

The European Economic Community: Thirty Years Later

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Abstract

The European Economic Community has been in operation for about 30 years. During this period an increased economic cooperation has been attained but the goal of a truly integrated Europe has remained elusive. The Single European Act, which was ratified in 1987, represents a recommitment to an integrated Europe by 1992. It is premised on a number of changes and reforms. Above all the effectiveness of the new effort will depend on the achievement of social cohesion and supranationalism among the EEC countries.

Introduction

About 40 years ago the U.S., under the visionary leadership of Secretary of State General George C. Marshall, initiated the Marshall Plan aid program. It is well known that this aid program was aimed at helping the reconstruction of war-ravaged Europe and the 17 nations which received the \$13.3 billion of aid experienced remarkable economic reconstruction and recovery. In addition to the rather immediate tangible economic benefits that accrued to Western Europe, a new spirit of cooperation was also a side-product of the Marshall Plan program. This new spirit manifested itself in the signing of the Treaty of Paris on April 18, 1951 which gave rise to the European Coal and Steel Community in 1952. Because of the success of this venture, its founders, Belgium, the Federal Republic of Germany, France, Italy, Luxembourg and the Netherlands decided to widen its scope and to cover their entire economies. Thus, on March 25, 1957 they signed in Rome two treaties which led to the establishment of the European Economic Community (EEC) and of the European Atomic Energy Commission (EAEC) in 1958.

This study reviews the objectives, accomplishments, and difficulties of the EEC; it assesses the likely impact of the amendment to the EEC, i.e., the Single European Act, on the EEC economies.

The European Economic Community

The basic purposes of the EEC, as provided in Article 3 of the Treaty of Rome (1987, pp. 125-126), include the following:

- 1 The elimination of customs duties and of quantitative restrictions on the import and export of goods;
- 2 the establishment of a common customs tariff and of a common commercial policy toward third countries;
- 3 the abolition, between member states, of obstacles to freedom of movement for persons, services and capital;
- 4 the adoption of a common agricultural policy;
- 5 the adoption of a common transport policy;
- 6 the creation of a European Social Fund in order to improve employment opportunities;
- 7 the establishment of a European Investment Bank to facilitate the economic expansion of the Community;
- 8 the association of the overseas countries and territories in order to increase trade with them and to promote jointly economic and social development.

To help implement the purposes of the EEC a number of institutions were created including the European Parliament, the Council, the Commission and the Court of Justice.

The major accomplishments of the EEC are both political and economic. Politically, a reconciliation between France and Germany has

been achieved ending the conflicts which had led to wars in Europe every few decades. Economically, the EEC has made progress toward a large single market. Since 1970 the EEC tariffs between the original six members have been eliminated. A common external trade policy has been agreed upon and a common agricultural policy has become operational. There has been some freedom in the movement of workers and some liberalization of capital movements. The European Investment Bank has played an important developmental role particularly regarding the less developed areas of the EEC; and the establishment of the Lome' Convention has been a significant step in EEC's assistance of poor countries in Africa, Caribbean and the Pacific. The group of the six original members, Belgium, the Federal Republic of Germany, France, Italy, Luxembourg and the Netherlands, has been enlarged three times. In 1973, Denmark, Ireland and the United Kingdom joined. In 1981, Greece did. Finally, in 1986 Spain and Portugal joined the EEC.

Over the years the EEC has evolved into a major force in international trade. In 1987, the EEC was the world's largest exporter accounting for about 20 percent of world trade while Japan's share was 9 percent. EEC exports contributed 10 percent of EEC's GNP as compared to the U.S. exports which accounted for 5 percent of the U.S. GNP (1). It is also interesting to note that in 1986 57.8 percent of the EEC imports

and 57.2 percent of the EEC exports represented intra-EEC trade while 9.3 percent of EEC's exports and 7.1 percent of its imports were with the U.S.A (2). In actual amounts the EEC imported \$56 billion of goods and services from the U.S. in 1986 and \$6.4 billion or 25 percent of U.S. agricultural products (3). Finally, the EEC trade balance had a surplus of 10.95 billion ECU's in 1986 while the U.S.A. had a deficit of 155.19 billion ECU's (4,5).

The EEC efforts toward integration have been plagued by a number of problems or difficulties. They include the following:

1. A troublesome area and one of great concern to the U.S.A. has been the EEC common agricultural policy (CAP). It will be remembered that developing a common agricultural policy was a main objective of the Treaty of Rome. This policy emphasizes the need to increase agricultural productivity and the standard of living of community farmers. Its implementation, however, has included a rather generous system of import levies and export refunds. A result of this system has been that about 70 percent of the EEC budget is used to support the Common Agricultural Policy (1987, p. 54). The critics of CAP see the import levies as a major bottleneck to non-EEC agricultural imports and the export refunds as export subsidies designed to increase EEC's share of world agricultural exports. A related consequence of CAP is the

Table 1
European Economic Community Trade
in billions of ECUs

Areas	Imports			Exports		
	1985	1986	1987	1985	1986	1987
World	874.67	796.00	829.13	849.93	806.95	829.91
Intra-EEC	466.74	459.70	487.39	466.59	461.34	486.83
Extra-EEC	406.41	334.56	340.05	378.65	341.93	339.33
U.S.A.	68.94	56.64	56.21	85.52	75.15	71.89

Source: External Trade, Eurostat, 1988.

generation of large agricultural surpluses. There have been surpluses in wheat, barley, sugar, beef, wine and dairy products (6) which seek outlets in overseas markets. In this regard, it may be pointed out that the U.S. share of wheat in the world market has fallen from 49 percent in 1981-82 to 36 percent in 1984-85 while the EEC share has increased from 14 percent to 16 percent (7). Again the critics of CAP urge that EEC agricultural products be sold in the world markets without subsidies. For instance, on July 6, 1987 the US proposed in Geneva, Switzerland that all forms of agricultural subsidies be eliminated within 10 years. Notwithstanding the intra-EEC political pressures in support of the CAP, the EEC Commission has made a number of proposals which if adopted would freeze support prices for agricultural products and thus help reduce agricultural surpluses (8). Nevertheless, given the present structure of the EEC, continuation of the basic objectives of the CAP is most likely.

2. The enlargement of the EEC to 12 members has posed a number of problems. A major problem derives from the considerable disparities in the size of population and in the per capita output of the member countries. For instance, in 1986 the population of the Federal Republic of Germany, Italy, United Kingdom and France was 60.9 million, 57.2 million, 56.7 million and 55.4 million respectively. On the other hand, Greece, Belgium, Denmark and Ireland had a population of 10 million, 9.9 million, 5.1 million and 3.6 million respectively (9). Moreover, GNP per capita in 1986 varied from \$12,600, \$12,080 and \$10,720 for Denmark, the Federal Republic of Germany and France to \$5,070, \$3680 and 2250 for Ireland, Greece and Portugal respectively (10). The 12 member countries represent 10 cultures, 9 official languages and 9 currencies. The expanded EEC comprises more Mediterranean countries, i.e., Greece, Spain, Italy and France (Southern France) and more peripheral countries, i.e., United Kingdom, Denmark, Ireland, Portugal, Spain, Italy and Greece. According to Kondonassis (1976), differences in social and economic structure and the rule of unanimity have precluded EEC's functioning on a decisive manner on a variety of issues involving the development of common policies. Because of these differences, which have given rise to conflicting interests, each enlargement of the EEC has been marked by long periods of accommo-

modation and adjustments, Kondonassis argues (1977).

To address the income disparities and to promote the economic development of the Mediterranean member states, the European Investment Bank and the European Regional Development Fund have allocated about 45 percent of their resources to Mediterranean projects. The European Social Fund has also provided assistance in job training and retraining in Greece and Southern Italy. During the 1975-81 period the Mezzogiorno area of Italy and southern parts of France and Greece have received more than 3.8 billion ECU's in EEC loans. On July 23, 1985 the so called Integrated Mediterranean Programs (IMPs) were approved by the EEC Council. The targets of these programs are agriculture, infrastructure, crafts, industry, fisheries and tourism. For the 1986-1993 period 6.6 billion ECUs are to be allocated for the IMPs (11). Obviously, the general objective of these programs is to promote the development of the less developed areas of the EEC and to bring about greater harmony between the North and the South. According to Kondonassis (1982) this is a goal which will require persistence and a long run perspective.

3. Another problem is that, although on paper a customs union has been in existence for more than 15 years, the reality at intra-EEC frontiers is not unlike that at EEC's frontiers with non-members. Member EEC states impose separate national import quotas on a variety of products including steel, textiles, Japanese cars, Eastern European cars. In addition, Cheeseright argues (1985) that EEC members impose national export restrictions on military sensitive goods because of their NATO membership. All and all a plethora of non-uniform standards and different regulations and tax systems prevail.

The above relatively brief comments and analysis suggest that during the last 30 years the EEC has experienced some successes but also continuing problems. Recognizing the reality that it has not become a truly integrated single market, the EEC endorsed the European Commission's *White Paper on Completing the Internal Market*. As a result, a comprehensive detailed legislative program signed early in 1986 and ratified in July 1987 has come to be known as the Single European Act.

The Single European Act

The Single European Act is an amendment of the 1957 Treaty of Rome. It also represents a recommitment of the EEC to complete the internal market by 1992. The Act crystallized when it also became clear that the European economies needed a stimulus toward more rapid economic growth and higher levels of employment. The program encompasses about 300 points and deals with improvements in the functioning of EEC institutions, with removals of all barriers to the free movement of goods, persons, services and capital, with cooperation in economic and monetary policy and with improved cooperation in the areas of social cohesion, research and development, the environment, foreign policy and defense.

A recently completed study by Paolo Cecchini (1988) attempts to quantify the costs and benefits of the EEC with and without frontiers. It focuses on market barriers arising from red tape and delays created by customs formalities, from restrictive practices in public procurement, from divergent product standards and from conflicting business and tax regulations inhibiting transborder business activity.

Microeconomically, the study estimates the cost of border formalities and red tape at 1.8 percent of the value of goods traded within the EEC. The average cost to companies of technical regulations and similar barriers to cross-border trade is valued at about 2 percent of their total expenses. Furthermore, the study estimates that industries and services which are now subject to market-entry restrictions will experience cost and price reductions of 10 percent to 20 percent in a more competitive environment. Finally, the cost savings benefits to industry from economies of scale are estimated at about 2 percent of Gross Domestic Product.

According to the study the macroeconomic influences of the Single Market are no less impressive. It is estimated that in the medium term the downward pressures on prices and costs would result in a 6 percent cumulative decline on consumer prices; about 2 million jobs would be created; government balances would improve by about 2.2 percent of Gross Domestic Product; and EEC's external balance of goods and services would improve by 1 percent of Gross Do-

mestic Product. Overall, EEC's Gross Domestic Product would be increased by about 5 percent.

The substantial benefits from the Single Market as outlined in the Cecchini study are premised on a number of required changes and/or reforms. Many of them are unresolved issues that have confronted the EEC since its inception. At the risk of being repetitive these include changes and/or reforms in the Common Agricultural policy and in the use of the structural funds. The EEC Commission has repeatedly underscored that the effectiveness of the single market depends in no small measure on reforms in agricultural policy (CAP). These reforms must aim to make European agriculture more competitive, to eliminate the large agricultural surpluses and to check the increase in the burden that the agricultural policy imposes on the EEC budget. In addition, the increased use of structural funds in the EEC budget to assist the less developed areas of the EEC e.g., Portugal, Ireland, Greece, parts of Spain, the South of Italy and Northern Ireland is also viewed as a necessary condition for a successful single market. Other key issues that need to be addressed are monetary and fiscal harmonization, the development of internationally competitive enterprises and the avoidance of protectionism.

The Treaty of Rome in 1957 was not concerned with the goal of monetary integration. At a time of fixed exchange rates, the possibility of a common monetary policy took second place to other objectives such as a customs union and a common agricultural policy. But with the collapse of the Bretton Woods system in 1973 the Europeans have gradually recognized that floating exchange rates represented a risk and a cost to their economies which were involved in a large volume of intra-EEC trade. Thus, through a series of initiatives they eventually agreed to establish the European Monetary System (EMS) in 1979.

The primary purpose of the EMS is to promote monetary cooperation and monetary stability in Europe. It is comprised of three components: the European Currency Unit (ECU), the exchange-rate mechanism and the financial solidarity mechanisms. ECU, which is an artificial monetary unit, is calculated as a basket of set amounts of each EC currency (10 EC currencies). It is used for fixing central rates in the

exchange rate mechanism and for denominating creditor and debtor balances in the process of intervention in EC currencies; also, it serves as a reserve and settlement instrument among the central banks in the EMS (12). Although there have been a number of exchange rate readjustments among the EC currencies since 1979, and the non-participation of the sterling in the EMS has been a negative influence on its functioning, a substantial degree of exchange rate stability has been attained. But now, given the objective of the Single Act for economic and monetary cooperation leading to a union, greater progress in exchange rate stability will be needed. In addition, the establishment of the ECU as a common currency, the liberalization of capital movements among the EEC countries and the creation of a European central bank are issues that will need to be moved forward. Their resolution will require, apart from coping with a myriad of technical details, a spirit of supranationalism as the transferring of monetary and fiscal authority from the national governments to European institutions takes place. Prime Minister Thatcher's repeatedly negative position on these issues shows that the road ahead will probably be long and rough.

Another issue is the establishment of uniform value added taxes (VAT) among the member countries. Currently there is wide variability in these taxes. Some countries have high VAT and others quite low (13). Some depend on VAT for a large source of their revenues and others not so much. To reduce the variability and the height of these taxes and to move toward fiscal harmonization is not going to be easy. However, without such changes tax evasion would be encouraged and the smooth functioning of the single market would be jeopardized.

A common assumption of the establishment of a single market of 320 million people is that it will induce the formation of large-size enterprises via mergers and consolidations and will bring about corresponding economies of scale to these firms. Notwithstanding the possibility that these firms may become internationally competitive, there are a number of potential problems associated with this eventuality. One of them is that the emergence of large European firms may have deleterious effects on the large numbers of small size firms prevalent in the countries of Southern Europe. Many of these small firms

have operated in an environment of red tape and bureaucracy for quite some time. They are local in scope and undercapitalized. Located in the periphery, they are not the beneficiaries of externalities as the firms of the center are, i.e., Northern Europe. What it comes down to is whether the small businesses of Southern Europe, under the impetus of the Single Market, will be able to restructure and become competitive by 1992. If not, would they be eliminated or would they seek the protection of their governments which in turn may ask for exceptions?

In this connection, Pierre Pescatore, former Judge on the Court of Justice of the European Communities, expresses his concern about the effectiveness of the Single Act by pointing out that a number of exceptions are allowed in the Final Act for unilateral protective measures under the guise of "safety" and "protection of the environment" (1987, p. 12). He further emphasizes that unilateral reservations about the Single Act have already been expressed and recorded by Denmark, Greece and Portugal (1987, p. 17). In this regard, it should be pointed out that the Final Act, which is a document attached to the Single Act, contains twenty declarations. Some of them are interpretations of the Single Act and others are reservations by individual countries regarding the Single Act. These declarations are likely to generate difficulties in the implementation of the Single Act. A related issue has to do with the so called qualified majority system which the Single Act has introduced to take the place of the unanimity rule of the past. According to this new system, each member country is allocated a given number of votes according to its size. For instance, France, Italy, Germany and the United Kingdom are assigned 10 votes each. Belgium, Greece, Netherlands and Portugal have 5 votes each, Spain has 8 votes, Denmark and Ireland 3 votes each, and Luxembourg has 2 votes. Decisions can be made by a minimum of 54 votes out of the possible 76. It takes 25 votes to block a motion by a large country. Given the differences in the economic and social structure among the 12 members, the likelihood for deadlocks is real. Thus, it appears that the qualified majority system may not necessarily improve the decisiveness and hence the effectiveness of the EEC.

Just as it was the case when the EEC was first established in 1958, non-member countries

are once again concerned about the possible protectionist policies of the Single Market. The EEC has tried to allay these fears by suggesting that Europe of 1992 will not be a fortress Europe but a partnership Europe (14). The EEC further claims that because the EEC is the world's biggest exporter, i.e., about one-fifth of world trade, it is highly dependent on international trade and in fact, has a vested interest in free international trade. The Single Market will be beneficial not only to European companies but also to companies from non-member countries. The Single Market will mean only one frontier with uniform standards, rules and certification procedures and possible economies of scale for all (15). The EEC Commission, however, adds that the benefits of 1992 to non-member firms will be conditional upon a guarantee for similar opportunities in those firms' own countries. Reciprocity is the key word in the vocabulary of the EEC (16). But given the ambiguity associated with the concept of reciprocity and the Single Market emphasis on uniform standards based on European practices, one can understand the concerns of the U.S. and of other non-member trading partners of the EEC. Obviously, the challenge facing the EEC and its trade partners, e.g., the USA, is to help accentuate the positive aspects of the Single Market and to enter into discussions and/or negotiations in order to avoid the formulation of standards and restrictive practices which may lead to the establishment of a protective wall.

The European Council in its Rhodes, Greece, meeting on December 2-3 1988 observes somewhat optimistically that approval of the legislative program toward the establishment of a single market is at a half-way point. It adds, however, that the pace of work must be accelerated in the future as several difficult tasks remained to be resolved (17).

Conclusions

There is no doubt that the establishment of the European Economic Community has meant increased cooperation for Europe. It has attained some of the goals of the Treaty of Rome but not others. It certainly has become a loose customs union, that is one with several frontiers rather than one. Its common agricultural policy has been a boost to the incomes of the European farmers but has encouraged large agricultural

surpluses and has also imposed a great burden to the EEC budget. The enlargement of the EEC to 12 members has increased the size of the potential market but also the economic, social and political diversity of the EEC.

The Single European Act represents a recommitment to the general goals of the Treaty of Rome and a concerted effort to amend it in order to attain an integrated Europe. The potential benefits of the Single Market, both on the micro and macro levels, may be substantial. However, these potential benefits are premised on a number of changes and/or reforms in areas such as agricultural policy, monetary and fiscal harmonization and international competitiveness. In turn, the implementation of these changes depends on the political will of the members to act in unison. If there are differing perceptions in the distribution of these benefits among the member countries, national concerns may dominate European initiatives. If this proves to be the case, the establishment of a Single Market and of an integrated Europe may continue to be an elusive goal. In that event, Europe, notwithstanding its current dynamism, may have to be satisfied with a half loaf rather than a full loaf, at least in the short run. Thus, a loose customs union or free trade area may continue until Europe attains greater social and economic cohesion and learns to embrace and practice supranationalism.

Footnotes

- 1 EC Office of Press & Public Affairs, *European Community News*, Washington, D.C., October 20, 1988, pp. 1-7.
- 2 See *Eurostat*, 1986 pp. 267 & 269.
- 3 *Ibid*, p. 266.
- 4 See Table I.
- 5 The exchange rate ECU/U.S. dollar varies daily as the various EC currencies that make up the ECU vary against the dollar. One ECU was worth \$1 from 1960 to 1972, \$1.24 in 1975, \$1.12 in 1976, \$1.39 in 1980, \$1.12 in 1981, \$.98 in 1982, \$.89 in 1983, \$.79 in 1984, \$.76 in 1985, \$.98 in 1986 and \$1.15 in 1987.
- 6 Clinton, Mark, "Farm Trade: Return to Gatt Urged," *Europe*, March 1986, pp. 16-17 & 48.
- 7 *Ibid*, p. 48.
- 8 Krause, Axel, "U.S. - EC Strains seen Continuing into the Fall," *Europe*, September 1987, pp. 14-15.
- 9 World Bank, *World Development Report* 1988, Oxford University Press, 1988, pp. 22-23.
- 10 *Ibid*.
- 11 Arvanitopoulos, C. and Yannas, P., "EC Policy Sets Special Programs for Mediterranean," *Europe*, December 1986, pp. 28-29.
- 12 European Affairs/Dossier, "The European Monetary System," *Europe*, December 1987, pp. 22-25.
- 13 For instance, a liter of pure alcohol in the United Kingdom is subject to 24.83 ECUs in tax, in France 11.49 ECUs and in Greece .48 ECUs.

- 14 EC Office of Press and Public Affairs, *European Community News*, Washington, D.C., October 20, 1988, p. 1.
- 15 *Ibid*, p. 2.
- 16 *Ibid*, p. 3.
- 17 EC Office of Press and Public Affairs, *European Community News*, Washington, D.C., December 6, 1988, pp. 2-3.

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