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THE EUROPEAN COMMUNITY AND THE WORLD: PROSPECTS FOR 1992*

The European Economic Community is supposed to constitute a "Common Market", but so far this has been an ideal rather than reality. Of course, tariff barriers have been removed and there is a great deal of trade within the community, but red tape and non-tariff impediments to free trade are considerable. They are like so many threads which keep the European Gulliver tied to the ground and prevent him from rising to his full stature. In 1992 all this is going to change dramatically. All these threads will be cut and Gulliver will jump up, startling the world with a revelation of his real height. Europe will dwarf the USA and Japan. The additional potential for economic growth generated by a truly "common market" will enable Europe to forge ahead and claim a larger share of world trade than it has at present. The European Currency Unit (ECU) may well replace the American Dollar as the leading currency of the world, and it will be a far more stable one than the Dollar which is affected by policy decisions of American Presidents such as cutting taxes but running up a budget deficit, relying on the rest of the world to fill the gap by buying US government bonds, etc.

But these dramatic prospects for 1992 are still to be realised and critics may say that there is much wishful thinking at present. In

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discussing these prospects we shall first look at the internal potential as well as the internal disparities of Europe. We shall then turn to the crucial topic of non-tariff impediments to free trade. Subsequently we shall examine the problem of a common currency supported by a European central bank, and finally we shall try to gauge the impact which the European Community of 1992 will have on the world and how it will fit into a new world market.

The Present Potential and the Internal Disparities of Europe

The 12 nations of the European Community have a total population of 323 million, and a total private spending power of 2,683 billion ECU which corresponds to approximately 3,000 billion US Dollar. Average per capita spending power thus amounts to 9,800 US Dollar. But the disparities between the rich and the poor nations in Europe are very great. Germany is the richest one with a per capita private spending power of about 11,800 US Dollar, and Portugal the poorest with 2,500 US Dollar. Great Britain with 7,550 US Dollar is already far below the European average. The three major continental nations, Germany, France and Italy which together have a share of 54 per cent of the population of the European Community contribute about 58 per cent of its total private spending power. They will probably stay ahead of the others even after 1992. Spain with a large territory and a fairly big population may have a chance to catch up at least with Great Britain by the year 2000 unless British industries benefit to such an extent from the common market that they experience a major spurt of growth.

As the reduction of barriers to free trade in 1992 also include the removal of restrictions on the mobility of labour one could expect a diminishing of regional disparities by a migration of labour from the poorer to the richer countries, forcing wages down there and raising them in the countries of origin of the migrants. But this will not happen, because the rich countries have a fairly high degree of structural unemployment and an elaborate system of social benefits which makes wages even more sticky than they are normally supposed to be. In fact, the great differences in social benefits are the main obstacles to the reduction of regional disparities within Europe. Unlike other barriers which can be removed if there is a political will do so, the discrepancies in social benefits which acrue within a lifetime cannot be removed at once and 1992 will hardly make a difference in this respect. Even optimists who expect much from market integration admit that as far as employment is concerned the creation of about 1 million jobs as a result of the economic growth which they project would only be a drop in the bucket. Structural unemployment has come to stay in Europe and this problem must be tackled by other methods than those usually prescribed in textbooks.

As labour migration will be limited in practice though uninhibited in theory, there is, of course, the other option of the mobility of capital from rich countries with high wages to poor countries with low wages. This has already happened in Europe, and, in fact, there used to be a substantial investment in low wage countries in Asia where consumer goods for the European market could be produced more cheaply. But the trends of technological change go against this line of development. With the progress of automation which reduces the reliance on cheap labour but requires skilled supervision, investment in productive capacity close to the consumer is more profitable than going abroad.

Another option is that of vagrancy. If there is free mobility, poor people may find it attractive to go to a rich country and live on the dole rather than on a pittance at home. This may become a problem mainly for the local town administrations who are charged with the financial responsibility of looking after the destitute in their area of jurisdiction. If this does become a problem it would immediately lead to a demand for restrictions of mobility and this would be a big blow to the experiment of 1992. If one does not want to go back to square one when faced with this challenge, there would have to be a major regional development programme financed by the richer nations for the backward regions of Europe so as to improve the standard of living there. The funds for such a programme could be derived from the substantial savings due to cost reductions once market integration is achieved. The Cechini Report on "The Cost of Non-Europe" commissioned by the European Community estimates that approximately 200 billion ECU (230 billion US Dollar) are wasted each year due to red tape, controls, delays, a variety of national norms rules and regulations, etc. We shall turn to a brief survey of these impediments to market integration now, because they are of major importance and are often neglected in discussions on the prospects of the European Community.

Non-Tariffs Impediments to Market Integration

European governments have pursued for a long time a policy of controlling the quality of commodities in the interest of the consumer. The famous German regulations concerning the purity of beer which date back to 1516 are a typical example. Germany had to suffer a national defeat when the European Court ruled in March 1987 that the sale of foreign beer which does not measure up to these standards cannot be precluded by this regulation. Germany brews the largest share of European beer and imports negligible quantities, but this may change if German consumers who may now buy cheaper foreign beer disregard "purity".

Similar - and more serious - problems have come up with regard to contamination by radiation and the use of hormones in animal husbandry. Here some nations are more sensitive than others and regulations concerning critical limits differ. In addition to such public norms and controls there are many norms whose adoption is voluntary, but which nevertheless have quasi-legal status, because of of their general validity due to long and widespread usage. The German Industrial Norms (DIN) are a case in point. They fix the shape and size, content and extent of almost everything made by machines. There is no law which prescribes that German writing paper should be of a specific size (DIN A4), but nobody would think of using anything else, because office machines and envelopes etc. are all geared to this standard size. Again this is one of the more obvious examples, other instances which are of much greater economic relevance could be listed ad infinitum. Take only the production of automobile parts : The Cecchini Report mentions that many producers of such parts manufacture at the most 500,000 items of any particular specification per year whereas real economies of scale could be realised only if they could produce more than that.

The problem of norms and specifications plays an even more important role in the field of procurement of commodities on behalf of government or local governments. From pencils to nuclear power stations such governments call for tenders specifying certain standards which are almost exclusively circumcribed by national norms. Often this may be due to more routine, but it may also be used so as to favour specific national producers. As such producers sometimes enjoy a quasi-monopoly due to such favours, they can charge high prices and need not worry about international competition. According to the Cecchini Report about 15 per cent of the net domestic product of the European Community is spent on such procurements and only a negligible amount of this is spent on items produced beyond the respective national borders.

Another major irritant is the heterogeneous pattern of taxation in Europe. This applies to direct personal and corporate taxation as well as to indirect taxes such as Value Added Tax (VAT) which is a very important source of government revenue everywhere in Europe. This VAT varies from about 7 to 22 per cent and in some countries with the highest VAT in Denmark where the whole system of public health and welfare depends on it.

A European Currency and a European Central Bank

The non-tariff impediments to market integration pose major problems as we have seen but monetary integration is a field of as much importance and it is best by similar problems. We shall discuss the world context later on, at this stage it may suffice to refer to the general anarchy which has prevailed ever since the demise of the Bretton Woods system of fixed exchange rates. Free floating frequently interrupted by more or less successful interventions by the central banks of major nations has been the order of the day. The Special Drawing Rights of the Internal Monetary Fund were created so as to cope with international reserve requirements and the European Community sponsored the ECU as a parallel or a counterweight to the SDRs. Just as the SDRs the ECUs are notional entities and nothing tangible which one could put into one's purse. But there are ambitious plans to make the ECU tangible as a real European currency and there are many supporters of this plan who argue that without such a currency there can never be a true market integration. Europe has managed to keep its many floating currencies within tolerable range of fluctuation and this pattern is referred to as the "snake", because of its more or less graceful ups and downs controlled by a couple of snakecharmers in various central banks.

A tangible European currency could not rely on diverse snakecharmers, it must be issued by some monetary authority which optimists would like to call a European Central Bank. This raises the issue of the principles of central banking. The conservative approach to this art stresses price stability as the primary concern and the independence of the central bank as a necessary concommitant of this aim. The control of inflation requires a discipline which can only be maintained if the central bank is not at the back and call of politicians who are influenced by short-term considerations of expediency. The German Bundesbank, the most important central bank in Europe, follows this line and does enjoy a great deal of independence. Its presidents usually become orthodox defenders of the faith once they are appointed, whatever political affiliation they may have had before that time. The present incumbent, Karl Otto Pohl, a member of the Social Democrats, is as orthodox in this respect as any conservative would be.

The rival approach to central banking considers general economic stability in terms of output, employment, etc. as more important than price stability. This approach is naturally combined with a greater influence of government on central banking, because economic policy and monetary policy must be closely coordinated in order to achieve this goal. Most European nations follow this line regardless of their political differences. Governments which are used to this approach would not like to yield a great deal of their sovereign control to a European Central Bank which would enjoy an independent position like the German Bundesbank. On the other hand the German Bundesbank would not like to be confronted with a European Central Bank which would not enjoy the kind of independence which it has and which it considers to be the very essence of central banking. But even if a European Central Bank would be created in the image of the German one, President Pohl or his successor would have no reason to rejoice, because such a bank would necessarily be a formidable rival of the German Bank which so far has a unique position in Europe and practically calls the tune of the "snakecharmers" whom we have mentioned earlier.

Actually the "snakecharmers" have performed fairly well in recent years and in the absence of a European Central Bank their concert could very well conjure up an ECU which may still not be tangible but nevertheless emerge as a potent force in world affairs. But the process of market integration may create some turbulences which could disturb the snake. The "snakecharmers" may have to pass this test first before they can present a unified front to the world outside. Of course, one could also argue that by presenting such a united front they would be able to control internal turbulences, too. Thus an external challenge could prepare them for the internal one. This leads us to the question of the role of the European community in the world.

The European Community and the World

In discussing this role we may well begin by referring to the volatility of the US Dollar which constantly disrupts trade relation and encourages wild speculations which are completely beyond the control of any snakecharmers. The general free for all system which is euphemistically called the Euro Dollar market has attained fantastic dimensions. Millions can be gained or lost within a day by going into or out of the Dollar. Such deals by now dwarf all transactions in the so called "real economy". On the other hand barter trade which is normally associated with a more primitive stage of economic development assumes more and more importance. A stable ECU could be an attractive alternative to the Dollar. Europe would then have a lot of money to play with which otherwise flows into the Euro Dollar market which is "Euro" only in name and should better be called an off-shore Dollar market.

Whereas the emergence of a stable ECU world be a positive European contribution to the world economy, the other contributions which Europe may make are still rather uncertain. The outside world looks askance at European protectionism. Tariffs are not the most serious problem in this respect. Non-tariff impediments to trade which now beset the internal operations of the European market may become obstacles to external trade as the bureaucrats in Brussels are churning out European norms which are supposed to promote internal integration but at the same time effectively debar the entry of foreign products. The Americans are already very much concerned about this and their worries are going to increase. Germany as the biggest exporter in Europe is vitally interested in free trade and does not like restrictive practices. But Germany is also very norm-conscious and is therefore not exactly in a position to fight against norms. Moreover, it is hard to draw a line between legitimate insistence on norms and their discriminatory abuse. A practical example, reported in the European Wall Street Journal of Jan. 19, 1989, shows this : An American manufacturer of Forklift trucks who tried to comply with all norms and changed his product accordingly was finally faced with the requirement that the electrical wires in his machine were supposed to pass an acid test in the literal sense of the term. No American supplier could be found for such wires and he had to look around until he found a German one. This requirement was probably not due to successful lobbying by the German supplier and may be truly in the interest of the consumer. But norms of this kind can be easily turned into tools of protectionism. So far the Europeans have accused the Japanese for indulging in this kind of protectionism. It would be a pity if they apply the same tricks now. At least all norms should be well defined and published well in advance, If they are reasonable, they may even be accepted by the outside world and the label "Conforming to European Norms" would become an internal quality mark istead of a red rag for exporters everywhere.

This is a rather idealisttic interpretation of European "normative" endeavours and bureaucrats could use it so as to justify their exercises instead of trying to cut red tape as much as possible. Actually Europe should try to set an example in the field of economic manegement and regional development. As we have seen Europe has an internal disparity ratio of about 1 to 5. Large countries in Asia like China and India have similar internal regional disparities and would look to Europe for ways and means of reducing such disparities. As far as development aid is concerned the European Community is still a non-entity with funds of less than 500 million US Dollars available for non-associated countries. And yet even this rather small cake has attracted attention and it has been reported recently that Asia which so far has received three quarters of that cake is afraid that the new Spanish commissioners in Brussels will see to it that Latin America gets a larger slice of the cake. Larger members of the community like Germany which are generally in favour of getting away from bilateralism and avocate the routing aid through international organisations like the World Bank should also see to it that the European Community emerges as a major factor in this field, but they should then also exercise their influence so as to prevent the French from pampering their former African colonies or the Spanish from favouring Latin America.

But fiirst and foremost Europe should follow the motto "Better Trade than Aid" and accept more manufactured goods of developing countries rather than raw materials only. The terms of trade for the producers of raw materials have deteriorated and if Europe does not encourage the import of manufactured goods it cannot hope to export them to the same extent in future years. Trade within Europe has long since been a trade in manufactured goods defying all old doctrines of comparative advantage and the international division of labour. Why should Europe which is a living example of this new pattern of trade treat its external trade relations as if these old doctrines were still valid ? Europe can set a dynamic example for the world, but it will do so only if it is extrovert and not introvert.

With the world's largest reservoir of educated and skilled people the the European Community can afford to be openminded and generous and need not be protective and defensive. There was once an age of European expansion promoted by bold navigators and discoverers and followed up by conquerors and imperialists. This is a story of the past and not a very glorious one in many respects, the second age of European expansion should be one in which Europe freely and peacefully shares its achievements with the rest of the world. In doing this Europe would also benefit, because there are economies of scale not only in the purely material sense of the term but also in the field of communication and information which will be the dominant forces of the new age.