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EUROPE 1992

THE GOOD AND THE BAD

JOHN REDWOOD MP

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Europe 1992
the good and the bad

1992 OFFERS MANY OPPORTUNITIES TO BRITISH ENTERPRISE. IT WILL mean that Europe is more open for business, and that should bring with it increased prosperity. But schizophrenia reigns in the political councils of Europe. On the one hand there are the ringing phrases and clauses of the Treaty of Rome favouring competition, the roll back of subsidy, the limitation of the role of government in running business. On the other hand there is the growing strength of the socialist groupings in Europe which favour ever more involvement by the Brussels Commission in regional policy, social policy, company law and taxation.

These policies are pulling the European mind apart. In Britain anyone who attacks any Commission proposal is immediately branded as anti-European. It is time the debate moved on and the public was allowed to see that there is a major ideological divide which needs exposing and debating in Europe as elsewhere. The two strands of European policy are mutually incompatible, and one needs to triumph. It is the purpose of this paper to argue that it must be the free market strand that wins.

Regional Policy

The poorer Mediterranean countries of Spain and Greece and Spain's Atlantic neighbour, Portugal, joined the European Economic Community in the hope that it would make them more prosperous. They see the European Community primarily as a means of modernising their countries and economies. They look forward to exploiting the wider European market. All three have relatively cheap labour compared with their northern neighbours and have attitudes towards the length of the working week, social legislation, environmental controls and the like, which give them a far lower cost base than countries in the north.

Despite this, the conventional wisdom in Brussels argues that these poorer Mediterranean countries need special cash help in addition to the benefits which access to the market will bring

them. The European Commission is drawing up the outlines of a huge regional policy designed to produce a 'level playing field'. Furniture factories in Galicia, water works in the south of Italy, manufacturing plant in Greece are already benefiting from the Commission's largesse. Monies raised in taxes levied on northern European consumers and businesses are now routed through the Commission to pay for subsidised competition in the south of Europe.

This conventional wisdom used to be the life blood of British regional policy. We lived through decades of large, regional transfers, taxing London and the South East and sending the proceeds to the North East, the North West, Scotland and Wales. The results were puny. Thousands of talented hard working people moved from the north and west of the country into London and the South East where the jobs were being created in abundance. Some branch factories were established in the North and West, only to be the ones that suffered most in any downturn of trade. Profits and production were often disappointing, as Ford discovered in Liverpool; or else very capital intensive industries used grants to help invest in low employment projects, as ICI did on Teeside.

By the mid 1980s Britain was concluding that expensive regional subsidies were <u>not</u> the way to rejuvenate declining areas. It was only with the advent of urban development corporations and enterprise zones -- designed to move the land out of public ownership into the private sector -- and with the build up of market pressures which forced up ever higher the costs and congestion in London and the South East, that the regional economies started to advance. This advance took place at the very same time that capital subsidies to the regions were abolished.

Must Europe repeat the lesson which has already been so painfully learnt? The latest auditors' report on the European budget pulled no punches. For example, it demonstrated that some of the projects financed are outside the terms of reference for regional funding. It showed how little monitoring or follow-up there is. The European taxpayer is already being milked by regional policy, funding a large number of projects which have

little economic value. Meanwhile the furniture manufacturer rebuilding his business in the North of England is to be told that, in the interests of a level planning field, he has to compete against a Spanish manufacturer whose costs are substantially covered by grant from the European Community. It is difficult enough for the profit conscious British businessman if his southern competitor is happy to run at a loss, without the added hazard of lopsided EEC subsidies.

The Commission aims to increase its total budget, and at the same time to make a large increase in the proportion going to regional subsidy (set at 8bn ecu in 1989 and 16bn by 1992). The bulk of the money will be routed to the Mediterranean countries. The rules require 60% to go to regions of especial need, classified at 'NUTS level II' by Brussels. This excludes England, Scotland and Wales from any share of regional fund cash, since they do not qualify for this aid.

Table 1

The European budget financial year 1989

Item	Billions of ecus
Agricultural subsidies	29.1
Agricultural structures	1.5
Fisheries	0.4
Regional	4.3
Social	3.2
Research Industrial	1.4
Developing countries	0.9
Reserves	3.0
Commission & other institutions	2.0
Total	46

By 1992 the profile of the budget will have changed. Structural, regional and social expenditures will have risen from 7.5bn ecu to 13bn and the total from 46bn to 52.8bn.

The Commission plans, in its own words:-

> Community support frameworks;
> multinational budget forecasts;
> where expedient, integrated operational programmes;
> monitoring and assessment of operations under the fund, carried out in connection with a single objective and of those carried out in connection with a number of objectives on the same territory.

The Commission is looking for projects in excess of 100m ecu each: such major commitments are likely to carry the greatest risks. Groundnut schemes for Nuts level II regions? No -- even more costly.

The shape of the new Regional policy will make it even more difficult for Britain to receive its just return. Once, the theory was that what Britain might lose on the common agricultural policy it could largely recoup on the regional and social policy. This comfortable notion has been overtaken by our own growing prosperity, and by the access of Spain, Portugal and Greece. As a result the regional policy, just like the agricultural policy, may have a net cost to Britain.

As the Court of Auditors has revealed, too many of the schemes already committed have too little genuine economic value. And the new giant projects now proposed are likely to have even less. The Audit Report stated that in 1987

> In two thirds of the cases studied the net utilisation rate of the projects was found to be less than 50%.

and

> In some cases the work has no related economic development objective.

When will the Commission learn that trade, not aid, is the way to harness prosperity in the south? You cannot make the poor countries rich by making the rich countries poor.

It is bonus enough for Portugal, Spain and Greece to enjoy access to the wider European market. That will provide them with the export opportunities and the challenges they need. Europe should abandon regional policy immediately, and be fair to all regions of the Community.

The European Monetary System

Whether Britain should join the EMS or not is coming to be taken as a litmus test of being pro or anti Europe. This is absurd.

The idea behind the European monetary system is that all currencies should be fixed at fairly stable rates between each other; and that these rates should be maintained through ever vigilant central banks intervening across the exchanges. As a result, exporters and importers should see their risks reduced as they can with some confidence predict the exchange rates from one year to another. Even better, convergence of interest rates and inflation rates should result from a knowledge that currencies are going to be stable one against the other.

Academic evidence and history suggest that this idea does not hold water. Devaluations are common within the European monetary system, as countries opt for, or are forced into, divergent monetary or other policies. Each country has elections at different times, a different composition of government, a different banking system, different rates of credit generation and a different history of price stability and monetary control. The Italians have never been able to live within a narrow band against the deutschmark and their currency has depreciated almost continuously. The French have been forced into several periods of rapid devaluation against the deutschmark. Satellite currencies of the Dm, like the Belgian franc and the Dutch guilder, track the deutschmark more accurately, reflecting the great influence the German economy has upon their own. Allsop and Graham in the <u>Oxford Review of Economic Policy</u> (1987), arguing

for the EMS, are representative of academic opinion. They agree that because sterling is a widely traded international currency it would be much more difficult to keep it within a narrow band. They also concede that the EMS has kept some stability because of the capital and exchange controls, which are now being abolished as part of the 1992 programme.

The idea of the EMS is theoretically flawed. The history of the pound against the deutschmark over the last year illustrates why this is so. Despite government efforts to get the pound to shadow the deutschmark and to hold it around the level of Dm3 to the pound, there have been periods of intense pressure leading to substantial fluctuations around that level.

The main method for trying to keep the currencies in line is the sale or purchase of quantities of the given currency by the European central banks acting in concert or individually. If people find the pound particularly attractive compared with the deutschmark all the central banks sell pounds and buy deutschmarks in an effort to counter the substantial commercial forces ranged on the other side.

This action is intrinsically <u>destabilising</u>. If the Bank of England sells a large amount of sterling in order to buy deutschmarks it then has a monetary problem. If it simply creates the pounds it has sold it adds directly to the money supply. Foreign banks and other buyers then have more pounds at their disposal. If they go into the banking system these become high powered money, enabling a bank to lend this money several times over expanding the amount of sterling credit in circulation. This produces upward pressure on the British price level, causing inflationary worries and forcing a further rise in interest rates. Once there has been a further increase in interest rates sterling then looks even more attractive from the point of view of the overseas purchaser, leading to a further demand for pounds requiring more pounds to be manufactured and sold by the Bank of England!

The Bank does have some means of trying to offset this monetary problem. It puts itself into the ridiculous position of selling large quantities of gilt edged securities to the private sector in order to counteract the monetary expansion caused by the intervention. In the year to March 1988 a government which collected £3.6billion more in taxes than it spent on public goods and services had nonetheless to borrow an additional £7000 million through the gilt edged market in order to counterbalance the short term monetary consequences of trying to shadow the deutschmark. This has burdened British taxpayers for 20 to 25 years with an additional £700million a year of interest charges. Against this the Bank of England has acquired claims on Germany and Japan that offer very low rates of interest and in the short term is sitting on a substantial exchange loss, the £ moving up from under DM3 to DM3.27.

If the British authorities had not been trying to shadow the deutschmark monetary, interest rate and even exchange rate policy might have been more stable. Let us assume in the quarter to March 1988 the Government had bought no deutschmark nor yen. Instead of needing to borrow to counteract the monetary effects of issuing more pounds the Government could have repaid debt, further strengthening its strong financial position and cutting the interest burden in subsequent years. The monetary effects of repaying debt from the financial surplus are neutral. As a result of issuing less new debt and having better monetary control, interest rates would have remained at a lower level. In consequence, the pound would have been slightly less attractive to overseas buyers and might, therefore, have risen less fast and less far than it did under the interventionist scheme.

In pursuit of the EMS the government has also been forced into borrowing foreign currencies. Again it is paradoxical for the Government itself is awash with surplus cash and has no real need to borrow from any source. Because, however, the Government has wished to have the resources to intervene to try and stablise the pound, it has made substantial borrowings overseas just in case it needs to buy pounds at some future date. These have had to be matched by monies flowing out of the country in the private sector and this has, therefore, exacerbated the balance of

payments deficit by making more foreign currency available in the exchange intervention account. Again, it would have been simpler not to have borrowed the money and not to have to intervene in the foreign exchange markets. Had the Government pursued this tighter line there might have been a smaller balance of payments deficit.

It is also wrong to think that joining the EMS is a major step toward creating a common European currency. It is true that the businessman's risk in terms of exposure to varying interest rates and exchange rates could be eliminated by creating a common currency in Europe. It would undoubtedly be easier to trade in Europe if all business was conducted in ecu and if every European consumer bought his beer and his jumpers with ecu tcoins and notes.

It is difficult to see how belonging to the EMS makes this any more likely. The EMS depends upon the concerted action of 12 independent central banks. The creation of a single European currency would require a single European central bank combined with a single central European currency issuing authority and mint. This in turn would require a pan European government in order to provide some political control over the actions of that central bank. Interest rate, currency and monetary policy lie at the core of government authority. All governments wish to preserve some independence of action given their different electoral timetables and their different views on what the economy requires whether in stimulus or counter inflation strategy. A single European currency would make for an integrated European economy and would reduce industrial costs through cutting out foreign exchange commissions. It requires first of all an integrated European government to decide on how this should take place.

James Capel, in a recent review of the EMS, has highlighted how it works as 'a DM zone' and keeps the DM undervalued. As a result, in the last two years ten of the eleven other EEC members have run trade deficits with Germany, most of them substantial. They point out that 'Europe has performed sluggishly throughout the 1980s, in large part because the German economy has grown

more slowly than expected'. The Commission does not explain how it can support the systematic undervaluation of the DM when Articles 104-108 of the Treaty expressly require action to be taken to reduce disequilibria in balances of payments between member states. The one action needed is to allow market pressures to create a better valuation of the DM against all the other EEC currencies.

Trade barriers

The decision by the European authorities to ban beef imports from America that contain certain growth hormones is most disturbing. The brilliant simplicity of the idea behind the Treaty of Rome was that free trade and competition across national frontiers and the breaking down of barriers would produce greater prosperity. Instead, in the case of the beef decision, we see one small example of how producer interests are subverting the underlying idea of the Treaty of Rome and threatening us with a damaging trade war.

The use of this artificial hormone in the US is not considered by any reputable medical authority to represent a serious threat to human health. As the hormone replicates natural hormones, the consumer who buys beef from a bull producing substantial quantities of the hormone testosterone may well be eating more of it than in the banned American meat. Given the negligable health risk, a proper way to proceed in an open market would be to encourage a free debate about the advantages and disadvantages of this type of farming, and to insist upon clear labelling of the product so that the customer could make up her own mind. Instead the EEC agricultural interest has banned the imports, thereby further limiting the embryonic competition to European agricultural production.

Japan and America are right to be concerned about the attitude of the European authorities. Japanese manufacturers producing products in Britain are finding difficulties in exporting to other European countries. The French and the Germans are being particularly recalcitrant about the export of Nissan cars from the North East of England, claiming that the proportion of British manufacturing is not high enough to justify

their importation into continental Europe. They are afraid, because the cars have established good standards of quality, performance and price, and would doubtless prove attractive to continental European customers just as they do to English ones. Even more remarkable is the story of Amstrad. Amstrad has succeeded in designing and building what many regard is a cheaper, better and more robust video recorder than those of the European giants. Because parts are imported from the Far East the European competition authorities imposed an import tax on the Amstrad product into Europe, clearly trying to protect the domestic continental producers.

Actions in banning the import of products from overseas, or imposing taxes on domstically produced products where components are imported, are flagrant violations of the spirit of the competition provisions of the Treaty of Rome. More importantly, they directly impose an additional tax burden upon European consumers. If I had to pay £100 more for a motor car than I need do because the motor car producer is banned from importing enough Japanese components, I have £100 less to spend on other items. If I had that extra £100 available it would produce demand for other goods and services, and add to the jobs and prosperity of the wider European economy.

The European competition authorities must surely accept that manufacturers in any given territory within Europe may wish to import components or parts from overseas, and should be free to do so. Europe should participate wholeheartedly in the GATT rounds in order to try and remove more of the remaining barriers to world trade. The EEC's response to the US offers in the present Uruquay round has been disappointing.

Agriculture

Agricultural policy is at the centre of the interventionists' argument. It illustrates the absurdities that public policy can reach when government authorities decide to intervene and prevent markets from working.

The idea behind the common agricultural policy is simple. Because producers in Europe are high cost and inefficient they

need to be protected. And this entails buying up large quantities of their produce at prices way above the world market price in order to guarantee the European farmer a certain level of income.

Once Europe has decided to do this all sorts of consequences flow. First, produce from overseas which could be sold more cheaply to the European customer has to be kept out or taxed. This is particularly damaging to third world countries whose main source of potential export revenue comes from their agricultural sectors, where they may have an advantage from relatively low labour rates or from particularly favourable climate or soil. If they dare to try to compete with temperate products the European system is penal, either preventing importation or exacting a large import duty. Sugar producers in the third world have been especially hard hit by this EEC product policy.

A second consequence is that the European Community, using European taxpayers' money, buys up more produce than European customers wish to purchase. This produces the famous wine lakes and butter mountains. The European Community has to dispose of these surpluses, often preferring to sell them off cheaply to Russia -- at a large loss -- desperate to avoid allowing the market price to fall within the European community, which would undermine the whole system. Recent 'successes' in cutting these surpluses owes much to a series of knock-down sales.

As the exactions for the taxpayer rise, in order to pay for large surpluses and maintain farm incomes, the distortions multiply throughout the system. No satisfactory way has yet been discovered for limiting agricultural subsidy. There have been some attempts to introduce some market pressures into the European agricultural structure, but small ones. As a result the European housewife is paying about 10% more than she need for her food; while the European taxpayers are paying £220million a week in order to prop up farm incomes. It has been calculated by the National Consumer Council that the average family of 4 in Britain is paying £9 a week more than it need.

Runaway farm spending continues to bedevil European policy and debate. Between 1974-1984 the cost of the agricultural

policy more than trebled. Despite reforms designed to limit or cut this, in the following three years spending rose from 18bn ecu to 27bn ecu.

Much of the cost arises from storage and the subsequent losses on disposal of the food. These latter can be huge (as with the butter the sale price of which to the USSR has sunk as low as 7% of the price paid to the farmers). Wheat sold between November 1985 and July 1986 was sold at half the price paid for intervention purchases. With sugar, losses of three quarters of the cost were reported. The Commission regularly buys up and destroys large quantities of fruit which cannot be stored for long periods.

The effects on price have been large. During the 1980s, according to the NCC survey, agricultural commodities have been 70% dearer in the Community on average, with some commodities costing up to three times the world market price.

Nor has the system improved quality. People have come to regard EEC minimum standards as acceptable. But the British Food and Drink Federation has stated:-

> the CAP has encouraged large quantities of low quality agricultural produce to be grown which is either sold straight into intervention stores or exported outside the Community with the aid of large export refunds. Food and drink manufacturers are then forced to import raw materials of the required quality, such as hard bread making wheat or long grain rice, from third world countries and pay an additional import levy which in the case of wheat is over 100% of the cost of the raw material.

As a result of these distorting policies the CAP is estimated to be responsible for a loss of up to 1% of total EEC gdp, a colossal figure implying inefficiencies of up to a quarter in the agricultural sector.

The impact on the total EEC budget has been considerable. From 1970 the EEC was meant to finance all its activities from customs dues, levies on agricultural imports and 1% of the VAT base. In 1984 the VAT ceiling was raised to 1.4% to pay for the large increases in agricultural spending. This proved insufficient, and so in 1988 a 'fourth resource' was introduced, a proportion of member states gdp. On present trends there will be further sharp increases in the tax burden on member states.

The Court of Auditors 1987 budget report criticised many aspects of the financial control over Commission programmes. Its review of the agricultural budget stated:-

> the calculations the Commission made when it came to draw up the schedules of payment forecasts were inaccurate and even slapdash.

And on stockholding it stated:-

> the extent to which member states conduct physical stocktaking of intervention stocks was at best inadequate and at worst non existent....the average error rate of quantities declared as having left public storage, which determined the losses on sales from intervention be made good by the Community, was as high as 45%.

The auditors pointed out that the control was totally inadequate over the stocks themselves, the quality of the stock and the rate of removal from stock. They tracked down irregularity in the export of beef meat which attracts subsidy. In one State tested in 1985 30% of the cases investigated were irregular. Many examples are cited including:-

> refunds were paid by one member state on exports declared to be beef meat. National controls had failed to detect that the consignments were in fact chicken scraps and the exporters concerned received irregular export refunds totalling about 1.4m ecu.

It is always said that it is politically too difficult to change this system. But it would seem the easiest thing in the world to persuade most voters that they would be better off if their food bills were cut by 10%, and their tax bills cut by £220mn a week. It is true that farming lobbies would find this most disagreeable, but the shake-outwould be short and sharp, similar to that in the coal mining industry, whilst the European economy would be greatly strengthened and more prosperous. National governments in the worst affected areas like France and South Germany could decide if they wished to cushion the impact of these changes. Europe cannot afford to duck this issue for much longer. It owes it to the third world as well as to its own food consumers.

The impact on British public expenditure has also been unfortunate. In 1989/90 contributions to the EEC will be one of the fastest growing items of expenditure, with the total more than doubling from £950m in 1988/9 to £1970m in 1989/90.

Fiscal policy and taxation

Under the Single European Act, taxation is a reserve matter where unanimity is still required. Without this provision national sovereignty would have been surrendered entirely to the European authorities, and Europe would have to proceed to the abolition of national governments and the development of a federal one.

Many federalists do see the single European market as but one step along the way to a united European government. For them, taxation is an important part of the journey. Seizing on the general agreement that a more prosperous common market is desirable, they go on to argue that a European market can be unified only if tax rates are common -- both taxes on spending and taxes on income.

They have made most progress in the case of VAT. All member states have introduced VAT and have agreed to pass a proportion of their receipts to the European authorities. The British Government has traditionally not wished to place VAT on a wide range of items from food and childrens clothing to construction.

This decision is gradually coming under attack from the European court, with the recent announcement that Britain has to impose VAT on new construction other than houses, whether it likes it or not.

The United States of America demonstrates that you do not need common taxation in every part of a large geographical area in order to have an effective unified market. The United States open market is of course greatly strengthened by the existence of a common language, a common history and culture, and by a common currency: all things which Europe does not have. Taxes vary from state to state.

There are also theoretical reasons why you do not need to have unified taxation in order to make the market work. What matters in Britain is that the customer should have free choice between the German car, the British car and the Spanish car, and that each producer should face a comparable level of tax on their vehicle. It does not matter very much if the level of tax on cars in Britain is modestly higher or lower than the level of tax on cars in Spain. Not many people will go to Spain to buy their vehicles if the tax is rather lower there. But if the gap between the tax becomes so large that people start to damage the British market by buying in Spain then the British Government would have to take this into account when next considering the appropriate level of taxation.

Similarly, there is no need to have identical levels of income tax throughout the community, but if the rates get too far out of line between countries then the one with the lowest rates will become the most attractive place for businesses to locate. Other countries may decide to follow suit and cut their taxes

A sensible policy towards fiscal harmonisation in Europe would therefore be to allow competition to develop between the national taxation authorities. Lower tax rates would tend to drive out higher tax rates if all the other barriers to trade were removed. A thoroughly benign process would be underway, tending to put pressure downwards on tax rates and thus raising the general level of prosperity within the member nations.

The European Commission could itself give a lead by reducing its claim upon national taxation resources. The proposals in this paper to eliminate all regional subsidies and to make the agricultural sector go over to a market pricing basis would greatly reduce the need for European expenditure. This would be an important first step in cutting VAT rates around Europe. The pressures for further reductions would grow as the low tax countries demonstrated their superior performance.

This is very far from happening now. A good example is the decision of the European Court to impose VAT on British new construction -- ridiculous since it forces the British Customs and Excise to bring more revenue into the British exchequer at a time when the country is already running a huge budget surplus.

European bureaucrats plan sweeping changes in all member states' taxation systems. They favour imputation tax on company profits, a witholding tax on all dividends routed abroad, harmonisation of all excise duties, and a VAT clearing house with each member state holding its VAT within a specified tax band.

The VAT proposals include an end to zero rating (currently used in Britain to protect food, childrens clothing, books and periodicals) and the introduction of a two band system with rates of 4-9% and 14-20%. Here are the present member states' rates:-

% VAT

Country	Reduced Rate	Standard Rate	High Rate
Belgium	6.17	19	25.33
Denmark		22	
France	5.5	18.6	33.3
Germany	7	14	
Greece	6	18	36
Ireland	10	25	
Italy	2.9	18	38
Luxembourg	2.6	12	
Netherlands	6	20	
Portugal	8	16	30
Spain	6	12	33
Britain	0	15	

Britain would have to break election pledges and raise more money from VAT than it needs in order to conform with the Commission proposals. The policy would hit those on lower incomes the hardest, given the higher proportion of their budgets spent on food and clothing. Other countries would face substantial revenue losses from the proposals.

Excise duty harmonisation is equally problematic. Current duty rates and the EEC proposal are set out beneath:

Country	Duty in ecus		
	Petrol (per litre)	Wine (per litre)	Cigarettes (packet of 20)
Belgium	0.25	0.33	0.05
Denmark	0.46	1.57	1.52
France	0.39	0.03	0.03
Germany	0.24	0.00	0.52
Greece	0.42	0.00	0.01
Ireland	0.38	2.79	1.00
Italy	0.53	0.00	0.03
Luxembourg	0.20	0.13	0.03
Netherlands	0.29	0.34	0.24
Portugal	0.41	0.00	0.04
Spain	0.20	0.00	0.01
Britain	0.31	1.54	0.96
EEC proposal	0.34	0.17	0.39

The table shows very different attitudes towards drink and tobacco country by country. Britain's policy of keeping duties high for health reasons would be overthrown by these proposals. The Institute of Fiscal Studies estimates that there would be a loss of £2.6bn in revenues on these items, more than offset by £0.4bn extra tax on petrol and substantial extra revenue from VAT on food and fuel. These forecasts allow for some changes in buying patterns as a result of the price changes.

The danger lurks that if the EEC did harmonise more taxes it would also annex more of these revenues and find ways of spending them. This would offset the excellent low tax enterprise policies which have done so much to rebuild the economic strength of Britain.

Social policy

Those who believe that a common market requires more central control to create common trading conditions favour the evolution of a large European programme of social legislation. It is not fair, these thinkers urge, that the Germans or the French should be burdened with higher employee costs as a result of their particular social legislation. The Portugese and the Spaniards will take advantage of this; so they too must be saddled with similarly high employee costs through a common European approach. And this in turn requires further substantial regional subsidies to Portugal and Spain, to cater for the additional costs imposed on them by the evolution of such common legislation. A gigantic merry go round is thus created, raising costs, raising taxes and raising subsidies throughout the Community.

Europe must be careful. In a world moving towards more free trade and greater prosperity it must compete with the Far Eastern countries. If it burdens itself with restrictive legislation it will be forced into accepting an ever bigger tide of Far Eastern exports, or into trying to erect new barriers against trade on the grounds that the competition is 'unfair'.

Matters relating to employee legislation have also been a reserved issue requiring unanimity. This is another case where national authority requires independent judgments country by country. The main agents to raise standards generally will be those companies operating across frontiers of whom many are, or will be tempted into, granting common conditions and standards of employment throughout Europe.

Many of the measures taken to complete the internal market represent welcome progress. A directive to recognise vocational qualifications in different member countries has been adopted. Co-operation has been encouraged between higher education and

industry. A general system has been established for the recognition of higher education diplomas, diplomas in pharmacy. Professional qualifications are covered by a directive on higher education. Following the passage of the directives, progress is needed to ensure comparability and to encourage the exchange of trained people.

The proposed fifth Company Law Directive, however, causes very many problems. It provides for boards of directors on which non executives outnumber executives, and compulsory worker participation. The proposed tenth Directive also proposes compulsory worker participation on boards following mergers. The Commission's proposal for a new type of European company may be made optional in the hope of avoiding the host of objections by many member states.

Britain is particularly concerned lest some of the flexibility gained in the British economy should be lost through restrictive European legislation. It is not by accident that ours has proved to be the fastest growing job creating economy in the late 1980s. 40,000 additional jobs have been added to the total each month for more than thirty months, partly as a result of the measures to liberalise the labour market. Some European legislation would retard this growth and lead to rising unemployment in Britain (just as it has done in France and Germany).

Mergers and Competition policy

The European Commission has taken a useful lead in several European mergers. Their decision to force the British Government to reduce the level of subsidy to be paid to British Aerospace to take over the ailing carmaker British Leyland from the Government was an excellent manoeuvre which saved the British taxpayer money and created fairer trading terms between car groups in Europe. Similarly the sceptical attention given to the BA/BCal merger was a sensible development in EEC merger competence.

In the run up to 1992 many companies will be looking at possible acquisitions in the false belief that pan european size will be good for them. The national authorities would be wise to

settle upon a size of merger above which the European authorities would be the sole interested competition authorities and below which the national authorities would remain the sole authorities. To have different competition authorities examining the same bid leads to extra delay and costs. It is pointless. If a business has a combined turnover of more than say £2000m and operates in two or more European countries there is a case for Europe and Europe alone deciding whether the merger is in the interests of the wider community or not. If a merger involves a turnover of under £2000m a year or is concerned with only one country there is every argument for leaving the deal to the attentions of the domestic competition authorities. Competition considerations should be the sole reason for referral tothe EEC body.

The balance of payments in manufactures with Europe is adverse for Britain. In the ten months to October 1988 there was a negative balance of £417m on iron and steel, £5049m on motor vehicles, £426m on beverages and even on food and live animals a deficit of £2,666m. In textiles the deficit was £1,139m.

By far the worst imbalance is the substantial deficit on motor vehicles with the Federal Republic of Germany. It is vital for Britain's interests to make sure that where Japanese motor manufacturers establish themselves and manufacture cars in Britain their product should be regarded as British for EEC purposes. Harnessing Japanese technology, management and investment will help to exploit the full potential of the European market, and to rebuild all sections of the British vehicle industry.

The European authorities have rolled back the level of subsidy to coal, steel and other declining industries. This work too should be encouraged through a strengthened competition directorate at the EEC Commission.

Frontiers and Controls

Europe already has a flag, although it is little used, and has persuaded national authorities to adopt a common format for passports. Under the formula suggested above for encouraging competitive reductions in taxation whilst preserving national

sovereignty, customs formalities will need to remain. The single administrative document and the efforts to streamline the customs procedure are welcome, and it should be possible to move to a world where tax was paid in only one terrritory. Goods could be made in a duty free area in country A and exported to country B where the correct level of tax was levied.

Abolition of all frontier controls would make it harder for countries to track down terrorists and police immigration. Germany, for example, offers asylum to anyone who arrives at her frontiers. Again, these are matters which go to the heart national sovereignty. Only if there was a paneuropean government with clear rules over who was and was not allowed to enter Europe would it be possible to remove all internal frontiers and concentrate only on external ones with the rest of the world. We are still a long way away from this position.

Conclusion

The struggle for Europe's soul is intense. Eight out of the twelve member countries have in recent elections chosen left of centre Governments. At the centre of the European Commission under the influence of Monsieur Delors a great deal of socialist thinking is trying to undermine the excellent precepts of the pro competition Treaty of Rome.

Most British people agreed to join the European Community and voted to stay in it because they saw it as a common market capable of generating more prosperity for them. They were not asked to vote to join a federal European Government where Westminster would be demoted and sovereignty would rest in Brussels. Had that been the question the answer might well have been different.

Britain can be proud that it was largely a British initiative which put the single market by 1992 on the European agenda. This must now encompass rolling back subsidies to state organisations, opening up public contracts to competitive tender for any European company, imposing upon the largest mergers a paneuropean view on the desirability of bids and deals and allowing national tax policies to compete to put downward pressure on taxation.

It also requires some new initiatives, most notably the abandonment of the common agricultural policy and its replacement by a market based system of pricing to equate supply with demand. It requires Europe to take a more prominent role in the GATT talks, offering multilateral disarmament of agricultural subsidy and removal of remaining tariff barriers on trade, in return for similar moves by the USA and Japan.

It also means that Britain must prevent the adoption of policies which would subtract from European prosperity. She must contest the recent increases in the total budget, both by urging agricultural changes and by resisting development of regional policies. The British Government rejects the idea of common taxation, and should resist the lure of the European monetary system.

1992 can and should be a great opportunity for British business to expand, gaining access to new markets. It requires understanding of the new rules and standards, investment of cash and people in addressing the demands of EEC markets, and a new enthusiasm for the varied languages, histories and cultures of the diverse European peoples.

Above all it needs repeating that it is eminently possible to be a good European, believing in the market opportunity, whilst at the same time thoroughly disagreeing with those strong strands in federalist thinking which have their origins in plain old fashioned socialism.

Appendix

Extract from Lord Young's speech of 10 March 1989:-

> We will not agree to tax harmonisation being imposed by the Commission; the setting of taxes is a matter for national, sovereign governments.
>
> We will not agree to any increase in the threat of terrorism or drugs resulting from the abolition of border controls; Britain's natural advantages will not be squandered.
>
> We will not agree to the imposition of particular forms of worker participation from Brussels; good companies involve their workers in a manner best suited to their own circumstances, and should not be expected to conform with some corporatist structure of a civil servant's devising.
>
> We will not agree to a single currency in Europe; such a currency would involve a single economic policy and a single political policy - and, with a blindingly obvious logic, a single government in Europe. That is unthinkable.
>
> We will not agree to 'job protection' being written into part-time workers' contracts; that way lies the destruction of hundreds of thousands of British jobs.
>
> We will not agree to protectionist trade policies with the rest of the world, the so-called 'Fortress Europe'; protectionism always destroys jobs and prosperity.
>
> None of these things are part of the single market. And they will not happen.

But the single market will happen. Look at the achievements of the last year or so;

- abolition of exchange controls

- freeing international road haulage quotas

- opening up telecommunications equipment markets

- freeing non-life insurance

- tougher rules on tendering for government contracts

- the first steps to a more open market in civil aviation

This is a real record of achievement, tackling the ingrained protectionism of decades. The European Community is opening up its markets in an unprecedented and extremely encouraging way. The deregulation that has released the enterprising spirit of the British people is not being applied to all the member states of the Community. The result is expanded markets and expanded opportunities for British business.