CHAPTER 2

EC SHAPING UP AS A SINGLE EUROPEAN MARKET

SECTION I

EUROPEAN "SCLEROSIS" IN THE EARLY 1980s : REMEDIAL PERSPECTIVE

BACKGROUND

The decade of eighties was dominated by growing protectionism in Western Europe, which was the consequence of increasing obsolescence in the European industry coupled with less profitability as a result of higher real wage compared to its productivity\(^1\). This neo-protectionism was in the form of non-tariff barriers in addition to customs tariffs. In fact, neo-protectionism had started to surface from the second oil shock in 1979. Protectionism has always been anti-competitive in the sense it does not allow free imports, which causes domestic price of competing goods to rise due to inelastic demand for their imports\(^2\). This inelasticity of demand causes wide difference between demand and supply price. Restrictions induce importers to get lower price whereas consumers are forced to pay higher price due to supply constraint. The difference between the demand price and supply price is the quota rent, which is enjoyed by the traders of the country that enforces protectionist measures\(^3\).

Competitive policy is characterized by free movement of goods and services without any barrier. Despite the fact that tariffs have been reduced significantly over the years in the industrialized economies but the emergence of non-tariff barriers has endangered trade prospects of developing countries in general and India in particular to the Western hemisphere. It is estimated in several studies that tariff-equivalent of non-tariff barriers is well over 100 per cent in agricultural goods as well as textiles and garments\(^4\). A USITC study shows that average (wtd) tariff in the US market ranges from 15 to 20 per cent but the

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tariff equivalents of quotas in textiles vary from 80-100 per cent over basic level tariffs. Therefore, the horror of protectionism engulfs the trade prospects of most sensitive items of India in which it has comparative advantage.

Several studies on protectionism show that EC is more protectionist than the USA and Japan. The root of protectionism may be due to growing obsolescence of several traditional labour-intensive industries like textiles. In textiles, EC has been facing tough competition from the Asian countries including India. In order to protect its domestic industry, EC has enforced stringent quotas on textile imports since 1961 under short-term and long-term arrangements (STAs & LTAs) and thereafter under the Multifibre Arrangement (MFA). This type of restriction is certainly anti-competitive. Where competitiveness weakens, protectionism flourishes.

For the last 15 years, developed countries have been witnessing increasing use of protectionist measures coupled with the international economic insurgency through the oil-price buoyancy. This exogenous factor is basically responsible for economic sluggishness in the Western countries. The situation became so critical that (as observed in 1970, 1973 and 1975) economic cycle which was the major business cycle in the US history percolated to Western Europe as well. In the later half of the 1970s inflation during slack period was more than that of peak season by 8.4 percentage points. Before that (i.e. in the first half of 1970s) inflation was basically used as a tool of demand management. During that period an increase in prices of raw materials induced high inflation and low output. This was the basic reason for supply shocks.

Besides the two oil-shocks in the 1970s, another major influencing factor for "Euroclerosis" in the early eighties was increase in real wages proportionately much higher than the productivity in the European industry. The result of such ominous trend was the fall in profitability, increase in unemployment which kept investment in a relatively stagnant position. Furthermore, oil price hike resulted in increased obsolescence of the capital stock.

This growing obsolescence in capital stock was the major reason of supply side weakness, because the structure of capital stock got increasingly stalle at a new factor price. The phenomena of supply-side weakness, growing unemployment and increasing obsolescence in capital stock led the western countries to be more protectionist in their trade policies.

"The Second oil shock" in 1979 caused a major set back to European economies which was further exacerbated by the imposition of high interest rates in the USA and over-valuation of its dollar. US allies did not take this step casually and they exerted pressures upon it to lower its interest rates and also to devalue the US dollar so as to restore the parity between US dollar and other major currencies. According to a European analyst Western Europe suffers in export competitiveness in relation to Japan particularly in two areas:

(i) Japan produces high quality labour-intensive manufactured goods; and

(ii) there is a significant lack of complementarily between these two economies. As a result, EC produces many of the same type of goods as Japan does. And since Japan is more competitive than EC, the former always maintains export surplus over EC and United States.

Degree of competitiveness of any country depends on many factors. Uptil now no reliable criteria have been formulated on the basis of which we can measure the degree of competitiveness. Competitiveness is a term which is relatively determined by various socio-economic factors. World Economic Forum, a Switzerland based organization has been publishing World Competitiveness Report since 1980. This report is now recognized to be the world's leading study, ranking the competitiveness of nations. So far it has covered 49 nations.

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8. A. Olechowski, & Gary Simpson, "Current Trade Restrictions in the EC, the USA and Japan", Journal of World Trade and Law, (Geneva), May/June 1980, pp. 230-231.
10. (a) Robert Long, "Japan Threatens USA more than Europe", European Affairs, no. 1/87, p. 53.
    (b) Reve Herrmann, "Europe's Technological Comparision with Japan", Aussen Politik, (Hamburg), 16/37, 3/86, p. 267.
World Competitiveness Report has evaluated competitiveness on the basis of eight factors. All these factors are also determined by the same criteria. To determine the importance of these factors in total 378 criteria have been taken into consideration. Determining factors are:

(i) Domestic Economic Strength
(ii) Internationalization
(iii) Government
(iv) Finance
(v) Infrastructure
(vi) Management
(vii) Science and Technology
(viii) People

Only forty eight (48) criteria have been taken into account for macro economic evaluation of the domestic economy. Degree of internationalisation i.e. the extent to which a country participates in international trade and investment flows, is measured in terms of sixty (60) criteria. The extent to which government policies are conducive to competitiveness is determined by fifty four (54) criteria. Performance of capital markets and quality of financial services are determined by thirty five (35) different criteria. Infrastructure is one of the most important factors determining degree of competitiveness, which takes into account fifty six (56) different criteria. Presently management skill has got the pivotal importance in determining the degree of competitiveness. It measures the extent to which enterprises are managed in an innovative, profitable and responsible manner. To determine the role of this factor, thirty seven (37) criteria have been taken into account. Scientific and technological capacity together with the success of basic and applied research is the another important factor of competitiveness which covers forty two (42) different criteria. Ultimately the availability and quality of human resources determine the value of product as well as its competitiveness in the market. To evaluate the role of human resources it takes altogether fifty six (56) different criteria.

13. Ibid n. 12 p. 36-42.
According to World Competitiveness Report 1995, the USA, after a long time regained the top position in world competitiveness (it also ranked first in 1994). This place has been occupied by Japan for nine years. In 1995, the gap widened even more between the USA, which is still in the lead and Japan now ranks fourth and continues to slide. The World Competitiveness Report further shows that USA forges ahead, Japan slips away and Europe diverges.\(^\text{14}\)

The USA and Singapore are not only ahead of other nations in the world competitiveness scoreboard but also they are increasing their lead in almost all areas of competitiveness. The USA ranks first in domestic economic strength, internationalisation and management, a unique position which reflects the US ability to thrive on a buoyant and large domestic market while maintaining a strong presence in the international market. The aggressiveness of industry in the USA is especially noticeable in new technologies like computers, software, telecommunication etc. Not only in the aforesaid areas but also it ranks first in science and technology. On the other hand the devaluation of the dollar is another factor of increasing US competitiveness in the international market. In spite of such strengths it has also some weaknesses like government where it ranks sixth and people, ninth position.\(^\text{15}\)

Japan having topmost position in the of world competitiveness for many years, it has now started sliding down in almost all important areas. In 1995, it ranked fourth in the world competitiveness. The unprecedented economic crisis of the past two years explains the country's fourth position in the domestic economic strength, and sixth in finance. The internal crisis has been revealing through stability of its government and that is the reason why it ranks twenty seventh, in government, a noticeable drop from second position in 1991. Japan also ranks sixth in people which had a long standing leading position in the past. Japan's sufferings seem to be socially rather than economically, which means that challenge will lie in country's ability to reform. In domestic economic strength Japan's position had declined from first to fourth between 1991 and 1995. In internationalisation, the same down-trend continued. It ranked first in 1991 but slid down to ninth in 1995. The slide-down became worst in government where its position declined from second in 1991 to twenty-seventh in 1995. In finance also the same trend continues. It ranked first

\(^{14}\) Ibid n. 12 p. 14-16.

\(^{15}\) Ibid n. 12 p. 14.
in 1991 but slipped down to sixth in 1995. In infrastructure also its decline was very prominent. It occupied first position in 1991 but declined to twenty eighth in 1995. In areas of management its position was a bit stable but even in this area its position slid down from first to fourth in the corresponding period. In science and technology Japan still holds the lead role, ranking second in 1995, but it has been holding first position until 1994. In availability and quality of people, Japan ranked first until 1992 but dropped to sixth position in 1995.

In the 1995 World Competitiveness Scoreboard, the European Union is more dispersed than ever, thus underlining the difficulties its member states have been experiencing in their efforts to cover their economies, a prerequisite for the Maastricht Treaty. In overall ranking Germany stands sixth. In domestic economic strength Germany's position is eighth and it ranks fifth in degree of internationalisation. Recently Germany too faces some problems in government policies especially after unification of Germany, that is why its position has slid down from fourth to thirteenth between 1991 and 1995. Germany is more or less stable in finance where its position was sixth. In 1991, it slightly declined to eighth in 1995. Germany also faces infrastructural problems these days, which bear out from the fact that its position in providing infrastructure has declined from sixth to eleventh between these two periods. Its decline in management is too pronounced where it slid down from third to fourteenth during this comparable period. Only in area of science and technology, it has improved its rank from fourth to third between 1991 and 1995. The availability and quality of human resources has been disappointing. Germany ranked fourth in this area but slid down to ninth in 1995. This is the indication of growing tension in industrial relations.

The northern European countries are relatively better in improving competitiveness, viz. the Netherlands (7th), Denmark (9th), Austria (13th), Sweden (15th), and Finland (16th). Even among these countries relative performance of Austria, Sweden and Finland has been relatively better because only recently (i.e. in 1995) they have joined EU. Better performance is the reflection of their confidence of being a member of the EU. France (17th) and the UK (18th) continue to fight for better ranking. Both countries perform very well in internationalisation

17. Ibid n. 12 p. 16, 27.
(6th to 8th respectively), thus departing from their former image of being rather self-centered countries. However, they seem to suffer from having a certain distrust in government. France has an extra-ordinarily poor ranking (35th), while the UK's position is relatively better (14th). Management is also considered to have some shortcoming in both countries (21st and 20th). More disquieting perhaps is the bad ranking given to the people factor (15th to 20th), which is also vital for the future of long term competitiveness.

Belgium/Luxembourg (19th) and Ireland (22nd) are smaller countries, which share a similar pattern of strong internationalisation (7th and 10th respectively), while still struggling with a government performance which is less satisfactory (42nd and 29th respectively), and it is the reflection of high debt level in both countries. The southern part of Europe continues to struggle. Spain (20th), Italy (30th), and Portugal (31st) are in a group of their own whereas competitive position of Greece has declined from 22nd to 43rd between 1989 and 1995. In all eight relevant criteria Greece has been showing a declining trend between 1991 and 1995.

COMPETITIVENESS : COMPARISON BETWEEN USA, JAPAN AND THE EUROPEAN COMMUNITIES

A Synoptic View

The competitiveness of an economy depends on its ability to increase market shares or to sustain a higher growth without deteriorating current account balance. The determining factors of trade and current account performance can be grouped in three main categories:

1. Relative Cyclical Position (Income Effect)
2. Relative Cost Development (Price Effect)
3. Relative Change in Productive Potential (Supply Effect)

Over the period 1987-1992, different critical developments seemed to explain the direction of change in external positions and trade performance in the USA, Japan and the EU.

18. Ibid n. 12 p. 16, 27.
19. Ibid n. 12 p. 16.
20. Ibid n. 12 p. 16, 27.
However, relative change in cost structure seems to have played a significant role in the intensity of these changes. For the USA the 22.3 per cent improvement in export market share can therefore be explained by the combination of domestic demand growth i.e. a cumulative 8 per cent below the average of its industrial partners, and an 18.8 per cent improvement in its cost competitiveness against the same partners in the fourth quarter of 1992 compared to the first quarter of 1987\(^{22}\). Such a reduction of its relative manufacturing unit labour cost in common currency resulted from both an effective nominal depreciation of the dollar (-11.5 \%) and decrease in relative unit labour costs measured in national currencies (-6.5\%)\(^{23}\).

For Japan, a 7.5 per cent loss in export market share looks very moderate in relation to an almost 15 per cent faster growth in its domestic demand and an 11 per cent deterioration in cost competitiveness measured in the fourth quarter of 1992 by relative unit labour costs in common currency. Such deterioration in competitiveness was the net result of nominal appreciation of the yen (+18.5 \%), and a reduction of relative unit labour cost measured in national currencies (-6.5 \%). It seem that other factors played a compensatory role in favour of Japanese external performance, such as the substantial profitability advantage that the Japanese manufacturing sector enjoyed at the beginning of the period\(^{24}\).

For the EC as a whole, the deterioration of export and current account position could be explained by cyclical factors (domestic demand growth 2.8 per cent above the average of its industrial partners) and deterioration in cost competitiveness. Until the third quarter of 1992, the loss of competitiveness (17.8 per cent) was merely due to a nominal appreciation of Community currencies (10.2 per cent) than to an increase in relative unit labour cost measured in national currencies (6.9 per cent). However, during the fourth quarter of 1992, the depreciation of Community currencies (-6.8 per cent) led to reduction of competitiveness by 10.4 per cent as compared to the first quarter of 1987\(^{25}\).

**Indicators of Competitiveness**

Degree of competitiveness is measured by several factors. The extent to which a country is competitive is reflected on its ability to increase its market share in export, or

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22. Ibid n. 21 pp. 159-178.
23. Ibid n. 21 p. 163.
24. Ibid n. 21 p. 163.
25. Ibid n. 21 pp. 163-164
to sustain a higher rate of growth of domestic demand without a deterioration in its current account balance\(^{(26)}\). The degree of competitiveness works in the following areas:

2. Trends in relative manufacturing unit labour costs.
3. Trends in purchasing power of each currency.
4. Developments in relative profitability in manufacturing sector.
5. Comparison of absolute levels of total wage cost and productivity.

1. **Current Account Balance and Trade Performance**

The main determinants of competitiveness are the relative position of current account balance and export performance. Besides, changes in relative cyclical positions (income effects), relative growth in productive potential (supply effect and output gap) and competitiveness (relative price effects) are three main categories of factors determining competitiveness\(^{(27)}\).

Comparing income effect and trade performance in 1992 against 1987, between the USA, EC and Japan, we observe that relative growth in domestic demand was 14.8 per cent higher in case of Japan which was 8 per cent less in the USA and only 2.8 per cent higher in the EC. Comparing the market share between these two periods, Japan’s relative share declined 5.3 per cent but for the USA it increased 22.3 per cent. Lastly and most important indicator is the current account balance as a percentage of GDP. Change in current account balance for Japan was -0.4 per cent, for EC it was -1.3 per cent but for the USA it was 2.5 per cent\(^{(28)}\).

2. **Relative Position of Manufacturing Unit Labour Cost**

The comparison is based on the nominal effective exchange rates of each of the respective countries (or group of countries) vis-a-vis other industrialised countries deflated by unit labour cost indices. The competitive position of the US manufacturing sector has improved substantially since the **Louvre Accord** (first quarter of 1987). The last quarter of

27. (a) Ibid n. 21 p. 165.
    (b) Ibid n. 26 p. 72.
28. (a) Ibid n. p. 166.
    (b) Commission of the European Commission, "European Competitiveness in The Triad Macro Economic and Structural Aspects", in *European Economy*, (Brussels), No. 2, 1993, pp. 113-116.
1992 registered a relative cost improvement of 18.8 per cent (estimated) compared to the first quarter of 1987. Such a real exchange-rate depreciation resulted from the combination of an 11.5 per cent nominal depreciation of the effective exchange rate of the dollar, despite the upsurge in the nominal exchange rate of the dollar at the end of 1992 and 6.5 per cent reduction in US relative unit labour costs measured in national currencies(29).

Since 1987, the competitive position of Japanese manufacturing sector exhibited mainly two divergent trends: first, a strong improvement in competitiveness until the second quarter of 1990, and since then a steady deterioration which put Japanese relative ULCM (Unit Labour Cost in Manufacturing) 11 per cent higher than at the time of the Louvre Agreement. During the first period, the sharp drop in relative ULCM for Japan was the combined result of a fall in the nominal exchange rate of the yen (-6.1 per cent from the Louvre Level) and a reduction in unit labour cost measured in national currencies (-9.9 per cent). During the second period, the increase of ULCM in common currency amounted to 33 per cent, as a result of both nominal appreciation of the yen against the 19 other currencies (26.2 percent) and an increase in relative unit labour costs measured in national currencies (5.4 per cent). Over a longer term perspective, the yen has been showing a trend of real appreciation(30).

For EC, the currencies taken as a group vis-a-vis third currencies, the real appreciation in the fourth quarter of 1992 compared to the first quarter of 1987 amounted to 10.4 per cent after a peak of 17.8 per cent in the third quarter of 1992. This 6.3 per cent drop in EC’s relative unit labour costs in the fourth quarter was due to appreciation of the dollar combined with the impact of the depreciation of the pound, lira and peseta. The weakening in the competitive position of the EC’s manufacturing sector could be examined bilaterally with respect to the USA and Japan. EC’s cumulative losses in the fourth quarter of 1992 in relation to the “Louvre quarter” were around 20 per cent against the US dollar and 1.3 per cent against the yen. In the third quarter of 1992, these losses reached 27 per cent against the dollar and 12 per cent against the yen(31).

29. (a) Ibid n. 21 pp. 167-170.
30. Ibid n. p. 117-120.
31. (a) Ibid n. 28(b) p. 125-130.
   (b) Ibid n. 28(b) p. 169.
3. **Purchasing Power of Each Currency**

Normally, index of relative inflation is used as an indicator to assess currency prospects. Relative consumer price indices measured in a common currency, i.e., they correspond to the ratio of the consumer price index in one country to consumer price indices in its trading partners, multiplied by index of the nominal exchange rate of this country against its partner currencies.

According to this indicator, real exchange rate developments since the Louvre have been less marked in the fourth quarter of 1992, the competitive improvement of the US economy amounted to 8 per cent, while the deterioration for the yen was limited to 5.6 per cent and 3.6 per cent for the EC currencies. However, compared to mid-1989, real appreciation of the EC currencies reached 10.5 per cent\(^{(32)}\).

4. **Relative Profitability in Manufacturing Sector\(^{(33)}\)**

Cost-competitiveness indicator can not alone capture complex nature of competitiveness of a nation. Due to several reasons, it is not treated as an ideal indicator of competitiveness. Rather profitability is regarded as the best indicator of competitiveness. However, one can better assess the net impact of cost-competitiveness and structural competitiveness by referring to the relative evolution of the labour share in manufacturing value added that is the ratio of the relative unit labour costs to the total manufacturing value added and relative deflectors of the corresponding wage-share value added. The trend of relative wage-share which gives implicitly (in inverse) a relatively profitability indicator. Relative labour cost share in gross value added in 1992 reveals that it is lowest in case of the USA and highest in case of Japan. This means labour productivity is higher in Japan and lower in the USA. Since labour-share is highest in Japan and lowest in the USA, this means profitability in USA is higher as compared to Japan. Trend of labour share for EC has been coming down means EC industry was also approaching for more profit\(^{(34)}\).

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33. (a) Ibid n. p. 120-130.
(b) Ibid n. p. 174-175.
5. **Comparison of Absolute Level of Total Wage Costs and Productivity**

Until 1987, the USA was having the highest level of total wage costs per employee. In 1992, Germany and Belgium workers had taken over. The ranking of EC members has remained unchanged since 1987. Among G-7 countries, France maintains its rank of third position, after USA and just before Japan. Italy is fifth and has narrowed down its gap with France. A partial catching up appears for Spain and also for the UK. Of course, these wage gaps also reflect some average productivity level gaps as the comparison with the value-added (at current price and exchange rates) per employee. However, with the increasing mobility of capital and entrepreneurship in the EC, the existing average productivity level gaps are not necessarily a constraint to new investment flows. But on the other hand, there have been still some opportunities to reap the benefits of the wage level gaps.

**SECTION II**

**THE COCKFIELD REPORT 1985 : OUTLINING THE PROCESS OF EUROPEAN UNION**

2.1 **Introduction**

The programme of single economic market of the European Community was a grandiose one. The idea of internal market gathered momentum in 1968 through the creation of customs union and in December 1992 with the emergence of the Single European Market, a largest trading bloc in the world then composed of 12 and now 15 developed countries of Western Europe. The factor which seems to have expedited the completion of the internal market was the emergence of other regional trading blocs, like NAFTA, ASEAN, APEC etc. In order to counter the mushroom growth of regional trading blocs, EC has already brought down its tariff level to a very low level for making its industry internationally more competitive. Yet, the EC is having plethora of non-tariff barriers (NTBs) in the form of...

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physical, fiscal and technical which cause severe damage to its internal as well as international competitiveness.

Perturbed by rapid change in international economic scenario characterized by the proliferation of regional trading blocs, the EC statesmen assembled together and discussed the future prospect of EC. The completion of Single European Market (SEM) was the only way of economic integration through which member countries would make concerted efforts to remove all internal barriers. Finally, in order to give this idea a concrete shape, and to find out the modalities of economic integration, the European Commission in 1985 appointed a Committee led by Lord Cockfield. He was asked to identify the factors required for shaping up the Single European Market (hereinafter SEM) and also to prescribe what type of structural changes were needed for the completion of internal market and to locate the areas where these changes could be carried out.

Lord Cockfield prepared a White Paper portraying the current scenarios of different sectors and the changes that are required for the completion of SEM. The objectives of the committee were consistent with the resolution adopted in principle by the Heads of States in Milan in June 1985. Cockfield had completed his task on 6 June 1986. Initial progress report showed that 27 out of 61 targeted proposals had been accepted by 1986 and 71 proposals were accepted during 1987. The White Paper proposed a time-bound programme for the completion of SEM. In this regard following suggestions were made:

(i) Removal of non-tariff barriers existing between the member countries in the form of customs, posts, immigration and passport controls during inter-state transactions. Harmonisation of public health standards among the Community members and finally the abolition of transport controls.

(ii) Fixing up a time-schedule for the removal of technical barriers.

(iii) Ensuring smooth and steady flow of capital (both physical and human) among the member countries, and taking appropriate measures to protect industrial and intellectual property rights. Harmonization of indirect taxation (VAT and excise tax) was also the focal point of the reform programme.

2.2 Basic Premises of the Cockfield Report

For the completion of SEM, Cockfield proposed following measures that were essential to rejuvenate the European economy on one hand, and to counter the threat of growing menace of regionalism on the other.

- Removal of physical barriers
- Removal of technical barriers
- Removal of fiscal barriers
- Harmonization of rules and standards
- Approximation of legislation and tax structure
- Introducing common Exchange Rate Mechanism (ERM)
- Common Economic and Monetary Union

The SEM had three objectives viz.

**First**: To bring 12 different European countries having wide diversities in socio-economic and culture, into one platform. The programme envisaged single market and single monetary and political entity comprising the member states.

**Second**: In order to counter the growth of regionalism and to fight with the increasing competitiveness emerged from Japan and the USA, it was imperative for the Community to make concerted efforts for cost reduction through the removal of all barriers.

**Third**: Ensuring the maximum flexibility in respect of inter-state movement of man and material, and to exploit economies of scale through changing the scale of operation.

1. Removal of Physical Barriers

Non-tariff barriers in the form of physical controls are mainly of two types, viz. 
(a) control of goods and (b) control of individuals.

(a) Control of Goods

Every member state has its own national regulations on border control which restrict free-flow of goods between the member states. The Commission proposal was that all different
rules pertaining to internal control were to be harmonized and the border controls (in the form of administration of transit procedures) were to be removed and "single administrative documentation system" would be introduced. The entire gamut of policy framework has the following four areas:

(i) Commercial and Economic Policy

The White Paper had set the time-limit for abolition of all types of national protective measures and regional quotas by 1992 except agriculture due to its special features.

(ii) Health and Environment

Health protection was mainly in the form of veterinary and plant health checks in the border, the extent of which varies from country to country because of different national regulations. The White Paper proposed harmonization of all national rules on health standards for the establishment of SEM (Single European Market). As a precondition of SEM all veterinary controls (on live animals and animal products) and plant health control would have to be limited to the places of departure. As regards, environment, special care was taken to control over transportation and disposal of dangerous and hazardous toxic materials that would emerge after the abolition of internal frontier.

(iii) Transportation

In the area of transportation the White Paper proposed a common transport policy among the member states for ensuring smooth flow of goods. Until recently transport operators in the EC were guided by the intra-Community quota system for which every vehicle must have to carry transport authorization certificate. These certificates and books of record sheets were subject to rigorous checks at the frontier. Therefore, after the abolition of frontier control transport quota was likely to be dismantled except some dangerous products on safety grounds.

(iv) Statistics

The harmonization of statistical methods for compilation, storing and documentation of data was an integral part of the SEM.

(b) Control of Individuals

Movement of persons among the member states was controlled by national regulations, which were basically of two types, viz: (i) Police check relating to the identity of
the persons, and (ii) tax checks. As regards Police check, the White Paper proposed to make the check at internal frontier for EC nationals more flexible except in case of tourists and drugs. As a part of the move, Report proposed the introduction of a common passport testifying the position of an individual as a citizen of any member state and also introduction of "self-identification" system. With a view to dismantling checking system by 1992, EC proposed the following directives:

(i) Approximation of arm legislation which meant that absence of checking must not provide an incentive to buy arms from countries with a liberal legislation.

(ii) Approximation of drug legislation was proposed in 1987 and implemented in 1989.

(iii) Personnel of non-member states will also seem to be the beneficiaries of liberalizing control because after abolition of checking system, people of member states would be able to move from one state to another without any rigorous checking. The White Paper proposed to frame suitable policies for non-Community nationals in respect of employment, residence and entry.

(iv) Together with the removal of internal barriers, the White Paper provided a comprehensive package to streamline the Community's visa policy for non-Community personnel. Besides, Commission (Cockfield) mooted a common extradition policy which was proposed to be adopted in 1990 and 1991.

2. Removal of Technical Barriers

Existence of technical barriers to trade was another major non-tariff barrier applied on the intra-Community movements of goods, services, labour and capital. There was no reason to believe that rules and regulations pertaining to health, quality and protection of human life would necessarily be the same for all countries. What was more important that selling products of one country to the markets of others required uniform system. Removal of technical barriers would work upon following areas:

- Free movement of goods
- Public procurement
- Free movement for labour and persons
- A common market for the Community members
- Free movement of capital
- Creation of suitable category for industrial cooperation
- Application of Community Law.
Free movement of goods between member states was often restrained by health and sanitary standards, phytosanitary regulations and different national standards. In order to ensure the free-movement of goods, the Commission proposed the following measures:

— identifying areas for harmonization or for mutual cooperation.

— legislative harmonization was proposed to be restricted to health and safety requirements; and

— harmonization was proposed to be at par with the European standard rather than multiplicity of national standards.

Public procurement policy was discriminatory between the members. It was normally alleged that a sizable portion of public procurement/purchase contract was awarded to the national agencies which was detrimental to the healthy growth of common internal market. In this regard Commission proposed to make the auction/bid as transparent as possible in respect of timing, quality and speed of publication of tenders. Four major groups were excluded from liberalisation process, viz. water, energy, transport and telecommunication.

Regarding free-movement of labour and professionals, the Commission was very particular in removing all barriers. Though it was a proven fact that the standard of education was not same in all states. In such cases Commission favoured introduction of “vocational training card” and harmonization of professional qualifications. This measure would enable the nationals of member states to be eligible to get jobs across the Community.

Common Market for Services was the most potential sector, which remained untapped until recently. Regarding traditional services like banking, insurance and transport, the Report favoured opening up of the cross-border market.

Regarding credit institutions, especially banking and insurance services, Commission had emphasised coordinated action in respect of fund allocation to the priority sectors and extending the facility across the border. In security services, Commission had proposed harmonization of investment norms across the border, harmonization in management and distribution of portfolios and dissemination of information across the borders. In addition to that, the Commission was in favour of establishing a Common European Security market in line with the European Stock Exchange which would facilitate the security transfer on a day to day basis.
Transport Services comprised 7 per cent of the Community's GDP. Recognising the importance of transport services in trade and industry, the Report had suggested the following measures:

- Abolition of quantitative restrictions (quota) to transport operators (by road) among the members and creating opportunities for non-resident operators.
- Freedom of transport of passengers by roads.
- In case of international transport of goods through inland waterway, members were given priority but some facilities were proposed to be given to carriers from non-member countries.
- The same facility was proposed to extend to air cargo also.

New-Technology and Services

All the members of the Community were not equally advanced in high-tech areas. Therefore, Commission's proposal was that there should be an intra-Community network in disseminating any innovation in areas of audio and visual services, information services, data processing services and computer marketing and distribution services. Regarding audiovisual services, Commission was in favour of setting up a Community wise broadcasting area through which it would transmit all information on trade and commerce and economic activities to all of its members. Common broadcasting services, common banking services and common information services are essential ingredients of common market.

5. Capital Movements

One of the major ingredients of "Europe 1992" was the free-movement of capital across the border. Henceforth, liberalisation of capital market is required for three proposes, viz:

- Free movement of goods, services and persons across the border requires access to efficient financial system.
- Monetary stability through the European Monetary System (EMS) was the essential precondition for development of the internal market which required greater dynamism of capital market.
The decompartmentalisation of financial market would boost economic development of the Community by promoting optimum allocation of savings of members and non-member states.

6. Creation of Suitable Conditions for Industrial Cooperation

Active cooperation between member states was constrained by excessive legal, fiscal and administrative bottlenecks. The protected measures are given as below:

(i) Creation of Legal Framework Facilitating Corporations

Due to complex legal framework of the Community, a large number of joint projects were not getting materialised. In order to cope with the situation, it was suggested in the Report to harmonize different national legal systems under the aegis of "European Economic Interest Grouping".

(ii) Intellectual or Industrial Properties

Three main areas in the intellectual properties were, viz. copyrights, trademarks and patents. These were suggested to be made more dynamic consistent with the rapid technological change in areas of computer, software, micro-circuits and biotechnology. The Luxembourg Convention on the Community patents was signed in 1975. The Commission wanted its members to get it ratified and it had prepared a patent protection on biological inventions and legal protection.

(iii) Taxation

In the Community there had been several national laws on taxation which were again characterised by the lack of coordination between different tax authorities. This was due to different tax treatment of the partner companies as well as subsidiaries. Therefore such tax differentiation between parent and subsidiaries taxation on managers and incidences of double taxation were some of the important obstacles of internal markets. In order to remove such multiplicity of taxation, the Commission intended to publish a White Paper on the taxation of categories of the Community and the Community-wise harmonization of tax rules.

7. Application of Community Law

If the necessary infrastructure are not properly built-up for the creation of internal market then the entire political and legislative efforts are likely to be endangered. It has
increasingly been observed that some members are taking recourse to quantitative restrictions (QRs) as a tool of restraining imports. About 60 per cent of the total complaints (on an average 225 every year) are related to QRs. Due to lack of enforcement mechanism it only settles around 100 complaints every year.

3. Removal of Fiscal Barriers

The EC has been under customs union since 1968 which meant removal of customs tariffs among the member states. But this was not enough because EC already protected by exorbitant turnover tax. In 1967, all members unanimously decided that existing turnover tax would be replaced by the VAT and 1 per cent of VAT would be given to the Community for financing its activities through own source. The most urgent reform which is required in the fiscal area is the harmonization of the direct taxes including VAT. In its first move, Commission identified tobacco, alcoholic drinks and hydrocarbon oil are the products on which excise duties were levied. In case of tobacco, a limited degree of harmonization has already been over, and in alcoholic drinks and hydrocarbon oils little progress has been made so far in spite of clear directive.

(a) Commercial Traffic and Value Added Tax (VAT)

According to 14th VAT Directive the entire accounting procedures on VAT have been shifted from frontiers to the inland tax offices which is expected to be the first step for removing border control on the operation of commercial traffic. Since then now sales and purchase operations across the border have been treated similar to that of member states.

(b) Individual Traveler

Due to prevalence of differential structure in the member states it is an impossible task to check illegal transactions until harmonization of indirect tax is done. If a traveler buys a product from a country and sells it to another, then there is no mechanism to stop it. Therefore, it is suggested that "travelers' allowance" should be introduced enabling the genuine travelers to buy some dutiable products.

(c) Excises

The variation of excise is not so significant in case of individual travelers, but, certainly it matters in case of goods which are traded like "bonded house" because levies are not charged when the goods are kept in "bonded house" but when it is not routed
through such system levies are charged. The excise duty would not be charged until the goods were taken out of "bonds" in the country of destination. If frontier controls are dismantled then excised goods will be routed through a bonded warehouse in a low-rate country, taken out of "bond" there and shipped on for consumption in a high rate country. Thus removal of frontier control will require not only setting up a "clearing house" system of VAT but also approximations of excise duties.

(d) Approximations

Removal of border control and harmonization of tax structure would help to eliminate the variation of tax rates. In case of the USA, the variation is about 5 per cent which could easily be accommodated. It is estimated to be around + or -2.5 per cent in case of the EC. But in case of VAT, the Community would provide sufficient flexibilities. If the standard rate is 16.5 per cent then the actual rate for member states would be at the range of 14 to 19 per cent which was supposed to be imposed by the six of the nine members those who introduced VAT in 1985. In 1982, the average share of EC’s VAT was 7.05 per cent of GDP which was 3.63 per cent for excise of all commodities and 3.37 per cent for tobacco products including bear, wine, spirit and mineral products. But weighted average of EC’s VAT and excises was 10.68 per cent of GDP in 1982.

(e) Value Added Tax

EC’s VAT has mainly three interlocking issues, viz.

- the common base or coverage,
- the number of rates, and
- the level of rates particularly the mean or standard rate.

Regarding common base, the Second VAT Directive laid down main principles and Sixth VAT Directive went a long way to fulfill the necessary details of a common VAT base in the EC. In spite of that, areas of differences were in food, second hand goods, fuel and transport and the treatment of small trades and firms. As regards rates, seven out of nine member states imposed VAT at a reduced rate in addition to the standard rate and three of them imposed higher rates. But regarding level of rates six out of nine states adopted VAT approximations range of 14 per cent to 19.8 per cent for the standard rate (i.e.+ or -2.5 per cent). A range of 15 to 20 per cent (a norm of 17.5 per cent + or - 2.5 per cent) was for five members states out of nine.
(ii) Excises

According to Commission's observation, member states had common coverage in excise duties in case of manufactured tobacco, alcoholic beverage and hydrocarbon oils. The rate of taxation varied from 0.28 ECUs per packet of 20 cigarettes (Greece) to 1.96 ECUs (Denmark). The most important feature was that for bear, wine and spirit highest rate of taxation was found in Denmark, Ireland and the UK. Excise duties were disproportionately high to the retail price (up to 69 per cent for cigarettes, 52 per cent for petrol) and these were bound to affect the market rate.

As a part of the completion of internal market, the Commission proposed to rationalise VAT and excises. Regarding value added tax, Commission emphasised on common base. They covered subjects like works of art, antiques, used goods and the import of second hand goods by final consumers. Regarding approximations of excise rates, following proposals were made:

- the rate structure whether the common VAT system should be one or two or have more rates, and
- the target rate(s) together with the permitted ranges of variation around them.

SECTION-III

CECCHINI REPORT ON THE “COST OF NON-EUROPE”

The entire study was carried out in five countries, viz. Belgium, France, Germany, Italy and the UK. The rationale behind selecting only five countries in the EC was that the value of transactions, carried out by these countries was more than 80 per cent of the total value.

Though the EC has been in the customs union since 1968, yet there exist labyrinthine non-tariff barriers within the Community which restrict free movement of goods and services. Existence of such barriers is a major constraint to completing the internal market. In order to estimate the probable cost of these barriers and cost saved after the removal of these identified barriers, European Commission appointed a committee under the Chairmanship of Mr. P. Cecchini, then Vice-President of the European Commission in 1986 (39). Mr. Paulo Cecchini was the head of a project initiated by the Commission whose objective was to evaluate the economic impact of completing internal market by 1992 and was asked to submit final report by 1988.

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39. Commission of the European Communities, The Costs of Non-Europe Vol.1, (Brussels, 1987), This Report was prepared by a Committee chaired by Mr. P. Cecchini, Vice-President of the European Commission : The Report is Known after his name i.e., Cecchini Report.
Other members of the Committee were:

1. External Members:

2. Commission of European Communities:
   (i) Director-General of Economic and Financial Affairs: Michael Emerson, Michael Catinat, Alexis Jacquemin, Michael Anjean, Phillippe Goybet.
   (ii) Director-General for the Internal Market and Industrial Affairs: Micheal Loy (Coordinator), Michael Ayral, Jean-Francois Marchipont.

The Committee broadly covered sixteen broad product areas and had shown the tentative cost reduction and change in other macroeconomic variables after the elimination of controls restricting free movement of intra-Community trade. He estimated the "Cost of Non-Europe" in the following areas:

- Border related controls and administrative formalities
- Road haulage sector
- Public sector procurement
- Case study of technical barriers in six-industries
- Obstacles to transborder business activities
- Business services
- Financial services
- Benefits of competing the internal market for telecommunication equipment in the EC
- Automobile industry
- Food staff industry
- Textiles and clothing industry
- Pharmaceutical industry, etc.

The quantitative findings of Cecchini Report are shown in Tables 2.1 to 2.4. While estimating economic benefits the study mentions that total gains will be around 200 bn ECUs, responding an annual growth of GDP of around 5 per cent. European prices are expected to decline by 6 per cent, and this change will generate 2 to 5 mn. additional jobs.

Table : 2.1

Estimate of the total economic gains from completing the internal market, according to partial equilibrium estimation method (EUR 7, based on benchmark data for 1985 = 100)

<table>
<thead>
<tr>
<th>Stages</th>
<th>Variants</th>
<th>billion ECUs</th>
<th>% GDP</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>A</td>
<td>B</td>
</tr>
<tr>
<td>Stage - 1 :</td>
<td></td>
<td>8</td>
<td>9</td>
</tr>
<tr>
<td>Cost of barriers affecting trade only</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Stage - 2 :</td>
<td></td>
<td>57</td>
<td>71</td>
</tr>
<tr>
<td>Cost of barriers affecting all products</td>
<td></td>
<td>65</td>
<td>80</td>
</tr>
<tr>
<td>Total direct cost of barriers</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Stage - 3 :</td>
<td></td>
<td>60</td>
<td>61</td>
</tr>
<tr>
<td>Economies of scale from restructuring and increased production</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Stage - 4 :</td>
<td></td>
<td>46</td>
<td>46</td>
</tr>
<tr>
<td>Competition effects on X-inefficiency and and monopoly rents</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total market integration effects :</td>
<td></td>
<td>106</td>
<td>107</td>
</tr>
<tr>
<td>Variant - I</td>
<td></td>
<td>(sum of stages 3 &amp; 4 above) (b)</td>
<td></td>
</tr>
<tr>
<td>Variant - II</td>
<td></td>
<td>(alternative measures for stages 3 &amp; 4) (c)</td>
<td>62</td>
</tr>
<tr>
<td>Total of costs of barriers and market integration effects :</td>
<td></td>
<td>171</td>
<td>187</td>
</tr>
<tr>
<td>Variant I = (a) + (b)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Variant II = (a) + (c)</td>
<td></td>
<td>127</td>
<td>142</td>
</tr>
</tbody>
</table>

Notes : Variants A and B relate to the use of alternative primary source of information introduced in the calculation of stage 1 and 2. Variants I and II relate to different approaches to evaluating competitiveness when the total figures, ranging from 127 to 187 billion ECUs for seven Member States at 1985 prices are scaled to represent the same GDP share for the 12 Member States in 1988 prices, the range becomes 173 to 257 billion ECUs.

Table : 2.2
Macroeconomic Consequences of the internal market: Community as a whole in
the medium term

<table>
<thead>
<tr>
<th>Relative Change</th>
<th>Frontier control</th>
<th>Public Procurement</th>
<th>Financial Services</th>
<th>Supply Effects</th>
<th>Total Average</th>
<th>Range</th>
</tr>
</thead>
<tbody>
<tr>
<td>As % of GDP</td>
<td>0.4</td>
<td>0.5</td>
<td>1.5</td>
<td>2.1</td>
<td>4.5</td>
<td>(3.2 to 5.7)</td>
</tr>
<tr>
<td>Consumer prices</td>
<td>-1.0</td>
<td>-1.4</td>
<td>-1.4</td>
<td>-2.3</td>
<td>-6.1</td>
<td>(-4.5 to -7.7)</td>
</tr>
</tbody>
</table>

Absolute Change

<table>
<thead>
<tr>
<th>Employment (X 1000)</th>
<th>200</th>
<th>350</th>
<th>400</th>
<th>850</th>
<th>1800</th>
<th>(1300 to 2300)</th>
</tr>
</thead>
<tbody>
<tr>
<td>General government borrowing requirement as a % of GDP</td>
<td>0.2</td>
<td>0.3</td>
<td>1.1</td>
<td>0.6</td>
<td>2.2</td>
<td>(1.5 to 3.0)</td>
</tr>
</tbody>
</table>


Table : 2.3
Potential consequences of the Internal market for the Community in
the medium/long term

<table>
<thead>
<tr>
<th>Micro economic approach</th>
<th>Welfare gain as % of GDP</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>4.5 to 6.5%</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Macro economic approach</th>
<th>GDP as %</th>
<th>Prices as %</th>
<th>Employment in million</th>
<th>Public balance as % point of GDP</th>
<th>External balance as % point of GDP</th>
</tr>
</thead>
<tbody>
<tr>
<td>Without accompanying economic measures (1)</td>
<td>4.5</td>
<td>-6.0</td>
<td>1.75</td>
<td>2.25</td>
<td>1.00</td>
</tr>
<tr>
<td>With accompanying economic measures (1)</td>
<td>7.0</td>
<td>-4.5</td>
<td>5.00</td>
<td>0.5</td>
<td>-0.25</td>
</tr>
</tbody>
</table>

(1) Margin of error ± 30%

Table 2.4

Estimates of costs of barriers based on sectoral studies or working hypothesis

I. Cost of specific types of barriers

<table>
<thead>
<tr>
<th>Description</th>
<th>bn. ECUs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Custom formalities</td>
<td>8 - 9</td>
</tr>
<tr>
<td>(1.7 to 1.9% of intra-community trade flows)</td>
<td></td>
</tr>
<tr>
<td>2. Public procurement</td>
<td>21</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>29 - 30</td>
</tr>
</tbody>
</table>

II. Cost of barriers in specific industries

<table>
<thead>
<tr>
<th>Description</th>
<th>bn. ECUs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Food (0.75 to 1.5% turnover)</td>
<td>0.5 - 1.0</td>
</tr>
<tr>
<td>2. Pharmaceuticals (1 to 2% turnover)</td>
<td>0.3 - 0.6</td>
</tr>
<tr>
<td>3. Automobiles (5% of turnover)</td>
<td>2.6</td>
</tr>
<tr>
<td>4. Textiles and clothing (0.5 to 1% of turnover)</td>
<td>0.7 - 1.3</td>
</tr>
<tr>
<td>5. Building materials (1.75% of turnover)</td>
<td>2.8</td>
</tr>
<tr>
<td>6. Telecommunication (equipment) (10 to 20% of turnover)</td>
<td>3.0 - 4.8</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>9.1 - 13.1</td>
</tr>
</tbody>
</table>

III. Cost of barriers in specific Service sectors

<table>
<thead>
<tr>
<th>Description</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Financial services (10% of turnover)</td>
<td>22.0</td>
</tr>
<tr>
<td>2. Business services (3% of turnover)</td>
<td>3.3</td>
</tr>
<tr>
<td>3. Road transport (5% of turnover)</td>
<td>5.0</td>
</tr>
<tr>
<td>4. Air transport (10% of turnover)</td>
<td>3.0</td>
</tr>
<tr>
<td>5. Telecommunication (services)</td>
<td>6.0</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>38.3</td>
</tr>
</tbody>
</table>

Source: Commission of the European Communities, *Cost of Non-Europe*, European Commission (Several Volumes, i.e., 1-16), Brussels, 1988.

Notes: The table reveals the result of special studies undertaken by the consultants except the transport case which rely on earlier published sources. Working hypothesis have also been adopted, for the purpose of the partial equilibrium calculation below:

for cost of price reduction for agriculture (0 to 5%) and energy (2%). Addins' categories I and II would imply double counting, since some but not all the costs of customs formalities and government procurement are covered under branches in
The quantitative results of the report which have been depicted in Tables 2.1 to 2.4 are more optimistic. In reality this may not be achievable. But the positive aspects of such estimation is the identification of strengths and weakness of the European industries and to restructure them according to emerging global competition. So far only big industries were expected to enjoy the fruits of EC-92, but the credit of the Report lies on the fact that due to identification of potential areas, small and medium industries will also equip themselves to face the competition emerged from the members themselves after the completion of the SEM. Cecchini Report is certainly not very ambitious but it confirms and crystalises expectations of the Europeans. The success of results depends on fulfillment of some conditions, viz, (i) all measures proposed by the Commission must be adopted and implemented, and (ii) the national governments of the various member states must pursue orthodox and mutually compatible economic, social and financial policies.

It is true that after customs union tariffs and quantitative restrictions on trade have largely reduced in the Community. But in spite of that fact, there have been other barriers which restrict the movements of goods, services, capital and labour.

These can be broadly defined as:

(i) differences in technical regulations between countries which impose extra cost on intra-EC trade.

(ii) delays at frontiers for customs purposes and related administrative burdens for companies and public administrations which impose further costs on trade.

(iii) restrictions in competition for public purchases through excluding bids from other Community suppliers which often result in excessively high cost of purchase.

(iv) restrictions on freedom to engage in certain services transactions, or to become established in certain service activities in other Community countries. This concerns particularly financial and transport services where the cost of market entry barriers also appears to be substantial.

In economic terms, the barriers can be grouped as:

- tariffs
- quantitative restrictions
- cost-increasing barriers
- market entry restrictions
- market distorting subsidies and practices

The estimation of the cost of non-Europe is very approximate in nature in the sense that the success of newly adopted measures depends on the interaction of several complicated economic and non-economic factors in majority of the cases which may not be. It also depends on better coordination of policies across the members disregarding their difference in political and economic parameters. While estimating the cost of "cost of non-Europe" CECCHINI Report finds:

(i) the direct costs of frontier formalities and associated administrative costs for the private and public sector may be of the order of 1.8 per cent of the value of goods traded within the Community or around 9 billion ECU at 1985 prices.

(ii) It is estimated that total cost of identifiable barriers affecting industry in the internal market is about 40 billion ECU or 3.5 per cent of industrial value added.

(iii) Some studies show that removal of existing barriers would result in cost reduction of 1 to 2 per cent for food and beverages industry, construction materials, pharmaceuticals and textiles and clothing. It is 5 per cent for automobiles.

(iv) Savings would be enormous if the restrictions on market entry are removed from service sector branches. After removing the barriers, the gain in the area of public sector procurement alone could be 20 billion ECU. For financial services also a range around 20 billion ECU in potential savings has been estimated.


45. Ibid n. 44 p. 3-5.
Taking note of the present industrial structure with a more rationalized but still less than optimal one, it is estimated that about one-third of European industries could profit from varying cost reductions of between 1 to 7 per cent yielding an aggregate cost-saving of the order of 60 billion ECU.

Encouraging competition among member states results reduction in X-efficiency. Such inefficiency can be minimised by proper allocation of resources i.e. human, physical and financial. Weak competition causes X-inefficiency. The cost of X-inefficiency may often be as great as those resulting from unexpected economies of scale. The total effect of moving to a competitive integrated market, with fuller achievement of potential economies of scale and reduction of X-inefficiency may be twice to three times the direct cost of identified barriers in the situation.

After removing all barriers, the estimated gains range starting with around 70 billion ECU or 2.5 per cent of the GDP. This is rather a constructive estimate of the benefit, but markets become more competitive and integrated than the potential benefit which may be around 125 to 190 billion ECU i.e. 4.5 to 6.5 per cent of GDP.

The gains discussed above need not be in the short-term in nature. In normal cases a) it may take five or possibly more years for the larger part of the effects to be realised, and b) in any event it is assumed that micro and macro economic policy would ensure that the resources released as costs are reduced, are effectively re-employed. The effects of internal market programme can be grouped under four major categories, each having a different type of macro economic impact, a) the removal of customs delays and costs, b) the opening of public markets to competition, c) more general supply side effects, reflecting changes in the strategic behaviour of enterprises in a new competitive environment, d) the liberalisation and integration of financial markets.

Pursuing a relatively passive macroeconomic policy, it is unlikely to achieve perceptible results at least in the short run, though there would be some manifestation in the earlier

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46. Ibid n. 41 p. 18.
49. Ibid n. 41 p. 19.
years. Most of the desired results showing impact of the removal of barriers will start coming from medium-run i.e. after 5 to 6 years of the integration. It is estimated that after this period GDP will grow by 4.5 per cent while the magnitude of price decline would be around -6 per cent. On employment the impact is slightly negative in the initial years, but in the medium-term it is expected that about 2 mn new jobs (nearly 2 per cent of the initial employment level) may be created. As an aftermath of SEM, budget balance is likely to increase significantly and the current account balance of payment may improve remarkably. Removal of barriers results in improvement of all macroeconomic variables\(^{50}\).

The above phenomenon is in case of passive macro-economic scenario, but after this phase if we follow active macro economic policies by improving monetary and financial equilibrium, then certainly one can set growth on a higher trajectory. This is possible by adjusting macro economic variables like inflation, budget or balance of payment deficit. In the medium-term if all these macro economic variables are set together and work properly, it is expected that this will yield 2.5 per cent more GDP in addition to 4.5 per cent which means GDP would increase by a spectacular rate of 7 per cent. There is an apprehension that increase in income would lead to higher inflation, but in our model economic growth this remains well-below; the projected level due to successful implementation of the internal market programme by making the budget balance and BOP situation remains at a sustainable level\(^{51}\).

Synthesising the macro and micro economic policies, we can say all the quantitative estimates presented above are approximate and based on certain assumptions. The estimates have been assembled in an eclectic manner. The estimates have been worked out through various macro and micro economic methodologies to produce desired results. Different approaches coverage together and suggest consistent results. It is not a trivial job to calculate the exact magnitude of the potential gain of the competitive integration.

The above estimates are based on the static framework where we have ignored some important categories of dynamic impacts on economic performance. Especially three important dynamic factors are very important in this connection.

\(^{50}\) Ibid n. 41 p. 19.

\(^{51}\) Ibid n. 41 p. 19.
First: Role of technological change has been ignored here. Better competitive condition offers more technological innovation that can only be absorbed if there is scale economy. Only united market can guarantee such conditions.

Second: There is evidence in fast growing high technology industries of dynamic or learning economies of scale, whereby costs decline as the total accumulated production of certain goods and services increases. Market segmentation highly limits such benefits and damages performance of high technology industries.

Third: The business strategies of European enterprises are likely to be affected in the event of a rapid and extensive implementation of the internal market programme, full integration of the internal market will foster the emergence of truly European companies who can face the global challenge of intense competition.

Regarding macroeconomic policies, in order to be truly competitive in the international market first condition should be the frontiers must be truly open to the extent that economic agents should easily be able to engage in arbitrage between national market to profit from the price differentials across the border. Second condition the basic pillar of the successful competition policy is to do away with the public subsidies. When any cooperation becomes truly international and operates across the border, then its competition policies would be based on its own economic competence without any government support through subsidies. In short run it may be feasible but in the medium-run competitive policy should be purely judged on the free market criteria. Third condition of competitiveness relates to the opening up of the external market. At present price discrimination among different markets is the common practice of a private enterprise. Competition policy should be based on the commercial antitrust without creating any burden to the consumers. Commercial dominance is the common practice where the market is regulated by suppliers. Competition policy for the market to be fully integrated, should be guided by the principle that if prices of inputs are cheaper then imports should not be restricted on any grounds.

On macroeconomic front, the main objective of the demand management policy is to follow non-inflationary growth at best in the medium-run. It is also conceptually true

52. Ibid n. 41.
53. Ibid n. 41 p. 20.
that successful implementation of the internal market programme will put downward pressure to the cost and prices which leads more production employment and income with price stability. The more competition, markets will be more free and open and prices will be determined by the buyers not sellers. In the buyer market price is always non-inflationary provided that there is adequate supply in the market\(^{54}\).

One of the important drawbacks of the CECCHINI Report is that it always gives community wise averages. It does not take into account the different socio-economic regime of the members states which are not at all equal. This implies even after the implementation of the internal market programme there is every probability that there will be skewed distribution of the benefits among the members. Relatively richer members will be more beneficial than smaller one. Smaller members have already expressed their apprehension of the effect of market integration into their economies. They opine that removal of national frontiers may lead to more mergers and acquisitions and gradually uncompetitive domestic industries will be wiped out. This will aggravate economic problems of weaker members. Business activities will be entirely governed by the profit criteria. Extensive competition generates more profit which attracts more foreign companies to operate whether they are EC-based or not. The most dynamic and competitive business and economies will derive the greatest gain from the 1992 Programme\(^{55}\).

Another drawback of the CECCHINI Report is that while estimating the costs of non-Europe, it does not take into account the world and European business cycle. The implementation of SEM can not be successful if we ignore the reality. As a matter of fact, early 1988 exhibited weakening of world as well as European business cycle. As a result, European exchange rates were higher than US dollar and currencies linked to it. Taking advantage of such situation some international competitors garnered strategic gains in their share of weakening European market. In order to counter this situation, European industries should have sufficient safeguards which are: i) support of the European business cycle, sufficient to counter its weakening in the short run in favour of accelerated growth thereafter b) endeavors to assume that international exchange rate adjustment are adequate but not excessive\(^{56}\).

54. Ibid n. 41 p. 21.

55. Willy de Clercq and Leo Verhoef, Ibid n. 41 p. 41.

56. Ibid n. p. 21.
The study supports following conclusions:

(i) Presently European industries are in a state of segmentation and weak competition in many markets which means it has greater potentialities of rationalising production and distribution structures leading to improvement in productivity and reduction in costs and prices.

(ii) If the SEM is properly implemented in both community as well as member states, then certainly it has a very positive impact on their economic performance. Improvement in economic performance includes non-inflationary growth in employment and output, price stability and sound fiscal, monetary and balance of payment position.

(iii) In order to tap maximum benefits from the market integration all important features of the internal market programme would need to be implemented with sufficient speed and conviction.

(iv) In order to achieve higher growth trajectory through internal market integration more than full implementation of the White Paper is required. There must be a strong competition policy making the supply potential of the Community economy more flexible. Demand side management policies should be fully consistent with the competition policy so as to ensure the price stability and economic growth.

SECTION IV

THE SINGLE EUROPEAN ACT: REMOVAL OF NTBs AND CREATION OF SINGLE EUROPEAN MARKET (SEM)

All members of the EC have reached a consensus for removing all internal barriers restraining smooth flow of goods, services, capital and human resources between the members. These barriers are erected on the ground of economic health of the individual countries consistent with their national priorities. The existence of internal barriers are quite antagonist to the idea of common market.

Being worried about such divergent national laws and the plethora of internal barriers the Commission enacted Single European Act (SEA) to deal with the Single European Market. The basic objective of the SEA was to harmonize the national laws and to enforce uniform system throughout the member states. The SEA also emphasised the removal of tariffs and non-tariff barriers. Tariff barriers between the EC members were transparent. The removal of these barriers was an integral part of the overall measures undertaken for the completion of internal market.

The White Paper had fixed up time table for the removal of barriers in a phased manner. The probable areas of actions were as follows:

(i) The removal of non-tariff barriers prevailing in the member states in the form of custom posts immigration and passport controls, the harmonization of public health standards, the abolition of national transport controls and the approximation of arms and drugs legislation.

(ii) The White Paper has also proposed the removal of all technical barriers to trade between member states and provision for free movement of goods and harmonization of technical standards.

(iii) The Report also envisages the liberalisation of capital movement within the territory of the Community, common provision of industrial and intellectual property. Finally it had strongly recommended the harmonisation of indirect taxation (VAT and excise duties) and national regulations concerning the completion of internal market.

The White Paper had given a broad outline of the removal of non-tariff barriers. Prior to the setting of the Cockfield Commission, only customs tariffs were considered to be the most effective barriers to the completion of internal market. This was due to the variation of national laws for setting up customs tariff limit. But afterwards it was found that apart from tariff barriers, there have been innumerable non-tariff barriers which are more active in distorting the prospect of the Single European Market. Over the years


through several tariff reduction measures, tariff rates have been declined to a considerable extent but, on the other hand, due to labyrinthine of NTBs, inter-state transaction of goods and services are severely affected.

The Commission had basically proposed two types of reforms tailored for SEM:

(i) the rate structure, i.e. whether the common VAT system has one; two or even more rates, and

(ii) the target rates together with the permitted ranges of variation around them.

In the earlier sections of this Chapter we have discussed in details about the existing NTBs in the EC, its nature and dimension, and the Commission's step to remove these barriers. It will be meaningless to discuss in detail about them in this section, but we will present the probable timetable for phasing out of the mentioned NTBs as proposed by the Cockfield Report.

Review of the Progress of the Single European Market.

While reviewing the progress of the single market up to now, we can divide the entire gamut of the operation in six major areas. These are:

(i) completing and streamlining the legislative framework of the single market.

(ii) making the single market work

(iii) confirming the single market as the cornerstone of economic and monetary union

(iv) securing single market for the citizen.

(v) adapting the single market to technological and other changes, and

(vi) preparing the single market for enlargement.

As regards legislative framework for the completion of the single market, all measures are yet to be adopted. An estimation done by Mr. Ciampi, Chairman of the Competitiveness Advisory group shows that due to non-implementation of the European company statute, the loss incurred by the European business is around 30 billion ECU's a year:


61. Ibid n. 60 p. 4.
The incidence of double taxation is still there. Due to differential fiscal regime among the member states, European are yet to get the product at competitive rates. The rejection in March 1995 by the Parliament of the draft directive on the protection of biotechnological inventions means that European industry is still a significant competitive disadvantage.

Control of free movement of people across the border remains to be one of the major irritant factors of the completion of single market. On 14 June 1985, the Commission approved its White Paper on completing the internal market. Among other aspects White Paper also recommended the elimination of control at internal border. This recommendation was subsequently incorporated into Article 8a (now Article 7a) of the EC Treaty by the Single European Act.

The basic objective of the single European market was to dismantle all barriers for the movement of goods, services, capital and labour. But the member states are failure to come to a consensus on a common policy permitting free movement of persons across the border. This is due to:

— stubborn attitude of UK, Ireland and Denmark.
— inability to check drug trafficking across the border.

Considering the need of universal policy in controlling the movement of personnel across the border, the five states signed the Agreement on 14 June 1985 in Luxembourg city of Schengen. The Schengen agreement came into force from the date of its signature (i.e., 14 June 1985). Actually Schengen Agreement originated from the Saarbrucken signed between France and Germany on 13 July 1984. The State of Benelux (Belgium, the Netherlands and Luxembourg) were later associated with the initiative. The Schengen Agreement was followed

by the signature of its complementary convention on 19 June 1990 when Italy, Greece, Spain and Portugal have joined the Agreement. Austria asked for its membership on 6 March 1995. Sweden and Finland do not exclude themselves from joining the Schengen Club in the long run provided that Scandinavian Agreement on passports can be respected. U.K. Denmark and Ireland remained outside of the agreement but this did not pose any problem because Schengen Agreement were concluded outside the framework of the European Union. Consequently, these Agreements are part of international law and not European law.

Schengen Agreement does not discriminate between members and non-members once any one enters into the national frontier. It grants common visa which may he was one day to three months, then it is decided by the immigration policy of the national governments. Seven member States have committed themselves to implementing the Schengen Agreement irreversibly with effect from 26 March 1995.

Though free movement of personnel among the member states is still a controversial one, yet in July 1995, the Commission prescribed three proposals to eliminate restrictions on controls on the clearly stated condition that they would enter into force only when the essential security measures have been implemented. The Council also adopted two regulators relating to the free movement of people. The first one is the introduction of model type of visa ( Regulation (EC) No. 1683/95 ) and second one is the preparation of a list of third countries whose nationals must have a visa to enter Community territory ( Regulation (EC) No.2317/95 ).

**Competition policy** is another major area where much action is yet to be initiated to complete the single market. In telecommunication sector, the deadline of 1998 remains as the date by which full liberalisation will have to be achieved, while the use of alternative infrastructures for liberalized services will be allowed in two years earlier. Acceleration in the pace of liberalisation in the telcom sector may pave the way for setting up European Information Society in 1995.

64. Ibid n. 62 p. 1.
55. These Several States are: Belgium, Luxemburg, Netherlands, France, Germany, Spain and Portugal.
Divergency in national legislations is still a deterrent factor for the successful implementation of single market. Community policy makers have been making considerable efforts to harmonize the national rules. It is a cause of concern that in 1995 itself 438 proposals for technical legislation at national level were notified to the Commission. Simultaneously unification proposals involving the repeal of about 350 instruments were before the Council and Parliament by the end of 1995.

Among the major achievements in 1995 was the proposal by the Commission of the Customs 2000 Action programme to modernise customs administration. The Council responded positively to the Commissioners request. In spite of this the Council recently agreed to a new notification system for national measures to come into effect in 1997, strengthening the instruments available for tackling illegal restrictions in framework of goods across the frontiers. As a result the number of complaints about such measures increased from 202 in 1994 to 259 in 1995.

Efforts to harmonize national laws and then to enact them into the Community laws has been going on steady in 1995. During this period the member states had adopted 93.4 per cent of the national measures required to implement the Community's single market legislation. Extent varies among the states. Denmark, Netherlands, Spain and Sweden are substantially above the Community average of 93.4 per cent, while Greece, Germany and Austria are substantially below. Implementation of agreed Community law remained seriously below the desired level in some key areas which was the major cause of concern for the Community in 1995.

Formation of the European Monetary and Economic Union is still a distant prospect as there exist considerable amount of divergencies among the member states regarding the modalities of the Union. Though there remains ambiguity, but the Commission is going ahead with the target of monetary union by 1999. Major bottleneck of monetary union are the wide fluctuation of currencies of these states in recent years. In October 1995, the Commission firmly rejected demands for compensatory measures that would imply new barriers to trade.

As regards technological and other changes, the vision of the Community is very dynamic. The Commission is determined to do away with the regulatory environment for inviting more technological progress. Through several legislative enactments Commission makes
much progress in protecting intellectual properties. In July 1995, the Council and the European parliament adopted a directive on the protection of individuals with regard to the processing of personal data and on the free movement of such data. The Council also reached a common position on the proposal for a directive on the legal protection of data bases. In 1995, the Commission has produced Green Papers and carried out extensive consultations among the members as how to protect copyrights and related rights in the information society as well as the protection of pluralism in the media\(^{66}\).

SECTION V

MAJOR OBSTACLES TO THE FORMATION OF SINGLE MARKET : MONETARY AND POLITICAL UNION

In order to establish the economic and monetary union, it was essential to amend the Treaty of Rome. Article 236 of the Treaty of Rome laid down the provisions for an Internal Conference of the representatives of the member state governments to amend the original treaty catering to the formation of economic and monetary union. Single European Market (SEM) was to be shaped up by 1992 with the objectives of setting up a Single market. Success of SEM depends on the implementation of the provisions relative to setting up monetary and political union\(^{67}\).

Through the establishment of SEM, it is now possible to enhance the mobility of goods, services, capital and human resources across the border, but yet there exist plethora of constraints to the successful operations of SEM\(^{68}\) especially in the are of free movement of persons across the border. Treaty on European Union was signed at Maastricht on 7 February 1992, which came into force on 1 November 1993 after being ratified by 12 Member States in accordance with their constitutional requirements. The basis of the formation of the European Union were:


68. Movement of persons is still restricted due to drug trafficking across the border, hence seven countries of the European Community have concluded Shengen Agreement. This agreement introduces a common Visa Policy of the agreed members which enables free-movement of personnel within the countries covered by the Agreement.
While forming European Community through Treaty on European Union (Maastricht Treaty), much emphasis was given on the issue of "economic and monetary union". On 27 and 28 October 1990, the European Council met at Rome where 11 members states gave their nod to go ahead with the second phase of economic and monetary union which was slated to start on 1 January 1994. In the Intergovernmental Conference of Economic and Political Union in Dublin, in June 1990, the Heads of the States decided to convene another conference on the issue of political union which would deal with political and institutional reinforcement of the Community. As a result of such decision two Intergovernmental Conferences on Political Union and Economic and Monetary union were formally opened in Rome on 15 December 1990. On 9 and 10 December 1991, the Heads of the States reached agreement on a Draft Treaty at Maastricht incorporating the results of the draft Intergovernmental Conferences. As a result of that draft treaty, Treaty of Maastricht was signed on 7 February 1992.

Single European Market does not entail only the free movement of goods, services, capital and labour across the border but it also sets the target of the harmonization of policies relating to European monetary and economic policies, which are *sine qua non* for pursuing a unified policy framework for economic, monetary and political aspects. In terms of importance and feasibility, political union comes last, but its actualisation depends on the success of harmonized European monetary and economic policies to be materialized through single currency and single rate of exchange amongst the member states.

Monetary and Political Union are two important ingredients of the European Single Market. Monetary Union implies single representative currency pegged with the several national currencies of the member states. One has to fulfill three criteria before getting enlisted as a member of the Monetary Union:

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Peg the inflation rate at 2.25 per cent per annum, maintain a consistent level of budget deficit, and liberalization of financial and capital market.

A complete Monetary Union is still at a nascent stage. Stage-II started from January'93 which implied that completion of internal market programme through the reduction of margins by 1 per cent except for Greece and Portugal. Quantification of the impact of Monetary and Economic Union is not feasible at this moment though the programme of Economic Union has achieved some success, but Monetary Union is still at the nascent stage.

**Definition of Monetary Union**

Monetary Union is recognized as either irrevocable fixed exchange rates or a single currency; a single monetary policy is the central characteristic of this regime. The single currency is clearly the first best in terms of the economic benefit/cost ratio. Economic Union would see a much lesser concentration of policy competence than Monetary Union. In order to achieve success in completing economic and Monetary Union among the members of the Community, it requires the EC to have common economic objectives and a close coordination between the economic policies and the policies related to monetary operations of the EC. Budgetary policy at national and EC levels is also likely to be uniform and should actively support the speedier implementation of Economic and Monetary Union.

**Current Position of Economic and Monetary Union**

According to the recommendations of the Delors Report in 1988\(^{(71)}\), Stage-I of Monetary and Economic Union started on 1 July 1990. The principal steps in Stage-I were as below:

**For Economic Union**

(i) removal of physical, fiscal and technical barriers within the Community, in line with the programme for completing the internal market by the end of 1992;

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(ii) increased mobilisation of resources, and improved machinery for the accumulation of Structural Fund in order to promote regional development and/or correct regional imbalances, this is a part of the overall policy regime required for generating resources that are needed for regional development through structural fund and this was agreed to in 1988; and

(iii) strengthening economic and fiscal policy coordination. This was the aim of new convergence arrangements adopted in March 1990 based on multilateral surveillance.

For Monetary Union:

(i) complete freedom in the movement of capital which is already in vogue in some member states, the existing system should be modified and to be made as comprehensive as possible;

(ii) elimination of all barriers to financial integration of the Community which means complete liberalization of banking, financial and insurance services across the border;

(iii) effective participation of all member states in European Monetary System (EMS);

(iv) removal of all obstacles to private use of ECU$; and

(v) strengthening machinery for active coordination of decisions on monetary and exchange rate policies.

In case of Monetary Union, the European Commission, European Parliament and the European Council are unanimous on a single common currency, i.e. ECU$. The single monetary policy along with the single currency (i.e. monetary unit) will be managed by a new institution like the European System of Central Bank (ESCB), which has the following characteristics:

(i) the main objective was to maintain stability in prices;

(ii) it would be the federal structure with central decision making system;

(iii) it was thought to be independent of national governments and Community authorities;

(iv) it would be democratically accountable.

Cost and Benefits of Monetary Union

(i) **Efficiency & Growth**: Volatility of exchange rates, higher degree of uncertainty, higher transaction cost and sluggishness in the progress in monetary and economic union are deterrent to economic growth and efficient production. Elimination of such odd factors would obviously strengthen the growth of investment and employment;

(ii) **Price Stability**: Though a mild fluctuation in prices is essential for sustaining growth in capitalist system because it provides initial incentive to productive forces, but, at the initial stage, price stability among the member states is *sine qua non* for Monetary Union. It is decided that upper limit of inflation would be around 2.25 per cent.

(iii) **Public Finance**: Maintaining a sound financial and budgetary discipline is the basic precondition for successful implementation of Monetary and Economic Union. Macro economic stability through maintaining a persistent low level of budgetary and fiscal deficit, reduction of interest rates, monitoring exchange rate regime and eliminating inflationary pressure and exchange rate premia are some of the factors conducive to Monetary Union.

(iv) **The International System**: After maintaining a reasonable degree of price stability and budgetary deficit, ECU will be an international currency like US dollar and yen of Japan. Presently ECU is a token currency and it is used as a unit of account. But the moment it is pegged with the national currencies at a fixed rate, it will be deemed as an international convertible currency to be acceptable to the business community for national as well as international transactions. Moreover, the monetary authorities will be able to economise scarce foreign exchange and achieve some international seigniorage gains.

(v) **Employment and Regional Balance**: The improved economic activity will augment investment and employment. But the potential cost of Economic and Monetary Union is the loss of the nominal exchange rate as an instrument for economic adjustment. In international transactions, nominal exchange rate will remain as an important tool

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for adjustment, but among the member states it is broadly abandoned. The urge for globalisation, competitiveness and Economic and Monetary Union will encourage some national level changes in the EC itself. Due to universal acceptability of EUROs, the current account constraints will disappear for the individual members even with some disturbances at the national (EC) level.

**European Monetary Union: A Proposed Timetable and Future Prospect**

The process of EMU has just started, but many things are yet to be achieved. Most important thing is that the agreement on EMU and Political Union must be unconditionally supported by all member states and should be ratified by their parliaments. All the member states met in Maastricht, the Netherlands, and pledged to unite themselves both economically and politically. But until now, all member states are not in a position to get it passed from their national assemblies through referendum. Surprisingly people of the Netherlands have rejected the Maastricht Treaty and the UK has not yet taken any decision to support it. Towards the European Monetary Union (EMU), four important issues are expected to emerge during the 1990s, viz:

(i) Institutional/legal issues in the negotiations of Treaty revisions in the Intergovernmental conferences and the subsequent ratification process.

(ii) Convergence in the monetary policy as specified in the Delors Report. This convergence among the member states will be completed after ensuring the price stability, fixation of exchange rates and maintaining sound fiscal policies.

(iii) All members are not equally sound in all macro-economic aspects especially inflation and public debt. This is true for Greece, Portugal, UK, Italy and Spain. Some adjustments are necessary to grapple with some abnormal situations.

(iv) Question of enlargement of the Community, incorporating ACP countries Yugoslavia, members of the EFTA countries and Central European countries is to be solved.

**Transition from Phase-I to Phase-II**

Stage I started on 1 July 1990 without citing any date for its completion. The first stage did not require any institutional arrangement. It was simply culmination of the *nodus operandi* of EMS. Most important transition was from Stage I to Stage II.
The first major step on EMU was taken on 1 January 1994, when European Monetary Institute (EMI) was set up to monitor the modalities of the completion of EMU. But till today its tasks remain non-transparent. But in spite of all odds, EMI is the first important step towards EMU. Differences in opinions among the member states to ratify the Maastricht Treaty for political Union and Monetary Union may be attributed as one of the major reasons in exorbitant delay for EMU. Ratification of Maastricht Treaty by all members is unlikely to happen near future. Most disappointing part is the rejection of referendum by the Dutch people, the UK till does not raise this issue to its parliament and France narrowly escapes the rejection which is true to almost all other states. Thus delay in ratification leaves both the Political and Monetary Union at an ambiguous state. Furthermore, it will be much exaggerating to contemplate that there will be sweeping of powers from the national levels to the EC in the immediate future. It is also unrealistic to expect that EC will be able to take complete charge of power from its members as they are willing to transfer so easily. This is so because no member state is in a mood to surrender its national sovereignty to the EC without much guarantee of reciprocal benefits to maintain national superiority. Coming out from the European Monetary System by the UK on the issue of interest rates is the burning example of this idea.

Two essential ingredients of the functioning of EMU are: (i) price stability, and (ii) budgetary position which are unlikely to be implemented by all member states. The UK and Spain were in a position to accept the fluctuation margins of + and -2.25 per cent by 1992. Spain and Ireland were ready to remove the capital control at the end of 1992. Despite these facts, there still exist so many other factors which are deterrent to the completion of EMU.

At the first stage, no substantial economic policy adjustment was needed for these member states which had been maintaining normal fluctuation margin. But in case of Italy, the UK and Spain substantial adjustment was needed before participating in Stage-II. Regarding convergence requirement, fact shows that Italy has to make a sustained effort to reduce its budgetary deficit for qualifying to enter into Stage-II. The same was true in case of Portugal and Greece, because until they make substantial improvement in their budget deficit they are unlikely to qualify for Stage-II.
Fixation of exchange rate is another precondition towards EMU, which was slated to be completed before 1 January 1994 (at the beginning of Stage-II). The institutional commitment to go well beyond the EMS towards a full EMU would provide a guarantee or at least a major assurance of stable nominal exchange rate for the future. Before taking major realignment, some fundamental differences are to be removed, that is over valuation of lira is to be checked and also the differences in national inflation rates.

Stage III: Collective Authority Over Monetary Policy

The main task of Stage III is to fix up exchange rates. This fixation will be made after getting detailed report from the European Commission regarding adequate convergence necessary for this purpose. The yardstick of the convergence will be less inflation, lower interest rates and soundness of budgetary policies. Greece is unlikely to make necessary adjustments due to its poor macro-economic conditions for early participation in Stage III. It is expected that European Commission will prepare this report by the end of 1996. Therefore, the most likely date for Stage III is early 1997. Meanwhile, it is reasonably expected that exchange rates and price movements will be established and European System of Central Bank (ESCB) will be created to take the entire charge of monetary policies of the member states who may like to participate in this programme. The European System of Central Bank will be entrusted with monitoring price stability independent of political interference. The European Monetary Union is understood to be completed after (i) exchange rates are fixed, and (ii) common currency replaces the national currencies.

From the entire analysis of this Chapter, we come into some conclusions. These are:

i) Europe is lagging behind USA and Japan in World Competitiveness Scoreboard

ii) In industrial Competitiveness, USA regains top portion after nine years, Japan slides down after nine years of supremacy and Europe continues to divert from the top position.

iii) The Cost of non-Europe is enormous as estimated by Paulo Cecchini in his Report. While estimating the cost of non-Europe, he had taken major industries of the European Community and through comparative static he had shown the enormous amount of Cost reduction after the full implementation of Single European Act for establishing the Single European Market.
iv) Single European Act provides the basis for removal of non-tariff barriers among the members. Since EC has been already under Customs Union since 1968, and has erected Common External Tariffs (CET) to non-bloc countries, it will extract enormous benefits after the removal of physical, fiscal and technical barriers.

v) Political Union among member states is a distant dream. Work towards establishing economics and monetary union is in progress. Though first phase of European monetary union (EMU) is over, in spite of the fact it is yet to achieve any remarkable success. European Commission has already fixed time table for the completion of EMU at the end of the century.

vi) Progress of monetary union has been stalled due to non-cooperation from relatively affluent states. Norway has rejected the referendum and UK has come out of the monetary union for its individual interest. This poses a serious threat in achieving monetary union by the turn of the century.