Europe 1992

Status and Prospects

Claude Barfield

Two years ago, in a now famous speech at Bruges, then–Prime Minister Margaret Thatcher threw down the gauntlet to proponents of a centralized, all-powerful European government. Mrs. Thatcher warned that she had "not successfully rolled back the frontiers of the state in Britain, only to see them reimposed at a European level, with a European superstate exercising a new dominance from Brussels." Such a supranational European leviathan, she vowed, would "never come in my lifetime." Mrs. Thatcher's fears concerning the internal trends of the European Community were matched at the time by a strong suspicion among EC trading partners—particularly the United States—that the EC 1992 process, whatever its formal goals, would result in the emergence of a Fortress Europe that, while lowering trade barriers among EC nations, would raise them for non-Europeans.

As 1992 looms nearer, is there reason to fear that the ultimate result of EC 1992 will be a socialist leviathan lodged behind a Fortress Europe? To answer this question, it is necessary to understand the direct linkage between the European Community's internal social and economic decisions and its external trade decisions.

A struggle is unfolding between two visions of the European Community. One vision looks to a Europe that would allow diversity and competition among national economies to lead to a market-determined outcome. A second vision of the community argues that some market forces must be deflected in the name of "harmonization" and "higher" social or national goals.

The first vision accepts as the ultimate goal of EC 1992 the "free movement of goods, persons, services and capital" as set forth in the Single European Act. For adherents to this market-oriented vision of the European Community, the 1979 *Crème de Cassis* decision handed down by the European Court of Justice constitutes the most important symbolic political act of recent EC history. In that decision the court established the principles of "mutual recognition" and "diversity" as the guidelines for competition among national EC economies.

The market-oriented EC model thus assumes that within the European Community, national factors of production will compete freely without interference from Brussels. Included among the competing elements are both the regulatory and welfare systems of individual countries. The *Financial Times* has noted: "The radical element in the entire internal market programme is the mutual recognition of regulatory regimes. There is no reason why that principle should not apply to the labour market, with different approaches operating side by side."

It is this prospect of competing labor markets and regulatory regimes, coupled with ideology and bureaucratic imperatives, that has led to a second vision of the community. Although most top EC officials give lip service to competition and open markets, important exceptions are often enunciated. It is argued, for example, that the "social dimension" of the common market can only be

Claude E. Barfield is director of science and technology policy at the American Enterprise Institute.

achieved through the "harmonization" of national welfare systems and labor market regulations at a high level of public costs and promised benefits. This harmonization would be characterized by bureaucratic, centralized decisionmaking, and it would be combined with a communitywide redistribution system to buy off the poorer countries.

Harmonization and a leveling up of social costs combined with centrally imposed economic regulations would inevitably lead to a less competitive European economy and thus would increase pressures for protection against outside competition. Indeed, economist Victoria Curzon Price has recently written: "The link between socialism and protection is perfectly straightforward. To the extent that socialism distorts relative prices (say of labour relative to capital, or of current consumption relative to future consumption, or of labour-intensive physical goods over skill-intensive products), it sets up relative price structures which are not compatible with the pattern of international prices. Protection is asked for and protection is granted (textiles, agriculture, steel)." To Price's list of candidates for subsidies and protection many adherents to the second vision of the European Community would add several high-technology industries viewed as "strategic" in assuring the future competitiveness of the community in world markets.

Thus, the defining theme of the EC 1992 process can be seen as a struggle on many policy fronts between those who advocate harmonization through centrally imposed laws and regulations enforcing uniformity and those who promote competition among national laws and systems with market forces holding sway. Internally, the key test will be decisions regarding the "social dimension" of the single European market. Externally, trade issues will be greatly affected over the long haul by the internal social decision.

Concern about long-run trends, however, should not lead us to ignore key decisions that are being made today. In the short run, trade news coming out of Europe is very much a mixed bag. Early concerns about the European Community's post-1992 attitude toward non-European banks and standard-setting procedures have given way to more optimism as recent moves have been toward working out national treatment and mutual recognition agreements. In the areas of agricultural subsidies and European industrial policies designed to protect certain high-technology sectors, however, trends have been less favorable for trading partners outside the European Community.

What Does It Matter?

EC 1992 and the future of the West European economy are of importance to the United States because the European Community constitutes our most important trading partner and our primary area of investment. During the 1980s the community accounted for 22 to 23 percent of U.S. exports and 18 to 20 percent of U.S. imports. In 1989 the European Community was the single most important market for U.S. goods; Europeans bought some $82.5 billion in U.S. exports. (Canada was the second largest U.S. export market ($75 billion) and Japan the third ($42.8 billion).) While the United States ran a substantial trade deficit with the European Community from 1984 to 1988, our trade balance with Europe has now shifted to a small but growing surplus in 1989 and 1990.

The United States and the nations of the European Community also have longstanding investment relationships, many dating from the nineteenth century. In 1988 U.S. direct investment in the community amounted to $126.5 billion and represented almost half of total U.S. foreign direct investment. This figure undoubtedly understates the real value of U.S. investments in Europe because only the original values of the investments are reported, not the current values. Total direct investment in the United States by EC countries in 1988 was even higher, at $193.9 billion or just under 60 percent of total foreign investment in this country. Contrary to popular opinion, the EC nations, not

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Japan, lead the way in direct investment in the United States (the United Kingdom, $102 billion; the Netherlands, $49 billion; Germany, $24 billion; Japan, $53 billion).

The most optimistic analysts predict that European integration will result in a 7 percent increase in gross domestic product, a 6 percent reduction in prices, and the creation of 5 million jobs. Even discounting somewhat this robust optimism, the longstanding economic, political, and social ties between Western Europe and the United States suggest that the creation of a single European market will present U.S. businesses and consumers with great opportunities. This assumes, however, that the goals of a single market will be carried through with concrete, specific actions that allow for the free movement of goods, services, labor, and capital as promised in the Single European Act.

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The Institutional and Economic Framework

Creation of a single common market was envisioned from the outset in the Treaty of Rome, the European Community's founding charter, ratified in 1957. The treaty required the member states to eliminate quantitative restrictions in trade, and it established a customs union. Further steps toward a true common market were delayed, however, until 1985, when economic stagnation, increased foreign competition, and the obvious inability of EC institutions to deal with these problems finally combined to produce the political will necessary for two major advances: publication of the white paper "Completing the Internal Market" and passage of the Single European Act.

The white paper set forth a detailed plan for achieving a single market, including a list of almost 300 physical, technical, and fiscal barriers to a fully integrated market. December 1992 was set as the deadline for removing these obstacles to free movement within the European Community.

The Single European Act is a critical political complement to the economic and social goals set forth in the white paper. The act, which represents the only major constitutional change enacted since the creation of the European Community, substantially reformed the voting procedures of the EC Council. Weighted voting was introduced as votes on internal market issues are now apportioned according to population, with the four largest members each having the maximum number of votes. In addition, no single member can block passage of a measure as was possible in the past. Instead, two large and one small member, or one large and three small members, or various combinations of small members are required.

These rule changes apply to all issues before the EC Council relating to the internal market except taxation, professional qualifications, and the rights of employees. While not so great a change as some reformers would have liked, weighted voting has removed many obstacles to resolving important policy questions. The new voting procedures have also forced member states to work through coalition building to further their individual national interests.

Progress toward implementing the white paper recommendations has been substantial. As of January 1991, the EC Council had formally addressed 184 of the 282 barriers included in the white paper list. The record for changes that require action by individual national parliaments is considerably less impressive, however; here only 24 of the 120 directives that should have been enacted into national law have been. The EC Commission is vigorously conducting infringement proceedings against recalcitrant national legislatures for failure to implement its directives.

The Social Dimension

Thatcher's Bruges speech was in large part a response to her fears regarding the costly consequences of the social programs and regulations proposed by the European Commission. In May 1988 EC President Jacques Delors promised the European Trade Union Confederation a 60 billion Ecu ($72 billion) fund for social and regional redistribution and a charter laying out the fundamental rights of workers.

The charter that the commission bureaucracy produced in December 1989 consists of a number of parts. The most important, and the most controversial, are the company statute and the social charter. The company statute could be used to dictate a specific form of labor participation in the management and control of a company (for example, codetermination). The social charter, meanwhile, consists of an extended list of the "basic rights" of workers that the commission is trying to transform into detailed, legally binding statutes.

Efforts to adopt a communitywide company statute are currently at a standstill, largely because Germany and Great Britain hold polar positions. In 1988 the European Commission drafted a company statute that would allow multinational companies to choose either a national or a common European legal framework. If a firm chose the European framework, it could adopt any of three models: a German model of codetermination in which labor sits on the company's governing board, a Roman model that provides for a workers' council but not representation on the corporate board, or a Scandinavian model that allows the individual company and its labor union to determine the appropriate kind of labor representation in company decisions. The British oppose the draft statute because they believe that there should be no central directives whatsoever on corporate governance. The Germans also oppose the commission's compromise, but out of fear that including less stringent options would inevitably undermine their own system of mandated codetermination. There seems little prospect for a breakthrough any time soon—a fortunate consequence for the proponents of market-based adjustment.

In the area of the social charter, however, the convergence of political forces is less favorable. The commission concedes that it does not have the authority to establish a common minimum wage, but the commission bureaucracy has continued to prepare some 40-odd social and labor regulations on such matters as minimum duration of work, rest periods, holidays, night work, weekend work, part-time workers, and overtime. Recently, it published five proposals concerning part-time or, as it labelled them, "atypical" workers. In effect, the commission proposes that such workers be given the same entitlements as full-time workers.

The commission defends such proposals on the grounds that they are necessary to forestall "social dumping," by which employers would displace workers receiving higher wages with individuals willing to accept lower wages. The commission argues that variations in labor costs distort competition. This is an absurd and pernicious argument. The ability to compete on labor costs is, in fact, central to adjustment, particularly as the European Community moves toward economic and monetary union.

The struggle over implementing the new regulations is likely to be resolved finally by the European Court of Justice because of ambiguous and conflicting wording in the basic EC constitutional

documents regarding workers' rights and social policy. Briefly, one section of the Single European Act states that regulations designed to improve the working environment shall be adopted by a qualified majority, while another section states that the qualified majority shall not be used when dealing with the "rights and interests of employed persons."

Should the qualified majority procedure prevail, extremely costly and intrusive labor and social regulation would be more likely to be adopted throughout the community. Some commentators expect that an unholy alliance of North and South European states will create an overpowering coalition. Northern countries such as Germany will vote to protect their hugely expensive social welfare systems against lower-cost Southern systems. Southern countries such as Greece and Portugal will happily go along in the belief that funds from a central EC pot will bail them out and pay much of the potentially large cost of leveling up their own social welfare systems.

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If extensive labor regulations are adopted, over time they could lead to a ratcheting up of protection as the extra costs of regulation would reduce Europe's ability to compete against nations with lighter regulatory and welfare burdens. The South would demand increasingly massive income redistribution programs to compensate for its lack of growth, and the North would almost certainly turn to protection in a misguided attempt to shoulder the burdens of inefficiency.

Trade Policy

In the long run the European Community's internal social and economic policies may control the shape of European trade policy, but many important decisions in the trade policy arena are being made today.

Certainly, the rhetoric of top EC officials embraced the goal of free trade and competitive markets. In practice, however, EC trade policy is schizophrenic. Some actions point in the direction of open markets and unrestricted competition, while others lead in the opposite direction. An analysis of developments in four trade policy areas illustrates this bifurcation. It is useful to examine policies toward banking, standards and testing, and agriculture and a mix of actions related to industrial policy, including antidumping, rules of origin, and domestic content.

In response to concerns from the United States and other major EC trading partners, the European Commission has acted to remove potential barriers to effective competition from non-EC firms in its banking markets. EC officials initially leaned toward a policy of strict or "mirror" reciprocity.

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That is, the community would grant to outside corporations only those banking privileges granted to EC banks in the foreign banks' home countries. This would have created substantial problems for U.S. banks, given our state banking controls and the federal laws that provide for a separation of commercial and investment banking. In response to U.S. protests, the Second Banking Directive of December 1989 contains more flexible reciprocity wording that stresses national treatment and effective market access in the foreign country as criteria for full operating privileges in the European Community. Although the final details remain to be worked out, U.S. banking executives foresee no major obstacles to establishing and expanding U.S. banking activities in the community.

Similarly, in the area of product standards and testing, the community has acted to accommodate the United States and other major trading nations. Because over half of the 1992 initiatives relate to standards, this is an issue of immense importance for U.S. corporations.

The new EC policies regarding standards and testing were laid down in the white paper of 1985. Two principles guided the proposed new approach to eliminating technical barriers: "mutual recognition" of existing national standards and "harmonization" where conflicting national regulations occurred on essential health and safety matters.

The potential benefits to both EC and non-EC firms from substituting one standard for twelve may be substantial, but for non-EC firms the move to common standards raises a number of potential issues, including nondiscrimination in approval procedures, transparency in the formulation of the standards, and some form of expedited testing procedures to achieve mutual recognition for non-EC national certification systems.

EC officials initially rejected a demand by Secretary of Commerce Robert Mosbacher for a "seat at the table" of EC standard-setting bodies. (This is understandable. Imagine the reaction of the U.S. Congress if the European Community had demanded a "seat at the table" when Congress was considering the 1988 Omnibus Trade and Competitiveness Act.) Since this rebuff, however, EC officials have taken a number of steps to allay U.S. fears in this area. They have agreed to open up the process to allow time for comment and reaction to proposed new standards, and the Europeans have promised, where possible, to adopt rules recommended by existing international standardization bodies. Finally, the European Commission has modified its original position, which denied accreditation to U.S. testing labs, by agreeing that in certain circumstances U.S.-generated tests will be accepted. This clears the way for U.S. officials to negotiate a series of formal mutual recognition agreements in various product areas. While small and medium-sized U.S.

its industrial country partners, has proposed outlawing all mandated obligations that demonstrably distort trade. Despite the better repute enjoyed by foreign direct investment now that servicing foreign loans has become so burdensome, the developing countries and some others as well remain reluctant to part with these handy instruments of industrial policy.

As it happens, the United States in 1982 brought and won a GATT complaint against local-content requirements laid down under Canada's Foreign Investment Review Act. That case was dredged up in the Geneva talks and led to an exhaustive search of the GATT articles for language that might put in question—or, more likely, validate—performance requirements. Here, as elsewhere in the negotiations, the "special and differential" position of the developing countries, so unwisely written into GATT, has proved to be a stumbling block to sensible decision-making. The temper of the performance requirement talks can be gauged by noting that it was not possible initially even to reach agreement that the finding against Canada should have general application.

Still, an agreement of less than complete specificity and force might have been desirable. That outcome would probably have led to a spate of GATT litigation and through that avenue some further restraint on the more egregious performance requirements. A limited agreement on trade-related investment measures, of course, would not have given excessive discomfort to the many American voices calling for an industrial policy applicable to foreign firms located here.

Revision of GATT Articles

At Punta del Este the ministers, without further comment, opened the GATT text to review and to "appropriate" negotiations. With that broad mandate, the articles negotiating group heard a range of ideas for clarifying, expanding on, and otherwise amending GATT provisions. Some useful changes seemed to be in prospect, for example, revisions of Article XVII to make clear that GATT obligations extend to the state trading enterprises of a contracting party.

Among the less fortunate decisions made by the original GATT authors are those found in the several articles relating to balance of payments (XII, XIII, XIV, and XVIII). Taken together, these allow a GATT member pleading problems with balance of payments to resort to quantitative import restrictions, otherwise illegal, and to do so in a discriminatory

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way, a violation of Article I's most-favored-nation rule. Article XVIII, which spells out at length the special status attaching to GATT's developing country members, is differentially permissive. And while the industrial countries have come to recognize that import controls do not provide a suitable response to difficulties with balance of payments, the Third World has not been so persuaded. The United States, Canada, and the European Community proposed that access to these GATT provisions be narrowed for all contracting parties. This modest move toward a more rational trade policy charter was first termed

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nonnegotiable by the developing countries, but the books had not been closed on the question when the Brussels meeting came to its abrupt end.

What Comes Next?

In retrospect, the highest expectations for the Uruguay round were destined for frustration. The scope of the agenda and the relative novelty of some of its items were themselves stumbling blocks. Third World positions, against the lessons of experience, continued to center on claims to special and differential treatment. The European Community's preoccupation with the vista of 1992 and beyond undoubtedly was a factor. Japan's contributions fell well short of what could have been expected from a major player in world trade. And the U.S. negotiators had to carry unhelpful baggage on issues such as antidumping.

Yet a respectable package seemed possible until the eleventh-hour confirmation of the impasse on agricultural trade. The package would have promised an eventual restoration of GATT discipline to trade in agricultural goods and textiles. Tariffs and nontariff measures would have been made less trade-inhibiting, something especially important for market reform in Eastern Europe and the Third World. A framework of GATT-like rules would have provided the basis for liberalized trade in services. Intellectual property rights would have been made more secure internationally. A modernized GATT escape clause would have made it possible to roll back present and to deter future protectionist evasions of GATT commitments. The GATT subsidies code might have undergone balancing and desirable changes. At least a small start might have been made toward ending the special and differential status that has been so harmful to the developing country members of GATT.

The Uruguay round was a missed opportunity to facilitate the movement toward free markets among the erstwhile GATT laggards and GATT newcomers alike—as it was a missed opportunity for the governments of the United States, the European Community, and Japan to begin a mutual shedding of outmoded and costly policies of microeconomic management.

Losing these prospective gains was especially unfortunate at a time when the free-market version of economic organization has acquired unrivalled status. Not only the command economies of Eastern Europe but also the less comprehensive Third World interventionist models have been shown to be disasters. Structural reform is the order of the day. Thus, the Uruguay round was a missed opportunity to facilitate the movement toward free markets among the erstwhile GATT laggards and GATT newcomers alike—as it was a missed opportunity for the governments of the United States, the European Community, and Japan to begin a mutual shedding of outmoded and costly policies of microeconomic management.

In 1971 the Nixon administration's decision to impose a sweeping tariff surcharge on imports was so wholesale a violation as putatively to threaten the survival of GATT. That fear proved to be quite groundless. Within less than a year, the contracting parties were ready to undertake a new negotiation with an agenda broader than in any previous round.

That something of the sort could happen after the shelving of the Uruguay round seems improbable. GATT is not in danger of being abandoned. If governments have often wavered in their dedication to GATT commitments, they have remained attached to the central idea of rules designed to keep national trade policies from becoming collectively destructive. But to convene a successor multilateral trade negotiation in the near future would require that both the United States and the European Community see it as a priority matter.

The European Community is on its way toward a very large modern-day customs union. Switzerland, Austria, and the Scandinavian countries already are attached to the community by bilateral free-trade understandings. All seem likely to request full membership. Thereafter, pressure will be strong to admit the East European states as they work themselves out of their present difficulties. Turkey has been at the door for a long time and eventually will have to be accommodated. This enlarged community will exert greater pulling power than ever on the North African countries, which will seek and doubtless receive more and more preferential treatment.

Of course, a customs union need not be a semiclosed system. The European Community surely will not be. Still, the enlargement process itself promises to engage West European energies for some years to come, to the exclusion of global ventures. Realism says, moreover, that in the post–cold war era the European Community will have less reason than in the past to respond affirmatively if the United States were to suggest a new GATT round.

Nor does the United States appear likely to take the initiative. In Congress and to some significant extent in the business community, the Uruguay round breakdown has been seen as a welcome indicator of U.S. resolve to make trade more "fair." Unilateral action is considered to have brought substantial gains already, with more to come. The important intellectual property lobby, for example, firms are likely to continue to face obstacles in the standards and testing area, good-faith consultations between EC and U.S. officials should provide the means for avoiding the creation of major barriers.

Unfortunately, the good news regarding banking and standards is matched by bad news in two other policy areas—agricultural subsidies and incipient industrial policies. The clash between the European Community and the United States (in reality the community and much of the trading world) over trade-distorting agricultural policies was played out in the recent GATT negotiations, although the roots of the dispute between the two major antagonists go back several decades in a series of pasta, poultry, and canned tomato trade wars.

Although the United States and other nations subsidize their agricultural sectors with various programs, no other nation comes close to matching the European Community in either the size of the subsidies or the distortive effects on agricultural trade. Over the past several decades, the community has created an inefficient and inequitable agricultural commodity monstrosity that combines a policy of high internal prices for its own consumers, ever-increasing subsidies to its farmers, and an expanding warehouse of commodities frequently dumped onto the world market.

By 1989, the European Community's Common Agricultural Policy resulted in a transfer of $54 billion from EC consumers to producers and an additional $44 billion in direct subsidies paid by the EC taxpayers. According to OECD calculations, these two payments together constituted over a third of the total worldwide transfers ($245 billion) from consumers and taxpayers to producers.

In the recently concluded GATT negotiations, the United States first demanded that nations commit themselves to eliminating all trade-distorting agricultural subsidies over the next ten years. In the final stages of the negotiations, however, the United States and other proponents of agricultural trade reform modified their proposals to call for a less ambitious package of reforms, including a reduction of the current level of export subsidies (say 50 percent), a reduction of domestic subsidies (including deficiency payments and price supports), conversion of all quotas to tariffs, and the removal of most nontariff barriers over the next decade.

Achieving a substantial reduction of agricultural trade subsidies and barriers is, indeed, the linchpin of the Uruguay round, and, given the obduracy and political clout of European farmers, the United States and the European Community almost certainly face a series of future trade disputes over agriculture that could poison trade relations overall.

The final issue that has great potential for damaging U.S.-EC relations—and ominous implications for the entire international trading system—is the creation of a high-tech, protectionist industrial policy through the manipulation of antidumping actions combined with local-content and rules-of-origin regulations. Though aimed primarily at the Japanese, the resulting tangle of regulations has already hit U.S. manufacturers.

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The semiconductor sector provides an illustration of the protectionist system at its most advanced. EC antidumping actions are based on assumptions and calculations stacked against importers. (To be fair, the same is true in the United States.) In 1987 the commission tilted further in the direction of increasing the hurdles faced by foreign semiconductor manufacturers by instituting anticircumvention rules that stated that a finished product containing 60 percent or more of its components from the country subject to antidumping duties would be considered a product of that country and subject to the duties. In addition, in 1989 the commission determined that to be counted as "European," chips had to be "diffused" on the continent. (Diffusion is the process by which the chip is given its intelligence.) Foreign companies without diffusion plants in the community are subject to a 14 percent tariff on chips.

U.S. companies thus face the choice of building very expensive ($400 million) chip plants in Europe or absorbing a 14 percent tariff on their products. In addition, Japanese firms, reacting to the combined antidumping and local-content rules, have begun diverting business from U.S. firms to European chipmakers to avoid the stiff antidumping penalties.

The rules-of-origin regulations have implications far beyond semiconductors. For instance, EC nations remain greatly divided over the question of how to count Japanese cars manufactured in Great Britain and Spain—and, more important for the United States, how to count the increasing number of Japanese cars manufactured in this country and exported to the European Community.

EC officials quickly deny that these separate actions are part of an overall industrial policy plan. (There is no across-the-board local-content rule, they argue.) Whether planned or not, the web of regulations that surround key technology sectors seriously distorts trade and investment decisions. Should they spread and deepen, they would undoubtedly cause a major reaction in the United States and increased trade friction.

Powerful U.S. and EC interests are arguing that semiconductors—and indeed the entire electronics sector—are indispensable to high-technology competitiveness. In both political systems, pressures are rising for higher and more widespread subsidies (more Sematechs and more JESSIs) combined with protection from outside competition. (The U.S. and EC semiconductor trade pacts with the Japanese are examples.)

If the European Community adopts costly social systems including the more rigid labor regulations being pressed by some political interests, the resulting slow growth, continuing unemployment, and lack of industrial adjustment would raise the specter of Fortress Europe.

Neither antidumping reform nor a major advance on the question of industrial subsidies emerged from the recent GATT negotiations. These issues along with the merger of technology (industrial) policy with trade policy will constitute a major focus of trade negotiators during the next decade.

Prospects

Before finally assessing the implications of EC integration for the United States, two outside events must be taken into account: the liberation of the East European nations and the reunification of Germany. Each will exert a major influence on the future of the European Community.

The newly reorganized East European economies present both significant problems and significant opportunities for the nations of the European Community. Eastern Europe will provide important new frontiers for investment and trade. Although the least developed of them are not likely to become significant economic actors for several decades, the more advanced—Czechoslovakia and Hungary, for example—may well be ready for full partnership in the European economy in the next few years. To help speed this process, the European Community has taken the lead in creating a major development bank for Eastern Europe. (There are also non-European members of the bank, including the United States (10 percent) and Japan (8.5 percent).) The new European Bank for Reconstruction and Development will lend some $12 billion to the East over the next several years. Inevitably, over the next decade the European Community will focus on developing the Eastern economies, with the effect of lessening investment in other areas of the world, including the United States.

The former West German economy also assumed a massive investment responsibility as the principal fallout from reunification with East Germany. Current estimates put the costs at almost $800 billion over the next five years. Although German political leaders have been slow to admit it, the new obligations will force the government to borrow large sums and ultimately raise national taxes. As the implications and costs of reunification have become more clear to Chancellor Kohl and his lieutenants, they have consciously drawn back from the bold plans of Delors and others to speed monetary and political union of the European Community. Concomitantly, Bundesbank leaders such as Pöhl and Schlesinger have acted to slow the drive toward a common EC currency and a central bank. The Bundesbank will face the daunting and complex tasks as reunification proceeds, and its leaders do not want to lose control of European monetary policy to the more inflation-prone members of the European Community.

The overall impact of freeing the Eastern bloc nations and of German reunification, then, will be twofold: one, for the next few years the European Community will be preoccupied with affairs on the continent; and two, although there are powerful political pressures to "deepen" the community, countervailing forces to slow down the move toward economic and political union are likely to prevail.

What does this all mean for the United States? First, EC trade policy is likely to remain schizophrenic for the foreseeable future, and U.S. trade officials and the private sector will have to remain alert to EC actions that continue or increase barriers to trade. It should also be added that U.S. trade policy will itself have a sizeable impact on EC policy. If the United States persists in the unilateralism characterized by Section 301, in increased antidumping actions and voluntary export restrictions for the Japanese, in more state-sponsored Buy American programs, and in continued large-scale agricultural subsidies, the European Community is sure to follow suit.

Finally, over the longer term, much will depend on the balance of forces and the results of the internal EC debate over the "social dimension." If the community adopts wholesale the costly social systems of the northern countries, including the more rigid labor regulations being pressed by some political interests, the resulting slow growth, continuing unemployment, and lack of industrial adjustment would inevitably again raise the specter of Fortress Europe.

Selected Reading

Calingaert, M. *1992 Challenge from Europe.* Washington, D.C.: National Planning Association, 1988.