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EC 92: IMPLICATIONS FOR UNITED STATES TRADE POLICY

BY

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Defense Logistics Agency

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EC 92: IMPLICATIONS FOR US TRADE POLICY

AN INDIVIDUAL STUDY PROJECT

by

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Defense Logistics Agency

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U.S. Army War College
Carlisle Barracks, Pennsylvania 17013
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ABSTRACT

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EC 92: IMPLICATIONS FOR U.S. TRADE POLICY

CHAPTER I

INTRODUCTION

Europe 1992. It is a movement. It is a process. It is a goal and an obsession. It is a state of mind. Europe 1992 is many things to many people. It is the integration of diverse national policies into a single entity. It addresses economic, political and diplomatic issues from a European perspective rather than from individual country perspectives. The progress and dedication to the European Community (EC) concept "is by itself ample evidence that the individual countries perceive their own national capabilities and resources as insufficient to achieve their national goals. These national goals cover the full range of state interests and objectives: security, economic and social development, political stability, democratic institutions, and technological advancement."¹ The world must understand the implications of Europe 1992. It is true dedication on the part of member countries who are required to forego national sovereignty to gain the benefits of a unified community. The interdependence which results from integration greatly constrains unilateral behavior of individual member countries, but "the EC [members] perceive these interdependence costs to be far less than the benefits received."² This suggests that Europeans have certainly become sensitized to the importance of cooperation if they are to survive in the dynamic and competitive

world of international trade. This paper will examine the evolution, structure and current issues facing the EC and the implications of these changes on the commercial environment of the United States.

The European Community is a market of 323 million consumers making it "the largest internal market in the developed world."³ The combined Gross National Product (GNP) will be \$4.2 trillion. By comparison, the United States has a GNP of \$4.4 trillion with a population of 241 million consumers.⁴ These numbers reflect the significance of the EC in the international market place. Other than the US-Canadian Free Trade Agreement, designed to be implemented over the next ten years, the EC 92 project will have the most obvious impact on US trade into the twenty-first century. An expanded agreement which incorporates Mexico is being considered to compete directly with the EC.

Try as they might, the leaders of the European Community have been unable to limit their involvement in the international community to trade issues. The EC is a very complex system in which economic, financial and institutional issues are all tightly interwoven.⁵ The broad objective of the EC is "the harmonious development of economic activities, continuous and balanced expansion, increased stability, a more rapid improvement in the standard of living, and closer relations between its member states."⁶ More specifically, the

objectives include the following:

- (1) the removal of barriers to trade among the member nations,
- (2) the establishment of a single commercial policy toward non-member countries,
- (3) the eventual coordination of transportation systems, agricultural policies, and general economic policies,
- (4) the removal of private and public measures restricting free trade, and
- (5) the assurance of the mobility of labor, capital, and entrepreneurship.

These objectives are very ambitious given the fact that attempts at European unification have historically been unsuccessful. The EC is taking a different approach this time, that of "unity by mutual consent, and it is striving towards a union based on a freely accepted body of law. By the very nature of things[,] progress is slow and laborious and sometimes made only reluctantly, for it is never easy for any government to give up its powers and prerogatives, and no administration is happy to abandon its traditions."⁸ This is certainly understandable, but it has become clear that the member countries have realized that they have much to benefit from this cooperation and are becoming more receptive to the concept. There is, however, a long road ahead before achieving the objective of having Europe speak "with a single voice on all major international and world problems, and to act together whenever it can and wherever it must."⁹ While the objective appears clear, the last phrase seems somewhat ambiguous: clearly the Community has not yet found an acceptable mechanism to resolve internal differences and consistently present a unified position to the international community. By working together, the EC will encourage cooperation among firms from

different member states. This should greatly benefit EC firms while "Europe builds the muscle to match Japan and America in the world market."¹⁰

The United States has generally been supportive of a progressive Europe. Our interests in the region are numerous. Geopolitically, we are a major presence in NATO providing for a common defense to protect against a common threat. In the area of foreign policy, we cooperate heavily and present a common voice on such diverse issues as terrorism, South African apartheid, and events in the Middle East. Politically, we support economic development and provide assistance to emerging democracies. Most importantly, the US and the EC have an interdependent economic relationship. Recent figures indicate total trade between the US and the EC exceeded \$125 billion with direct investments totalling \$190 billion.¹¹

The foundation upon which US and European cooperation originated can be traced to three key factors:

- (1) mutual fear of Stalinist Russia,
- (2) Soviet rejection of the Marshall Plan (and thus rejection of US reconstruction aid), and¹²
- (3) need for each other's markets.

The US fully supported European integration at its inception because the unified Europe presented a formidable force against Communism. "The two sides of the Atlantic were united in the face of what they perceived as a threat from the Soviet Union, and the dominance of the United States in the field of defense ensured close cooperation."¹³
The US must now consider the effect that this changing threat will

have on the US/EC relationship. Some possible consequences will be examined later in this paper.

The development of a unified European Community has not been without obstacles. In fact, some would argue that to consider the EC as a unified community even now is premature. There have been numerous attempts at integration and cooperation at various levels within the Community during this century. Some, such as the European Coal and Steel Community (ECSC) have been remarkably successful while others such as the European Defense Community have been dismal failures. However, all attempts, successes as well as failures, have "contributed to the inexorable realization by Europeans that there was no viable alternative to political cooperation. In one sense, the failures might have contributed more to the [realization] because they sensitized the policymakers and the population to the risks of unbridled nationalism and unlimited sovereignty."¹⁴

As previously mentioned, one positive attempt at integration which proved the viability of an economic union was the European Coal and Steel Community. The ECSC did not attempt to unify the entire economy. Instead, as the name implies, it created a free-trade zone with the elimination of all artificial barriers to trade within the coal and steel sectors of the European economy. The concept behind this experiment was that "if governments could learn to cooperate in certain, limited 'non-political' areas, then perhaps spillover effects would lead to additional coordination, cooperation, and integration...as economic benefits mounted for participating

governments..."¹⁵ From this initial attempt, governments realized the importance of cooperation. They realized that individually, they were too small to compete effectively in the international market, but as a unified organization, they could wield significant influence and power. In short, governments finally came to realize their collective weakness and vulnerability and had a tool which could improve their situation.¹⁶ The concept of a European Community came from this realization. It was formed from a consolidation of the European Economic Community (EEC), the ECSC and the European Atomic Energy Community (Euratom). The EC was to initiate the economic and political unification of Western Europe.¹⁷

Perhaps the European Community was premature in striving for total integration and cooperation at all levels. As a result of economic integration, the EC has estimated that the economic growth rate will increase from two to five percent, that prices will decrease by six percent as a result of efficiency gained from economies of scale and that two million new jobs will be created.¹⁸ This is an ambitious projection if one compares the current performance of the Community against that of its strongest competitors¹⁹:

	<u>European Community</u>	<u>United States</u>	<u>Japan</u>
Economic Growth (since 1980)	1.6% per yr.	3.0%	3.6%
New jobs (since 1975)	<7 million>	13 million	4.5 million
Unemployment	11.0%	6.0%	3.0%

Success of European integration to the degree envisioned by its proponents will require unprecedented changes. To begin, "thousands

of laws and regulations governing the production and sale of goods and services and the movement of people and capital must either be abolished or 'harmonized' (a favorite Euroword, meaning that when complete agreement among the twelve nations is impossible, approximate agreement is okay).²⁰ Harmonization will reach into every aspect of the Community addressing such diverse issues as technical and industrial standards and regulations, differences in value-added taxes, standardization of property and bankruptcy laws, elimination of residence requirements, universal recognition of educational diplomas and removal of all licensing restrictions.²¹ The tasks are formidable, and many are doubtful that they can all be completed by the magical date of 31 December 1992.

The expectations for the success of 1992 among its members is as varied as the members themselves. France seems to be the most excited about 1992 which seems to indicate that it has the most to gain. "The advance towards an open Europe already dominates its economic policy."²² Italy and the Netherlands appear to be equally optimistic. Germany and Spain are working towards the success of 1992, but both have some reservations. Usually the optimist, Belgium is somewhat hesitant, and Denmark, while not enthusiastic, is resigned to 1992. The United Kingdom seems to be the most wary.²³ Europe 1992 will be a double-edged sword for its member countries and for outsiders such as the United States who have significant trade interests in the region. There will be both increased risk and increased opportunity to many companies. Markets which have long

been protected by economic nationalism will be opened. There is a risk that some companies could suffer at the hand of more efficient competitors. Likewise, there is a great opportunity for efficient companies to greatly expand their markets.²⁴

Despite all of the uncertainties, it is apparent that no one has yet to fully comprehend the changes which will occur as the economic market of Europe opens. The European Community clearly has the intention and determination to become "a unified economic force as powerful as the US or Japan".²⁵ While this goal is attainable in some form, there are still problems which plague the bureaucracy of the EC, and the resolution of these problems will directly affect the position of the US trade in the area. The principle problem for the EC unification is the fact that there is "too much national egoism and not enough Europe".²⁶ While each member country is willing to reap all of the benefits from the proposed unification, they are much more hesitant to implement the difficult changes which are necessary for this unification to work. They seem to forget that "some surrender of national sovereignty is the price West Europeans accepted when they ...endorsed that frontier-free vision of the 1990's".²⁷ If 1992 is to be fully successful, the national governments of the member countries will have to consciously raise the political will of the people to accept some loss of national sovereignty with an assured payback which will benefit everyone in the long term. "Europe's...people will, in principle, be allowed to vote with their feet, or their wallets, for the member-state that

offers them laws with the right blend of freedom and responsibility."²⁸ Everyone stands to gain if true cooperation is achieved. The EC has much at stake with the arrival of 1992, and Emile Noel, the Secretary General of the Commission of the European Communities, feels that the Community must succeed; failure would put "into question every member's general policy and handling of its economy...Given the importance of the Community's geopolitical role in the operation of international trade, the balance of the world economy and international relations..., its members have to rise above their disputes if they are to assume their joint responsibilities."²⁹ How has the EC arrived at this stage of development? Will its objectives be achieved? How will the United States be affected by these developments? The remainder of this paper will seek to answer these questions.

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CHAPTER II

HISTORY

Essential to understanding the concept of Europe 1992 is to understand the history of the European Community and its composition. Because of geographic proximity and common history, the countries of Europe have always been interrelated. The relationship has usually been friendly and productive; at other times, the relationship has been hostile and competitive. The EC member countries share a common history, but have often pursued different, and sometimes opposing, national goals. This chapter will examine the history of the EC, the convergence of national wills and the key events which have evolved into the concept of Europe 1992.

The current composition of the European Community is the result of a colorful history. Originally composed of six member countries, the EC now has twelve members and even this number is subject to change. The original members were united under the Treaty of Rome in 1957. They included Belgium, France, Italy, Luxembourg, the Netherlands and West Germany. Since that time, the membership has changed, but the general concept of a unified economic union has remained. In 1973, Denmark, Ireland and the United Kingdom joined the EC. In 1981, Greece gained membership. Most recently, Spain and Portugal were admitted to the EC in 1986. Greenland joined the EC as

a part of Denmark when it was a dependent state, but withdrew in 1985.¹ Turkey has recently applied for EC membership, but approval is unlikely.²

Conspicuously absent from EC membership are several key European countries. While not interested in limiting their sovereignty to pursue national interests, these countries realized the potential power of a union such as the EC. Shortly after the EC charter under the Treaty of Rome, these countries took steps to protect themselves. The result was the formation of the European Free Trade Association (EFTA) in May 1960.³ Current membership includes Austria, Finland, Norway, Sweden and Switzerland. Internally, the EC and EFTA have developed free trade provisions. However, outsiders such as the United States must deal with the EC as an entity and with each member of EFTA individually. More discussion on the implications for US trade within Europe will follow later in this paper.

The constitution of the European Community is composed of provisions contained in the Treaty of Rome which established the European Economic Community (EEC) and the European Atomic Energy Commission (Euratom), together with provisions of the Treaty of Paris (signed in 1951) which established the European Coal and Steel Community (ECSC).⁴ The union was considered necessary by the member countries as they became increasingly dissatisfied with their positions in the international economic arena. In most instances, "the continued strategic dependence of Western European countries on the United States and their very limited power turned them into

frustrated observers of international events over which they had very little influence...This was particularly hard to accept for some of the big countries which still seemed to entertain illusions of world power."⁵ With this mood prevalent in Western Europe, the stage was set for decisive action. The result was the Monnet-Schuman Declaration (09 May 1950) - this was Western Europe's initial attempt to address its frustration. The purpose of the declaration was "to start a long-term process of laying the foundations for a new relationship between France, Germany, and such other countries as were prepared to join, which could go so far as to lead to a European Federation".⁶

The original goal of the European Community was to abolish internal tariffs and quotas. The six original members were successful at achieving this goal until a series of economic setbacks tested the resolve of the members. Unfortunately, member countries were not willing to remain unified for the good of the union during trying times and reverted to the protection of their nationalistic interests. Some of the events of the early 1970's which led to this return of nationalistic spirit were the failure of the Bretton Woods accords which created monetary chaos and the Middle East oil embargo which virtually paralyzed the European economy. As a response to these events, member countries introduced new border taxes, "national production or trade quotas were reintroduced, national subsidies increased and non-tariff barriers to trade multiplied".⁷ As a result of these nationalistic actions, the move towards economic unification

was severely hampered, and in some cases, the gains which had been made were lost completely. The inability of the EC to speak with a unified voice to the rest of the international community significantly reduced its clout and influence. The outside world perceived, probably correctly, that the EC had evolved into a very inefficient and extremely bureaucratic organization which had seemingly lost sight of its goals.⁸

It is interesting to follow the evolution of the EC from a group of independent, nationalistic countries through its organization and restructuring to its present day structure. It is important to understand that the transition from national economic independence to Community cooperation has not been without significant problems. As previously stated, the EC was initially formed with the signing of the Treaty of Rome on 25 March 1957.⁹ The first significant action taken by the Community came in January 1962 when, after extensive political debate, the EC adopted its Common Agricultural Policy (CAP). This policy still remains a topic of emotional internal and external controversy. The major principles of the CAP are:

- (1) the establishment of a single market and consequently of common prices for most agricultural products,
- (2) agricultural workers will have comparable standards of living to workers in other sectors of the economy, and
- (3) there will be a preference for EC produce.¹⁰

Here we see the first concrete example of EC protectionism, and it is a problem which will grow in significance as the Community matures.

Today, as 1992 approaches, a primary concern for US exporters to the EC is the extent of direct and indirect protectionism which they will face.

By 01 July 1968, the provisions for the EC customs union were adopted; this was eighteen months ahead of plan. This union effectively removed all custom duties in trade between member countries and established a common external tariff.¹¹ This action is significant because, for the first time, the Community presents a unified policy to the outside. By March 1971, the European Monetary System (EMS) had been developed, and the Community hoped that this would be accompanied by a "greater convergence of economic policies".¹² The principle components of the EMS provide for the establishment of:

- (1) the European Currency Unit (ECU) which became the unit in which all internal transactions are valued,
- (2) an exchange and information mechanism,
- (3) monetary transfer arrangements, and
- (4) credit facilities.¹³

By 01 January 1973, free trade agreements had been established between the European Community and some of the EFTA members, specifically Austria, Sweden and Switzerland. Agreements with the other EFTA members would follow later. Under these agreements, EFTA members benefit from unrestricted trade with the EC and thus have significant trade advantages, but they are not restricted by EC common policies in their external commercial policy.¹⁴ In short, EFTA members have the best of both worlds: they have free access to the EC markets without having to limit national sovereignty.

In 1974, the EC began to take note of the importance of presenting a unified force to the international community. The inability to speak with a common voice was undermining the acceptance of the EC throughout the world. To correct this problem, the European Council was formed. It was composed of the Heads of State or Government and was chartered with the responsibility to meet three times per year to discuss and resolve importance issues on European affairs, economics, trade and foreign policy.¹⁵

In 1979, two important events occurred. First, the CAP came under the scrutiny of other sectors of the Community's economy, especially manufacturing industries. They greatly resented the agricultural policy feeling they were bearing an unfair burden for paying the subsidies.¹⁶ They felt that the profits from their efficient operations were being unfairly used to support an inefficient industry. As a result, agricultural subsidies were eliminated, and a system of intervention prices was implemented which essentially established price floors. Called by another name, agricultural prices are still artificially inflated to support an inefficient industry. These price supports account for a huge portion of the EC budget, and the issue is still an area of heated debate today. The second significant event of 1979 was the implementation of the EMS. It basically "linked the currencies of the [EC] member countries (excepting those of England and Greece, who declined to participate) so as to avoid large day-to-day fluctuations in currency rates while permitting periodic realignments".¹⁷

As economic pressures continued to mount following the oil crisis, EC member countries became increasingly nationalistic, losing sight of the advantages to be gained from an economic union. Each country pursued policies which were to its own national benefit without considering the implications for the Community as a whole. Realizing the lack of organization within the Community, member governments reaffirmed their dedication to the unified Europe concept in the Treaty of Economic Union, signed in February 1984. This treaty indicated the intention of members to cover "both revision of the Treaties of Rome and legal enshrinement of political cooperation, thus emphasizing the oneness of the European system and offering the chance of links between the Communities and political cooperation in the future."¹⁸ In other words, the member countries must get on with the business of total unification. The result of this realization was the Single European Act, developed in 1985. It "modifies EC decision-making with the aim of improving efficiency".¹⁹ The act promotes cooperation in high technology, social policy, environmental issues, research and development, economic convergence, and budgetary issues. It also stresses a "European external identity" by promoting movement towards a common foreign policy.²⁰

This brief history of the European Community indicates that it has been a rough road thus far, that the member countries are dedicated to a European unity at some level, that significant progress has been made and that a lot of work still remains. The evolution has progressed with varying degrees of inertia. "Until the

end of the 1970s, the route to a common market was thought to lie through 'harmonization'. Frontiers would wither as the pasta, taxes, company laws and anti-terrorist policies on either side of them were forced by the Eurocracy to conform to Euro-norms that would make the Community a seamless continuum. It was a hopeless prospect wherever countries were asked to take unanimous decisions over national quirks that were dear to them."²¹ It has been feared that the internal rifts and the inability to harmonize has "seriously eroded the EC's credibility as a force in international politics".²² This paper will examine this hypothesis in the following chapters. Much work remains to be done in preparation for Europe 1992, and the world will be watching closely as the Community invokes changes which will have a significant impact on the world trade situation.

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CHAPTER III
ORGANIZATION

The historical evolution of the European Community has been examined, but it is also important to understand how the diverse governing bodies were incorporated into a cooperative structure. As previously outlined, the European Coal and Steel Commission (ECSC), the European Economic Community (EEC) and the European Atomic Commission (Euratom) were the forerunners of the EC. When these organizations were consolidated, the challenge of creating a consolidated governing body was presented. Each organization had its own distinct, but similar governmental structure. The Treaty of Rome recognized this requirement and addressed it. The attempt to avoid the replication and confusion arising from three governing bodies, though somewhat ineffective, provided for a single assembly (or Parliament) and a single Court of Justice. The result was a body composed of "three Councils of Ministers, two Commissions and one High Authority, one Assembly, one Court of Justice, one Economic and Social Committee and one Consultative Committee. But since the Council of Ministers was identical under all three treaties, a strange ritual had to be observed. The Council of Ministers would convene and conduct business under the authority of, say, the ECSC treaty, but, before dealing with EEC matters, the Council would have to adjourn formally and then reconvene immediately under the authority of the second treaty. This charade lasted for almost ten

years."¹ Recognizing that this was a serious problem and an inefficient means to conduct business, the EC members signed the Merger Treaty on 08 April 1965 to consolidate the executive institutions of the three groups "into a single, unified framework".² The detail of the organization created by the Merger Treaty will be examined shortly.

The EC was formed to promote international cooperation and economic development. The Community shared similar interests and aspirations and understood the significance of a Europe without borders or conflict.³ It seems to be national interests which preclude this from occurring efficiently. Even the consolidation of governing bodies has not significantly improved the ability of the Community to cooperate on the difficult issues which effect national sovereignty. The slow, cumbersome and inefficient decision making process within the Community makes it slow to respond as a single voice to rapidly developing situations in the international arena. For example, the EC has not yet been able to respond as a Community "to increasing international pressure for economic sanctions against South Africa".⁴ The ability to present itself as a single entity is a challenge which faces the EC hierarchy if it is to gain the recognition and respect of the world economic community. An investigation of the actual structure of the governing body will provide some insights into why this goal has been so difficult to achieve.

The principle organizations within the EC as a result of the Merger Treaty include the Council of Ministers, the European Commission, the European Parliament (EP), the Court of Justice and the Economic and Social and the Consultative Committees. The bureaucracy employs 18,000 people divided as follows:

European Commission	12,500 employees	
European Parliament	2,700 employees	
Council of Ministers	1,800 employees	
Social/Consultative Committees	500 employees	
Court of Justice	500 employees	5
Court of Auditors	300 employees	

EC employees work primarily between Brussels, Luxembourg, Strasbourg and their member countries. While the number of employees may appear high, there is much concern that this current level of support will be unable to handle the workload created by the EC, especially as 1992 draws near.⁶

The real governing body of the EC is the Council of Ministers. It is composed of twelve members, one representative from each member country. However, the representative at different sessions may change. For example, if agricultural issues are being discussed, an agricultural minister may attend the session, while a finance minister might attend sessions dealing with tax issues.⁷ It appears that the potential exists for discontinuity as many of the issues are interrelated. For example, discussions concerning the level of agricultural subsidies should involve both the agricultural and

finance ministers. If each person is only concerned with his area of expertise, there appears to be no one who maintains a global view of all policies under consideration.

The Council of Ministers works independently of all other EC institutions, but dominates the EC decision making process. The President of the Council, who is strictly an administrator, changes every six months between members.⁸ This would appear to create an instability which is built into the system. The Council represents and protects the national interests of the member countries. "These national interests are often conflicting, and they are also quite frequently at odds with what other actors in the process perceive to be the 'European' interest."⁹ This is contrary to the concept of a unified Europe; protecting individual interests only encourages further exploitation of national sovereignty. The votes within the Council are weighted by country to prevent the domination of the larger member countries. The Council vote is apportioned as follows: West Germany (10 votes), France (10 votes), United Kingdom (10 votes), Italy (10 votes), Spain (8 votes), Belgium (5 votes), Netherlands (5 votes), Greece (5 votes), Portugal (5 votes), Ireland (3 votes), Denmark (3 votes) and Luxembourg (2 votes).¹⁰

The Council of Ministers is assisted by the Committee of Permanent Representatives (CPR), a group of diplomatic personnel who actually work technical, administrative and policy issues. Also working for the Council is the Committee of Jurists-Linguists, lawyers specializing in legal administrative drafting. These

language expert lawyers ensure that "texts say the same thing - or are as equally vague - in all nine Community languages".¹¹

The European Commission is composed of seventeen members which are, like the Council of Ministers, apportioned between member countries to avoid domination by the larger members. France, West Germany, Italy, Spain and the United Kingdom each have two members on the Commission; the other seven member countries each have one representative on the Commission. The representatives are nominated by their member countries and approved by the Council of Ministers. They serve four year renewable terms. The President and four Vice-Presidents are appointed by the Council of Ministers to serve two year renewable terms. The European Parliament is empowered to impeach the entire Commission, but it may not impeach any single representative.¹²

The European Commission protects and represents the global interests of the European Community, and counters member governments' more narrow, nationalistic interests represented in the Council of Ministers.¹³ The Commission is chartered to:

- (1) initiate and present policy proposals to the Council of Ministers,
- (2) supervise the execution of treaties and ensure that all member countries are adhering to EC legislation,
- (3) administer the operation of the EC, and
- (4) act as a conciliator of national viewpoints and secure acceptance of measures which are in the best interest of the EC.¹⁴

The Commission's summarized responsibilities as outlined above extend to every aspect of the EC. While not all inclusive, some of

the major committees (referred to as portfolios) of the Commission are:

- | | | |
|---------------------------------------|-----------------------------------|------------------|
| * Monetary Affairs | * Agriculture | * Fisheries |
| * Mediterranean Policy | * North-South Relations | * Environment |
| * Budget/Financial Control | * Consumer Protection | * Nuclear Safety |
| * Administration | * Forests | * Transportation |
| * Internal Market | * Customs Unions | * Energy |
| * External Relations | * Commercial ₁₅ Policy | |
| * Educational and Vocational training | | |

The European Parliament (EP) is a unique organization within the EC bureaucracy because of the fact that its members are elected by the EC voters to represent the interests of the European people.¹⁶ Membership is by universal suffrage for a five year term. The seats are allocated to each member country in approximate proportion to population. The total EP membership is 518 representatives. One of the major points of controversy is the fact that voting procedures are slightly different in each member country; therefore the basis for selection is not the same for each member. Some examples of the differences between member countries are minimum voting ages and the dates of elections. The EP is working to establish a uniform procedure for elections, but like many other EC initiatives, individual nationalism is hampering their efforts.¹⁷ Unfortunately there is a general lack of understanding and interest in the EP. Many voters are not even aware that it exists, and many more do not understand its function. For these reasons, voter turnout has been minimal since the first EP election in June 1979.¹⁸

Perhaps the reason for the general ignorance about the EP on the part of the voting public is the lack of power and authority vested

in this organization. The EP is chartered with the "explicit mandate to 'monitor' the activities of the Commission (the Commission is 'responsible' as a collective body to Parliament)".¹⁹ The EP has no real power, and as such, the implication is that the European people have no voice in the EC government. While the EP has the authority to force the resignation of the EC Commission, it would have no voice or influence over the replacement Commission. It is, in fact, the Council of Ministers which holds the real power and decision making capability within the EC hierarchy.

In essence, most of the Parliament's power is as a by-stander or a consultant. "It is only with certain parts of the Community budget that Parliament's opinion is binding on the Council of Ministers - the EP has the power to reject the entire budget by a majority vote of its members."²⁰ The EP also has the power to vote additional funding up to 20 percent for certain nonobligatory expenditures such as social and environmental programs. The EP does not, however, have the power to reduce or eliminate any programs from the EC budget.²¹

The President of the Parliament is elected by the entire EP as are the twelve Vice Presidents. There are eighteen specialized committees including Political affairs, Economic, monetary and industrial policy, EC budget, Agriculture, Transportation and Environment. "The membership demographics of each committee attempts to reflect the national and political characteristics of the Parliament as a whole."²² Unfortunately, this often results in membership assignment to specific committees because of nationality,

with no consideration of the member's interests or expertise. Because most of the EP work is done in committees (similar to the US Congress), this flaw in assignment also contributes to the ineffectiveness of the EP as part of the EC governing body. In short, "the EP is engaged in the symbolism of politics without its essence".²³

The judicial body of the European Community is the European Court of Justice (ECJ). The principle responsibility of the ECJ is "to represent the interests of law, justice, and equity in the interpretation and application of the threetreaties [EEC, ECSC, Euratom], other EC texts, and Community legislation and decisions made pursuant to the treaties".²⁴ There are thirteen judges on the ECJ, one from each member country except the Netherlands which has two judges. This was done to have an odd number and avoid any possibility of a split decision. The judges are nominated by national governments and approved by a unanimous vote of the Council of Ministers. EC legislation does allow for judges who are of non-EC nationality to serve on the ECJ, but this has never happened. Once appointed, a judge serves a six year renewable term. Actions can be brought to the ECJ by individuals, corporations, member country governments and any institution of the Community.²⁵

The majority of the time in the ECJ is spent "issuing preliminary rulings and/or advisory opinions" which usually deal with administrative technicalities.²⁶ It is very interesting to note the limitation on EC legal power: the ECJ can impose punishments, force

actions and levy fines, but it cannot send anyone to prison. "Criminal violations, and thus criminal sanctions, do not exist at the EC level, and the European Community does not have any law enforcement personnel or prisons."²⁷ The responsibility for criminal prosecution remains with the national law enforcement authority within the member countries. The Court of Justice is effective within the limits of its charter, but one would expect to see greater prosecution authority in the areas of fraud, contract violation and many other legal trade issues. Again, this should be part of the EC attempt to present a unified presence in the international marketplace.

The Court of Auditors is in essence the financial overseer of the EC. As one would expect of any auditing function, it is responsible for the examination of the revenues and expenditures of the EC. Additionally, "the Court of Auditors has the ability to issue preliminary rulings and/or advisory opinions, if requested, on financial regulations and the internal audit procedures of the individual EC agencies".²⁸ This court is composed of twelve members, all EC nationals, who have been appointed by a unanimous vote of the Council of Ministers in consultation with the European Parliament. Each member serves a six year renewable term. The members of the court choose a President who serves a three year term.

Within the EC structure, there are no fewer than 1,500 committees and working groups. The most important of these are the Economic and Social Committee (ESC) and the Consultative Committee.

These committees "represent the organized economic, social and functional groups across the Community".²⁹ Both committees act as links between the EC institutions and hierarchy and public opinion. While they have no decision making authority, the committees must be consulted by the European Commission or the Council of Ministers on most key issues.

The ESC serves a consulting role within the EC structure. It is "composed of representatives from the organized economic and social groupings within member-states of the Community, and it forms an integral part of the EC institutional framework and decision-making process. The ESC was established to involve, in an open and explicit fashion, the many European economic and social groups in the formulation of EC policy..."³⁰ While the ESC does not hold any binding authority, it does serve effectively in the function for which it was originally established: a forum through which "the organized European interest groups can influence the content of Community policy".³¹

As previously mentioned, the second important committee within the EC structure is the Consultative Committee. It focuses on the European Coal and Steel Community (ECSC), but is similar in scope to the ESC. The committee involves three groups: the coal and steel producers, the workers and the consumers, dealers and transporters. The committee is primarily concerned with the general objectives of the industry, markets and prices, labor problems and research and development projects. Membership is allocated to each member country

to approximate its share of the total EC coal and steel production. The members are appointed by the Council of Ministers for a two year renewable term. The President is elected annually by the committee members. As is true of the ESC, the Consultative Committee is a group of expert advisors who have no power to issue any binding decision, regulation or directive. They do, however, influence the policy making process.³²

While the focus of this paper is the European Community and the implications that internal changes will have on US trade in Europe, this is not the only organization which can impact the US trade position in Western Europe. As was briefly mentioned in the previous chapter, the European Free Trade Association (EFTA) was formed in response to the increasing influence of the European Community in the international marketplace. EFTA was an attempt "to patch together some sort of rival free-trade area organization both to protect their own interests and to compete with the EEC".³³ The goals of EFTA include "economic expansion, full employment, the rational use of resources, financial stability, and a higher standard of living".³⁴ EFTA addresses only trade between its members and the EC; all external trade policy is developed in accordance with national interests, goals and objectives. Therefore, when developing trade policy and strategy, the US must be aware of the differences between these two unique organizations and adapt to each environment.

This chapter has thus far focused on the structure of the EC and the organizations which influence the direction of the Community. An

understanding of this structure and its key influences is essential if the US is to position itself for continued trade in the next decade. There is, however, one final influence on the EC which must be analyzed to make the discussion complete: the European Community's budget. Resourcing Europe 1992 is an expensive and very controversial issue. As this chapter has illustrated, the EC hierarchy (often referred to as the Eurocracy) is expansive, and member countries see it as a drain on their resources. Keep in mind that while the European population is supporting the Eurocracy, they are also supporting their own national, regional and local government structures. The revenues required to support the seemingly unending bureaucracy are substantial. It is no surprise, therefore, that a major internal EC problem is the funding of the Community. The EC leaders must resolve the question of how to ensure sufficient funding in an efficient manner which is fair to all members. "Even more in dispute than the amount of money needed is the spending of it, and particularly the spending of huge sums on meeting the demands of the Common Agricultural Policy."³⁵ This issue will have to be resolved before the idea of a unified Europe can be pursued much further.

While one may be surprised by the amount of the EC budget, the real value becomes even more questionable when it is realized that very little of the budget directly benefits the general EC population. There are little, if any, services provided to the people; this is presumed to be provided by national governments. The total EC budget for 1987, for example, was \$35.6 billion. What

direct benefit did the average European citizen receive for his contribution? The typical expenditures of the EC budget are distributed as follows:

Agriculture	65.9%	
Regional policy	7.7%	
Social policy	7.5%	
Administration	4.8%	
Cooperation with developing countries	3.4%	
Research, energy and industry	2.6%	
Fisheries	0.6%	
Miscellaneous	7.5%	36

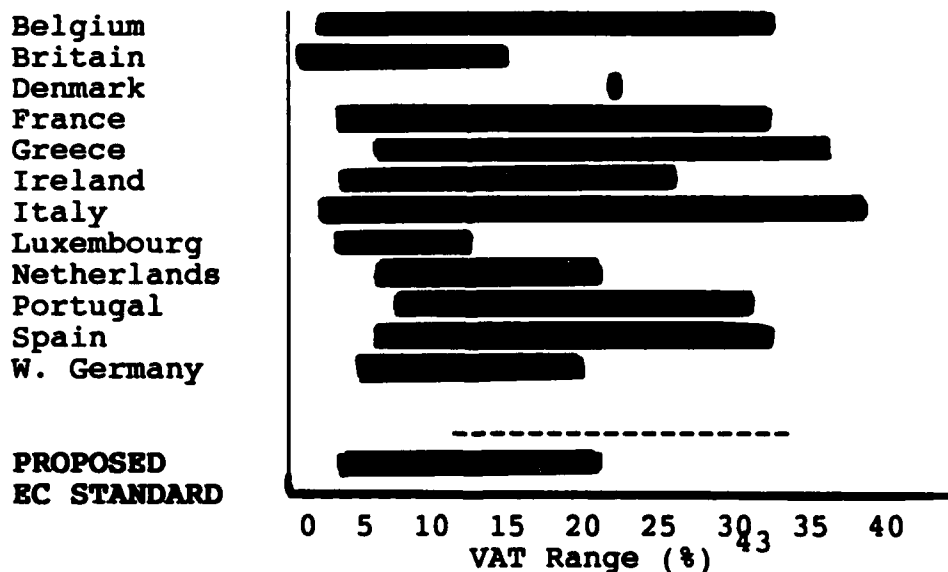
Notably absent from this budget are expenditures for education, infrastructure improvements, social security and health programs. Because these are provided by member countries, the EC does not fund them. What the EC does fund is artificial support to an inefficient agricultural industry and a large, and questionably inefficient, bureaucracy. It is no wonder that the people are beginning to question the cost/benefit ratio of the EC, especially when the EC policy makers are demanding more and more funding. As a example of this trend, the annual EC budget quadrupled between 1977 and 1986.³⁷ Unfortunately the Eurocrats seem oblivious to the public dissatisfaction. Jacques Delors, president of the European Commission, continues to advocate a larger EC budget despite opposition from many EC leaders (especially Margaret Thatcher). He plans to eliminate the EC budget deficit of approximately \$4.5 billion, increase spending by one-third and alter the rules for national contributions to the EC budget.³⁸ Stronger financial controls will improve the situation, but the bottom line will be a

larger budget which will require the EC to generate more revenue. The situation mirrors the current US dilemma: raise taxes or cut spending. The difference in the EC is that the population does not see any direct benefit from their contributions to the budget. An important key to the success of Europe 1992 will be its financial stability.

The largest single source of income in the EC budget is its share of the Community-wide Value Added Tax (VAT). This alone accounts for approximately 63 percent of the total EC revenues.³⁹ Currently, the EC structure receives 1.4% of all VAT collected within the Community. Other important sources of revenue are the import duties and levies collected by member countries.⁴⁰ Under this concept, each country is paying a fixed percentage of its revenues to support the EC. It is argued that a more equitable system of resourcing must be found so that contributions are based on each member country's ability to pay. One solution being considered is to base member contributions on each country's share of the EC Gross National Product.⁴¹

Unfortunately, the tax problem is not limited to member contributions. The difference in tax rates between member countries could be an important factor in the location of capital resources once the borders open completely. This could encourage a competition between countries reminiscent of the gas wars of the 1960s in the United States. In this situation, it is possible that countries would lower tax rates to attract more business only to have a

neighboring country lower its taxes even more to attract the same business. The implications of such a battle are obvious. "At present, rates of value-added tax vary wildly across the Community, from 38% for some luxuries in Italy to 0% for some 'necessities' in Britain. The Commission wants the differences in VAT rates reduced to the five-six percentage points which - America's experience with state taxes suggests - are the most a frontier-free market can bear."⁴² Otherwise there is incentive for people to go outside the country to make purchases, and this is not a truly open market. The disparity between the current VAT rates between member countries is illustrated in this chart:



Standardizing taxes will be important if the EC is to avoid large movements of capital to EC countries having the most liberal tax laws. Of course, it can be argued that this is the whole idea behind a free market economy: resources flow to meet demand. There

is a fear that standardized VAT rates will fuel inflation in countries currently having the lowest tax structures.⁴⁴ However, there is agreement that EC 1992 success will necessitate that all indirect taxes be brought more closely in line. Standardization would still allow for some individual country fluctuation, but even so, some countries such as Denmark and Ireland would lose a large part of their tax revenues. By contrast, Luxembourg would risk losing many businesses, particularly in the financial sector, which have thrived because of the low tax structure.⁴⁵

The final result of this debate is anyone's guess, but it is clear that member countries will be reluctant once again to relinquish their national sovereignty on the tax issue. The ramifications are many. For example, how does a country continue to function and provide services to its population when it experiences a forced reduction in budget revenue of ten percent or more? On the other hand, how does a population which has historically enjoyed a low tax structure (and has structured its lifestyle around this structure) deal with a sudden increase in its cost of living of ten percent or more? These changes may be too much for the EC population to accept, and this will certainly impact on the prospect of a total EC economic union in 1992.

This chapter has examined the organizational structure of the EC as well as some of the operational problems which plague the Community. This understanding is essential if we, and the rest of the international trade community, are to understand the movement

which is currently driving Europe. Failure to recognize the changes and understand the forces behind these changes will only ensure that we are left out of Europe 1992. The walls within Europe are falling, only to be replaced with a large wall around Europe, a movement unpopularity referred to as Fortress Europe. Anyone who fails to recognize this and take affirmative steps to prepare for the changes will find himself locked out of a very lucrative market. The next chapter will examine some of the trade issues which will face the world trade community over the next several years.

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CHAPTER IV
THE EUROPEAN COMMUNITY AND US TRADE POLICY

Conversations relating to the prospects of an integrated economic force in Western Europe by 1992 are very emotional. There seem to be two principle reactions by outsiders when they consider the implications of such a move. The first reaction is usually one of happiness because it is perceived that there are great opportunities for everyone. This is certainly true. However, when the realities of Europe 92 are discussed, there is often a second reaction: one of alarm. There is fear, and rightly so, that the European Community (EC) will turn inward and that protectionism will create a "Fortress Europe".¹ As one European International Fellow recently told me, "There is a real possibility that the EC will replace its numerous internal walls with a single wall that surrounds the entire Community". To further complicate matters, trade decisions are seldom made strictly on the basis of economics. "In many cases, international trade and politics have become so interlocked that conduct of one may affect the outcome of the other."² The EC has learned this lesson the hard way; it has been impossible for them to be recognized as a single entity within the international trade community without speaking with a single voice on political and diplomatic issues. As has been discussed previously, the Community has not readily mastered this task. There are some inherent discrepancies in the Community's legislation which

encourage national sovereignty. The concept of a customs union should dictate that "the only trade policy that a member-state can have towards the outside world is a Community one. Such a prospect does not square with Article 115 of the Treaty of Rome, which authorizes the Commission to allow member states to take their own protective measures to shield themselves from 'economic difficulties'".³ This interest in national sovereignty defeats the purpose of a union, and the EC has been very slow to understand this.

To protect against economic difficulties, member countries often take actions which result in internal and external friction. These "trade frictions are manifestations of basic structural maladjustments. Policies which inhibit adjustment to change hamper not only the domestic economy but also the global economy".⁴ In other words, countries tamper with the free market system and allocate resources inefficiently. The result hurts not only the rest of the Community, but the international market as well. Particularly affected by these actions within the EC are the US, Japan and developing countries.⁵ EC member countries have determined that certain sectors of their economies, specifically energy, transportation, water supply and telecommunications, are critical and will be exempt from all EC 92 legislation.⁶ It is certain that protectionism will remain in these industries.

The remainder of this chapter will examine the effects that EC trade policy will have on the rest of Europe and on the United States. It will also examine the issue of protectionism,

particularly in the agricultural and financial industries. The resolution of many problems within the EC remains uncertain, but it is certain that change will result in new opportunities. "Project 1992 presents businessmen with a gradually expanding opportunity in a European market that has long been there; and a gradual threat to any 'nice little earners' at home that have not already been spotted."⁷ These opportunities exist for EC businessmen, Americans, Japanese and the EC neighbors. Morocco, for example, has taken note of these changes as an historical opportunity to take advantage of a more efficient industrial base within the EC. From the Moroccan perspective, some of the lesser developed member countries such as Spain, Portugal and Greece will lose their comparative advantage in low-technology industries, and Morocco will be there to compete.⁸ Similarly, as historic changes occur in Eastern Europe, new opportunities present themselves, and the face of trade in Europe changes even more. Flexibility and ingenuity will be the keys to success in this changing environment.

What effect will EC trade unity have on the rest of Europe, particularly the European Free Trade Association (EFTA) (see Chapter 3)? These non-EC members, particularly Sweden, Switzerland and Austria, are worried about the implications of EC 92. They have bonded together as neutral nations strictly for the purpose of trade, and they now find that it may be necessary for them to follow in the EC footsteps if they are to survive. It is felt that "without rather radical changes in the domestic policies of the EFTA countries in

order to adjust to developments in the [EC] Community's internal market, it seems unlikely that EFTA exports will be able to escape greater discrimination within the EC, and EFTA countries will slide down the Community's pyramid of trade privileges".⁹ Until now, EFTA countries have enjoyed most of the trade benefits of the EC without losing their national sovereignty to deal with external trade partners. However, free borders between EFTA and EC member countries without a consolidated external trade policy would completely undermine the benefit of a trade union. It is certain that the EC will insist on the following if EFTA is to have open trade borders with the EC and maintain its preferential trade position:

- (1) No borders would require a common EFTA/EC external trade policy. EFTA would be required to adapt EC trade arrangements and replicate non-tariff trade barriers.
- (2) EFTA agricultural prices would have to be aligned to EC prices to prevent being undersold by the EC subsidized produce.
- (3) Indirect taxes (VAT and excise duties) would have to be aligned in adjacent countries. Otherwise, there would be tax induced trade and the effectiveness of tax policies in high tax countries would be eroded by imports from low tax countries. EFTA members would have to participate in the EC clearinghouse for VAT.¹⁰

Because the United States is an important trading partner with both the EC and EFTA, any changes in policy by either party will significantly impact on our trade position in the area. In addition, the EC has numerous initiatives being discussed which will also affect the future of our trade in the area. While the US does actively "pursue and promote positive, creative strategies that will lead to expansion of world trade and thereby to world economic

order", we promote this concept within the framework of the free market system.¹¹ While we espouse this ideology, we sometimes rely on protectionist measures within our own industries. Consider, however, the unfavorable reaction by US industry when they encounter protectionist initiatives abroad. "In return for a rebuilt and prosperous European partner, the United States tolerated - perhaps underestimated - the costs to its foreign commerce of the high EC tariff barriers, export subsidies, EC tariff reductions for privileged non-members, and competition with EC members in third markets. The seeds of future misunderstandings were sown with the founding of the Common Market: the very notion of a common market, with its customs unions and common external tariff, will by nature discriminate to some extent against the US vision of a postwar world trade order."¹²

Officially, the Bush administration has stated that the US wants the Europe 92 project to "succeed in creating a more open, competitive Europe - open fairly to the rest of the trading world as well as within itself. And we want to work with our European partners to help accomplish this ideal."¹³ The US does fully support an economically healthy Europe. While a healthy EC would be a stronger competitor, it would also provide us with a more important export market; therefore, both sides can benefit from the success of the project.¹⁴ What does the US propose to do to minimize the

protectionist pressures within the EC and thus promote an open European market? The response, sounding like a Euroresponse, proposes:

- (1) The US should intensify its commitment to free, open markets. The US would strive to open its markets globally, and we would expect Europe to work towards the same goal.
- (2) The US will ensure productive dialogue at all hierarchy levels to ensure fair and constructive solutions to trade problems.¹⁵

It is obvious that the US and the EC are primarily interested in what is best for their own trade situations. Self-preservation is the driving force, and any benefit to an outside party is strictly secondary. How much attempt is made by each side to understand the intentions of the other? After all, we use the phrase "trading partners" which would indicate that we work together. This may actually be a misnomer. "Members of the European Parliament and the US Congress exchange official visits biannually to discuss mutual political and economic problems, although how much substance in bilateral relations is dealt with in these visits...and how much common ground on difficult issues is found is questionable."¹⁶

Most of the trade problems facing the US and the EC today were also prevalent in the 1960's. This would indicate that while there may be dialogue between the two partners, neither side is listening to the other nor are they willing to seek compromise. One significant change has occurred which certainly diminishes the US bargaining position. The EC is much less dependent today on the US as an export market as other markets such as the Mediterranean Basin

and the Middle East have become more affluent.¹⁷ Unfortunately, there is no meaningful and effective "mechanism to facilitate EC-US coordination of the effects of global interdependence on their mutual interests. The lack of a unified US policy is ironic, given the close economic, political and security relationship between the two sides".¹⁸ By the same token, the US clearly lacks a coherent foreign policy towards the EC. The influence which the US has on the development and maturity of the Community should not be underestimated. We can encourage development of the EC by dealing with the EC hierarchy or we can hinder the EC development by dealing unilaterally with individual countries.¹⁹ It is obvious that we are not consistent in the way we approach the Community, and this can have a significant influence on the acceptance of the EC as an entity in the world marketplace.

Unfortunately the EC approach to the US remains equally haphazard. The EC has developed comprehensive commercial and foreign policies for over half of the countries in the international system, but none have been developed for the US. It should be noted that most of the countries for whom policies have been developed are at or near the EC boundaries. This would suggest that "the EC is more at ease in organizing relations with states closer to its own shores, closer in economic size or smaller than its own member-states, and whose pressures on the EC for trade access and other benefits flow from regional integration rather than from global interdependence".²⁰

Because we are each others largest external trading partners, a solution must be negotiated whereby the EC and the US work together. "The EC is now troubled by disagreements with the United States over foreign policy -- East-West and North-South relations, the Middle East, export credits, government subsidies, and competition for third-country markets."²¹ With the exception of military policy through the NATO structure, there is no formal mechanism through which the US and the EC can coordinate their policies. This will only lead to more misunderstanding and decreased cooperation if the situation is allowed to continue unresolved.

As a result of ineffective communication, the trade dispute between the US and the EC continues to worsen. US exporters feel that they are losing significant market shares within Europe to inter-European trade. The agricultural industry receives significant visibility in this area, and will be discussed in more detail shortly. What is clear to US exporters is the decline in the balance of trade with the EC. Until 1984, the US consistently had a balance of trade surplus with the EC, with a high of \$18 billion in 1980. However, since that time, the US position has decreased steadily, reaching a balance of trade deficit of \$28 billion in 1986.²² Does this indicate that US industry has become less competitive, that EC industries are benefiting from increased protectionism, or is there some combination of these two factors?

Until recently, American businesses have paid little attention to the changes resulting from implementation of Europe 92. Why? The

answer can be attributed to the fact that "a small percentage of our gross national product arises from foreign trade, unlike many of our allies who depend on foreign trade and a favorable trade balance for their survival. Also, for several years many Americans doubted whether the agreement to create a true Common Market by 1992 could actually be carried out".²³ However, as demonstrated in the preceding paragraph, the balance of trade is now a real concern to the US. Given that the EC is our largest export market and that some form of economic unity will be in place in 1992, the US is finally beginning to take note.

Unfortunately, few American firms have made a concerted effort to "create a European image or to shoulder [their] way into European markets".²⁴ They have historically been world leaders, and countries were willing to accept products for which little attention had been given to adapting to local markets. As competition grew and quality alternatives became available, US industries found themselves lagging behind. Numerous companies are now taking steps to integrate themselves into the European markets. For example, IBM has subsidiaries in all of the EC member countries, and it "stresses the 'Germanness' or the 'Britishness' of each subsidiary" in order to gain acceptance and to be entitled to equal treatment with local competition.²⁵ AT&T has taken a slightly different approach having the same result. It has formed alliances with local partners such as Philips of Holland, Olivetti of Italy and Marconi of Spain.²⁶ In both cases, companies gain acceptance and are not perceived to be

present simply to make a profit and repatriate earnings back to the parent companies. It would greatly benefit US industry to take note of the strategy used by the Japanese operating within the EC. Nissan, Toshiba and others "target direct investments to two or three EC countries, building factories from which they aim to serve the whole community".²⁷ This approach will probably be most effective in ensuring that the companies are granted local status within the EC, thereby having free access to the entire Community. Future benefits of this move will also include prepositioning to directly benefit from the increased opportunities which are expected to appear in East Europe. US industry should take note of this and act accordingly.

The US government reactions to changes within the EC have not been as positive as those reactions taken by industry. Instead of making allowances for new EC regulations and trying to work together on the resolution of differences, the US has instead proposed legislation "that would close the American market to firms from countries which discriminated against imports from the US. The government has also repeatedly warned against setting industrial standards that could serve as barriers against American-based suppliers".²⁸ This action seems contrary to the Bush administration's position that we want to create an open and competitive trading environment. Indeed, it is clear that the EC and the US need to work together on this problem because a war of protectionist retaliations will not benefit anyone.

Protectionist actions are not going to improve any world trade situation, and will certainly not promote the free market concept which we so vocally advocate. "Our goal as a country is not - cannot be - to limit imports, to go protectionist. Our goal has to be expanding exports. Increasing exports is the key to sustaining our economic expansion, lowering the US trade deficit, improving our budget deficit, and keeping the LDCs [Lesser Developed Countries] on the path of economic growth and development. The most viable impact of increasing US exports is a lower trade deficit. In fact, most of the recent improvement in our trade balance has resulted from higher exports."²⁹ What are the prospects for increased protectionism as EC 92 becomes a reality, and can we survive despite them?

There are two types of trade barriers prevalent throughout Europe, and are not limited just to the EC. They are:

- (1) psychological barriers: those which add costs such as tariffs and safety requirements, and
- (2) real barriers: those which restrict entry into a country. These are absolute because even if there is a cost advantage, the products cannot be sold if they do not reach the market.³⁰

There are many more psychological barriers within the EC than real barriers. Numerous subtle barriers are in place today which prevent the EC from being a real common market. US firms should not feel slighted because these barriers restrict movement between member countries as well as imports from third countries. These barriers "include a crazy quilt of national inspection laws, technical standards, regulatory regimes, and industrial policies that in

practice make it almost impossible for German companies to sell phones to the French telecommunications monopoly, or for the Dutch to market life insurance in Britain".³¹

As was predicted by a European International Fellow, there are indications that some of the internal walls will disappear. However, it is almost certain that the individual walls will be replaced by a large wall around the entire Community. What remains uncertain is how impenetrable this wall will be. There are signs that "as the EC nations eliminate trade restrictions among themselves, they will also transfer many of them [restrictions] to foreigners, effectively ushering in a complex era of broad European protectionism".³² This internal assistance will penalize outsiders.

The result of this action will be the replacement of single country import restrictions, which vary widely across countries, with EC-wide rules. For example, Italy currently restricts Japanese auto imports to 3,500 vehicles (less than one percent of the market) per year while no restrictions exist in West Germany. Some agreement will have to be reached between all members. At the same time, the EC wants to encourage the sale of EC vehicles in Japan, targeting an increase from two percent to five percent of the Japanese market. Politically, it will be very difficult for the EC to set import restrictions while requesting that the Japanese relax their own import restrictions.³³

It is certain that the EC will impose restrictions on the banking, textile and auto industries. What is unclear is the extent

of protection through an industrial policy in the high-tech industries. Some type of protection is sure to exist, but how much? Key areas which will be affected will include among others the communications, information management and aeronautics industries.³⁴

"Many non-EC companies are taking no chances. The smart ones are making sure that they are already inside before any new ramparts go up around the edges."³⁵ They are assuming that physical presence within the Community will assure them the same treatment as an EC firm. That is not yet certain. In theory, this larger, open market will allow everyone to compete at a lower cost resulting from a single set of standards for the entire market. This of course does not take into account national preferences and tastes which will never be government controlled.

In preparation for the likelihood of protectionist measures, foreign companies like IBM "are scrambling to organize their defenses".³⁶ Numerous countries outside the EC, notable the EFTA countries, are positioning themselves inside the EC by increasing their investments. At present, "the Europeans treat foreign-owned companies with European facilities, such as IBM Europe, as full-fledged European companies and let them participate fully in the various research consortiums".³⁷ These firms are betting that this favorable treatment will continue as a common EC trade policy is developed.

This "buy-European" movement is not a new concept by any means. Various American unions, particularly the autoworkers, have launched

similar campaigns over the years. The movement is even reaching the television industry. Currently, American television programming is most popular in the EC, especially shows like Dallas and The Cosby Show. The EC is now saying that the "majority" of the programming on European airwaves must be of European origin. One British television executive explained why the European television producers are so unhappy. The US producers are able to pay for their shows from the US market. Therefore any programming sold overseas is pure profit, and they can therefore sell more cheaply without regard to production costs. The Europeans perceive this as dumping, and are advocating that protectionist measures be implemented. While the definition of "majority" has yet to be defined, the EC is sending a clear message to the US industry that they will not continue to accept the current arrangements.³⁸

Once the EC's internal barriers have been dismantled, governments cannot continue to subsidize their industries. To continue this practice will circumvent the free market system and allocate resources to inefficient, uncompetitive industries.³⁹ This will only create more inefficiency, and harm all member countries. It is argued that the economic problems and slow growth which continue to plague the EC are a result of inadequate competition. Many economists argue that "the EC should be concentrating on freeing markets from subsidies, quotas and external tariffs so that the economy has the necessary flexibility to adjust to changing conditions".⁴⁰ The Common Agricultural Policy (CAP) is an example of

a protected industry which is causing a gross misallocation of resources within the Community.

Agricultural issues are hotly debated both inside and outside of the EC. Similar debates in the US question the reason for paying farmers not to grow certain products. There are two phenomena around which the debate centers. The first of these is the growing worldwide surplus of agricultural goods.⁴¹ Surplus stocks are at record highs while demand/consumption is decreasing. As stockpiles grow in the US and Europe, the problem is further aggravated. Yet agricultural subsidies continue which only encourages further production and a continued misallocation of resources. The second phenomenon which fuels the agricultural debate is the "steady and practically open-ended rise in agricultural productivity".⁴² The US has become extremely efficient in the agricultural industry using the latest in technology; it is in effect big business. In Europe, however, most farming is done on a very small scale by families. The US has a few, very large and highly productive farms; within Europe, there are numerous, low output farms. Yet instead of using the concept of comparative advantage where Europe would import those goods which it cannot produce efficiently, the government encourages inefficiency by supplying farmers with generous subsidies. "The EC now spends over two-thirds of its total budget in support of agriculture. The direct budgetary cost of EC agricultural supports was over [\$15.4 billion] in 1985 with export subsidies alone costing over [\$5.3 billion]."⁴³ Unfortunately these numbers have been

steadily increasing. An example of the subsidy is seen clearly in a recent sale of wheat to the Soviet Union. The grain was sold at a price of \$75. per ton which equates to an export subsidy of \$130. per ton.⁴⁴ Of course, the US has also supported its share of agricultural subsidies.

As discussed earlier in this chapter, the US has experienced a deteriorating balance of trade with Europe for several years. Competing agricultural policies have contributed greatly to the increasing imbalance. Since 1980, the US has experienced a forty percent decrease in agricultural sales to the EC while the productivity within the American industry has steadily improved. At the same time, the EC has become the world's second largest agricultural exporter. "Despite high production costs and the need to subsidize virtually all exports, the EC has become the world's largest exporter of poultry, eggs, beef, veal, refined sugar, and dairy products...While this may be good news for the European farmer, every increment to EC output of these products has cost the European taxpayers and consumers dearly. Massive misallocation of resources to agriculture may quite possibly be one of the reasons that Europe is falling behind Japan and the United States in high technology."⁴⁵ When faced with these facts, it is very difficult for anyone to oppose US retaliation through protectionist legislation.⁴⁶ However, the result could be a tariff war which would be harmful to everyone. The best solution to this problem is the establishment of effective dialogue and coordination of government policies. Otherwise,

everyone suffers from an inefficient market system and incurs numerous, unnecessary direct and indirect costs. This is hardly the result expected from an economic union.

While the CAP will receive much attention and be the subject of unending debate, it is the financial sector which will be the hottest battlefield for competition. There are not, as yet, any formal regulations on this industry in the international arena. Because services are not covered by the General Agreement on Tariffs and Trade (GATT), the EC Commission wants to be innovative and set a precedent for regulation of the service sector. They have already decided "not to grant new banking licenses to institutions from countries that do not treat EC banks equally. And banks already established in, say London, are at risk of being denied the right to expand freely across the EC".⁴⁷ By demanding full reciprocity in the banking industry, the EC is requesting that its banks in the US be allowed to operate in a way that American banks are currently not allowed. For example, in order for American banks to have full access to the EC, the EC banks must have complete access to the American market. Since the US does not currently allow total interstate banking, to allow EC banks such access would be to give them an unfair advantage in our own market. Therefore, a presence in the EC will not necessarily guarantee total access to the EC. "Europe will be open to universal banking while Tokyo and Washington still restrict the investment banking activities of commercial banks. The cozy feeling foreign bankers had that a foot in London would

guarantee them access to the enlarged European market is fading fast."⁴⁸ Another event which will greatly affect the financial industry is the lifting of all capital controls. This is scheduled to occur in 1990, and will certainly "curtail member-countries' monetary (and fiscal) sovereignty".⁴⁹ The fact that internal walls are removed may only mean that a larger wall around the Community will be constructed, and this will only further restrict foreign competition within the EC.

The EC hierarchy is beginning to understand the problems which have arisen because member countries were allowed to pursue their own national interests without regard to the effect on the entire EC. The result has been a Community which is lagging behind the US and Japan financially, technologically, and agriculturally.⁵⁰ As the member countries begin to understand the benefits which can accrue to them from an economic union, they are slowly changing their ways. EC 92 should increase the opportunities of all firms, both EC and foreign, to operate on a larger scale within the EC.⁵¹ American exporters have a very important lesson to learn if they are to be successful within the EC as 1992 approaches. "All of our companies, whether they engage in foreign trade or not, will have enormous new opportunities to trade in Europe, and it will be far easier to deal with one Common Market rather than 12 separate countries with 12 separate sets of rules for travel, trade, investment and the like. That, in turn, argues for a substantial American investment in research, planning and possibly the acquisition of European partners

or branches to avoid any possible protectionist attitudes that might develop in the [Common Market] after 1992."⁵²

As has been discussed, the threat of increased protectionism within the EC is very real. If the EC recession continues with the associated inflation and unemployment, the increase in protectionist measures are certain.⁵³ The US exporters must follow developments very closely if they are to avoid being effectively locked out of the market because they failed to properly position themselves. Now is the time for positioning. 1992 is not a magic year in which all trade restrictions will be lifted within the EC. For example, certain restrictions are placed on Spain's membership in the EC until 1995. It will experience export restrictions on certain products "which the Spaniards produce too cheaply for the comfort..." of the other EC members.⁵⁴ As should occur in a free market system, one should also expect some industries to fail in certain countries where they are already weak. For example, in Spain, one can expect that the bicycle, motorcycle and electrical appliance industries will flounder because they will be too inefficient to compete in the EC. While this will have a negative impact on the balance of trade in these industries, another member country will experience a positive impact on the balance of trade as a result of efficient production within these industries. The overall effect on the entire EC will be positive because resources are allocated where they are used most efficiently and the consumers have a high quality product at a lower price. Spain should expect to make up for these losses in trade with

increased sales of those products which it produces efficiently, namely low technology consumer goods. It has been very difficult to make member countries realize that they are going to have to experience some losses so that the entire Community can benefit. This has only had limited success to date.

There are key industries which member countries continue to protect, primarily in the interest of national pride and job protection. Most prominent among these industries are agriculture, telecommunications, steel, automobiles, and increasingly aircraft. Unfortunately, "by freezing labor and capital in inefficient activities, Europe missed opportunities to grow and expand into more dynamic activities where it might compete better in international markets".⁵⁵ Member countries are going to have to accept significant change if the European economy is to become more efficient.

While the EC is working to form a Common Market which will benefit all of its members, the world has become too interrelated to ignore the external ramifications of its actions. It must be understood that the economic structure of the EC cannot be divorced from all of the other internal and external forces. "Economic, legal, political and military issues are so closely interlinked that the task of advancing European integration has become a formidable challenge to all available intellectual, economic and political forces..."⁵⁶ None of them can be ignored, and this is a concept which has caused a great deal of difficulty thus far.

In the simplest terms, EC 92 is striving to create a Europe without borders. Unfortunately, many other obstacles have developed which make this simple concept a monster of bureaucracy. While many of the additions are consistent with the aim of a single market, they are not vital to its success. These additions include patent law, broadcasting standards, labelling rules, corporate structures, vocational training for young people, and the pedigree of bovine animals.⁵⁷ While innumerable hours and effort are expended debating the policy towards "sideline issues", the development of real implementation policy is hindered. There will be time for attention to detail, but the EC must use its energy and resources to first develop policy and resolve issues critical to the implementation of Europe 92.

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CHAPTER V

IMPLICATIONS OF GERMAN REUNIFICATION ON THE EUROPEAN COMMUNITY

The events of the latter part of 1989 were truly historical, and the implications, both direct and indirect, will continue to be far reaching for many years to come. Because of the growing interdependence of the entire world, every major world power will be affected by these events. Geographic proximity and a common history dictate that the events in Eastern Europe, and particularly in East Germany, will have a significant impact on the future of Europe. The recent changes in East Germany "have propelled the idea of German reunification from the realm of improbability to fast-looming possibility".¹ This is a matter of great concern to leaders of both the East and the West because the two Germanys are the most powerful countries in their respective blocs. The result of a reunification could be a German power in Central Europe which would rival the economic and political power anywhere else in Europe; Eastern and Western leaders realize that this is a possibility which cannot be ignored.

The following chart compares the size of the German states as they currently exist, and the power which would be consolidated if

reunification were to occur:

	<u>East Germany</u>	<u>West Germany</u>	<u>Total</u>
Population (million)	16.6	61.0	77.6
Area (square miles)	41,800	96,100	137,900
Trade(\$ billion)			
Exports	\$30.7	\$323.4	\$354.1
Imports	31.0	250.6	281.6
Trade Balance	<0.3*	72.8	72.5
Gross National Product (\$ billion)	207.2	870.0	
Real Growth	1.8%	3.4%	2

highest in Eastern Europe.

It should be noted that East German currency amounts are evaluated at an official exchange rate. If the black market rate (which more closely approximates the true value of the currency) were used, actual values would be lower by at least a factor of ten. For illustrative purposes, however, these figures explain why so many people fear German reunification. It is clearly possible that a united Germany could dominate Europe, but this is unlikely. It is more likely that change will be slow and calculated. "Germans, East and West, long seemed resigned to two states, each championing the ideological cause of a competing superpower. That mood of resignation is changing. Germans feel uncomfortably caught between worry and hope as they contemplate the implications of an astonishing transformation in East-West relations."³ There is a great fear on both sides that Germany, unable or unwilling to choose between "allegiance to the West and its commitment to a future that includes Eastern Europe could be tempted to go it alone".⁴ Neither side seems prepared to make this decision too quickly.

When asked about the prospects for reunification, former East German President Egon Krenz stated that "socialism and capitalism have never existed together on German soil".⁵ This attitude has changed in just a few short months, and Germans are considering alternative ways for the two opposing ideologies to unite. It would, however, "be naive to assume that countries which have been subjected to forty years of Marxism will suddenly explode in Western-style liberal capitalism. Nor will they quickly embrace the parliamentary party system..."⁶ While it is currently popular to refer to the GDR as the "Gradually Disappearing Republic", it is not likely that sweeping reforms will come overnight.⁷

The major changes which can be expected to result from the recent movements in Eastern Europe will be economic. "The revolution unfolding in one country after another opens up opportunities, unimaginable just a year ago, to create not just a new Europe but a new and far less menacing world order."⁸ West Germany is a significant influence on the European continent, but it is not a superpower by world standards. It is a powerful country whose prosperity is heavily dependent on the rest of Western Europe. Will reunification increase the influence of West Germany in Europe? There is no doubt that the opening of Eastern Europe will be a great economic opportunity for Western Europe, but the economic ties between East and West Germany are already significant. Currently, trade between the two countries exceeds \$7 billion per year, and this is expected to grow as relations become more open. What is ironic is

that "East Germany has enjoyed something like associate status in the E.C. because Bonn treats inter-German trade as internal commerce, unencumbered by tariffs and customs barriers. That arrangement allows East Germany to sell its products throughout the Community."⁹

From this, one can predict that Eastern Europe will become a more important player in West European trade, but to what extent will individual countries like Germany benefit more than the other trading partners? Reactions are mixed, and the world will be watching with great attention as the changes progress over the next year. What is certain is that "no one dares stand in the way of German national aspirations, but no one wants reunification now. That quiet consensus links allies and adversaries from Washington to Moscow, from Paris to Warsaw".¹⁰ Of course, the real answers lie in the German national will. The remainder of this chapter will look at the pros and cons of German reunification considering the concerns of Germany, its Western allies, and the Soviet Union.

The driving force behind German reunification is heritage. While there are numerous differences between the two countries and their citizens, the "Germans on both sides of the wall are bound together by a common history, culture and language".¹¹ The West German government recognizes that East Germans are in fact Germans, and the Constitution grants citizenship to any East German who seeks it.¹² The popular uprising and demand for democratic change in East Germany in effect removes the one significant difference between the two states. If the socialist political and economic system which

distinguishes East from West Germany is reformed, the reason for the existence of two separate states could be eliminated.¹³ As change occurs, it becomes more evident that the East will be heavily dependent on the West for reform assistance. East Germany's desperate need for Western capital and technological expertise is a huge opportunity for West Germany - indeed for all of Western Europe, the United States and Japan. West Germany will stand to benefit the most because it is already positioned geographically, politically and financially to take advantage of the opportunity.¹⁴ Therefore, a common heritage, political reform and mutual economic opportunity are factors which are having a positive influence on the question of German reunification.

Uncertainty best summarizes the negative influences on the question of reunification. While Germany may not be considered a superpower, it has substantial clout and influence in the international world, and the direction of its future concerns everyone. First, it is feared that a united Germany would become an independent power in an interdependent Europe. Consider the basis for this concern. "The West Germans have built from rubble the most powerful economy in all of Europe yet an even greater feat may have been performed by the East Germans. They have created a relatively productive economy [by contrast to other East European countries] under the impossible, absurd conditions of Marxist economics. Put these two together and you have what all Europe understands will be its dominant power."¹⁵ This concerns both the East and the West.

While they share a common culture and heritage, the East and West Germans are in fact significantly different. Since their separation forty years ago, they have developed very different values, styles and perspectives. Additionally, there are two distinct and very different sets of government institutions which are firmly imbedded in the cultures. One cannot assume that all East Germans want to give up their present structures to be governed by Bonn. Resolution of these issues will at least slow the reunification process and makes "a headlong rush to unity unlikely..."¹⁶

Those who remember World War II especially fear German reunification. A popular joke currently in Europe says, "I love Germany so much that I'm glad there are two of them"¹⁷. There is a real fear, both inside and outside of Germany, that reunification will create a Germany which "is perhaps too powerful and too aggressive to contain. Few have forgotten how an economically and militarily powerful Germany stood at the center of two world wars in this century".¹⁸ Stated another way, there are fears "that a reunited Germany will also be a restless one, eager to reclaim former territory".¹⁹ Opponents of reunification are basically afraid of the potential impact that a focused German nationalism would have on the rest of Europe. "The simple fear is that German nationalism could unfurl across Europe yet again, becoming an unstoppable force...Germany's neighbors, already overshadowed by the German economy, feel they could be flattened if the giant grew further.

They ask themselves what would be the new Germany's political and social profile."²⁰ There are indications from the current political climates in both countries that a militarily aggressive Germany is unlikely. "West German draft boards are overflowing with applications for alternative service, and the East German opposition has made anti-militarism a major theme."²¹ This certainly does not sound like an aggressive military society.

The final argument offered against reunification again finds its roots in the fear of the unknown. The Eastern bloc would want a unified Germany aligned with it, while the Western alliance understands the importance of Germany to the success of its plan for economic unity. Consider, however, the possibility of a neutral Germany. "As the strongest European power, a reunited Germany cannot remain in the European Community and it cannot join the East."²² Both sides are concerned about the possible loss of a strong and wealthy ally.

This view that unity cannot be for the good of Europe because it will upset the current balance is rather limited. Opponents fail to consider that a new and improved relationship may benefit everyone. Instead too many people are content to follow the old cliché which says, "if it's not broken, don't fix it". Consider now the positions of the German people and their government and those of the East and West blocs.

It is easy to analyze the pros and cons of a German reunification, but the whole discussion is purely scholastic if the

wishes of the German people are not discussed. After all, the ultimate decision lies with them. West Germany has begun to make assertive demands to the western alliance in the interest of its own national goals and objectives. Reunification is an issue which is gaining prominence, and some may argue has become the top national priority. Currently, West "Germany's immediate aim is to rid itself of the burden of being Europe's battlefield...Its medium range interest is to rid itself of foreign soldiers, which would turn it from an instrument of alliance policy into an entirely independent entity of its own. But its long range goal is reunification or,...dreams of a Greater Germany."²³ While this is a stated goal, the Germans on both sides realize there are problems to overcome, and each side periodically questions if this is what it really wants.

It seems that "West Germany, despite its vast wealth and growing clout on the world stage, remains sadly uncertain which way to turn".²⁴ While the West Germans accept the common heritage and culture shared with the East Germans, they are realistic about the implications of unity. "The West Germans do not wish to see their welfare state swamped by millions of new arrivals from the G.D.R. West Germany's political elite is in fact working closely with the Soviet Union to pressure East Germany to introduce reforms that could stabilize that state."²⁵ Perhaps optimistically cautious best describes the West German attitude. While working privately to

promote internal stability in East Germany, West German Chancellor Helmut Kohl publicly states, "We have less reason than ever to be resigned to the long-term division of Germany into two states."²⁶

Like the West Germans, the East Germans appear to be cautiously optimistic about reunification. It is not something that they want to occur immediately. They too realize that it is not a simple question; the ramifications are numerous. A recent survey indicates that 48% of the East Germans are in favor of reunification. For the East Germans, the most pressing issue at hand is the development of a national identity to include a political and social structure. Only then can the idea of reunification be discussed. The East Germans "want closer relations with their West German brethren, a growing together with the Federal Republic - but not necessarily reunification; they insist on being accepted as they are. And finally, they demand economic reward, even though they know they are not likely to catch up with the west any time soon."²⁷ It appears that this is a very large order, and West Germany may not be able to fill it under these conditions.

The question of German unity is of great interest to the east and the west, but the problem is a German problem and they are the only ones who can resolve it. "The Soviet Union is not in any better position to control events in East Germany than the US is to set West Germany's agenda."²⁸ The outcome is unclear, but it is probable that some kind of reunification will occur. When, in what form and how are questions which still must be answered. The rest of the world

watches intently because the direction chosen is sure to affect everyone. Kohl has tried to soothe concerns within the Western alliance by stating that "we aren't wanderers between East and West".²⁹ While this is meant to reassure the European Community, the actions do not completely support this statement. Fortunately, Germans on both sides appear to understand the importance of their actions and are being cautious. At the same time, they are realistic. "They know that reunification, if it is ever achieved, will come at the end of a long process which has only just started. They realize that unity might take many different shapes and forms, and that a loose confederation is a more likely outcome than Bismark's empire."³⁰ More discussion on the idea of a confederation will follow shortly. While Germans assume that the resolution of this question will take some time, it should not be assumed that this means years. After all, no one would have ever thought that changes could have occurred to the extent witnessed in the past six months, so it seems impossible to predict what the next six months might bring. All of these actions are critical as 1992 and the reality of a European Community draw near.

The Western alliance has much at stake in the final outcome of German reunification. The very existence of NATO and the future success of the Europe 1992 project are the most visible and significant issues. It appears, however, that what is said in public and what is espoused in private are very different positions. The West Europeans and the US "have paid lip service to the proposition

[of reunification] since World War II, so they are hardly in a position to object if it emerged as the freely chosen will of a divided people".³¹ Since the Kennedy administration's visit to the newly constructed Berlin Wall in the early 1960s, both American and western allied leaders have "ritualized demands that the ... Wall come down, secure in the conviction that it would remain standing..."³² It is becoming increasingly clear, however, that most European leaders agree, at least in private, with Italian prime minister Giulio Andreotti who insists, "There are two German states, and there must remain two German states."³³ The official US position as outlined by President Bush calls for "German self-determination because we are reasonably sure that most East Germans want to join the western alliance".³⁴ All of these concerns are related to uncertainty: will the Germans opt for the western alliance, an eastern alliance or neutrality?

There is great fear that a new Germany with neutralist tendencies would harm western interests. There is some concern that the reunification issue threatens to overshadow and compromise the EC 92 project. Germany has been one of the driving forces towards European economic unification, and many allies fear that this interest "could be deflected from the single market goal by its interest in reunification and the prospect of dazzling economic gains in Eastern Europe".³⁵ From a western alliance perspective, there are fears that change "in East Germany is progressing so rapidly that it might lead to a premature and dangerous form of reunification between

East and West Germany before 1992".³⁶ While everyone accepts the fact that some type of unity between the two countries will exist, the west would prefer that the change not occur until the EC 92 project is implemented. In this way, the new Greater Germany can be firmly anchored in the west. EC members agree that "the economic threat of a unified Germany is less worrisome than the possibility that Bonn will become preoccupied with pursuing its goals in Central Europe at the expense of strengthening unity within the EC".³⁷ It is a fear of instability that concerns both government officials and businessmen within the EC. They must consider, however, that a major purpose of the EC is to provide economic stability to the area. Jacques Delors, who currently heads the European Commission, feels that "the EC can help anchor the changes in Eastern Europe by granting economic assistance, trade concessions and eventually some form of associate membership".³⁸ The key will be to insure the integrity of the EC 92 project with West Germany as an active member.

The prospect that reunification and the EC 92 project can be accomplished in harmony is not unreal, and the entire European continent stands to gain. French President and recent EC president Francois Mitterand says "that if the twelve EC nations can truly integrate, they can become a magnet capable of attracting increasing economic and technological links with Eastern Europe and the Soviet Union itself. In the long run, he sees the EC growing to the East and developing into a world power."³⁹ If this were to occur and the EC continued along its present course of subtle protectionism, the US

might find itself locked out of the largest market in the world. This should be considered very carefully by policymakers because now is the time to gain entry. Historical changes are occurring, and if we do not actively participate to advance these economies through financial and technological assistance, the US may find itself as the odd man out in the next century.

The primary concern within the Western alliance is the assurance that Germany remains allied with the West. There is a great deal of concern on the part of many countries who were victims of the German power machine earlier this century, and they fear that history might repeat itself. Indeed, this has already been discussed as a negative factor of reunification. In Britain, France and Poland where memories of previous German nationalism are still quite clear, there is concern that reunification might occur "before the EC is ready to integrate a new Germany..."⁴⁰ A threat is perceived; while this is probably not a military threat, there is a potential for German dominance of Europe through economic means. Some countries are considering action to prevent this from happening. For example, there is talk of the French "trying quietly to renew prewar ties to the East (in the prewar period France had close ties with Poland and the countries of the Little Entente) as a flanking maneuver to contain any eastern expansion of German influence".⁴¹ While the official statements by the western alliance continue to promote a German unity, there are clear indications that they are very nervous in the face of uncertainty. This is a true test of the ability of

the EC to work together in promoting a solution which will benefit everyone.

The clear aim in this time of uncertainty is to promote a change which will ensure the stability and interdependence of Europe. The problems with individual nationalism have been highlighted throughout this paper. This is a case where everyone must work together for the benefit of the whole. It is certain that "the Germans will play a key role in articulating Europe's future. Committed as they are to the principle of self-determination, the United States and its allies can scarcely oppose the wishes of the two German states to unite in some way. But if reunification is to be beneficial, it should come slowly and in steps. West Germany should remain anchored in NATO and the EC...If the West ignores the lessons of history and the fact of European instability, the second millennium could indeed end in chaos."⁴² Even more precisely, a Germany which is tied to the West European integration is in the best interest of the US. We may find a fortress Europe which is not friendly to the American economy, but "a unified Europe with ties that bind Germany is the best hope for a tranquil post-cold war world".⁴³ This summarizes the concerns of the western alliance and its solution for a stable world order. How does this differ from the perceptions and concerns of the East bloc in analyzing the question of German reunification?

One certainty in this whole discussion is the fact that the agenda of the East bloc will be different from that of the Western alliance. As in the West, the concerns focus primarily on economic

and military issues. It is obvious that the Soviet Union would oppose the incorporation of a united Germany into the EC. This would create an enormous political and economic threat, but like the US, it will have little voice in the decision. In fact, the Soviet Union would go to great lengths to prevent EC 92 from incorporating Germany. It would accept the reunification under the condition that "the combined Germany would be a neutral, non-Atlanticist Germany, not unfavorable to 'socialism' and giving Moscow the benefit of its economic weight".⁴⁴ This is interesting if one considers that the West greatly fears a neutral Europe.

Of course each side would like to see the Greater Germany allied to its cause. From the Soviet viewpoint, the military question of alignment is the primary concern. The Soviets would never stand for a powerbase in NATO which included a unified Germany. It is feared that "a united West Germany in NATO would only serve to strengthen reactionary forces in Russia and bring a return to the cold war arms race...The only [solution], then, appears to be a Germany that is firmly in the West economically, but militarily unaligned and unarmed beyond the needs of self-defense."⁴⁵

So which way should Germany go? It certainly depends on who answers the question. It is clear, however, that there is no simple, clear-cut, yes or no solution to the complex question of reunification. The decision will affect all of Europe. "NATO and the Warsaw Pact will have to shed their military dimensions. The European Community will have to define its attitudes towards Eastern

Europe. The two Germanys will want to expand the web of existing agreements between them, an interweaving of interests that neither can unravel without harming itself."⁴⁶ While the West will have little voice in the question of reunification, it can influence the direction of change in Eastern Europe by encouraging countries to adapt freer economies and democratic political processes.⁴⁷ This may be an indirect, and perhaps the only, method of influencing the resolution of the German question.

Germany is clearly being pulled from the east and the west. Germany has always perceived itself as a Central European power, not West European. "Europe 92, which will establish a single western European market and might lead to...some kind of political confederation is the major force pulling Germany west."⁴⁸ The pull to the east revolves around "the gradual dissolution of the Soviet empire which will pull Germany into the geopolitical and economic vacuum left behind".⁴⁹

There are alternatives to German reunification. Most obviously, East and West Germany could remain as separate countries with their own governments and limited economic ties. This seems unlikely. The EC has promoted the concept of a German confederation where goods and services would be allowed to flow freely between the two states while each retains its national sovereignty.⁵⁰ It is surprising that the EC would support this while it is actively trying to get its member countries to forget their national sovereignty for the good of the Community.

No matter what the outcome, history is being made and reunification has raised the prospects for an entirely new order in Europe. There are three major interdependent events currently taking place which are going to determine the future order of Europe: "the progressive integration of Western Europe before and after 1992; the progressive emancipation of Eastern Europe from both Soviet domination and the shackles of Marxism-Leninism; and the progressive reestablishment of their former closeness between the two halves of Europe...Under a common European roof, both will be thinkable: the German nation united in one free state or divided into two free states."⁵¹ It is too early to predict the outcome of the reunification question, and indeed the larger question of what will become of other East European countries as they implement similar changes. What is certain is that the changes will impact significantly on the European Community and the United States as we compete for entry into these potential markets.

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CHAPTER VI
CONCLUSIONS

It is interesting to contemplate what the next three years have in store for the European Community. As has been demonstrated in this paper, there have been periods during the EC's history where significant progress has been made in just a short period of time. Likewise there have been certain stumbling blocks which have threatened to completely destroy all the accomplishments achieved within the EC. Clearly there are still many difficult and controversial decisions which must be made before a true Common Market can exist, and there is much debate over whether the Community can work together to achieve its goals. The problem of protecting national sovereignty will be the most difficult obstacle to overcome, but there have been recent concessions on the part of member countries which might indicate that they are now willing to work for the good of the Community and the long-term good of their individual countries.

The events in Eastern Europe are a new influence on the EC which was nonexistent until a half year ago. The entire world is watching as history is made almost daily, and these changes are of particular interest to Western Europe. Because of the East European geographic proximity and economic disrepair, the EC and other West European countries are particularly well positioned to take advantage of the new opportunities which are emerging. This may be a force which will

encourage the EC member countries to work together and hopefully solidify their own union.

For more than thirty years, the EC has "sought, with broad success, to create a customs union, a trade policy, a common agricultural policy, a set of anti-trust rules, [and] a monetary system...It also tries to speak with one voice on foreign policy; sometimes it succeeds".¹ The root of the problem is national sovereignty, and this usually relates to a member country's history and culture. "The cultural differences within Europe are such that no one is advocating the creation of a homogeneous entity with a veneer of 'oneness' superimposed over the continent. But the need for economic and political integration is recognized as an absolute necessity if Western Europe wishes to maintain its identity in the face of the political dominance of the United States and the Soviet Union and in the face of the economic dominance of Japan and the United States."² While the EC members have realized the importance of cooperation if they are to survive in the highly competitive world of international trade (and have made significant accomplishments towards this goal), the likelihood of a United States of Europe does not seem probable because of the cultural differences cited above. However, as an economic unity, the EC is emerging as a viable leader in the international marketplace. The US must absolutely pay more attention to these changes if we are to ensure that we remain competitive through this decade and beyond.

It is essential that the dangers of national sovereignty be completely understood. Member countries who continue to put their own interests above all else are doing great harm to the EC structure. It is not a problem to be taken lightly; in fact, a divergence of perceived national interests in a critical policy will easily cause conflict, crisis and possibly paralysis within the Community.³ They have overcome numerous obstacles to date, and the increased commitment to EC 92 will probably ensure that the project continues to advance. "The kind of cooperation which has been established between member countries on a voluntary basis has no parallel elsewhere in the world. This cooperation varies from one policy area to the other, usually depending on whether member governments feel that the benefits derived from joint action, mainly in terms of greater efficiency, outweigh the costs implied in any additional constraints on the independence of action."⁴ The scope of voluntary cooperation is slowly expanding to more critical issues as the members begin to see real examples of benefits which are derived when everyone works together. They are slowly understanding that to have a successful, single economy, it is necessary "to begin with sacrifices. The benefits will come later".⁵ After thirty years, some of the benefits are now visible.

One very important managerial task which must be accomplished by the EC will be to increase the public confidence in the EC as an institution. The EC hierarchy was very slow to solicit the EC "national will" towards this project, and without the support of the

general public, significant progress is impossible. The EC hierarchy is also perceived as a very expensive and very inefficient body from which the member countries gain little return on their investments. Important changes are still required for the continued progress of the EC 92 project. Determining the direction of these changes will "require vision, cohesion and vigor from the Commission, and open-mindedness and courage from governments and the Council".⁶ Equally important, the EC must demonstrate to the world that it can advance despite economic disparities between its members while achieving at the same time a greater cohesion by ensuring the economic development of its less prosperous members.⁷

The world outside of the EC also plays an important role in the future success of the Community. To continue to treat the member countries as individuals instead of members of an organized union will only encourage nationalism and will fail to give the EC the credibility it needs internationally. The world should not look to 1992 as the magic date when everything will fall into place.⁸ For one thing, it should be noted that Europe 1992 is somewhat of a misnomer. The actual date established for European economic integration is 01 January 1993. This date, however, is immaterial; what is important is the recognition of the progress that has been made and which continues to be made. Just twenty years ago, national interests always prevailed over those of the Community. A deeply ingrained attitude has been significantly changed in a relatively short period of time. The world can only expect that progress will

continue, and everyone should prepare for the changes in the world economic order which are inevitable.

The preceding paragraph should not imply that the EC is progressing on schedule and is not encountering any obstacles. In fact, this is quite contrary to reality. What faces the EC in the next three years is the implementation of the most controversial legislation - laws and regulations which significantly limit national sovereignty. There are even some problems between the EC and the US which were discussed extensively in the 1960's and 1970's, but have yet to be resolved. The most significant of these problems is the dispute over farm subsidy programs which are used to protect local farmers from the uncertainties of world markets. There is extensive disagreement on both sides over the magnitude and scope of the subsidies. As previously discussed, resolution of the Common Agricultural Policy (CAP) is critical to the future of the EC. The second EC/US dispute which remains unresolved is the competition for the same world markets. Understanding that both sides fiercely promote a free market system, one must wonder why this is such a controversial issue. The final dispute revolves around the effect on the EC economy of fluctuations of the dollar and manipulation by the Federal Reserve of interest rates which has a direct influence on the dollar exchange rate.⁹

Internally, the EC has had trouble prioritizing the issues to be resolved. Disagreements generally focus on the national perceptions of what is most important to the future of the Community. The key

issues in question include tax standardization, trade policy, social issues, monetary integration and the extent of free trade.

Reviewing this paper, there are some key points which appear to be potential troublespots for the EC. They relate primarily to the organizational structure and trade legislation of the Community. While certainly not the only problems within the Community, these appear to be structural problems which could significantly weaken the EC in the future. The first troublespot to be highlighted is the CAP. This policy has had a positive impact on the EC by "creating and maintaining a more than sufficient quantity and quality of foodstuffs and commodities in Europe..."¹⁰ However, at what cost to the population has this food supply been maintained? The economic and political costs have been high and are a visible negative impact on the international reputation of the EC. The CAP consumes 60-70% of the EC's annual budget and results in huge surpluses of butter, wine, sugar and numerous other commodities. The EC consumer pays the cost of much higher prices required to support the subsidies. These costs are reflected both in the actual food costs and in the tax structures where revenues are generated to support the EC budget. The international costs of lost markets due to protectionist actions are enormous. Clearly the EC must take actions which will allow the free market economy to shift resources which are being artificially held in the agricultural sector into other industries where they are really needed. Failure to do so only makes the EC more inefficient and less competitive in the international trade arena.

achieve more integration, it will have to shift some of the real power back to the European Committee and the European Parliament.¹²

This leads to the final potential troublespot for the EC: the inability of the European Parliament to wield any political power. It has been described as "an opera buffo [comic opera] with over 500 characters [the members], twelve acts [the member-states], seven plots [the transnational party groupings], playing in two theaters [Brussels and Strasbourg]. Nine languages are spoken, but none are listened to, and the Parliament is engaged in the symbolism of politics without its essence".¹³ In short, the European Parliament is a voice with no authority, influence or power.

While the resolution of internal problems will greatly impact on the success of the EC 92 movement, the Community must also be very attentive to the way it is perceived externally. It is impossible in the structure of the international trade environment to totally ignore external trading partners. The world is too interdependent for a strategy of isolation to be successful. There is a general feeling that the EC must develop more of a worldwide perspective. Unfortunately, there is little indication that the EC will allow a completely free trade policy to operate despite rhetoric to the contrary. It is improbable that "the EC intends to eliminate internal subsidies and quotas in agriculture, steel, fisheries and textiles...Nor is there talk of removing barriers to external competition - such as various types of quotas on cars, textiles, footwear and electronics - or of stopping voluntary export restraints

for textiles, footwear, cars and steel".¹⁴ The Eurocrats fail to realize that these actions are encouraging inefficiency, and the EC is failing to gain the most benefit from its economic union. If the Community plans to create a truly competitive international economy, "there must be a real commitment by the government to dismantle the restrictions embodied in their industrial policies...That means letting grossly inefficient businesses go out of business and allowing the mildly inefficient businesses to fire workers, redeploy remaining ones, and hire new workers without fear that the decision is permanent. It means assuring efficient businesses and new enterprises that the government" will not interfere.¹⁵ This statement reemphasizes the concept of the free market system. It will require some very unpopular decisions to be made which will harm specific sectors of the economy, but the end result will be greater efficiency which will benefit everyone.

As stated previously, 1992 is not a magic date on which everything relevant to a economic union will be implemented. "There might, perhaps, [be] a ceremonial burning of border posts."¹⁶ The prospects for a United States of Europe appears to have little hope. "Borders will continue to reinforce Europe's natural divergences: different languages, different mass media, different tastes, different habits. Europe will remain a Europe of national markets that have become steadily more accessible."¹⁷ If this is the case, what exactly can the United States and the EC's other trading partners expect from 1992?

First, it can be expected that transportation costs throughout the Community will be reduced. There will be numerous factors contributing to the reductions including easier movements across borders, deregulation of the trucking industry and increased pressure on the airline industry to reduce its artificially high prices. Currently, airline markets are dominated by the national airlines of each member country which have historically been very inefficient. Changes similar to those occurring within the US airline industry will lead to a consolidation of resources and an emphasis on efficiency.

As a result of 1992, it can be expected that there will be a greater pressure to make production facilities flexible enough to produce similar products adapted to cultural tastes. This emphasis on efficiency also recognizes the significant differences between national markets within the EC. For example, all soaps made for the EC markets will be produced in one plant, but that plant will be flexible enough to vary its products to suit individual tastes in the national markets. Another example would be Coca-Cola. While this is perceived to be the same product worldwide, it is in fact adapted to local tastes. One market might require a much sweeter product while an adjacent market might require a more heavily carbonated product. For any firm to assume that an economic union will ensure that the success of a product in one country will mean success in all markets of that union is headed for disaster. US exporters and firms operating within the Community must be aware of cultural differences

in their approaches to the EC and adapt to each market individually. They must avoid the pitfall of assuming that an economic union with standardized laws and regulations will equate to a homogeneous market.

Firms dealing within the EC can expect a standard set of industrial norms to be established by 1992. These standards, which might include anything from the material composition of a tire to the type of preservatives to be used in canned food products, will apply to the entire EC market. Dealing with the challenge of meeting industrial standards while remaining flexible to individual market preferences will be essential to the success of all firms, domestic and foreign, operating within the EC.

Finally, it is safe to predict that there will be reduced friction and restraints within the European market by 1992. This means that internal competition will be greatly enhanced as goods, services and capital move more freely. This does not indicate that external entry into the EC markets will be any easier. In fact, as already discussed, there is a real possibility that external entry into the market may be increasingly hindered.¹⁸

What predictions can be made for the future of the EC? The most obvious concern to the EC trading partners, particularly the US, is the question of protectionism. Potentially there will be an increase in protectionist actions, although they may be more subtle and indirect than those which we currently encounter. The southern and less economically developed member countries such as Greece, Portugal

and Spain have gained increased influence and clout within the EC. For these countries, a free market system of completely open markets would mean increased competition for manufactured goods which they are currently exporting. These are generally low technology goods such as textiles and leather goods. They will press for protection of these industries at least until the countries can stabilize themselves within the EC. A second problem which will further the EC argument for protectionism is the increase in goods available from newly industrialized countries. Many of these countries have their currencies tied to the dollar; as the dollar continues to weaken, there is an incentive for these countries to export more of their now inexpensive goods to the EC. As these EC imports increase, the likely result will be new import restrictions.

Unemployment continues to be a problem within the EC. It has historically been very high, and as long as inefficiency is supported within the EC, there is little possibility for improvement. This is a further incentive avoiding for protectionism within the labor markets. The free movement of labor is an important goal which must be achieved before the EC can become fully functional. The elimination of internal barriers such as labor restrictions or the movement of goods will probably result in the construction of compensating external trade barriers. There is indeed a risk that "'compensating protection' against external suppliers can easily take the form of domestic subsidies and strong preferences in public procurement for firms established in the Community".¹⁹ The result is

an internal bias which equates to indirect protectionism. Of course, the US can hardly complain about this situation since the majority of our public procurement must be "Buy American".

As would be expected, the EC will be most interested in the development of a healthy and cooperative relationship between its member countries. "It seems likely that the European Community will concentrate its efforts on the task of creating the internal market...the European Community will be less able than usual to form a coherent negotiating strategy for the multilateral trade negotiations."²⁰ In developing compromise trade positions with non-EC members on trade issues, frequent deadlocks are likely. This should be of great concern to US policymakers and businessmen. EFTA countries feel that they will be isolated from these problems and will be able to meet the challenges of EC 92 because "their markets are already fairly strongly integrated with those of the EC. EFTA favors the successful completion of the EC's internal market since all Europe will benefit from it".²¹

The signals are clear, and we must take note of them. Real changes have already occurred, but even greater changes are yet to come. To ignore them will only ensure that the US is completely isolated from any prospects of fair and equitable trade with the EC. "Only dreamers really believe that all the Community's internal barriers will fall by the end of 1992. Realists can hope that enough progress will be made in the next [three] years for the frontier-free idea to be taken seriously."²² It appears that many US policymakers

and businessmen are taking account of the work remaining for the implementation of a complete Common Market and are predicting that the date will not be met. This tends to lull them into a false sense of security; they think that they will not have to deal with the consequences of a protected European market. Nothing could be further from the truth.

One can expect to see substantial progress towards a frontier-free Europe in the next years. The EC hierarchy has realized that it must either demonstrate the ability to make significant advances to obtaining its goal of integration in 1992 or "the idea of European economic integration will be dead for a very long time to come".²³ It is true that the 1992 date is probably too optimistic for the program, but as has been stated, the date is immaterial. What cannot be ignored is the direction in which the EC is headed. Aside from the issue of protectionism, there are two important challenges which will face US exporters as the EC 92 program begins to solidify.

The first of these challenges will be the increased competitiveness of the EC. Due to greater efficiency in the management of all resources, the industrial competitiveness of the EC will be enhanced. The result will be a higher quality product at a better price, and this will make EC goods more competitive with US goods, not only within the EC but in competing export markets as well. Second, the US must realize that the financial power of all of the member countries will be consolidated to aggressively support EC

exporters. This will include the harmonization of EC export credit policies and monetary/banking policies.²⁴ This financial strength will open new possibilities to the EC and give it clout in the international marketplace. This too should be a concern to US exporters.

EC 92 is coming. It may be renamed EC 94 or EC 96, but the changes are occurring and progress is being made. The EC is slowly learning to "present a consistent face and a clearer identity to the outside world", and as it becomes better able to do this, it gains strength.²⁵ Several recommendations are made which should be considered by the US if it is to ensure the continuation of a friendly and cooperative trade presence in Europe:

(1) The US can no longer assume that it will always remain the political and economic leader of the Western world. We have witnessed the increased strength and influence of the Japanese, and the formation of a European economic union will further erode our position as a world leader. Steps must be taken to ensure that we maintain fair access to foreign markets, that we continue to modernize our industrial base and that our workforce remains competent and well trained. Failure would lead to inefficiency and the inability of US firms to compete internationally.

(2) The US must show to the EC and the rest of the world that it supports the actions of the EC and the resulting improved efficiency of the world economy. We must show by example that we are truly dedicated to the concept of free trade. Instead of undermining

the progress of the EC by dealing with individual countries, the US should insist on dealing only with the EC in all commercial matters. This support to the European cause will improve the US/EC relationship and hopefully give us a more favorable trading position in the event that protectionist actions are continued.

(3) US firms which have not already positioned themselves within the EC should consider such an action. This could be through direct investment or simply through some kind of partnership agreement with an established EC firm. A position within the EC will be critical to maintaining market access in the event that a wall is built around the EC (and there is little doubt that one will be constructed).

(4) A presence within the EC will also ensure that US firms are positioned to take advantage of new opportunities which will certainly arise as the East/West wall continues to fall. While Eastern investment will be risky, the potential is phenomenal. Firms must consider all of the risks before entering this new frontier, but a fear of the unknown should not preclude firms from investigating all potential opportunities.

(5) In today's complex trade environment, it will be impossible for the EC to operate in isolation. US policymakers should actively promote the importance of cooperation and work closely with the EC hierarchy to establish a fair trade agreement between the two trading partners. It is almost certain that the current membership of the EC will not remain static in the future. Switzerland and Norway are

currently reconsidering their policies of remaining neutral in trade. Turkey is pursuing EC membership, and of course the possibility of Eastern bloc memberships are on the horizon. All of this indicates that the EC could potentially become the world economic power by the year 2000, and the US must do everything possible to ensure that it retains a favorable working relationship as the organization matures.

In summary, the importance of the EC in the future trade environment cannot be overemphasized. The European Community is quite simply a market which we cannot ignore. More significantly, it is a market which we should not underestimate.

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