

THE ECONOMY
EUROPEAN UNION
AND THE ECONOMY
OF EUROPE



LARRY NEAL *and* DANIEL BARBEZAT

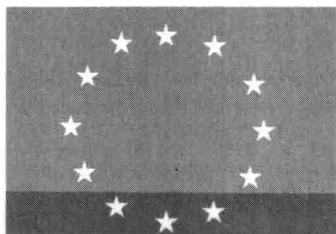
The Economics of the European Union and the Economies of Europe

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Preface

This is a textbook on the European Union by two American economic historians. It attempts to integrate economic analysis, political logic, and historical interpretation in an effort to convey an American perspective on the movement toward European integration, the external constraints it faces and has faced, and the interplay of national concerns, both economic and political, within the vision of a united Europe.

Beginning with the American perspective on Europe, Part I of the text treats Europe as a natural economic unit, irrationally and temporarily (1945–89) divided into separate political units that attempted to remain as distinct from one another as possible. The political and economic framework of the European Union, which has evolved since 1958 to achieve the economic possibilities of unifying this natural economic unit, is naturally the focus of Part I. To prepare readers, we first describe the abbreviations and acronyms that are used by the European Union officials and present the chronology of the European Union's development since 1945. Two maps then show the current (1997) political status of the economies of Europe with respect to the European Union and their relative economic status in terms of per capita incomes. These illustrate very effectively that economics alone does not explain either the past development or the present concerns of the European Union and the economies of Europe. The underlying economic logic of the EU's mode of operation is examined from an economist's point of view in the individual chapters. These take up the economic developments in the period 1945 to 1958 that led to the formation of the European Economic Community; the logic of the customs union leading into a single market by the end of 1992, the budget difficulties for the EEC that emerged over this period; the origins, growth, and eventual reform of the Common Agricultural Policy; the repeated attempts to move toward a permanent regime of fixed exchange rates within an economic area subjected to repeated external shocks and internal stresses; and the efforts to resolve these difficulties in its external relations with the rest of the world. Time and again, we will see the compromises that have had to be made with the forces of political separatism as the EU has evolved.

Part II, then, tries to illuminate the political and economic diversity of Europe by reexamining the post World War II economic history of the major states and groups of minor states. European readers take these adversarial positions

for granted, imbued as they are with the knowledge of centuries of distinctive national development for their particular nation. American readers seem increasingly ignorant of the significance of past European developments and the difficulty with which ethnic animosities have been subsumed into the national political entities now governing in Europe. Non-American and non-West-European readers will find many interesting analogies to their own concerns with respect to economic integration at a regional level and resistance to disruptions from the global marketplace. Each member state of the European Union has its own, overriding, domestic priorities in order to maintain its internal unity and the legitimacy of its government. Understanding the different concerns of the constituent member states is essential for comprehending the motivation of the European Union's policies and for appreciating the extent of its accomplishments to date. Moreover, the economic logic of European unification is viewed quite differently by each current member state of the European Union, as well as by each potential member. Part II attempts to lay bare these differences, using the approach of economic history to analyze the political economy of each constituency. It begins with "the problem of Germany" and continues by dealing with the concerns of the other three major countries as they have come to terms with the increased economic influence of Germany and their own reduced political power in international affairs. The remaining countries of Europe are then divided into groups depending on their economic relationship to the European Union: Belgium, Luxembourg, the Netherlands, and Denmark form one group of small, open, high-income countries; Ireland, Greece, Portugal, and Spain form another group of small, traditionally rather closed, and relatively low-income countries; the European Free Trade Agreement countries as of 1990 are then divided into those that entered the EU in 1995—Austria, Finland, and Sweden—and those that did not—Iceland, Norway, and Switzerland. Turkey, the perpetual applicant that is continually rebuffed, is included in the last group. The final chapter deals with the next wave of potential entrants, divided into the Mediterranean islands of Malta and Cyprus and the transition economies of Central and Eastern Europe.

The basic issue that confronts the EU at each step of its evolution is whether to go deeper or wider—whether to intensify the economic and political integration of the existing set of members or to expand the possibilities of economic expansion and political influence by increasing the number of members. The possibilities for progress in either direction are now greater than ever before, which makes the choice even more difficult. All the factors that have entered the decisions made in the past have to be reexamined more intensely than ever, if we Americans and other non-Europeans are to appreciate the significance of the European actions over the coming years.

The authors wish to acknowledge the help of many individuals and institutions in formulating and presenting the material that follows. Barbezat benefited from his time at the European University Institute in Florence, made possible by a Jean Monnet Fellowship and a grant from the German Marshall Fund. Neal's early experience as a staff economist with the Organization for Economic Cooperation and Development (OECD) has been supplemented by the monthly

briefings provided to members of "Team Europe" by the U.S. Delegation of the European Commission in Washington, D.C. The Statistics Directorate of the OECD has granted permission to use their detailed data available on diskettes only for the national comparisons that are presented in Part II. Students at Illinois and Amherst have commented on early versions of most of Part I and, at Illinois, on the lectures that eventually became Part II. Janice Hunter was especially helpful in collecting material and then suggesting how it could be presented most effectively. The anonymous referees for Oxford University Press were very constructive in their suggestions and the editorial efforts of Kenneth MacLeod were exceptional. Colleagues have read and commented on several draft chapters, notably Jeremiah Sullivan at Illinois, Henry Gemery at Colby College, Luciano Pezzolo at the University of Venice, and especially Nick Crafts at The London School of Economics and Political Science for his comments on Part II. Finally, Margaret (Peg) Neal read, proofed, and criticized the entire text to make it as comprehensible as possible to non-economists and non-specialists.

August 1997

L. N.
D. B.

Abbreviations and Acronyms

ACP	African, Caribbean, and Pacific countries
APEC	Asia Pacific Economic Cooperation
ASEAN	Association of Southeast Asian Nations
BLEU	Belgium-Luxembourg Economic Union
CAP	Common Agricultural Policy
CEEC	Committee for European Economic Cooperation
(1948–52)	
CEEC	Central and East European Countries
(post 1989)	
CEN	European Standardization Committee
CENELEC	European Electrotechnical Standardization Committee
CET	Common External Tariff
CFI	Court of First Instance
CFP	Common fisheries policy
CFSP	Common Foreign and Security Policy
Coreper	Committee of Permanent Representatives
CSCE	Conference on Security and Cooperation in Europe
DG	Directorate-General
EAGGF	European Agricultural Guarantee and Guidance Fund
EAP	Environmental Action Program
EBRD	European Bank for Reconstruction and Development
EC	European Community
ECB	European Central Bank
ECJ	European Court of Justice
ECSC	European Coal and Steel Community
ECU	European Currency Unit
EDC	European Defense Community
EEA	European Economic Area
EEC	European Economic Community
EFTA	European Free Trade Association
EIB	European Investment Bank
EIF	European Investment Fund
EMI	European Monetary Institute
EMS	European Monetary System
EMU	European Monetary Union
EPU	European Payments Union (1950–58)

EPU	European Political Union (1992 on)
ERM	Exchange Rate Mechanism
ERDF	European Regional Development Fund
ESCB	European System of Central Banks
ESF	European Social Fund
ESPRIT	European Strategic Program for Research and Development in Information Technology
EU	European Union
Euratom	European Atomic Energy Community
GATT	General Agreement on Tariffs and Trade
GDP	Gross Domestic Product
GNP	Gross National Product
IBRD	International Bank for Reconstruction and Development (World Bank)
IGC	Inter-Governmental Conference
IMF	International Monetary Fund
IMP	Integrated Mediterranean Program
JET	Joint European Torus
MCA	Monetary Compensation Amount
MEP	Member of the European Parliament
MFA	Multi-Fibre Arrangement
NATO	North Atlantic Treaty Organization
OECD	Organization for Economic Cooperation and Development
OEEC	Organization for European Economic Cooperation
PHARE	Poland and Hungary: Aid for Reconstruction of the Economy
QMV	Qualified Majority Vote
SAD	Single Administrative Document
SAP	Social Action Program
SDR	Special Drawing Right
SEA	Single European Act
TACIS	Technical Assistance to the Commonwealth of Independent States
TEU	Treaty of European Union
VAT	Value added tax
VER	Voluntary export restraint
WEU	Western European Union

Chronology of the European Union

- January 1, 1948:** Trade agreement among Belgium, Netherlands, and Luxembourg creates Benelux.
- April 16, 1948:** Creation of the Organization for European Economic Cooperation (in 1960 to become the Organization for Economic Cooperation and Development, OECD)
- May 7–10, 1948:** Congress of Europe met in the Hague.
- April 4, 1949:** Creation of the Council of Europe and the signing of the North Atlantic Treaty (NATO).
- May 9, 1950:** Robert Schuman, France's Minister of Foreign Affairs, called for integration in European coal and steel sectors.
- September 19, 1950:** Creation of the European Payments Union (EPU) to aid trade liberalization and make European currencies convertible.
- April 18, 1951:** Creation of the European Coal and Steel Community (ECSC) with members France, Germany, Benelux, and Italy. Entered force on July 25, 1951.
- June 1 and 2, 1955:** Messina Conference held, setting into motion the move toward multisectoral European integration.
- March 25, 1957:** Treaty of Rome signed, establishing the European Economic Community with same members as the ECSC. In addition, the European Atomic Energy Community (Euratom) was created. Both came into force on January 1, 1958.
- January 4, 1960:** Creation of the European Free Trade Association (EFTA) with members United Kingdom, Denmark, Sweden, Norway, Portugal, Austria, and Switzerland. (Iceland joined in 1970 and Finland became a full member in 1986.)
- January 29, 1963:** General de Gaulle vetoed United Kingdom's membership application.
- July 20, 1963:** Yaoundé Convention signed between the Community and eighteen mainly French-speaking African states.
- September 12, 1963:** Association Agreement signed between the Community and Turkey, coming into force September 1, 1964.
- April 8, 1965:** Merger Treaty signed, combining the Euratom, ECSC, and the EEC into the European Community with a common Council and Commission. Came into force on July 1, 1967.
- July 6, 1965:** France boycotted discussions concerning Common Agricultural Policy financing.
- January 29, 1966:** France returned, after the Luxembourg Compromise, and majority voting replaced unanimity on issues affecting a country's vital interests.

- December 18 and 19, 1967:** France once again opposed U.K. membership and vetoed any resumption of negotiations on the accession of the United Kingdom.
- July 1, 1968:** Common customs tariff introduced and the last internal customs duties were eliminated (18 months before the deadline).
- September 24, 1969:** Arusha Agreement signed between the Community and three English-speaking East African States.
- April 22, 1970:** Luxembourg Treaty signed creating the own-resource finance system.
- January 1, 1971:** Second Yaoundé Convention signed between the Community and nineteen African, Caribbean and Pacific (ACP) countries. Came into force January 31, 1975.
- June 23, 1971:** The six member states reached agreement on the conditions for U.K. membership.
- October 28, 1971:** Majority vote for accession in the British House of Commons.
- January 18, 1972:** *Ode to Joy* from Beethoven's Ninth Symphony chosen as the anthem of the EC.
- January 22, 1972:** Treaty signed on the Accession of Denmark, Ireland, Norway and the United Kingdom.
- September 25, 1972:** Referendum in Norway rejected EC membership.
- December 19, 1972:** Association Treaty signed between the EC and Cyprus, coming into force June 1, 1973.
- January 1, 1973:** Denmark (including Greenland), Ireland, and the United Kingdom became full EC members.
- April 1, 1974:** New British government pressed for new accession conditions pertaining to finances.
- February 28, 1975:** Lomé Convention signed between the EC and forty-six ACP states, coming into force April 1, 1976, and ending March 1, 1980.
- May 11, 1975:** Cooperation Agreement signed between the EC and Israel, coming into force November 1, 1978.
- June 5, 1975:** Referendum in United Kingdom achieved a majority on retaining membership.
- April 25–27, 1976:** Separate Cooperation Agreements signed by Tunisia, Algeria, and Morocco with the EC, all coming into force on November 1, 1978.
- January 18, 1977:** Cooperation Agreements signed between the EC and Egypt, Jordan, and Syria, coming into force in November 1, 1978.
- May 3, 1977:** Cooperation Agreement signed between the EC and Lebanon, coming into force in November 1978.
- July 6 and 7, 1978:** At the Bremen European Council, France and Germany presented a scheme for the European Monetary System (EMS).
- December 4 and 5, 1978:** The European Currency Unit (ECU) created.
- March 13, 1979:** The EMS replaced the leftover "currency snake." The United Kingdom remained outside the system.
- May 28, 1979:** Accession Treaty for Greece signed, coming into force on January 1, 1981.
- June 7 and 10, 1979:** First European Parliament elections by direct universal suffrage, with 410 members being elected.

- October 31, 1979:** Second Lomé Convention signed between the EC and fifty-eight ACP countries, covering the period March 1, 1980, to February 28, 1985.
- April 2, 1980:** Association Agreement signed between the EC and Yugoslavia, coming into force April 1, 1983, but later suspended.
- January 1, 1981:** Greece joined the EC.
- June 17–19, 1983:** Member states issued a declaration on “European Union” at the Stuttgart Summit. (Genscher-Colombo document served as basis.) Ten member states expressed their wish to move to a European Union.
- February 14, 1984:** Altiero Spinelli’s draft Treaty for the European Union released and approved by the European Parliament.
- June 25 and 26, 1984:** Fontainebleau European Council set out conditions for the United Kingdom to receive rebates on EU contributions.
- December 8, 1984:** Third Lomé Convention signed between the EC and sixty-six ACP countries, covering the period May 1986 through February 1990.
- June 12, 1985:** Treaties on the accession of Spain and Portugal signed, coming into force January 1, 1986.
- June 14, 1985:** France, the Federal Republic of Germany, and Benelux started process to allow open borders among their countries (the Schengen agreement).
- December 2–4, 1985:** Based on the Lord Cockfield White Paper, member states agreed, at the Luxembourg Council, to eliminate trade and border barriers by drawing up a Single European Act.
- January 1, 1986:** Portugal and Spain became members of the EC.
- January 21, 1986:** Danish Parliament rejected the Single European Act. Other member states refused renegotiations. Single European Act passed Danish referendum by majority of 56.2 %.
- February 17, 1986:** Signing of the Single European Act (signed by the nine on the 17th and by Greece on the 28th).
- March 29, 1988:** The Cecchini Report on the Costs of Non-Europe released.
- November 1, 1989:** Start of the Court of First Instance.
- June 14–16, 1989:** Approval of the Delors Report on Economic and Monetary Union at the Madrid Summit.
- November 9, 1989:** Fall of the Berlin wall.
- December 15, 1989:** Fourth Lomé Convention signed between the EC and sixty-nine ACP countries.
- December 18, 1989:** Creation of the PHARE program (Poland and Hungary: Aid for Reconstruction of the Economy. Later extended to Bulgaria, Romania, Estonia, Latvia, Lithuania, Albania, Slovenia, the Czech Republic, Slovakia, and the Former Yugoslav Republic of Macedonia).
- June 19, 1990:** France, the Federal Republic of Germany, and Benelux signed the Schengen Agreement eliminating border checks for people.
- July 1, 1990:** First stage of economic and monetary union begun—removal of capital controls.
- October 3, 1990:** Unification Treaty between East and West Germany came into force.
- April 15, 1991:** Official establishment of the European Bank for Reconstruction and Development (EBRD).

- October 14, 1991:** Chancellor Kohl and President Mitterrand announced the creation of a combined Franco-German military force.
- December 16, 1991:** Association Agreements signed between the EC and Hungary, Poland, the Czech Republic, and Slovenia.
- February 7, 1992:** Treaty of European Union (TEU) signed in Maastricht.
- May 2, 1992:** Establishment of a European Economic Area (EEA) between EFTA and the EC.
- June, 2, 1992:** The Maastricht Treaty narrowly rejected (50.7% against) in Denmark.
- September 20, 1992:** France narrowly accepted ratification of the Maastricht Treaty with a 51.01 percent majority.
- December 11 and 12, 1992:** The twelve agreed on a compromise for Denmark's ratification of Maastricht.
- January 1, 1993:** The European internal market, goal of the SEA, officially declared.
- February 15, 1993:** EC Finance Ministers, while keeping the overall timetable of the EMU, agreed that member states need not fulfill the convergence criteria (debt less than 60% of GDP, deficit less than 3%, inflation under 2%) by the end of 1996.
- May 18, 1993:** Denmark passed ratification of Maastricht with a majority of 51.8 percent.
- July 19, 1993:** The Technical Assistance to the Commonwealth of Independent States and Georgia, TACIS, program adopted.
- July and August, 1993:** Crises in the EMS with massive currency speculation driving rates outside of the set bands.
- August 2, 1993:** EC finance ministers broaden the exchange rate bands from 2.5% to 15%.
- January 1, 1994:** The European Union officially begun. Stage II of the EMU began with the European Monetary Institute (EMI), headquartered in Frankfurt-am-Main, beginning operations. It is to help establish the pre-conditions for Stage III, coordinating central banks and establishing the European System of Central Banks.
- January 1, 1994:** The EEA came into force. Much tighter integration with the EFTA countries, Austria, Finland, Iceland, Norway, and Sweden.
- June 12, 1994:** Austria's referendum on joining the EU passed with a 66.3-percent majority.
- June 24, 1994:** Accession Treaties of Austria, Finland, Norway, and Sweden signed in Corfu.
- July 15, 1994:** Extraordinary summit called in Brussels to appoint Jacques Santer, prime minister of Luxembourg, as president of the European Commission, beginning January 1995.
- October 16, 1994:** Finland's referendum on joining the EU passed with a 56.9-percent majority.
- November 13, 1994:** Sweden's referendum on joining the EU passed with a 52.1-percent majority.
- November 28, 1994:** Norway's referendum on joining the EU lost with a 52.5 % majority. (EFTA continued, then, with members Switzerland, Norway, Iceland, and Liechtenstein)
- December 6, 1994:** Adoption of the "Leonardo da Vinci" vocational training program.
- December 22, 1994:** Executive Committee of the Schengen Agreement agreed in

Bonn to the elimination of border checks between the seven signatories (Germany, France, Benelux, Spain, and Portugal), starting March 26, 1995.

January 1, 1995: Austria, Finland and Sweden joined the European Union.

February 1, 1995: Europe Association Agreements enter into force with Bulgaria, Romania, and Czech and Slovak Republics.

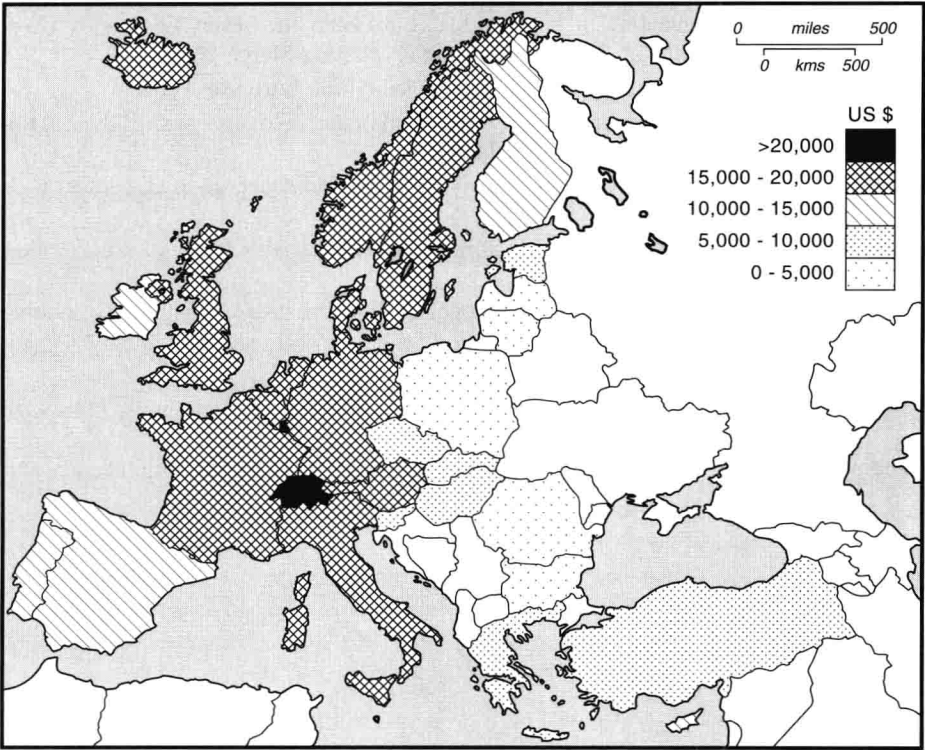
March 6, 1995: Council adopted framework for trade and cooperation agreement with the Republic of Korea.

July 17, 1995: Euro-Mediterranean agreement signed with Tunisia. Cooperation Agreement signed with Vietnam.

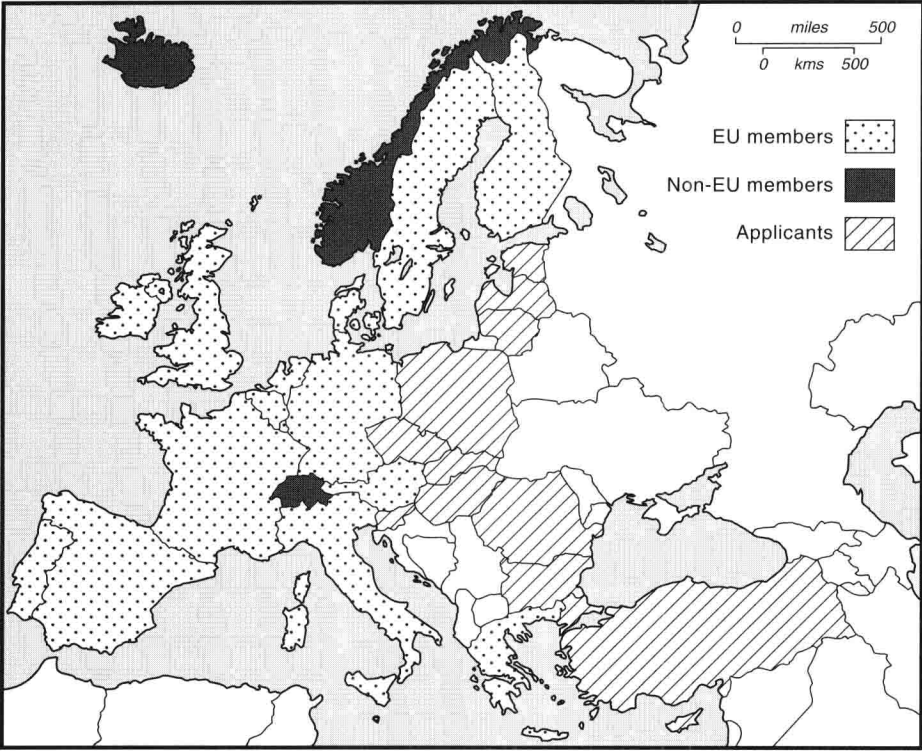
July 26, 1995: Member states signed Europol Convention, the Convention on Customs Information Systems, and the Convention for the Protection of Communities' financial interests.

November 23, 1995: "Partnership Declaration" adopted at the end of the Euro-Mediterranean Conference.

December 3, 1995: EU and the United States signed new transatlantic agenda and joint action plan.



Map 1. The Per Capita Income Levels in Europe, 1992.



Map 2. Europe: The EU Members, Non-members, Next Members, and the Rest.

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