those business transactions on European markets which are also open to European firms in the USA. McPherson has advised the Europeans to replace the principle of reciprocity with that of national treatment. National treatment implies that domestic and foreign companies should receive equal treatment on domestic markets, irrespective of the particular situation on the corresponding foreign markets. Two opposing principles are therefore at stake in the dispute between the USA and Europe.

The solution should lie somewhere between the two. When applied to financial services, the principle of national treatment seems to have a lot in its favour. Financial markets differ considerably from country to country in terms of regulations and supervisory procedures. Under these circumstances, the reciprocity principle would reduce foreign trade relations to the lowest common denominator. So, there is no reason why the principle of national treatment should not be applied to certain market segments and areas of European-American trade relations.

On the other hand, the US government should also recognize that – given the new opportunities available to American companies in an enlarged European market – we should not depart completely from the principle of reciprocity. It is hard to see why this principle should have adverse effects on liberal trade relations in general. It is the individual circumstances and market conditions that count. And in this context Europeans were quite surprised to discover that the new US Trade Bill also contains such reciprocity clauses. The seriousness of the legislative intentions can be seen from the following sentences in the transcript of the debate between Senators Bentsen and Quayle. Senator Bentsen said: “But we passed a trade bill that has this premise: That any country that has full access to our markets – we’re entitled to full access to their markets. Now that means that we are going to stand tough for America and we are going to protect those jobs and we are going to push American products.”

But one also has the impression that the whole

discussion has a certain tactical background, especially with regard to the current round of GATT negotiations and how to deal with Japan and the NICs. The best way of ensuring liberal trading relations in the future is to adopt a level-headed approach and to proceed with intensive multilateral consultations which give due consideration to the rights and interests of the other side.

Monetary Integration

Finally, a few remarks about monetary integration in Europe. The preparations for the Single Market quite rightly extend beyond trade matters and aim at creating an integrated monetary region in Europe. The free movement of capital is a major element in the internal market programme and is due to be realized by 1990. In this respect it is encouraging to see that all European governments have recently committed themselves to open up or to keep their capital markets open to the rest of the world! However, one should bear in mind that the functioning of the EMS so far was certainly made possible to some extent because restrictions on capital movements were in effect in major countries. In order to preserve the achievements of the EMS it would seem advisable to watch the developments on the financial markets carefully. Therefore it is agreed upon to proceed only gradually in this highly sensitive field.

It should be clear to everybody that the more stable the exchange rates between the individual currencies, the better the Internal Market will function and the greater will its economic benefits be. Yet, we do not necessarily need a common currency for the initial stage and functioning of the Internal Market. Not that this would not be desirable in itself, and should be striven for incessantly. But the barriers to the introduction of such a currency seem to be insurmountably high at present.

Even after the Internal Market has been established, there will still be a need for exchange rate realignments as a kind of safety valve for as long as the major differences between the individual EC countries persist – for example, in terms of inflation rates and balance of payments as well as public sector deficits. Another highly important factor for economic policy consideration in West Germany is the continuation of global co-operation on exchange rates of the major monetary areas – the dollar, deutschmark and yen zone. Since the Plaza/Louvre Agreements exchange rate co-operation has acquired a new quality, not least because the US government is no longer indifferent to the fate of its currency, and because all governments have realized that wild exchange rate fluctuations are detrimental to world trade and have to be stabilized accordingly.

At present, exchange rates correspond more or less to purchasing power parities so that they could help to reduce the imbalances in international trade. In Germany, however, it is believed that a further slight rise in the value of the deutschmark would be more likely to make a positive contribution – more so at least than a new expectation of a slight devaluation of the deutschmark. The Bundesbank has tried to contribute to the emergence of stabilizing exchange rate expectations by means of interest rate differentials or by interventions to sell off dollars. Yet, the way interventions were carried out (or not) has not been entirely satisfactory, nor have the results. In general, however, exchange rates at present are believed to be at roughly the right level. More so than in the past, every effort must be made to prevent massive exchange rate fluctuations.

Realistic Vision

The Single European Market is one of the inspiring visions of modern times. Visions that deserve this title are major undertakings which can advance mankind but at the same time run the risk of failure. To succeed, such visions demand great effort, courage and self-confidence on the part of all concerned. The European Commission marks the beginning of a supranational government embracing 12 more or less sovereign states. Each of these states has its own government, political parties, parliament and special interest groups. Each is dependent on public opinion. And public opinion is in turn influenced by economic success or failure, especially success or failure of the Single Market.

In view of Europe's snail-like pace of development over the past three decades, the four years left until the realization of the Internal Market are a very short time-span – especially in view of the number and scope of the agreements that have yet to be reached. The success of the single market programme is subject to two interdependent conditions, which are not solely under Europe's control: firstly, the growth of the world economy (which means more than just the absence of recession); and secondly, a better working economic co-operation between Europe, the USA, and Japan.

Given Europe's ambitious plans and realizing that the success of this policy will be embedded in global economic conditions as well as affecting them enormously, Europe can be expected to show great willingness to co-operate and engage in dialogue. Americans should recognize this fact and for their part make every effort to ensure their own economic and financial problems will be solved hand in hand with establishing mutually agreeable trade relations with the EC.