

Donges, Juergen B.

**Working Paper — Digitized Version**

## From six to ten and beyond: The European Community at the crossroads

Kiel Working Paper, No. 195

**Provided in Cooperation with:**

Kiel Institute for the World Economy – Leibniz Center for Research on Global Economic Challenges

*Suggested Citation:* Donges, Juergen B. (1983) : From six to ten and beyond: The European Community at the crossroads, Kiel Working Paper, No. 195, Kiel Institute of World Economics (IfW), Kiel

This Version is available at:

<https://hdl.handle.net/10419/46974>

**Standard-Nutzungsbedingungen:**

Die Dokumente auf EconStor dürfen zu eigenen wissenschaftlichen Zwecken und zum Privatgebrauch gespeichert und kopiert werden.

Sie dürfen die Dokumente nicht für öffentliche oder kommerzielle Zwecke vervielfältigen, öffentlich ausstellen, öffentlich zugänglich machen, vertreiben oder anderweitig nutzen.

Sofern die Verfasser die Dokumente unter Open-Content-Lizenzen (insbesondere CC-Lizenzen) zur Verfügung gestellt haben sollten, gelten abweichend von diesen Nutzungsbedingungen die in der dort genannten Lizenz gewährten Nutzungsrechte.

**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.*

# Kieler Arbeitspapiere Kiel Working Papers

Working Paper No. 195

FROM SIX TO TEN AND BEYOND  
The European Community at the Crossroads

by

Juergen B. Donges

Institut für Weltwirtschaft an der Universität Kiel

ISSN 0342 - 0787

Kiel Institute of World Economics  
Department I  
Düsternbrooker Weg 120, 2300 Kiel

Working Paper No. 195

FROM SIX TO TEN AND BEYOND  
The European Community at the Crossroads

by  
Juergen B. Donges

December 1983

A<sub>9</sub> 70 84 Kf Kiel  
Weltwirtschaft  
Kiel

Kiel Working Papers are preliminary papers written by staff members of the Kiel Institute of World Economics. Responsibility for contents and distribution rests with the author. Critical comments and suggestions for improvement are welcome. Quotations should be cleared with the author.

FROM SIX TO TEN AND BEYOND  
The European Community at the Crossroads\*

I. Introduction

The European Community (EC) is in a mess.

- Politically, the cohesion among member governments is weak, the creation of a European Union, which for many was the leading idea in the shaping of the Treaty of Rome twenty-five years ago, is more remote than ever, and the capacity to exert a strong influence on international affairs remains small.
  
- Economically, the EC is plagued by recurrent budgetary problems, it wavers between keeping open to the world economy and retreating into protectionism, and it actively spins the carousel of market interventions and cartelization.
  
- Institutionally, there have continuously been quarrels between the Council of Ministers, the Commission and the European Parliament about the aims of the EC and the means to achieve them, whereas an alarming excess capacity in bureaucracy has emerged which leaves much time for administering itself and for working out unnecessarily complicated regulations, and which stimulate the quest for more responsibilities at the supra-national level.

One cannot help feeling that much of the present integration in Europe is due to inertia rather than to conviction. It is more the rule than the exception that the Council of Ministers (or of Heads of State or Government) rests content

---

\* Revised version of a lecture delivered at the Sixth Annual Conference on "The EEC and the World Economy" of the Royal Irish Academy on 17-18 November 1983 in Dublin.

with agreements at the level of the lowest common denominator, inefficient as they may be.

According to a widely held view the difficulties which the EC is facing are to be seen against the background of the slowness of economic growth and the soaring unemployment in the member states (as in the industrial world as a whole) which has persisted since the early seventies. This amounts to saying that achievements in the integration process are only conceivable in a period of spreading and lasting prosperity, and that basically the Community is not a community at all but a group of nation states, each of which sticks to its own "national interests" (as they are perceived) and pursues them, if necessary, at the expense of others. In such a case it becomes difficult to understand the *raison d'être* of the EC. Each of the countries could reap the benefits of greater markets and specialization by opening up its economy to international trade and factor movements to the extent considered appropriate. The integration process then would develop along with the deepening of the international division of labour between countries. This would not, of course, prevent governments from resorting to some type of beggar-my-neighbour policies in case of domestic economic problems. But at least it would push bureaucracy back and remove the authority for shaping and applying common economic policies which contradict economic logic about the efficient use of scarce resources in market-oriented economies.

I shall argue instead that the impasse in the EC has much deeper roots<sup>1</sup>. They are related to constitutional weaknesses as well as to incorrect assignments between the Community and the member state governments. They already became apparent in the Community of the Six. The two subsequent enlargements

---

<sup>1</sup> The presentation draws extensively on J.B. Donges et al., *The Second Enlargement of the European Community - Adjustment Requirements and Challenges for Policy Reform* (Tübingen: J.C.B. Mohr, 1982, for the Kiel Institute of World Economics).

(in 1973 and 1981) have increased the trouble, but mainly because the new member states had to accept the "acquis communautaire", however doubtful its value may be in some cases. The same holds with regard to the incorporation of Portugal and Spain, which has been negotiated for years, with an increasingly uncertain outlook. The fact that the levels of economic development in these countries (and in Greece as well) are lower than the Community's average might justify more preoccupation among the negotiating parties than the relative underdevelopment of Italy and Ireland did in the late fifties and early seventies, respectively. However, the EC could go along with a greater economic heterogeneity if it were not for the obstinacy of some member state governments and some Eurocrats to preserve at any costs rules and policies which evidently are ineffective or distorting but can be presented to the public as indispensable symbols of European unity. The Common Agricultural Policy (CAP), the Regional Development Fund and the European Monetary System (EMS) are cases in point.

The purpose of this paper is to assess the main factors causing the impasse which the EC has reached. The next section examines the lack of consensus of the member states on the aims of the EC and on the means to achieve them. Subsequently, this is related to the EC enlargement. Finally, recommendations will be made on major policy issues in order to provide a new stimulus to the integration process in Western Europe.

## II. The Road into Deadlock

It is useful to recall that the development of the EC was based on three principles:

- the creation of a common market,

- the harmonization of economic policies and
- the pursuance of financial solidarity.

The two first principles are postulated explicitly in the founding treaties. The third one results from the objective, assigned to the EC, to reduce regional inequalities and to provide for balanced economic growth of the member states.

#### 1. On the Common Market

Out of these three principles, the former Six found it easiest to establish the Common Market; it is clear enough in retrospect that it was very helpful that no further inter-governmental agreements were required. By implication, the Common Market was to imply the creation of an international public good from which each member state could benefit without diminishing the wealth of others and from the use of which no country could be excluded. On theoretical grounds, specialization, economies of scale and intensified competition could be predicted to boost trade, incite investment and improve efficiency at the micro and macro level.

These expectations were to come true, as the rapid trade expansion within the Community (predominantly by "trade creation" rather than "trade diversion") and the sustained economic growth of the founding member states during the first fifteen years suggest. Though national economic policies remained crucial in determining overall economic performance in each country, the Treaty of Rome laid the ground for reducing foreign trade policy-induced risks for entrepreneurs, so that expectations on long-term investment improved and the scope for efficient horizontal and vertical specialization within the Community widened.

Notwithstanding this achievement, the Six did not manage to make trade liberalization binding and they were not pre-

pared to remove all internal barriers to trade. Tariffs and quotas were occasionally reimposed on balance-of-payments or market-disruption grounds. Important non-tariff barriers were maintained, especially in the form of national technical standards and norms, of selective public procurement policies, and of subsidies to domestic industries. A Common Market for services and factor movements has effectively been thwarted by protectionist national laws in various areas. Since the seventies matters have become worse. Open and convert subsidies constitute now a major instrument in distorting trade flows within the EC; chicanery in customs clearance procedures spreads; "voluntary" import restraints have come into being; and the agricultural markets have de facto be renationalized since 1969 when a system of border taxes and subsidies (officially called "monetary compensatory amounts") was introduced with the aim of delinking the "green" exchange rates from the currencies' market value.

Obviously, once the stock of common actions as laid down in the founding treaties was exhausted, no new, mutually acceptable conceptions for moving forward emerged. The new member countries did not provide any stimulus in this regard either. The result is that both the Council and the Commission have degenerated to a producer of technicalities and an operator of administrative fine tuning, with an astonishing neglect of the dangers to which they are exposing the solidity of the Community.

## 2. On Policy Harmonization

The lack of consensus among member states is also evident with regard to the second principle mentioned above - policy harmonization. Ever since the creation of the Community, individual governments have adhered to national preference functions, in particular as between price stability and full employment, and they have chosen a different policy-mix, in



particular with regard to fiscal and monetary policies, even when the aims were similar. In general, Germany has attached the highest priority to restraining inflation, whereas France has been more concerned about avoiding unemployment; in the other countries the ranking of priorities has varied over time, depending on which political party was in power.

As long as the national counter-cyclical and basic medium-term policies are not effectively coordinated and inflation rates differ, the Community is affected by recurrent balance-of-payment disequilibria of member states, which call for exchange rate adjustment. If the national authorities do not devalue or revalue their currency at the right time and to the extent needed, considerable distortions in resource allocation are bound to appear. On the one hand, both export industries and import substituting activities in countries with a strong but not appreciating currency will be artificially stimulated; the opposite occurs in countries with a weak but not depreciating currency. On the other hand, the member states concerned about price level stability will import inflation from inflation-prone partner countries ("adjustment inflation") and they will thereby have to put up with the well-known distortions of investment patterns which are typically associated with inflation.

The former Six made this experience time and again during the sixties. By resorting to trade restrictions and foreign-exchange control in order to alleviate the impact of currency over- or undervaluation, they created new distortions and made for increased uncertainty in investment decisions. At that time, the Council of Ministers thought that a monetary union should be established (though it is not provided for by the Treaty of Rome), which would make the adjustment to balance-of-payments disequilibria smoother (Werner Plan). But it turned out that no member country was really willing to satisfy an essential prerequisite for a monetary union to function under a system of pegged exchange rates: the transfer

of national competence over key economic policies to a Community authority. The "currency snakes" of the seventies failed for the same reason. Nor will the EMS, which came into operation early in 1979, be able to force the member state governments to co-ordinate their economic policies. The EMS does not provide for sanctions in case of infringing agreed rules and it creates "moral hazard" through the credit facilities at preferential terms which the central banks have to grant to each other in order to defend the peg. Moreover, its very existence is not assured: each country can leave the EMS if it feels that its own interests are not served (the French Government has already made a threat of withdrawal when the seventh realignment of currency parities was due in March 1983); and by the same token, countries need not join it (at present, the United Kingdom and Greece do not participate). Under such conditions on intergovernmental policy coordination in the Community any attempt to peg the exchange rates among the member country currencies constitutes a cause of economic disintegration rather than integration, and gives rise to political conflicts among member country governments.

### 3. On Financial Solidarity

Things went worse in connection with the application of the principle of financial solidarity. Originally, the Six set up this principle with the aim of bringing about redistributational policies at the Community level which reduce regional differences in income and employment opportunities. But soon two fundamental weaknesses appeared. One is the temptation for each member state government to call, in the pursuit of national objectives, for common policies and thereby to commit other members to the co-financing of those policies; this leads to a competition for an expansion of common policies, irrespectively of whether or not they make economic sense. The other weakness is the propensity of politicians, which have to justify before their constituency

the undertaking of expenditures, to promise that comparable benefits will accrue in return ("juste retour" doctrine); this easily becomes a source of claims on the EC's Common Budget which exceed budget revenues.

As a matter of fact, intergovernmental quarrels over common policies and over "fair" burden-sharing has plagued the Community since the mid-sixties. Most controversies were and are related, directly and indirectly, to the CAP. This policy, by choosing price-support measures and purchasing guarantees to farmers in pursuit of the objective of redistributing income to agriculture, not only has led to plain waste of resources and has imposed ever-increasing commitments on the Community's budget spending (which by itself is already a compelling reason for concern), but the CAP also has ended up with a ranking of income transfers between the member countries which does not strictly reflect the strength or the weakness of particular economies. In general, a country gains the more, the greater it is specialized in producing highly protected commodities and the more it generates export surpluses (mainly France), thereby paying less in terms of import levies than it receives in terms of export refunds; losers are those member countries which have low levels of self-sufficiency in food and therefore export little and depend largely on imports (mainly the United Kingdom). Equally embarrassing is the fact that Germany, though a net payer, can improve its transfer balance by producing surpluses of milk powder and butter; or that the Netherlands, which have a relatively high per capita income, receive more transfer payments in terms of agricultural value added than Italy, whose per capita income is much lower.

It should be recalled that such implications of the agrofincial system already in 1965 provoked demands by the Benelux countries to reshape the CAP and to make it less expensive. These demands and the harsh rejection by the

French Government, which temporarily even withdraw from the Council ("empty chair" policy), plunged the EC into its first institutional crisis. The famous "agreement to disagree", taken at the Luxembourg Summit in 1966, was then to prevent any serious reform of the CAP up to now. Meanwhile, the wealthy Benelux countries have got a positive transfer balance themselves. After the first enlargement of the Community it seemed that the United Kingdom would take the leadership on the road to the needed reforms; but soon it turned out that the costs of the CAP and its economic distortions were attacked only rhetorically, while much political pressure was exerted in order to obtain relief of financial contributions ("money-back" policy). As the British Government - not the British citizens - has had some success, the Greek Government now tries to play a similar game though the country already is a net beneficiary of the CAP-related redistribution within the Community. While the principle of financial solidarity may be essential for the member state governments to abide by the founding treaties, the way it is exercised in practice and the deleterious economic effects it reveals cannot but discredit the concept, if not the EC itself.

The experience with the CAP is only one example which shows that the Community has so far been unable or unwilling to find meaningful concepts for obtaining financial solidarity. Inefficient sectoral policies as a means of income redistribution have been applied also in other fields, such as textiles and clothing (since the early sixties) as well as steel (since 1977). In both cases the protection of domestic industries against imports from third countries is the chosen policy instrument; in the case of the steel industry, which operates as a cartel, the Commission has also established minimum prices. As with agriculture, the pursuance of financial solidarity by means of sectoral protection and price regulation imposes considerable costs on consumers within the Community; it perpetuates the structural weakness

of the regions in which the ailing industries are concentrated; it constitutes a tax on dynamic activities; and it generates continuous debates among the member countries about a "fair" distribution of production capacities (external conflicts apart). Moreover, the resort to sectoral policies has paved the way for other industries which refuse to adjust to changing comparative Advantages to claim Community-wide assistance (on the grounds of "equal treatment"), in which case the Common Market would be eroded further.

### III. Problems Associated with Further Enlargement

If substantial reforms are not undertaken, the enlargement of the EC to a Community of Twelve is likely to exacerbate current difficulties. Following their entry to the EC, Portugal and Spain will behave in the same way as the present Ten, i.e., they will try to enforce their own interests and will, if necessary, make use in the Council of the vetoing power which the unanimity principle confers. The policy-making process at the Community level will be obstructed even more than in the past. The new entrants, as their predecessors, can be expected to insist on financial solidarity and to request, on this account, the application of the CAP on their products and the concession of regional and sectoral aid. The present member states will ask for some form of compensation for the market losses they may suffer as a result of the increase in competition (most notably with respect to agriculture). This inevitably would lead to new, disintegrating tensions among governments. To some extent, such conflicts may be "solved" by means of policies which hurt third countries, thereby provoking external conflicts.

## 1. Potential for Internal Conflicts

In all probability, the enlargement of the Community will generate important shifts in comparative advantage (in addition to those occurring for other reasons). With regard to manufacturing, the shifts will be especially pronounced in those "sensitive" areas in which the present Community is already facing a considerable competitive pressure by low-priced supplies from third countries. Relatively labour-intensive products (such as textiles and clothing or shoes and leather manufactures) as well as standardized capital-intensive goods (such as steel and ships) are cases in point. Particularly the Spanish industry has a marked export potential in these areas. The present member state governments could find themselves under pressure from the trade-impacted interest groups to protect them against the newcomers, either by safeguard provisions or by subsidies. By yielding to such pressures, the governments would erode the Common Market further. If restrictions on intra-Community trade are avoided, there is still the danger that the absorption of additional supplies from the southern member countries would be carried out at the expense of third countries, particularly developing countries, by increasing the external levels of protection. The current, French-inspired ideas of taking recourse to a "protectionnisme de zone" in order to develop new, high-technology industries, could suit also the interests of the inefficient industries within the present Community.

Turning to agriculture, shifts in comparative advantage will result from the fact that the new entrants, though plagued by several structural and technological constraints, have a considerable potential for increasing their agricultural production. Nothing in their soil and climate conditions suggest that their farmers will be less responsive to price and income incentives within an extended CAP framework than the farmers in the present Community (including

Irish farmers after the Republic's accession to the EC). The competitiveness of the new entrants (particularly of Spain) is very strong with regard to "Mediterranean" products (mainly fresh and processed fruit, vegetables, olive oil, wine), so that farmers in Southern France and Italy will come under increasing adjustment pressure. This is one of the reasons why the French Government tries to make the accession of Spain to the EC as difficult as possible. As to the "northern" agricultural commodities, the present members (excluding Greece) will keep a comparative advantage in most cases, but it is not unreasonable to expect the new entrants (and in particular Spain once again) becoming serious competitors in specific products such as mutton, lamb, wheat and rice. On the whole, the degree of self-sufficiency in the EC-12 would presumably be substantially higher than it happened to be in the EC-6 and EC-9, and overproduction would extend to further commodities (such as olive oil, peaches and wine), if the CAP is not fundamentally reformed. CAP expenditures would soar even faster than they have in the past, whereas third country suppliers would feel protectionism and trade diversion more severely than they were used to.

Against the background of shifting comparative advantages within the enlarged Community redistributive questions will continue to get a decisive weight in common budgeting. On the revenue side of the EC budget, present regulations may burden the new entrants with financial contributions above their shares in the GDP of EC-12 combined, notably on account of levies and duties on temperate-zone agricultural commodities (which traditionally have been supplied to a large extent by third countries) and of proceeds of the (still to be implemented) value-added tax (in view of a relatively high share of consumption in the GDP of the new entrants). The discrepancy between financial contributions and shares in the combined GDP would be most pronounced in the case of Portugal and least marked in that of Spain, i.e.

inversely related to the income levels in the new entrants. On the expenditure side, the entrants expect to benefit from CAP spending as well as from assistance under the EC's regional and social policy to an amount exceeding their financial contributions. But the substantial increase of EC expenditures implied by these expectations cannot be achieved within the present framework of financial resources available for the Community as these resources are already almost exhausted.

Under these circumstances, the new intergovernmental conflicts which broke out during the negotiations on the southern enlargement did not come by surprise. Nor is any new element discernible in the way in which these conflicts are to be resolved. Instead of imputing the pressing budgetary problems to ill-conceived common policies (most notably the CAP), in which case the solution would suggest itself, the present member state governments still enjoy themselves with looking for agreements on the lowest common denominator. They can choose between protracting the negotiations and opening up new revenue sources, or they can do both.

## 2. Potential for External Conflicts

The more the Community tries to accommodate new members within the present institutional and policy framework, the greater is the prospect that the relations with third countries will become more complicated. It is not just the danger of the increased trade protectionism which matters. Equally disquieting is the possibility that the EC becomes even more selectively protectionist than it already is. This will not only hurt other industrialized countries (especially the United States and Japan), but also, and mainly, the developing countries.

The existing common preferential arrangements with the developing countries may undergo considerable erosion. More-



over, the prevailing limitations in these arrangements on free market access are unlikely to be eliminated when the export potential of the new entrants and the supply capacities of third country beneficiaries overlap (most notably in textiles and a variety of "Mediterranean" agricultural commodities). There will be a great temptation to invoke the application of the so-called graduation principle, by virtue of which successful suppliers from developing countries would have to grant reciprocal concessions to EC exports. Greece, Portugal and Spain, which traditionally have pursued relatively protectionist trade policies based on non-tariff measures, may try to induce the Community to freeze selective ceilings for successful suppliers and to establish as many new categories of "sensitive" items as necessary to keep "excessive" imports at bay.

All this is bound to escalate national sensibilities in the Third World and to aggravate the enduring political difficulties which the present Community is already facing in its North-South relations, particularly as most developing countries cannot effectively retaliate economically. The next formal opportunity for witnessing clashes might arise in connection with the third renegotiation of the Lomé-Convention (of 1975 and 1979), which has linked the EC to a group of (at present) 63 African, Caribbean and Pacific (ACP) countries. Two aspects should be noted: on the one hand, as suppliers of bananas, canned fruit and fish as well as vegetable oils the ACP countries will meet resistance by the new entrants to granting unconditional duty-free access to the Common Market; on the other hand, Latin America suppliers which compete with ACP countries but enjoy relatively liberal access to the Portuguese and Spanish markets (notably in sugar) hitherto, will be afraid of being displaced from these markets once the Iberian countries adopt the Lomé provisions. Another area of imminent conflict is the Community's Global Mediterranean Policy, which was initiated by the Nine in 1975. The enlargement will jeopardize the EC

tariff concessions to most countries of the Mediterranean basin, in particular with regard to agricultural products in which the levels of self-sufficiency will rise considerably. Israel and Morocco seem to be most vulnerable as suppliers of oranges, grapefruit and other citrus fruit as well as raisins and dates; Algeria, Cyprus and Tunisia will be adversely affected the most as suppliers of wine.

That the CAP, if not fundamentally reformed, will intensify its proven harmful effects on third countries should be beyond any doubt (in spite of the EC rhetoric putting this policy in a favourable light). The growth of excess supplies in combination with the impracticability of storing them infinitely will lead again and again to new dumping on world markets, whereas the combination of high internal prices and import protectionism tends to reduce import demand for food. World market prices of CAP temperate-zone and "Mediterranean" products will be depressed under these circumstances. Net exporting countries then obtain lower foreign-exchange receipts than they would under more liberal trade conditions. Net importing countries, particularly in the Third World, pay for the availability of artificially cheaper imported food (including food aid) with the neglect of the development of their own agricultural sector and thus the perpetuation of their dependence on foreign supplies. It should not pass unnoticed that the CAP, in its present form, increases the instability of world market prices, which in some third countries may create balance-of-payment problems and in others generate investment cycles carrying a considerable distortion of resources.

#### IV. The Inexorability of Reforms

If the integration process in Western Europe is to thrive and if the EC is to reconcile its internal objectives with its worldwide responsibilities, the Community has to carry

out a root-and-branch reform of the institutional framework as well as of the shaping of common policies. Many proposals for substantial improvements have been made in the literature for some time. They have not been seriously discussed at the political level, however. As so often happens at home, the Community had to run first into a crisis before politicians could be urged in the direction of a reform. For many observers such a powerful crisis is the current financial squeeze, which the Community now faces (for the first time in its 25-year history); and when the member state governments decided at the Stuttgart Summit in June 1983 to meet the challenge in a constructive way, things seemed to take a turn for the better. And yet, the course of the many ministerial meetings which took place recently does not justify hopes that agreement on a fresh approach to strengthen the Community will be reached soon, if it is reached at all. Progress has been negligible so far, the list of contentious issues is as long as ever, the defense of "national interests" does not abate; the temptation of using common policies for redistributing income between member countries remains great, and some governments (not only the French) bluntly take the applications of Portugal and Spain as pretext for putting through their own conceptions of the future Community.

The basic principles which should guide the reform are straightforward. Firstly, the old and new obstacles to the free movement of goods, services, labour and capital among EC member countries have to be removed. After all, the creation of a true Common Market was the original purpose of the Community. The founding treaties also call for a contribution by the Community to a harmonious development of world trade. Therefore, the Community also has to find its way back to a liberal trade policy with regard to third countries in industry, agriculture and services. A liberal trade policy does not necessarily mean free trade, but in any case it requires non-discrimination in trade relations

with non-member countries. A reaffirmation of this principle would make it clear to the new entrants that they could not be granted long transitional periods (say, ten years and more) to abolish the existing tariff and other barriers against imports from EC countries and to reduce protection against imports from third countries down to EC external levels, thereby exposing their economies to greater international competition; Portugal and Spain could then not afford to postpone their efforts to undertake the necessary structural adjustments in production and they would therefore not undermine their chances of reaping full advantage from integration in terms of accelerating economic growth.

Secondly, objectives of income redistribution as envisaged by the Treaty of Rome should not be striven for by sectoral policies, nor should price interventions be the chosen instrument. A non-tied system of financial transfers from the wealthier to the poorer member countries, including the new entrants, would be a more efficient alternative, since relative prices and thus the allocation of resources would not be distorted as much. At the same time, the financial contributions of member countries to the Common Budget should be based on their relative per capita incomes. For the rest, income redistribution should be made the responsibility of the member country governments on the grounds that they then would have to justify the cost to their national electorates. In this case, the Community would have to establish "rules of conduct" for such national redistribution policies in order to prevent the governments from engaging in unlimited aids to specific groups and industries and thereby distorting competition in the Common Market. If, for example, regional policy is the chosen instrument for redistribution, the Community would have to determine the maximum effective rate of subsidies (including equivalents of other assistance measures) as well as the maximum share of a member country's territory which would be entitled to receive aid. The new entrants would have to adjust downward

their expectations about the assistance they may receive from the Community to promote regional development in their countries. But they could take advantage of the fact that transfers become more predictable and that policy conflicts and the economic costs associated therewith are avoided.

Thirdly, the CAP has to be fundamentally reshaped, so that it neither leads to overproduction, nor diverts trade flows both internally and externally, nor escalates budgetary expenditures at the expense of other Community policies. The overdue reform would have to eliminate current price supports and factor subsidies, including the subsidies to destruct, to denature or to export production surpluses. The proposals made recently by the Commission in the sense that farmers should share the costs of disposal of production surpluses or that production ceiling should be established for the farmers to receive the price and purchasing guarantees by the Agricultural Guidance and Guarantee Fund do not constitute a sensible reform. As experience with policies on milk and sugar has shown, there is a strong risk that the Council of Agriculture Ministers would feel even more willing to increase the guaranteed prices, as such increases could be financed easier; overproduction would not disappear. The same holds if the super-levy on milk, which the Commission has proposed and which the Irish Government opposes so strongly, was implemented. Therefore, a strictly market-oriented price policy has to be pursued instead. Agricultural prices would then reflect worldwide conditions of supply and demand; the risks accompanying price fluctuations would have to be borne by the producers (though efficient price-stabilization schemes can cushion these risks). Income targets in favour of farmers should be pursued by a system of personal transfers which are delinked from the size of production. For the new entrants a market-oriented price policy may appear as less attractive than the CAP in its present form, but only at first sight. Upon reflection they will come to realize that there are also advantages: procurement of

"northern" agricultural products would be cheaper; a mis-allocation of resources in their own agriculture could be avoided; and the contributions to the Common Budget, which are necessary to finance the CAP, would be lower.

Fourthly, it is essential to improve the division of labour between the Community and the member state governments. A good policy for Europe does not require common policies in an increasing number of areas (as the Commission claims). In strict economic terms, common policies are an efficient response whenever technical externalities exist (the environment or in fisheries, for instance). Common policies are also necessary to assure the functioning of a Common Market (trade policy, common technical norms, transport). But many tasks can be dealt with effectively at the national level, including the objectives of price level stabilization (provided that exchange rate among member countries are made flexible), of employment creation, of technological innovation and of economic growth. Given the divergent national preference functions on such goals, any attempt to shape common policies would only end up with agreements based on the lowest common denominator and on compromises which lack internal consistency. This also holds for the extension of the EC' competence to industrial policies, in particular to promote the development of high-technology industries, as advocated in some quarters. A common industrial policy would most likely founder on disputes over which industries of which member countries had better prospects for growth (every government would like to see its national industries, and not the foreign ones, promoted at the Community level); moreover, competition across the border would be weakened, though competition is probably the most important factor to enforce success and to drive away inefficient producers; and finally, the existence of a common industrial policy would invite lobbying for protection and other market-distorting interventions in case of investment project failures. Taking all this into

consideration, there is reason to believe that by maintaining national sovereignty in a variety of policy fields, governments would be unable to evade their genuine responsibility for achieving stated objectives. The governments of the new entrants could not make their citizens expect that entry into the Community would automatically provide for a catching-up of their economies with the more advanced member countries; the conduct of appropriate domestic policies would remain crucial.

Fifthly, it is imperative that the division of labour between the Council and the Commission be improved. The Council should concentrate its activity on consensus building and policy making; it should not do the work which could be done by the Commission itself. The role of the Commission should be strengthened in conformity with the prescription of the Treaty of Rome, which implies the delegation of powers to administer and carry out the decisions which the Council has taken.

Once reforms are considered with a greater breadth of vision than hitherto, the pressing budgetary problems of the EC will subside, particularly because the expenditure side (largely determined by the present CAP) would come under control. It is important for the reforms to occur, however, that the current financial squeeze is allowed to generate a creative urge among the politicians. This means that the Commission has to manage with the financial resources actually at its disposal, including the proceeds of up to 1 percent of the member countries' value-added tax (the amount of which increases every year by about 10 percent). Proposals to expand the sources of EC's budgetary revenues, especially those from the value-added tax (increasing the ceiling to 1.4 percent according to the Commission, to 1.8 percent according to the Greek Government, or to

2 percent according to the Irish Government) would, if they were introduced, indulge the governments in the vain hope that the EC crisis has been overcome at last.

V. Concluding Remarks

This paper has been written around the hypothesis that the deep problems which the EC presently faces are largely self-inflicted and should not be hidden by references to the applications of Portugal and Spain for full membership. Solving these problems will require much more than technical adaptations here and there and call for more than solemn declarations at summits on the virtues of European integration. The challenge is to undertake genuine reforms. One may argue that it is not realistic to expect those reforms to be carried out for the foreseeable future, as most member country governments continue to regard the Community mainly as a redistributive machine and, for the rest, are keen to pursue toughly what they consider to be in their national interest. In that case the EC will fall into agony, with and without further enlargement. The comprehensive failure of the Athens Summit, in December 1983, is a serious warning.