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The EU Experience of the Process of Economic Integration: Successes, Failures and Challenges

By Sir Colin Budd LSE IDEAS Advisory Board



I must start with a caveat. Though I represent the LSE at this conference, I am myself no academic! As a diplomat turned politician my natural style, which I hope you will find stimulating, is nearer that of political journalism than it is to the drier groves of academe. Secondly, let me emphasise that, though the EU can always – as you can for us – provide ideas, and though you are naturally free to take out of what I say whatever you want, I realise full well that for all sorts of reasons it is by no means always appropriate to think of the EU as a model for the future of ASEAN. It must be for you to decide what in the European way of doing things is attractive, and what is not.

I say that with all the more clarity because we in Europe, though still decently proud of what the EU is achieving, know very well that overlapping with the speeding up of globalisation has been the declining validity of the assumption that what happens to the economies of the West matters much more than what happens to those of others. Whether one thinks in terms of pendulums swinging back or tectonic plates shifting, there are plainly in this century huge changes afoot in the world economy, adding importance all the time to your part of the world. Thirty years ago, emerging Asia was one eighth of the world economy, of which it is now around a third, with the fraction increasing by the day. Not least because of changes in the distribution of the world's population – of which Europe in 1957 had 21%, today has 11%, and by 2050 is likely to have only 7%. Many people in Europe are rereading Paul Kennedy's "The Rise and Fall of the Great Powers".

Among Kennedy's arguments, mind you, was the assertion that the strength of a Great Power – and much the same surely applies to a regional association of states – can only be properly measured relative to that of other such powers or associations. For that reason among others, study of the EU's strengths – and they are on any analysis impressive – no doubt has a proper place somewhere on ASEAN's agenda. The EU has made very substantial progress towards the creation of a single market, creating millions of jobs and generating much extra wealth. It has a huge trade surplus, is the world's leading exporter of services, accounts – excluding energy – for around 20% of global trade, and has just celebrated the tenth anniversary of its single currency, a reality already for 329 million Europeans.

When the Secretary General of ASEAN visited Europe in July 2007 he stressed that though ASEAN was certainly not planning to take the EU model lock stock and barrel, it was always on the look out for good ideas and best practice, as it pursued the ambitious task of Community building. Especially in connection with its drive to become a more rules-based organisation, with the task of narrowing the development gap between older and newer members of the group, and with the problems involved in cultivating a stronger sense of group identity.

The EU, I can assure you, has wrestled for decades with all those problems, and a myriad more. We have of course been in existence much longer than you, and have in certain respects chosen to go much further than you.

Many of you will know the dramatic story of how France and Germany emerged in 1945 from their third cataclysmic war against each other in three generations, causing some of their leading figures to be utterly convinced of the need to found a new type of organisation, which would eliminate for ever the threat of nationalism. As Helmut Kohl always says, it was Winston Churchill's Zurich speech of 1946 which first publicly stressed the importance of a new friendship between France and Germany, to transform the old enmity into a new cooperation. Although Churchill himself did not envisage the UK joining the new grouping, he nonetheless argued the case for "a European group which could give a sense of enlarged patriotism and common citizenship to the distracted peoples of this turbulent and mighty continent".

It took time to build the membership, which started with six member states in 1957, increased to nine in 1973, then 12, then 15, and now 27. Already from the start there was a common trade policy and a common agricultural policy – plus a plan for a single market, though that was not achieved till 1992. It took time to build the consensus that was needed for successive further steps towards integration, and to build the balance between the institutions which we have today. The European Commission was there from the start, with the sole right of initiative. So was the Council, representing the member states. And so was the European Court of Justice. But the European Parliament has taken a long time to evolve, and the whole idea of "co-decision" – the practice whereby decisions in many areas are now taken jointly by the Council and the European Parliament, is still today advancing into new areas (or will do if the Treaty of Lisbon is ever agreed).

We have the makings of a European polity, with political parties taking increasingly seriously the Europe-wide political groups to which they belong, but public opinion for the most part is still totally focussed on the national rather than the European level.

Many of you will know, and the rest will not be surprised to hear, that there has in Europe been endless controversy about advancing integration. As is no doubt true in Asia, too, states with long histories do not easily give up sovereignty. The reference in the original treaty to "ever increasing union" has been taken by the integrationists as a licence to drive onwards towards a vision of a single, omniscient

body – and by the nationalists as proof positive of the evil of the whole enterprise.

The truth, I think it is fair to say, lies somewhere in the middle. There is no reason why the EU should be regarded, much though Murdoch-owned newspapers love to see it that way, as some kind of inevitably hostile leviathan, forever devouring new fields of competence. The European Commission is no tyrant, the Court of Justice no enemy of the European peoples, and the European Parliament not the illegitimate cuckoo in the parliamentary nest some would make it out to be. If the checks and balances in the system are properly used, and if those at the helm exercise proper self-restraint, then the value of the Union's institutions is that they can play a key role as the guarantors of fair play and even dealing: the architects, groundsmen and referees who between them ensure both that the European playing field is made and kept level, and that those who play on it stick to the democratically agreed rules. Rules which dictate, *inter alia*, that action should only be taken at the EU level where the member states cannot by themselves sufficiently achieve the objectives of the proposed action, and where that action, by reason of its scale and effects, can be better achieved by the Union. A doctrine often referred to as the subsidiarity rule.

I can return, if it helps, in discussion later to the more political aspects of integration, but my main focus will, as advertised, be on the EU's movement towards further economic integration. And rather than recite a long list of successes, I will concentrate, since they are usually the more instructive cases, on the goals not achieved, the agenda still not realised – not least in the context we all now have in common: survival of and the fastest possible recovery from the current global economic crisis. I would therefore like to focus on the closely connected topics of the challenges – and where appropriate, the failures – confronting the EU in relation to the future of the Single Market, the Lisbon Agenda, and the euro.

The Single Market we have today represents a huge achievement. Business benefits enormously from the level playing field for the free movement of

goods and services and – between 22 (double check: 27?) EU member states – people. Phone calls in the EU cost a fraction of what they did ten years ago. Air fares have fallen significantly. Consumers have much greater choice when buying electricity and gas. Business has benefited from major economies and efficiencies of scale.

Much, however, still remains to be done. Partly because the original design has still not been completed; partly because enlargement has brought in new member states which have further to go than the older ones; and partly because the nature of any single market is that it can never be “completed”: it needs constant adaptation, constant change, constant modernisation.

The facts, for instance, show that the services sector has opened up to full integration more slowly than markets for goods – though a major new law was adopted in 2006, enabling companies to offer a range of cross-border services from their home base. Delays have also affected financial services. Most were liberalised by 2005; and in March 2007 it was agreed to unify national payments regimes, which has made it easier to use credit and debit cards abroad and to transfer money from one member state to another. But bank charges for cross-border payments are still higher than they should be, and the fragmented nature of national tax systems continues to put a brake on market integration and efficiency. Whether one looks at financial services or telecommunications, postal services or energy, the reform enthusiasts in Europe know how much further there still is to go before full liberalisation is achieved.

They also know, as the Treaty of Lisbon makes clear, that in future the focus will need to be not so much on the progressive establishment of the internal market and more on establishing and ensuring its functioning. The member states must move, faster and more efficiently than before, to translate EU rules into their national legal systems, and where necessary to enforce them. They need to set up administrative structures – such as points of single contact for businesses. And they need to make sure that consumers both know and can use their rights

– so that maximum choice and the best quality at the lowest prices become a reality.

All this is the more important because securing the implementation of the EU's Single Market rules and standards has long since ceased to be important solely for the EU. In recent years the EU has as you know increasingly been emerging as a global rule maker, shaping and influencing rules and standards worldwide. In many areas such as product safety, environmental protection, public procurement, financial regulation and accounting the EU has in effect become the global standard-setter. The GSM standard, for example, was created in Europe in 1982 but is now used by over three billion mobile phone customers in 212 countries, worldwide.

The Single Market, however, is only part of creating an effective modern economy. Another vitally important campaign is that known in Europe as the Lisbon Agenda. Nothing to do with the Lisbon Treaty – but the programme agreed at the Lisbon summit of March 2000 with the aim of modernising the European economy, the aim being to turn the EU by 2010 into the “most dynamic knowledge-based economy in the world”.

Progress towards that aim has, to say the least, been patchy! As already noted, the internal market in goods is well integrated, but that in services is still fragmented. Competition in the network industries, such as telecoms and energy, is uneven, with national champions continuing to dominate their home markets. Youth unemployment remains far too high. Far too many children do not complete secondary education. Some member states have made far less progress than others. And so on.

The goals of the Lisbon Agenda remain sound enough: the perfection of the information society, a European area of research and innovation, help for SMEs (small and medium enterprises), the completion of the internal market, coordinated macroeconomic policy, better education and training, and an active employment policy. But the EU remains only partially integrated, with a lot of variable geometry, and is still of course in some key respects less well integrated

than the United States, having after all no common language, an only partially common currency, and very rigid labour markets.

The simplest and best guide to the EU's Lisbon Agenda progress is produced every year in February by the London-based Centre for European Reform. Its latest report – “Scorecard IX” – is entitled “How to emerge from the wreckage”. As it points out, a good number of Europeans have long regarded the Lisbon agenda as an attempt to import into Europe the dreaded “Anglo-Saxon neo-liberalism”. Not surprisingly, they are now trying to argue that the financial crisis discredits the Anglo-Saxon model, and hence Lisbon. To which one can of course respond that though some assumptions about the financial sector certainly need to be rethought, the baby should not be thrown out with the bath water: we need more regulation, but should clearly not go so far that we end up with a financial system so safe that it stifles long term growth. Lisbon's broad conceptual thrust has not been invalidated by the crisis. Put simply, countries which fail to lift their educational performance will condemn themselves to lower living standards, and be all the more exposed to rising income inequalities flowing from globalisation and technological change.

The immediate danger for the EU, as for others round the world, is that in the face of the rising social unrest often engendered by recession it becomes even more difficult to push through much of the reform regarded as essential by the architects of the Lisbon agenda. There is indeed a risk that some European governments will be tempted to row back, undermining the single market in the process, and putting strain on some of the disciplines associated with the single currency. For the health of the EU economy it is most important that they should not. Europe badly needs more innovation, faster liberalisation, a keener spirit of enterprise, and a more flexible approach to employment. And it needs these qualities on a more uniform basis. The best Europeans – for instance as regards E-readiness, or the quality of a country's ICT infrastructure and the ability of its people to use ICT well – the best Europeans are among the best in the world, six

being in the global top ten. The level of broadband internet access in France, Germany and the UK is comparable to that of the US, while the latter is well behind the Nordic world and the Netherlands. But a clutch of other Europeans have records which are much less impressive.

The EU will certainly not meet its original 2010 Lisbon agenda objective – but the agenda's aims remain valid. Its methods – often benchmarking and peer pressure rather than central direction – are likely to survive, since the EU treaties leave such areas as labour markets, social security and education in the hands of the member states. Its targets remain an indispensable guide to the desirable direction of reform, and an essential contribution to the task of meeting the great challenges we face: those of ageing populations, increasingly rapid technological change, and globalisation. There is no magic bullet, but an unremitting drive to improve education and skills must on any analysis remain high on the agenda.

And what, finally, of the euro? As I mentioned already, last January it reached its tenth anniversary. For those interested in the detail, there is a 300 page European Commission assessment of the progress made so far, and the goals that still remain to be achieved. The euro's contribution as a factor of dynamism for the EU economy needs little emphasis. It has done much to promote price stability: average annual inflation in the euro area in its first decade was 2.2%, the same as in Germany in the 1990s, despite the nearly 600% rise in the price of oil between 2002 and 2008. It helps to bring down the costs of borrowing. It has enhanced price transparency and convergence, increased trade, and promoted economic and financial integration, both within the euro area and with the rest of the world. It has greatly facilitated the completion of the Single Market, being one of the reasons why cross-border trade in the euro area since it was introduced has increased by about ten percentage points in relation to GDP.

Yet all too obviously, as the President of the ECB said last January, this is no time for complacency: there are challenges aplenty ahead.

First, the financial crisis, which is imposing much strain on the euro area as a whole, and even more on some EU member states – both inside and outside the euro zone. Precisely because of its relatively advanced state of integration, the zone has to absorb a number of country-specific shocks which in the absence of internal exchange rates and with fiscal policies constrained by the SGP (Stability and Growth Pact) are in some ways less easy to deal with than they used to be: the onus of internal adjustment now falls on relative wages and prices, along with the need to ensure labour market flexibility.

Second, Economic Union. The solidity of the single currency rests on two pillars: an effective monetary policy, and a set of sound economic policies – including the firm implementation of the SGP and constant efforts to make the EU economy more productive, innovative and dynamic (You see there the connection to the Lisbon agenda). The ECB lays much stress on the importance of structural reforms, both of the markets for goods and services and of the labour market (especially to promote labour mobility).

Third, making a success of enlargement, both of the EU and of the euro area. It is inspiring to have a single market of 500 million people, but its newest segments still need much nurturing to make them a decently homogeneous part of the whole.

Fourth, all the other Lisbon agenda objectives I have already mentioned – especially the need to improve education and thus develop an increasingly skilled work force, to maintain Europe's competitiveness in the global market place.

Fifth, the rapid ageing of the EU's population, due to change from the current situation of four people of working age for every elderly person to a new ratio of two to one, with potentially far-reaching economic ramifications. This will call for a variety of counter measures, at a time when public indebtedness is already high.

And sixth, the ever clearer requirement – as well as opportunity – for a stronger EU foreign economic policy. As Commissioner Almunia argued earlier

this month, Europe should play an international role commensurate with its economic weight. It has the world's second most important currency, plus shares in world GDP and trade flows surpassing those of the United States, and is the world's largest aid donor. It arguably needs a stronger voice in the international financial institutions – though needless to say there is much dispute about what form that could or should take. One clear insight emerging from the wreckage of the world's financial system is surely that global economic integration demands stronger global governance – which inevitably for any regional association of states begs some sensitive questions about how it organises its governance.

That in turn connects to the underlying wider philosophical challenge that confronts and has to be kept under review by every new EU generation – namely the question of how far further economic integration will require more political integration. That same supranational element in the EU which creates some asymmetry between the EU and ASEAN also continues to give rise, as it always has done, to debate inside the EU. The integrationist purists believe that the greater the role of the union in the economic sphere, the greater the need for political integration, while there is also no shortage of Europeans who think, to put it mildly, that political integration has gone far enough.

This is of course a very old debate. Over sixty years ago, in 1947, the League of Nations Secretariat produced an analysis of customs unions which included this passage:

“For a customs union to exist, it is necessary to allow free movement of goods within a union. For a customs union to be a reality, it is necessary to allow free movement of persons. For a customs union to be stable, it is necessary to maintain free exchangeability of currency and stable exchange rates within the union. This implies, inter alia, free movement of capital within the union. When there is free movement of goods, persons and capital in any area, diverse economic policies concerned with maintaining economic activity cannot be pursued. To

assure uniformity of policy, some political mechanism is required. The greater the interference of the state in economic life, the greater must be the political integration within a customs union”.

That sequence of lapidary statements can only prompt a wry smile, since logical though it undoubtedly is, on one plane, it fails to take account of the complexity of human nature and the force of historical experience. Immanuel Kant, the 18th century German philosopher, used to warn that using reason without applying it to experience would only lead to illusions. “Out of the crooked timber of humanity”, he said, “no straight thing was ever made”.

European statesmen have learned over time since 1957 that they need to work with the grain of the people of Europe, not against it – which some of them have found an easier lesson than others. They need, to switch metaphors, to chart a way forward which is both navigable and inspiring. Integration, as European history since 1957 very clearly shows, can be hugely advantageous, and there is a strong case for taking it further, but it is an undeniably complex and sensitive process, which requires careful planning and good advertising, if it is not to run straight into pavlovian nationalist opposition.

The United Kingdom's experience of this story is perhaps especially instructive. It was a Briton – Lord Cockfield – who designed the European Single Market, in which the large majority of the British have always believed, while resenting what many have seen as excessive standardisation. But we have had our difficulties, to say the least, both with freedom of movement of people and with the idea of a single currency. These and any other issues which interest you I would be very happy to explore further in discussion. ■