Implications of the Euro

A critical perspective from the left

Edited by Philip Whyman, Mark Baimbridge and Brian Burkitt

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Implications of the Euro

To date, critical analysis of the Economic and Monetary Union project has largely been advanced from the centre-right spectrum of British politics. Comparable questioning from the centre-left, whilst once a powerful phenomenon, has more recently failed to find a coherent voice. Yet the European fault-line cannot be characterised as a neat left–right issue. There are noticeable divisions in opinion across British business, the trade union movement and within the Labour Party.

Implications of the Euro offers a unique insight into this key debate from the 'centre-left', eurosceptic viewpoint. This book provides a rigorous analysis of the salient economic and political issues of concern, such as: the economics of a single currency, employment and social implications, in addition to issues of sovereignty and political determination. The arguments presented in this volume highlight the emergence of a coherent alternative to deepening economic integration as a platform to build a just and equitable society.

Contributions are drawn from leading academics, trade union leaders and prominent politicians, both from the Labour Party and the wider progressive left in British politics. This informative and thought provoking book will be indispensable reading for students and practitioners in economics, politics and international relations, as well as those interested in this highly contentious topic.

Philip Whyman is Reader in Economics at the University of Central Lancashire. **Mark Baimbridge** and **Brian Burkitt** are Senior Lecturers in Economics at the University of Bradford.

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Debating Britain's future
(*co-editor*)

Economic and Monetary Union in Europe
Theory, evidence and practice
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This book is dedicated by the editors to the memory of the Rt Hon Lord Shore of Stepney PC (1924–2001). Throughout British politics, whether his views were accepted or not, he commanded respect as a man of principle.

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Tony Benn is the son, grandson and father of MPs. The longest serving Labour MP in the history of the party, which he joined in 1942, he retired from the House of Commons in May 2001, after 50 years in Parliament, to 'devote more

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Janet Bush was until recently Director of New Europe. Following education at Somerville College, Oxford and the Centre for Journalism Studies, Cardiff, she joined Reuters in 1982 as a correspondent in Frankfurt (1983–4) and then joined the *Financial Times* in 1986 as deputy economics correspondent before becoming their New York correspondent (1987–90). In 1990 she joined BBC Television as a presenter of economic documentaries for BBC 2's *The Money Programme*. She joined *The Times* in 1992 as economics correspondent and was made economics editor in January 1997. In February 1999 she took a leave of absence from *The Times* to serve as Director of New Europe, the cross-party campaign against UK membership of the euro. Having launched 'No', a joint campaign between New Europe and Business for Sterling, she returned to *The Times* in August 2000 as economics editor and leader writer. In 2002 she was co-author of *In or Out? Labour and the Euro* (Fabian Society).

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Bryan Gould was a Rhodes Scholar attending Balliol College, Oxford. He served as Labour MP for Southampton Test (1974–9) and Dagenham (1983–94). He was a prominent member of Neil Kinnock's Shadow Cabinet, serving as Shadow Trade and Industry Secretary. He contested the 1992 Labour leadership election and subsequently formed the Full Employment Forum to promote Keynesian economic ideas within the labour market. He resigned from John Smith's Shadow Cabinet, in a dispute about Europe, and left British politics in July 1994. He returned to his native New Zealand and took on the role of Vice-Chancellor of the University of Waikato, where he served until his retirement in 2004. His books include *Goodbye to All That* (Macmillan, 1995), *Monetarism or Prosperity?* (Macmillan, 1981), *A Future for Socialism* (Jonathan Cape, 1989) and *Socialism and Freedom* (Macmillan, 1985). He is a committed anti-federalist and was a consistent critic of Labour's embrace of monetarism under Jim Callaghan and Dennis Healey.

Billy Hayes is General Secretary of the Communication Workers Union (CWU). Prior to this, he had spent nine years as the National Officer representing the union's outdoor postal members. He joined the Post Office, and the union, in 1974 and took on a number of local responsibilities, including magazine editor, TUC youth conference delegate, trades council nominee, union conference delegate and finally Branch Secretary. In 1992, four months after being voted onto the National Executive, he was elected a National Officer. Billy has been active in the Labour Party for many years and held a range of positions from Young Socialist secretary to GMC member. He supports the Labour government, but not unreservedly. 'There are issues where we cannot be afraid of criticising the government', he says, citing as examples index linking of pensions and the repeal of anti-trade union laws. Billy has always advocated less centralisation of union structures. 'We need to lecture less and hear more about the real impact of management's policies', he says. 'Stirring up apathy is not a solution.'

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David Owen trained as a doctor before becoming Labour MP for various Plymouth constituencies between 1966 and 1992. He was appointed Minister for the Navy (1968) before resigning from the Shadow Cabinet in 1972 over the Labour Party's refusal to support British entry to the EEC. Subsequently, he was appointed Minister of Health (1974) and Secretary for Foreign and Commonwealth Affairs (1977–9). In 1981 he was one of the founders of the Social Democratic Party, served as Deputy Leader (1982–3) and Party Leader (1983–7). The continuing SDP was re-established under his leadership in 1988, but was finally wound down as a national party in 1990. He was created a life peer in 1992. He went on to become joint author of the Vance–Owen Peace Plan to settle the conflict in Bosnia in the 1990s. He was until recently leader of the 'No Campaign' against British membership of the euro. His books include *Face the Future* (Cape, 1981), *A Future that will Work* (Penguin, 1987), *A United Kingdom* (Penguin, 1986), *Human Rights* (Cape, 1978), *In Sickness and in Health: The Politics of Medicine* (Quartet Books, 1976), *Negotiate and Survive* (CLV Publications, 1988), *Our NHS* (Pan, 1988) and *Politics of Defence* (Cape, 1972).

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Foreword

Rt Hon the Lord Owen

It is peculiar to Labour governments that they have been bedevilled by mistaken decisions over the handling of monetary policy. Ramsay Macdonald, as Prime Minister, and Philip Snowden, as Chancellor of the Exchequer, from 1929 to 1931, should have left the gold standard much earlier and devalued. Similarly, Hugh Dalton and Stafford Cripps as Chancellors of the Exchequer, in Clement Atlee's post-war government, were too slow to devalue. The delayed devaluation also damaged Harold Wilson's period as Prime Minister from 1964–70.

Fixed exchange rate controls have been one of the dominant issues of my 40 years in politics. I entered Parliament in the March 1966 General Election full of idealism and hope that a majority Labour government would end Britain's post-war economic decline. Yet by 20 July, in a mood of utter disillusionment in the House of Commons, we were told about a deflationary package which meant Labour was back in the same stop–go economic cycle which we had so often attacked the Conservatives for inflicting. The decision not to devalue after the 1964 General Election, something clearly envisaged by the outgoing Conservative Chancellor, Reginald Maulding, was politically understandable. In office after 13 years of opposition and facing the necessity of an early election since Labour only had a majority of five, it was quite widely felt that to devalue would be politically hazardous. But in 1966 with a large parliamentary majority there were no credible excuses. It was a lamentable failure of the government not to devalue in order to pursue economic growth. To oppose the government's refusal to devalue was to be labelled unpatriotic. Before the 1967 Labour Party Conference I and two other Labour MPs, John Mackintosh and David Marquand, publicly advocated devaluation in a pamphlet called *Change Gear*. We were considered then on the centre right of the party, and we joined with Eric Heffer and other MPs clearly on the left to form a so-called 'Snakes and Alligators' grouping to campaign for the devaluation that was later forced on the government in November of that year. Exchange rate policy should not be a left–right issue in the party, nor should priority to be given to the pursuit of economic growth. It is ridiculous to see today's Labour Front Bench demanding that all Labour MPs have a political duty to go along with early membership of the eurozone, and once again we hear the argument of patriotism being used against the doubters.

Ever since my experience in the 1960s I have been very dubious about exchange

rate control systems, for even when they are technically capable of being adjusted and are not a fixed system, experience shows that politicians tend to shrink from making any downward adjustment, for fear of being depicted weak and a failure.

In 1972 Edward Heath's Conservative Government was unable to live with the disciplines of the Snake for longer than six weeks.

In 1978 Prime Minister Jim Callaghan was determined to keep our options open over joining the European Monetary System. As Foreign Secretary, with Denis Healey as Chancellor, I helped negotiate the dual role of being members of the European Monetary System and being free to decide later if we wanted to join the actual Exchange Rate Mechanism (ERM). This was the forerunner of the Maastricht Treaty compromise over the euro.

In 1987, after the Louvre Accord, Nigel Lawson, as Chancellor of the Exchequer, intervened by buying Deutchmarks to hold sterling below DM3. It was a largely undeclared policy of shadowing the Deutchmark, which was eventually uncapped in March 1988. Its main purpose was to arrest the fall in sterling but it was also hoped by some that it would demonstrate that sterling was ready to join the ERM, which Lawson had wanted to do since 1985. Entry was refused by Margaret Thatcher then, and again when he tried after the 1987 Election. What shadowing demonstrated was not so much that intervention was inflationary but that the overall policy, taking the exchange rate and interest rates at the time into account, was not tight enough. Any government within a floating system of exchange rates is wise to reserve to itself the option of intervening. But it should be rarely used. It is very difficult to flatten out irrational currency moments while respecting the reality that any intervention cannot hold out against determined market pressures.

As Leader of the SDP I had advocated joining the ERM in the mid-1980s and thought the rules over adjustment would be sufficient when we joined in 1990. The inability to adjust within the Economic and Monetary Union (EMU), however, meant that I and many other MPs would never have supported John Major's Maastricht Treaty negotiation without the British opt-out from the euro. I have yet to be convinced that the UK can achieve sustained economic growth within a permanently fixed exchange rate system.

It needs to be remembered that John Major, and subsequently Tony Blair, only very reluctantly accepted that a decision to join the euro had to be one for the British people in a referendum. They were forced into this concession by public opinion. The United Kingdom's failure to achieve a revaluation inside the ERM in 1992 created much hardship, and it demonstrated to me that the design of the mechanism was flawed. For the United Kingdom it had systemic failings, with speculation being a one-way bet from which many speculators safely made substantial sums of money. The United Kingdom would risk much by re-joining the ERM, even for the EMU qualifying period, without special safeguards being introduced into the mechanisms. It is very noticeable that Labour Ministers, when advocating early entry into the eurozone, evade the question of the ERM qualifying period. They believe that it will be waived – but that may be too optimistic given the rule that other EU nations aspiring to join must demonstrate the stability of their currencies within the ERM.

When it became clear that Prime Minister Tony Blair was only waiting for a change in the opinion polls to join the euro, I made public in a speech in Manchester in January 1999 my intention to campaign for staying out of the single currency. This was despite considering myself no longer a party politician, being a cross-bencher in the House of Lords. That decision was, however, always conditional on any campaign being fully committed to continuing membership of the European Union. Later I went on to help create New Europe (whose publications can be accessed through www.no-euro.com including the most recent pamphlet by Geoffrey Fitchew entitled *Economic and Monetary Union and the European Constitution*). Without the 'Yes to Europe, no to the euro' campaign, I believe Tony Blair, after the 2001 General Election, might well have been able to swing public opinion and to hold and win a referendum on joining the euro – with very adverse consequences to the UK economy. It is particularly important that if a somewhat similar campaign were ever needed to be revived in the future it should have an even stronger Labour Party element within its cross-party mix. The torch must now pass on this issue from my generation to a new wave of politicians whose political future will be made in the years after the 2005 General Election.

Publication of this book at this time seems to me, therefore, very timely in that it starts to build the broad base of an economic astringency about the eurozone. I deliberately do not use the word scepticism because that has come to be understood as embracing hostility to our membership of the European Union. I note with interest, and pleasure too, that at last a significant number of Liberal Democrat MPs are speaking out about the euro and do not share the enthusiasm of their leaders, who like many New Labour leaders want quick entry on political grounds as soon as public opinion allows after the next election and have no qualms about the economic consequences of entry.

One of the major successes of Labour in government since 1997 has been its record of sustaining the economic growth which it inherited and which restarted so quickly after Norman Lamont, as Chancellor, dug out enough space for export-led growth following the debacle of our forced exit from the ERM. In part, that growth record has stemmed from the ability of the government to set the inflation target while the Bank of England's Monetary Committee sets the interest rates. I have never excluded joining the euro at some stage in the future, but it should only be contemplated if the eurozone economies have come very close to converging and there is convincing evidence that all the nations within the eurozone are irrevocably committed to policies that will allow any such convergence to be maintained. Hopefully the eurozone countries will improve their economic growth record, and there is already some sign of improved economic activity in France, Spain and Italy. But there is a long way to travel before the eurozone economies converge.

The July 2004 Report of the European Commission, *The Euro Five Years On*, says: 'The available evidence is in line with a positive impact of monetary union on cyclical convergences.' That is a conclusion based on little evidence. It was rubbished only a few weeks later by a Deutsche Bank research note – 'Contrary to what the European Commission says, we do not see that the euro economies have

converged' – and the note went on to say, 'there are currently no signs that growth differences across the region are narrowing' and that in fact 'there have even been signs of greater divergence'. It goes on to question implicitly the very concept of the eurozone by saying, 'economic instability in the euro area is likely to be higher and trend growth lower than it would have been without monetary union'.

The German Bundesbank cut interest rates in five periods, responding to recession in 1967, 1975, 1982–3, 1987 and 1994–6. It is only because the European Central Bank (ECB) has to target inflation in countries in very different stages in the economic cycle that interest rates have not been lower in the eurozone, and this inability to have lower interest rates in Germany has been very damaging. Some have calculated that to help the German economy grow faster over the last five years, the interest rate should have been nearer 1 per cent than 2 per cent.

Five years ago I used to argue that though the United Kingdom should stay out of the eurozone there was too much political capital invested in it by other eurozone countries for there ever to be any question of some members withdrawing from the zone. I am no longer so sure of that. I can imagine the eurozone collapsing under the weight of its own economic contradictions. I am strengthened in that view by an article in the *Financial Times* by Wolfgang Munchau (6 September 2004), which warned that even 'with the reformed stability pact, EMU will be more like an eccentric club than an economic union'. He goes on to say that:

> No matter whether the trigger is high inflation, a banking crisis or some other channel, one common cause underlies the failure of all monetary unions: the lack of a political union with the authority to enforce economic and financial policy among its members.

I doubt that the eurozone countries can agree to a far tougher regime to increase its effectiveness, but if they wish to do it they are free to do so as long as they do not try to impose that regime on other non-eurozone EU nations. On 13 September 2004 the ECB's Chief Economist, Otmar Issing, commenting on the Commission's attempt to relax the existing rules, said: 'Without the existence of a credible threat of sanctions, the pact is losing its bite. As a result the current situation is intolerable.'

The British public have no wish to embrace full political union and refuse, rightly, to believe political leaders' reassurances that the two issues – political union and the eurozone – are unconnected. So far, those reservations, both political and economic, have forestalled any attempt to take the United Kingdom into the euro. The public suspect, correctly, albeit in a vague way, that to make EMU work political union is necessary. They suspect also that the same politicians are misleading them when they pretend that this new European Constitution, on which again the politicians have been forced to concede a referendum, does not carry within it some paving techniques to bring about political union. The public are right to be suspicious.

On the face of it euro membership and the new Constitution are different issues on which it is possible to take different positions. This is why New Europe, while

commenting on the Constitution, has kept to the euro as the core campaigning issue and not embraced the campaign against the Constitution. But if we are to avoid full political union it is vitally important that we retain the independent conduct of foreign policy as a means of determining sovereign status. In that context it is relevant to economic arguments, too, to consider the proposed new Constitution. In my judgement the Constitution fails to fully protect our ability to conduct an independent foreign policy over the next few decades. The establishment of a new post of EU Minister for Foreign Affairs will probably pave the way for eventually establishing an EU Minister for Economic Affairs. The Constitution fails to make clear a precise delimitation of competence between the member states and the European Union over foreign policy, and that is also the case for economic policy. There will be renewed attempts to give the European Union power over social security and tax policy, not helped by the acceptance of wide-ranging constraints by the European Union – through the language of coordination in the Treaty – over employment policies and social policies. The risk – by a qualified majority vote on the Council – that the President of the European Council could be double-hatted with the role of the President of the Commission is the single most dangerous potential power in the new Constitution. The government assert in their White Paper that this could not happen, but this is not the view of others; for example, the Dutch government has specifically told their parliament that it is both desirable and legally possible to double-hat the two posts. If it is done this would in effect create, by the backdoor, a political union.

Ensuring that the British public view remains 'Yes to the EU, no to the euro' will be greatly helped if the left keeps the maintenance of economic growth as high on its political agenda as it has in the past. I do not pretend that having our own currency is the only factor in a growth agenda for Britain, but it remains as far as the eye can see a vital ingredient. I also believe that the social Europe, which the right – particularly in the United Kingdom – dislikes, can, if well judged, reinforce industrial stability and competitiveness. I hope that the new Commission under the former Portuguese Prime Minister, José Manuel Barroso, will demonstrate the inner coherence and the confidence to concentrate on the all-important Lisbon agenda for economic and market reform that does aim for the right balance between social and competitive agendas. There is no urgent need for a new Constitution.

The Treaty of Nice did all that was vital to handle the greatly-to-be-welcomed enlargement. The weighted voting formula agreed then is now to be changed by the new Constitution, and this we are cynically told by Giscard d'Estaing was done in part to make it less likely that other countries would vote for Turkey to enter the European Union in view of its large and growing population. The Euro Group did not wait for the Constitution but in September 2004 appointed one of their number, the Luxembourg Prime Minister, to chair the Euro Group for two years. This immediately provoked the French Chairman of the ECB to hit back saying, 'I am evidently Mr Euro'. If the European Council really does want to give up the six-month rotating presidency of the Council, it can appoint one of its own members to chair the Council for two years along with the grouping of countries holding the

Presidency. There is also little to stop the new Commission starting to give back powers to the member states under the existing Treaties. Sadly, in practice, there is no real simplification in this Treaty for those who will have to work it, and it has not achieved the clarity that the Laeken Declaration hoped for. It also remains very likely that the abolition of the separate intergovernmental pillars established at Maastricht will over time erode the intergovernmental nature of most foreign and economic policy decisions, which is the intention of many of those who champion the Constitution. The Constitutional referendum in the United Kingdom may come only after 24 other countries have ratified the Treaty. Hopefully before then one or more country that has to hold a referendum will have voted no, making it far less disruptive for the United Kingdom to do the same.[1] When our referendum comes one can best make a judgement as to exactly how a British ‘no’ vote might impact inside the European Union, but provided it is not a vote taken as a first step to leaving the European Union there will be many European citizens who will be glad to see this unfortunate Treaty blocked.

At a time when 25 European nations have still to develop their working relationships and are facing the political imperative of further enlargement to include Romania, Bulgaria and, hopefully, Turkey, it would be better to concentrate on making the existing Treaties, which the new countries have spent some years getting to know, work more effectively. The eurozone countries should also develop their own budgetary disciplines and monitor their own tax and spending policies, while letting those outside the eurozone grow and compete without the necessary constraints of EMU. The way forward for the European Union is to allow the pattern of working together in the Union on foreign, defence and economic policy gradually build its own pragmatic consensus from the ground up. Instead, we are being urged to accept a new, more highly centralised and uncertain constitutional model for an already strained and unsettled Union in which many of its citizens are already showing their political discontent.

Note

1 Foreword written prior to EU Constitution referendums in France and the Netherlands.

Preface

Bryan Gould

This book is long overdue. The debate about Britain and the euro – so far as there has been a debate at all – has been largely the preserve of the right, and has been pretty much dominated by simplistic posturing. On the one hand, those in favour of British adoption of the euro have stressed the lower transaction costs and the convenience to travellers, and – if they are a little more knowledgeable – the familiar argument that to stay out would be to threaten trade and investment.

The opponents, on the other hand, go for the nationalistic pitch, stressing the importance of national symbols like the pound and the Queen's head on our currency. Neither side seems greatly interested in exploring the fundamental issues of economic and political significance that could help shape both Britain's and Europe's future.

The left has hardly entered the debate, reflecting an unwillingness to be identified with either position adopted by the right, a broad but rather fuzzy commitment to internationalism, and an unthinking suspicion that exchange rates and currencies are properly the concerns of right-wing businessmen and technicians. Some – like the commentators – prefer to see the issues in terms of domestic and, especially, personality politics. Could Tony win a referendum? Or will Gordon use opposition to the euro to open the door to Number Ten?

All of this misses the point – or rather several points. As a policy issue, the euro poses real challenges, and real opportunities, to the left. The careful exploration and successful resolution of these issues could determine the prospects of Labour governments for years to come.

The economic consequences of embracing the euro can hardly be overstated. A single currency inevitably requires and dictates a single set of monetary conditions brought about by a single monetary policy. In an economic zone as large as the current European Union, it is inherently unlikely that a single monetary policy could conceivably meet the interests of all the diverse parts of that economic zone. A monetary policy that suits the stronger countries (who have the major say in what that policy should be) will harm the interests of the weaker, reinforcing the natural tendency in any economy for productive capacity to concentrate in the stronger parts.

A single currency means the renunciation of one of the major (and potentially beneficial) instruments for dealing with this misalignment. Correctly aligned

exchange rates allow differently developed economies to interact with each other to mutual advantage, encouraging each to move resources to the potential growth points where they enjoy a comparative advantage. With a correctly aligned exchange rate, a weaker economy can trade productively with a stronger one, with both concentrating on the things they do best.

In the absence of that possibility of adjustment, inequalities do not disappear. They simply re-emerge in other forms. Those parts of the wider economy that find the going tough will experience a further loss of economic activity, investment and employment. The consequent fall in demand will in turn depress the wider economy, affecting even the stronger parts who were the initial beneficiaries of the single monetary policy.

It is for these reasons that the United Kingdom's decision on the euro is important for Europe as well as for the United Kingdom. A decision to stay out of the eurozone could be argued not only to be in the United Kingdom's interests but also to point the way to a better economic future for the European Union as a whole. The European economy would function better if component parts had the freedom to set their own monetary conditions and exchange rates so that they can trade with each other in optimal conditions.

These arguments are not purely theoretical. The experience of European countries over the last 20 years (bearing in mind that the Exchange Rate Mechanism gave us an early test of the economic consequences of currency union) testifies to the damaging effects of compressing diverse economies into a single monetary and currency zone. It is no accident that the European Union continues to struggle while the United Kingdom has, by comparison and since leaving the ERM, prospered.

In the absence of any possibility of exchange rate adjustment, there are only two escape routes for depressed parts of a wider currency zone. First, they can wait until a lower level of economic activity so depresses comparative living standards and wage rates that investment is attracted by those lower labour costs. The problem with this is that it takes a long time and that the loss of output while this slow and painful adjustment takes place will harm both the particular component part and the wider economy. This is, nevertheless, where the eurozone now is.

Second, the depressed area can throw itself on the mercy of the wider entity, arguing that it is making a sacrifice of its own economic prospects for the sake of some wider goal, and that it is therefore entitled to all the benefits (such as they are) of the wider entity's regional policy and, ultimately, social security largesse, in order to offset the loss of economic welfare.

The wider goal for which this sacrifice is made is presumably a degree of political integration which is also the necessary precondition for the assumption of regional policy and social security responsibilities by the wider entity. It is only in a political union (and even then the strains are immense) that the parties recognise such a community of interest as to make possible both the sacrifice on the one hand and the assumption of responsibility on the other.

The economic aspects of a single currency, in other words, inevitably elide into the political aspects. The deleterious economic effects of an inappropriately wide

currency union can only be made tolerable – so it is calculated – if the parties agree to throw in their lots with each other to the point where the value they place on their common political identity outweighs the economic sacrifice. Those who do not dare propose such a step in its own right calculate that it can be achieved by a detour.

Such a step remains, however, fraught with difficulty. We know from our own experience in the United Kingdom that even a long-established political union suffers huge strains that are only exacerbated by economic divergence. Major questions of concern to any democrat arise – issues of self-determination and accountability, representation and identity. Democracy is, after all, about more than voting. It means being governed by those by whom we choose to be governed.

The price we are asked to pay for a less than optimal economic performance is, in other words, a political step which we might be prepared to take one day, but which even its proponents do not dare to describe openly right now. This should be of real concern to the left – indeed, to any democrat – and this book is a valuable step towards a proper exploration of that concern.

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Any remaining errors and omissions we gladly attribute to each other.

Haworth, Heaton Norris and Guiseley
March 2005

1 The left and the euro

Philip Whyman, Mark Baimbridge and Brian Burkitt

Introduction

Britain's relationship with the European Union (EU) has long been the focus of conflict, as advocates of further economic and political integration clash with those who are sceptical about the rationality of the process and who prefer a looser, national-orientated approach. The issue of 'Europe' has generated passions in Britain's political system, resulted in disagreements and even threatened splits within unusual political parties and interest-representation organisations. The tensions caused within the Conservative Party – caused by conflicting attitudes towards European integration, in particular whether Britain should join the European Exchange Rate Mechanism (ERM) – have been well documented. These led to the dramatic deposing of Margaret Thatcher by her own MPs after a decade as Prime Minister, and subsequently the events of the 1992 currency crisis fatally undermined the administration of John Major. Furthermore, policy towards European integration continues to be a significant barrier to the realisation of the ambitions of various prominent Conservative MPs to lead their party, whilst the remarkable success of the UK Independence Party (UKIP) in the 2004 European Elections has been interpreted as a direct challenge to the Conservative strategy of combining a eurosceptical stance with determination to retain EU membership. Thus, with the Blair–Brown leadership of the Labour Party committed to playing a role 'at the heart of Europe', and indeed advocating membership of the single European currency subject only to five 'tests' of Britain's compatibility with the eurozone economy, observers might be forgiven for concluding that euroscepticism in Britain is restricted to the political right.

This would be a false conclusion, because the European fault-line cannot be characterised as a neat left–right issue. There are noticeable divisions in opinion across British business, the trade union movement and within the Labour Party. Recent events even indicate the beginnings of an internal debate within the Liberal Democratic Party on the issue, whilst the UK Green Party advances a distinctive critique of the orthodox economic case presented in favour of further European integration. Moreover, as contributions to this volume attest, these divisions over the future relationship between the United Kingdom and Europe are recurring themes throughout the entire post-Second World War period, with the balance of opinion oscillating over time. Indeed, Conservative opinion was overwhelmingly

pro-European at the time of the 1975 Referendum on continued membership, whilst leading members of the Labour Party campaigned on both the 'Yes' and 'No' sides, with many of the contributors to this book taking different viewpoints. Moreover, as recently as 1987, the official policy of both wings of the British labour movement supported withdrawal from the European Union. Thus, a historical review of the post-war period demonstrates that there has been a consistent 'progressive' left critique of Britain's role within European integration.

This book focuses upon one manifestation of this 'progressive euroscepticism', namely the attitudes of the left towards the current project to create an Economic and Monetary Union (EMU) among participatory member states of the European Union. Quite simply, EMU is one of the most far-reaching economic reforms of the current generation, and one that the British electorate will have the opportunity to endorse or reject through a national referendum, if the government of the day wanted to apply for membership.

In addition to the psychological impact of the introduction of a new common eurozone currency this initiative would have a dramatic impact upon the lives of British citizens. Advocates claim that it would enhance competition, through price transparency and completing the European Single Internal Market (SIM), thereby reducing prices for consumers and ensuring a superior allocation of resources as corporate restructuring facilitated a renewed global competitiveness. The economic infrastructure, moreover, has been established to focus upon the delivery of low inflation, and it is claimed that this will result in a superior economic performance for the UK economy.

Critics of UK participation in EMU, in contrast, point to the combination of substantial initial transfer costs and the danger of being trapped within a permanently fixed exchange rate system, magnified by the potentially deflationary impact of the monetarist-inspired institutional and policy framework within which the single currency has been introduced. The transfer of significant economic policy instruments to the European Central Bank (ECB), designed to operate independently of all democratic influence, has weakened the potential for national economic self-governance, whilst the target of price stability without reference to all other macroeconomic goals is likely to undermine progressive goals of full employment, social solidarity and the promotion of economic growth. Keynesian measures are further constrained by the Stability and Growth Pact (SGP), which places firm limits upon budget deficits and thereby restricts the ability of counter-cyclical economic strategy. This is quite intentional, based upon monetarist assertions that Keynesian economics no longer works, if indeed it ever did. However, progressive eurosceptics argue that the loss of national economic autonomy, combined with the multiple restrictions that EMU participation places upon the pursuit of macroeconomic policy, reduces the scope for achieving traditional democratic socialist–social democratic objectives. In short, EMU membership, under its current rules and institutional framework, would be an economic disaster for the UK economy, whilst undermining the democratic sovereignty of the British people.

The progressive eurosceptical case rests, therefore, largely upon Keynesian rather than monetarist-neoclassical assumptions, so that the market economy is perceived as experiencing significant cases of market failure and of cumulative causation. Consequently, government intervention has the potential, if properly directed and accurately timed, of improving economic performance. Progressive eurosceptical economics therefore rejects the new classical assumption of time inconsistency, which implies that all government intervention worsens those circumstances it is intended to improve, together with the monetarist belief in a long-term equilibrium rate of unemployment determined solely by labour market factors. Moreover, it rejects the viewpoint that globalisation and the international free flow of capital has rendered national economic policy instruments impotent, so that it is difficult (if not impossible) to maintain a distinctive monetary policy and pursue exchange rate management. If this were true, tying economic policy within the monetarist EMU framework would make little difference, since government autonomy would have already been effectively eroded by the external economic environment. The contributors to this book clearly reject this viewpoint and base their alternative vision upon active government macroeconomic policy, whether within a national or reformed supra-national framework.

In terms of the political vision expressed by the progressive eurosceptics featured in this volume, the predominant arguments focus upon the importance of democracy and sovereignty. The nation state is seen as the best available means of empowering British citizens to determine their own social and economic development. The EU is criticised as exhibiting a democratic deficit, whilst the status of its legitimacy, being based upon international treaty, claims predominance over national self-determination in those areas that have been ceded to supranational competence. The tendency for the EU Commission to criticise Gordon Brown's current spending plans, despite Britain's opt-out from full membership of EMU, demonstrates the dilemma neatly: whether the democratic left should prioritise the regeneration of public services or submit to the budget restraints imposed as an integral feature of participation in EMU.

This book contains contributions from leading academics, trade union leaders and prominent politicians both from the Labour Party and the wider progressive left in British politics. The advantage provided by featuring direct contributions from the selected group of individuals arises from the opportunity to compare and contrast their arguments, assumptions and proffered alternatives. However, interesting though the (sometimes subtle) differences in emphasis prove to be, the significant feature that arises from reading this volume is the degree to which the contributors share a common perspective relating to the importance of democratic self-determination, a preference for national economic management, or at least the importance of securing substantial reform of EMU's policy and institutional framework before supranational collaboration becomes compatible with progressive democratic socialist–social democratic objectives.

Book outline

The book is (loosely) divided into three thematic sections: first, contributions primarily concerning the economics of a single currency; second, employment and social aspects; and, finally, issues of sovereignty and political determination.

In the foreword, David Owen provides a unique personal insight into the development of the British left's attitude towards European monetary integration. He commences by reviewing the relationship between administrations since the 1920s and various exchange rate mechanisms, evaluates the operation of EMU to date and concludes that 'there is a long way to travel before the eurozone economies converge'. When analysing the future developments within the European Union he notes, first, the importance of separating the politically focused Constitution from the economics of the eurozone; second, that the agenda of 'social Europe' is essential to reinforce economic stability and competitiveness. Finally, he welcomes the widening of EU membership to 25 countries. Owen's overall conclusion is that 'it would be better to concentrate on making the existing treaties . . . work more effectively'. This would permit the EU to 'gradually build its own pragmatic consensus from the ground' rather than 'accept a new, more highly centralised and uncertain constitutional model for an already strained and unsettled Union in which many of its citizens are already showing their political discontent'.

Bryan Gould, who has observed the debate within the British left from both near and far, contributes the preface for this edited collection. Gould clearly states his view that 'as a policy issue, the euro poses real challenges, and real opportunities, to the left'. He then outlines the key arguments regarding the difficulties of adopting the euro, together with the wider implication 'that the United Kingdom's decision on the euro is important for Europe' since it could 'point the way to a better economic future for the European Union as a whole'. In particular, Gould emphasises the very real implications for economic management and the inevitable pressures of political union.

The chapter by Andy Mullen, provides an informative background to the later contributions through its historical summary of the changing attitudes and policy positions within the British Labour movement. Any study of contemporary reactions to European integration can only satisfactorily seek to analyse this phenomenon if placed into a historical context, whereby labour movement attitudes have oscillated sharply from fundamental support for EU membership to outright opposition and subsequently to renewed, albeit hesitant, enthusiasm. Thus, the Labour Party opposed EU membership between 1971 and 1974, and again between 1980 and 1987, although, with the exception of Michael Foot, the party leadership remained supportive of continued EU membership throughout most of this period. The trade union movement, however, remained largely critical towards EU membership throughout this entire period, until the famous 1988 speech by Jacques Delors to the TUC Congress provoked a complete reversal. Subsequently the TUC, together with a number of leading individual unions, have been at the forefront of advocating support for European integration.

The second feature arising from Mullen's chapter relates to the nature of the many arguments forged during the European debate 30 years ago and their continued relevance for the contemporary debate over Britain's future relationship with Europe. Mullen states that 'the fundamental issue is whether the ongoing process of European integration [towards the objectives of ever-closer union] assists or hinders the advance of socialism'. In other words, the questions that require an answer are fundamental. Should progressive movements in Britain favour a national or supranational economic and political strategy? Is European integration the necessary prerequisite for the creation of a progressive European strategy capable of regulating globalisation in such a way as to promote the interests of working people and their families? Or is the entire project designed according to pro-market, monetarist principles, and therefore inconsistent with traditional progressive-left objectives, such as full employment, economic democratisation and developing a welfare state designed to decommodify citizens and protect the vulnerable from the worse excesses of market determination? Many of these themes are explored in greater detail in the subsequent chapters.

The first section of the book seeks to provide a broad overview of the key issues considered significant in terms of those progressive economists who exhibit scepticism towards the benefits of British participation in EMU. Attitudes vary between those who consider that membership of the euro can be compatible with progressive objectives if necessary structural and policy reforms are completed, and those whose analysis leads them to conclude that pursuit of a national, progressive strategy would produce superior results.

Jonathan Michie highlights the monetarist nature of the Maastricht superstructure designed as a fundamental feature of EMU, intended to empower capital at the expense of national government. EMU therefore represents one element of a neo-liberal strategy to 'roll back' the state. It has caused participatory member states to pursue deflationary policies for more than a decade, with the resulting high unemployment and rising inequality reminiscent of the disastrous return to the Gold Standard in the 1920s and the resulting Great Depression. Rigidity in economic rules creates divergence in the real economy, which generates social tensions and raises further questions that democrats cannot ignore. Hence, Michie concludes that:

> Unless current European economic policy is reorientated towards the objective of full employment . . . rather than being stuck on the myopic concern with zero inflation, the route forward must once again be based on independent national growth strategies which would not only allow countries to help themselves, but by doing so would help each other.

Philip Arestis and Malcolm Sawyer join Michie in providing a detailed critique of the Maastricht version of EMU. They argue that the existing monetarist version of monetary union is far from an inevitable consequence of establishing a common currency. Therefore the European system could have been designed quite differently. In particular, they highlight the undemocratic ECB with its too limited

policy remit and inadequate (sole) policy instrument of interest rates. Consequently, Arestis and Sawyer emphasise the 'woeful lack of institutions and policies operating at European level to support the development of a successful European economy'. Without significant reform, the authors consider that participation in EMU is unacceptable since it mitigates against the maintenance of full employment and the achievement of progressive economic objectives.

Janet Bush concurs with the analysis provided in the previous chapters through her identification of the monetarist orthodoxy that has dominated Europe as the main cause of the sluggish growth and high unemployment that has plagued many continental European economies for more than a decade. Moreover, Bush views EMU as representing 'a battering ram towards free market economics', and points to international precedents, most notably in Scandinavia, where it is the progressive forces who oppose membership of EMU on the basis that it threatens traditions of generous social welfare and labour market protection. Bush concludes that there is 'no prospect' of successful reform of the SGP and the creation of an active federal fiscal policy. Therefore, for progressive economists, Bush argues that EMU is fatally flawed and the combination of 'continued low growth, economic instability and political tensions will wreck the system in the years ahead'.

Paul Ormerod adopts a different perspective, seeking to examine EMU from the position of a prospective member of the eurozone; with particular emphasis placed upon less developed nations from eastern Europe, who have struggled to complete the transition from quasi-command to market economy. According to Ormerod's analysis, EMU reinforces centralising tendencies within the EU, thereby exacerbating the lack of democratic validation; many of the key economic decisions are taken by political elites, central bankers insulated from democratic influence and senior managers of large corporations. Each of these groups has benefited from the EMU process, yet discontent with the remoteness of decision-making processes continues to increase, as measured by the electoral performance of a number of political parties across the EU member states. Ormerod singles out the ECB for particular criticism, suggesting that the sole economic institution established to sustain the eurozone has been 'designed to fight yesterday's battles', due to its obsession with inflation and neglect of all other economic objectives.

The chapter by Mark Baimbridge builds upon this critique by providing a detailed analysis of the ECB, in terms of its objectives, institutional structure and policy effectiveness. Having noted that the European Union deliberately set out to create the most independent central bank in the world – no doubt influenced by the literature claiming that central bank independence from political influence facilitates its anti-inflationary policy – Baimbridge develops a detailed critique of this approach, listing inconsistencies in the literature and the likely hindrance of wider macroeconomic policy coordination. Thus, in conclusion, Baimbridge suggests that the continued existence of an independent ECB would hamper the realisation of a progressive economic strategy, since it would 'ensure that monetarists remained in power if not in office, because it would steer the economy by financial indicators to the detriment of the real economy'.

The *Guardian*'s Economics Editor, Larry Elliott, provides a short, pithy

commentary upon the inadequacies of the current EMU design and the need for the progressive left to pursue an alternative approach. Scepticism, argues Elliott, is ‘the beating heart of democracy’, and therefore the left should rediscover its natural tendency to mistrust the agenda set by political and economic elites by developing a radical alternative to the monetarist-dominated EU economic framework. Elliott argues that those on the left who offer their support to EMU, on the basis that it is part of a package leading towards a ‘social Europe’, are ‘living in cloud-cuckoo-land’, since the ECB and EU Commission have, for a number of years, consistently rejected an expansionary macroeconomic platform for one based upon labour market flexibility and supply-side reform. Ultimately, Elliott suggests that the real choice lies between a progressive-left critique of contemporary European economic policy, based upon the importance of active industrial policy and macroeconomic management, and a right-of-centre alternative, focused upon extending Thatcherism across the EU.

The final paper in the first section concludes with a chapter by the editors, which seeks to develop a post-Keynesian analysis of the EMU. Whyman *et al.* argue that membership of the euro

> requires the separate formulation of money policy from nationally determined fiscal policy, leading to a resultant lack of policy coordination. . . . The resultant slow-growth, high-unemployment outcome will be further exacerbated by the transfer of monetary policy to a European Central Bank.

In particular, they note the ‘incompatibility between the monetarist model, upon which EMU is constructed, and the possibility of creating an alternative economic strategy grounded in post-Keynesian tradition’. A post-Keynesian framework is developed through discussion of disequilibrium and cumulative causation; increasing returns to scale and economic growth; aggregate demand, full employment and output capacity; socialisation of investment, together with the interrelationship between demand and supply side. From this standpoint ‘in order to implement post-Keynesian economic policies, the United Kingdom needs to avoid the uniform monetary policy and the constraints upon budgetary measures imposed by the adoption of a single EU currency’.

The second section of the book is concerned with the impact of EMU upon employment and industrial relations. The first contribution, made by Brian Burkitt, examines the widely held perception that the euro should be embraced because it would enable the United Kingdom to enjoy the benefits of participating in the European Social Model (ESM). However, Burkitt argues that the weight of evidence from social policy research is that such an assumption is problematic. Four different kinds of welfare state have been identified within the European Union; to which of these models, does the ESM relate? The traditional ESM requires large welfare expenditure backed by public support for a positive state presence in social policy, but tensions exist within the model from a democratic socialist perspective. These are sufficiently serious to undermine centre-left arguments for UK membership of the euro. At best the ESM provides a number of

minor micro pension and workplace benefits, but from within a failing macro framework. Aggregate demand management, rather than supply-side 'reforms' that impose the costs of structural adjustment upon the most disadvantaged citizens is the key to creating a future socially inclusive community.

The chapter by Matthew McGregor reviews the potential impact upon the welfare state from euro membership, focusing upon the major serious flaw: the voters. Labour voters have consistently opposed the United Kingdom's membership of the euro and show no sign of changing that stance. The answer relates to working-class voters understanding that the economic effects of joining the euro far outweigh any political considerations. The flexibility that economies need has, in Europe at least, been based on regional and national planning accompanied by fiscal and monetary policy. In the euro, these levers are taken away and governments are unable to react quickly and effectively. It is jobs, public services and welfare that Labour voters are interested in, and it is the jobs, public services and welfare policy spheres that offer the most convincing case for staying out of the euro. Voting 'yes' would lead to high unemployment and low growth, whilst voting 'no' would protect the advances the Labour government has won and keep our ability to continue building our corner of social Europe secure. Labour voters are against joining the euro because it is not in the economic interests of people in this country.

The next contributions come from industrial relations practitioners. Firstly, Joe Marino, the General Secretary of the Bakers, Food & Allied Workers Union (BFAWU) notes that trade union support for European integration is based largely upon the perception that it was preferable to the Thatcherism of the late 1980s. However, Marino points to the fact that many of the anticipated advantages are susceptible to shifts in key personnel in the EU Commission and the balance of political power across the EU member states. Thus, such social gains as have actually been made are being watered down by recent initiatives championed, among others, by New Labour. Rather like the 'irreversible' gains trumpeted by the 1974 Labour Party manifesto, a neo-liberal drift in economic approach threatens the modest social advances secured by the European Union. Marino further suggests that the European Union favours the interests of capital at the expense of workers, and this is likely to become more apparent with the establishment of EMU and as employment protection is gradually dismantled in favour of flexible labour markets.

This chapter is complimented by that of Doug Nicholls, General Secretary of the Community and Youth Workers Union (CYWU) who argues that it is time for trade unions to reconnect with their roots in the democratic struggle and reject the EU altogether. The drive towards one legal and political entity under one currency and constitution has reached a crossroads. These developments are not socialist, nor can they be subject to a programme of reform from within by socialists. Whilst trade unionists have always supported others in their struggles for national independence, we have been slow to apply this principle to ourselves. It therefore comes as a shock to recognise that we are now being taken over, with an external power seeking to remove our national powers and democratic structures. Much of the slovenly thinking in the trade unions relates to the seductive illusions of European legislation. The general pragmatism of trade unionists, born of

continually negotiating between a rock and a hard place, has dulled the sense of what could really be achieved: huge capital reserves to re-invest in manufacturing renewal and public services; the ability to plan our economy for ourselves; an independent energy policy; government procurement that is exclusively British based; employment laws that are regulated to fit our circumstances; taxes and interest rates levied to suit our pace of change.

A third trade union General Secretary, Billy Hayes of the Communication Workers Union (CWU), argues for the development of a left strategy in Europe comparable to the type of hegemony that the neo-liberals have gained in the United States of America. The practical question is how to secure the most favourable development of the EU in the context of contending international forces. Unfortunately, the left critique of the single currency has yet to suggest an alternative in which extended capital reproduction can be demonstrated. Whilst defending the 'social gains' of the EU the left has yet to demonstrate what pan-European economic policy can deliver the material basis for sustaining these gains. A left strategy would start from the needs of hundreds of millions of people in Europe and billions across the planet; first, to outline an alternative economic policy to neo-liberalism; second, a large expansionary economic block is an essential precondition for a 'social Europe'; third, to be a defender in Europe of developing countries against the United States; and, finally, to seek greater integration and coordination to assist the struggle and needs of the workers and oppressed.

Philip Whyman documents the shift in British trade union policy from opposing many aspects of European integration towards enthusiastic support for a 'social Europe' and subsequent acceptance of EMU. Whyman's evaluation of this shift suggests the existence of a basic contradiction between the reality of EMU, its monetarist framework and the progressive objectives that the trade union movement believes can be advanced by support for EMU. Whyman points towards the net cost of EMU membership, due to its deflationary infrastructure and restrictions upon counter-cyclical policy, together with restrictions upon public sector expenditure and the likely deterioration in public sector provision and relative public sector pay. Moreover, he notes the determination of leading figures in the ECB, EU Commission and, not least, the current British Labour government, who have rejected the 'old social model', to achieve labour market flexibility. Whyman concludes that the trade union case for supporting EMU is 'fatally flawed', and that the British trade union movement should develop an alternative strategy to secure its goals – either through bargaining with the European Union to facilitate necessary structural reforms or via the emphasis upon a national basis for social and economic policy.

This section concludes with a chapter by Matthew Watson, who notes the tendency for the left to desire the creation of a 'social Europe' to counter the free market globalisation of the American variety. However, Watson suggests that, in practice, it is more important to defend national models and that a simple 'Europe versus globalisation' dichotomy is based upon the unjustifiable assumption that most aspects of European integration are progressive in nature, whereas in reality they have tended to bind the ability of nation states to regulate capital. Moreover,

Watson argues that EMU will cause a shift in the governance of European firms, increasing the importance of capital markets and diminishing the influence of banks as the main source of investment finance. This, Watson claims, will encourage the growth of short-termism and thereby undermine the ability of firms to sustain their element of the European social market approach, whilst the SGP squeeze upon public spending means that the state will be unable to compensate for this reduction in social protection.

The final section of the book is concerned with political issues of democratic determination and sovereignty. Here, a variety of academics and prominent politicians discuss the likely impact of EMU upon the goals pursued by progressive-left political movements. For example the European Policy of the Green Party has changed significantly over time. The short-term objective of the Ecology Party (1975–85) was withdrawal, whilst its long-term objective was the creation of a federal 'Europe of Regions'. In 1988 the Green Party reversed its withdrawal policy to one of 'reform from within', that is, maintaining membership while seeking to fundamentally reform the EU.

In light of this, Scott Cato develops a 'Green' critique of EMU, which focuses primarily upon its origins as a result of pressure from 'big business' – intended to reinforce trends towards globalisation, the expansion of free trade and promote the free movement of capital. The result is that transnational corporations are capable of 'bargaining' with trade unions and governments to lower taxes (hence public spending) and labour standards. Instead of pursuing this line, Cato outlines an alternative vision, based upon 'localisation' and utilising *multiple* time-based local currencies to keep liquidity and purchasing power within deprived communities. Cato rejects EMU on the basis of its association with efforts to support globalisation and increasing international trade, since these do not help the poorest nations, whilst being linked with over-consumption, obesity and the destruction of the environment.

Brian Burkitt advances this debate through combining the issue of EMU membership with British democracy and sovereignty. He argues that federalists are seeking to 'build a United States of Europe from the top down', but that 'such a process of building a federal union is the opposite of how every other nation has been created'. In relation to the impact upon democracy, Burkitt argues that 'the parliamentary democracy developed and established in Britain is based upon the sovereignty of the people' from which 'five basic democratic rights emerge . . . each of which is fundamentally diminished by British membership of the European Union'. This process has commenced with powers 'substantially ceded to the European Union, whose Commission and Council of Ministers are neither collectively elected nor collectively dismissed by the British people, or by the peoples of the EU countries put together'. In relation to sovereignty, Burkitt comments: 'such a major change in the operation of the UK constitution carries profound implications for the exercise of national sovereignty'. For example, the notion that sovereignty 'can be "pooled" is an evident absurdity. Power can be pooled, but authority cannot. "Pooling" is a dangerous concept, because it falsely implies that authority can both be retained and given away simultaneously.'

The following chapter, written by Austin Mitchell MP, claims that EMU represents the largest 'assault' upon national democratic sovereignty that European integration has thus far introduced. Claiming that sovereignty is a zero-sum game, and that 'pooling' simply results in the loss of influence over key issues of national importance, Mitchell argues that EMU takes away the most important economic tools from the control of British parliament and people, whilst the fact that it is based upon international treaty means that membership binds future governments to abide by policies over which they have only minority impact.

Tony Benn's contribution to this book centres upon a Bill he presented before the House of Commons, intended to establish a progressive 'Commonwealth of Europe'. The proposal was designed as a clear contrast to the monetarist institutional and policy structure contained in the Maastricht Treaty, which would undermine democratic accountability. The 'Commonwealth' alternative demonstrates the fact that progressive-left euroscepticism can be compatible with a strong support for internationalism. Rather than Benn's proposals representing a narrow nationalism, they would have established a cooperative relationship between neighbouring countries that would be both outward looking and facilitate (rather than, like EMU, constrain) progressive economic policy.

The final contributed chapter to the book comes from the late Peter Shore, who highlights what he describes as New Labour's strategy of downplaying the significance of EMU, even though it is, and always was, meant to be part of a transition towards a United (Federal) Europe. Moreover, Shore concurs with Mitchell that EMU destroys the capacity of future UK governments to use the power of the state to influence and control the UK economy. Instead, these powers have been transferred to unelected European institutions, located in Brussels and Frankfurt. In addition, referring to the loss of monetary and exchange rate policy, Shore concludes that progressive-left policy requires control over the policy tolls that EMU takes away.

The book concludes with a chapter by the editors that seeks to advance the overall argument and debate contained within the contributed chapters. Whyman *et al.* argue that 'the national interest of the United Kingdom requires the implementation of a long-run opt-out from EMU, given that its participation is neither inevitable nor desirable'. In particular, 'a decision to reject participation in the single currency would restore to national government those economic instruments essential to the management of its economy' such that they 'will be able to pursue a more balanced economic programme'. The first policy outlined concerns 'national monetary authorities seek[ing] a higher long-term growth rate by providing a favourable climate for industrial expansion through low inflation. . . . Fiscal policy is used to support the more dominant monetary policy by restraining inflationary pressures.' A second policy involves the 'active use of fiscal as well as monetary policy' whereby 'an approach of this nature would probably be accompanied by an industrial policy'. Finally, Whyman *et al.* advocate the retention of a national exchange rate policy since, 'over a period the desired objectives of exchange rate policy are short-term stability and long-term flexibility. The dangers to avoid are long-term fixity and short-term volatility.'

2 The great debate[1]

The Labour Party and European integration

Andy Mullen

Introduction

Following two failed applications to join the European Union (EU) in 1961 and 1967, Britain's accession in 1973 was preceded by a national debate, which Nairn (1973) parodied as the 'great debate'. More than 30 years later, however, the relationship between Britain and the European Union continues to be a controversial issue in British politics. The focus of this chapter is the historical and contemporary division of the Labour Party over European integration. It analyses how Labour's European policy has changed over the post-war period, suggests a number of factors to explain these changes and concludes by advancing four main reasons why a Labour Party which seeks the socialist transformation of Britain should oppose the European Union.

The process of European integration presents the Labour Party with the particular puzzle of how to respond to the paradox that is the European Union. On the one hand, the progressive environmental and social policies of the Union, plus the rhetoric that European integration is internationalism in action, delivers peace in Europe and constitutes the only immediate way to contain the forces of globalisation, hold a logical appeal. On the other hand, the evidence that it is expanding its power over EU member states, whilst enforcing pro-market and monetarist doctrines without a democratic mandate to do so, leads to the conclusion that the European Union is a threat to democracy and a socialist economic and social programme. The fundamental issue is whether the ongoing process of European integration assists or hinders the advance of socialism. The competing answers to this question determine whether the Labour Party has pursued, and should pursue, a predominantly national or European economic and political strategy.

The European policy of the Labour Party

The official European policy of the Labour Party between 1945 and 2004, as agreed by the Annual Conference, together with the policy pursued by the party leadership and by the Foreign Office, is summarised in Table 2.1.

Table 2.1 The European policy of the Labour Party and the Foreign Office (1945–2004)

Year	*Annual Conference policy*	*Party leadership policy*	*Foreign Office***
1945 (G)			Imperial third force
1946 (G)		Imperial third force	
1947 (G)	Support for European integration		
1948 (G)	Socialist third force*	Intergovernmental European cooperation	
1949 (G)			Limited liability
1950 (G)	Intergovernmental European cooperation		
1951 (G)			
1952 (O)			
1953 (O)			
1954 (O)			
1955 (O)			
1956 (O)		Support for the FTA	Partial engagement
1957 (O)			
1958 (O)			
1959 (O)		Conditional support for the EFTA	Near identification
1960 (O)			Pro-entry
1961 (O)	Opposition to entry without safeguards*	Opposition to entry without safeguards	
1962 (O)	Conditional support for entry	Conditional support for entry	
1963 (O)			
1964 (G)			
1965 (G)			
1966 (G)			
1967 (G)			
1968 (G)			
1969 (G)	Conditional support for entry*		
1970 (O)			
1971 (O)	Opposition to entry on Conservative terms	Opposition to entry on Conservative terms	
1972 (O)	Renegotiate the terms, hold a general election or referendum and boycott EU institutions	Renegotiate the terms, hold general election or referendum and boycott EU institutions	
1973 (O)		Renegotiate the terms and hold a referendum	Pro-membership
1974 (G)	Renegotiate the terms and hold a referendum	Renegotiate the terms and hold a referendum	Pro-membership
1975 (G)	No vote in the 1975 Referendum	Yes vote in the 1975 Referendum	
1976 (G)	Withdrawal, plus opposition to Direct Elections	Pro-membership, plus support for Direct Elections	
1977 (G)	Reform of the EU	Reform of the EU	
1978 (G)	Reform of the EU, plus opposition to EMU	Reform of the EU, plus opposition to the ERM	

Table 2.1 Continued

Year	*Annual Conference policy*	*Party leadership policy*	*Foreign Office***
1979 (O)	Reform of the EU, plus withdrawal from the CAP	Reform of the EU, plus support for enlargement	Pro-membership
1980 (O)	Withdrawal commitment in the manifesto	Withdrawal commitment in the manifesto	↓
1981 (O)	↓	↓	↓
1982 (O)	↓	↓	↓
1983 (O)	↓	↓	↓
1984 (O)	↓	Support for coordinated European reflation	↓
1985 (O)	↓	Opposition to the Single Market	↓
1986 (O)	↓		↓
1987 (O)	↓	Pro-membership	↓
1988 (O)	Pro-membership		↓
1989 (O)	Support for enlargement, foreign policy coordination, EU institutional reform and the Single Market	Support for enlargement, the ERM, foreign policy coordination, EU institutional reform and the Single Market	↓
1990 (O)	Support for EMU, enlargement, the ERM and EU institutional reform	Support for EMU, enlargement, the ERM and EU institutional reform	↓
1991 (O)	Support for CAP reform, EMU, enlargement, the ERM and the Social Charter	Support for CAP reform, EMU, enlargement, the ERM and the Social Charter	↓
1992 (O)	Support for CAP reform, enlargement, EU institutional reform and Maastricht Treaty ratification with the Social Chapter	Support for CAP reform, enlargement, EU institutional reform and Maastricht Treaty ratification with the Social Chapter	↓
1993 (O)	Support for CAP reform, the CFSP, a coordinated employment and growth strategy, EMU, enlargement, a European Environment Agency, a European Investment Bank, EU institutional reform, JHA, the Social Chapter and EU-wide workers' rights	Support for CAP reform, the CFSP, a coordinated employment and growth strategy, EMU, enlargement, a European Environment Agency, a European Investment Bank, EU institutional reform, JHA, the Social Chapter and EU-wide workers' rights	↓
1994 (O)	Support for a coordinated employment and growth strategy, EU institutional reform, Maastricht Treaty revision, the Social Chapter and EU-wide workers' rights	Support for a coordinated employment and growth strategy, EU institutional reform, Maastricht Treaty revision, the Social Chapter and EU-wide workers' rights	↓

Table 2.1 Continued

Year	*Annual Conference policy*	*Party leadership policy*	*Foreign Office***
1995 (O)	Support for the reform of the EU Budget, CAP and CFP, the CFSP, EMU, a co-ordinated employment and growth strategy, enlargement, an EU industrial policy, EU institutional reform, JHA, the revision of the Maastricht Treaty, plus the Social Chapter	Support for the reform of the EU Budget, CAP and CFP, the CFSP, EMU, a co-ordinated employment and growth strategy, enlargement, an EU industrial policy, EU institutional reform, JHA, the revision of the Maastricht Treaty, plus the Social Chapter	Pro-membership ↓
1996 (O)	Support for CAP reform, the CFSP, economic policy coordination, EMU, enlargement, EU institutional reform and a revised treaty with an employment chapter, plus the Social Chapter	Support for CAP reform, the CFSP, economic policy coordination, EMU, enlargement, EU institutional reform and a revised treaty with an employment chapter, plus the Social Chapter	
1997 (G)	Support for the Amsterdam Treaty, CAP reform, the European Employment Strategy, enlargement, plus conditional support for euro entry	Support for the Amsterdam Treaty, CAP reform, the European Employment Strategy, enlargement, plus conditional support for euro entry	
1998 (G)	Support for EU budget, CAP and CFP reform, the CFSP, economic reform across the EU, enlargement, environmental cooperation, the European Employment Strategy, EU institutional reform, JHA, Social Dialogue, plus conditional support for euro entry	Support for EU budget, CAP and CFP reform, the CFSP, economic reform across the EU, enlargement, environmental cooperation, the European Employment Strategy, EU institutional reform, JHA, Social Dialogue, plus conditional support for euro entry	
1999 (G)	Support for the CFSP, enlargement, plus conditional support for euro entry	Support for the CFSP, enlargement, plus conditional support for euro entry	
2000 (G)	Support for the CFSP, enlargement, plus conditional support for euro entry	Support for the CFSP, enlargement, plus conditional support for euro entry	
2001 (G)	Support for the CFSP, economic reform across the EU, enlargement, the Nice Treaty, plus conditional support for euro entry	Support for the CFSP, economic reform across the EU, enlargement, the Nice Treaty, plus conditional support for euro entry	

Table 2.1 Continued

Year	*Annual Conference policy*	*Party leadership policy*	*Foreign Office***
2002 (G)	Support for the CFSP, economic reform across the EU, enlargement, EU institutional reform, plus conditional support for euro entry	Support for the CFSP, the Convention on the Future of Europe, economic reform across the EU, enlargement, EU institutional reform, plus conditional support for euro entry	Pro-membership ↓
2003 (G)	Support for the CFSP, the Convention on the Future of Europe, economic reform across the EU, enlargement, plus conditional support for the euro	Support for CFSP, a European Constitution, economic reform across the EU, enlargement, plus conditional support for the euro	↓
2004 (G)	Support for economic reform across the EU, plus conditional support for euro entry	Support for a European Constitution, holding a referendum on the treaty, economic reform across the EU, plus conditional support for euro entry	↓

Notes

G = Labour in government; O = Labour in opposition.

* ‘Qualified acceptance’ was a procedural device used by the party leadership to neuter Annual Conference decisions.

** Historically, the Foreign Office tended to dominate the formulation of the British State’s European policy.

There are three notable features about Labour’s European policy. The first is the propensity of the party leadership to follow the generally pro-EU policy of the Foreign Office when in power. The second is the emergence of policy discord between the Annual Conference and the party leadership during the 1946–50, 1975–9 and 1984–7 periods. The third is the seven significant shifts in policy that have occurred over the post-war period.

Support for European integration (1946–60)

Although Labour’s manifesto for the 1945 General Election contained no reference to European integration, it featured significantly as a foreign policy objective of the 1945–51 Labour governments. The post-war aim of the Foreign Office was to maintain an independent foreign policy to safeguard Britain’s Great Power status. A restoration of Empire strategy was deemed unrealistic, whilst the feasibility of an imperial third force strategy was explored by the Foreign Office and Labour’s Foreign Secretary, Ernest Bevin. It was envisaged that the latter would involve some form of European union, and three schemes were devised: Anglo–French economic coordination, the ‘Euro-Africa’, plan based on the common

exploitation of Europe's colonies, and a European customs union. However, the party leadership's *imperial third force* policy, which was not debated or ratified by the Annual Conference, was abandoned in 1948.

The 1947 Conference adopted a resolution in favour of European integration, whilst the 1948 Conference adopted a resolution in favour of a federal United States of Europe as a socialist third force. However, the *socialist third force* policy was limited in its impact, for two reasons. First, the resolution received only conditional support from the National Executive Committee (NEC), which deployed the procedural device of 'qualified acceptance' to neutralise it. Second, although there was a long history of support for federalism within the Labour Party,[2] it had no Cabinet-level champions.

The party leadership ignored the 1948 Conference decision, opting for a policy of *intergovernmental European cooperation*. It insisted that the Organisation of European Economic Co-operation and the Council of Europe should operate on an intergovernmental basis, refused to participate in the Schuman Plan negotiations, opposed British participation in the proposed European Defence Community and opted out of two articles of the European Convention on Human Rights. The NEC subsequently formalised the party leadership's position by publishing a policy statement. Endorsed by the 1950 Conference, the document opposed any moves towards federalism, arguing that European cooperation should not prevent the Labour government from implementing its national Keynesian programme.

Following the creation of the European Union on a supranational basis in April 1951, the Conservatives promoted the concept of a Free Trade Area (FTA) in an attempt to supplant the Six and reinstate the principle of intergovernmentalism. However, France and the United States of America rejected the FTA proposal. Nevertheless, the Conservatives and six other European governments established the European Free Trade Association (EFTA) in November 1959. The Labour leadership supported the original FTA proposals and offered conditional support to the EFTA. However, neither the EFTA nor the principle of free trade was debated or ratified by the Annual Conference.

In October 1961 the Conservatives initiated entry negotiations with the Six, having submitted a formal application in August. During this period, pro-EU forces began to promote entry within the Labour Party, through the cross-party Common Market Campaign and the Labour Common Market Committee. In the late 1960s anti-EU forces, such as the Forward Britain Movement and individuals such as Michael Barratt Brown, Douglas Jay and Peter Shore promoted a number of alternatives to the European Union. These included a trading bloc centred on the Commonwealth and the EFTA, a North Atlantic Free Trade Area and an economic and political alliance with non-aligned countries.

Opposition to entry without safeguards (1961)

At the 1961 Conference the party united to support a policy of *opposition to entry without safeguards*, specifically safeguards regarding the protection of British agriculture, Commonwealth and EFTA interests, and the right to pursue economic

planning and public ownership. However, as George Brown, the pro-EU Deputy Leader, explained, NEC support for the resolution was based on the understanding that if such guarantees were obtained, the party would consider joining the European Union. Once again, the party leadership used the procedural device of ‘qualified acceptance’ to weaken an Annual Conference decision and to maintain the option of entry.

Conditional support for entry (1962–70)

The 1962 Conference agreed five conditions that would have to be satisfied before Labour would support entry: safeguarding Britain’s Commonwealth trade, freedom to pursue an independent foreign policy, obligations to the EFTA, ability to plan the economy and commitment to British agriculture. However, the NEC policy statement declared that, if the five conditions were satisfied, Britain should join. During the Annual Conference debate, Party Leader Hugh Gaitskell stated that entry would result in the loss of Commonwealth markets and that food prices would rise. Politically, he warned that the European Union was not merely a customs union and that political integration would mean the end of 1,000 years of history. However, Brown argued that, on balance, the economic advantages of entry outweighed the costs, asserting that this view infused the NEC policy statement. The policy of *conditional support for entry* was therefore biased in favour of entry. Indeed, the party leadership tabled an amendment in the House of Commons in November 1962 stating that it would support entry, subject to the five conditions. However, French President Charles de Gaulle vetoed Britain’s first application in January 1963.

At the 1963 Conference, in an attempt to avoid party division before the general election, the party leadership instituted the ‘three-year rule’ so as to prevent any debate on the European Union. Consequently it was not debated again until the 1967 Conference.

The 1964 General Election manifesto stated that although Labour would seek closer relations with the European Union, its primary responsibility was to the Commonwealth. Back in power, Prime Minister Harold Wilson reaffirmed the commitment to the five conditions. However, under the influence of pro-EU civil servants, Wilson began to shift in favour of entry. In December 1965 he accepted Articles 25 and 46 of the European Convention on Human Rights, reversing the opt-outs negotiated in 1950. Taken as an executive decision using the Royal Prerogative, neither the Cabinet nor Parliament discussed the change, despite its constitutional significance.

The 1966 General Election manifesto declared that Labour would join the European Union, provided essential British and Commonwealth interests were safeguarded. In November 1966 Wilson announced to the House of Commons that Labour, having reviewed its European policy, had decided to explore the potential for further negotiations. Between January and March 1967 Brown and Wilson toured the European Union to meet representatives of the Six.

The European Commission Vice-President, Robert Marjolin, published the EU

Medium Term Economic Policy (MTEP) in March 1966. Its objective was to coordinate member states' policies so as to tackle the regional, social and structural inequalities caused by integration. Stuart Holland, economic assistant at the Cabinet Office, sent a memorandum to Wilson arguing that the MTEP was Marjolin's attempt to 'get the French planning model adopted by the EU'. Wilson was delighted, 'because it meant that Labour's National Plan was not only compatible with EU membership, but could be reinforced by the MTEP' (Holland 1997: 2–3).

A further indication of Wilson's shift was the European Technology Community (ETC) proposal. In March 1967 Holland suggested that Labour should revise its negotiating strategy, recommending that it should support intergovernmentalism, endorse the MTEP and cooperate with the Six on advanced technology. Wilson subsequently sent Holland on a secret mission to sound out de Gaulle, who was amenable. In the meetings that followed, Wilson argued that an ETC treaty should be signed before any detailed programme of cooperation was agreed, whilst de Gaulle insisted that it should be created on the basis of specific projects. However, Wilson refused to make such a commitment. Reflecting on this episode, Holland (1997: 10) concluded that Wilson's agenda was 'classic Wilsonian short-termism. He appeased the right by applying, and pleased the left by failing in the attempt.'

In April 1967 the Cabinet voted 13 to 8 to reopen negotiations. Labour subsequently published a White Paper setting out its terms. These included transition arrangements for the implementation of the Common Agricultural Policy (CAP), plus safeguards on the balance of payments, Commonwealth trade and regional policy. In the House of Commons debate that followed, Wilson argued that, economically, industry would probably benefit from entry. However, he acknowledged the problems posed by the CAP and the end of Commonwealth Preference. It was estimated that the cost of living would increase between 2.5 and 3.5 per cent, that food prices would increase between 10 and 14 per cent, and that the net cost to the balance of payments would be between £175 and £250 million per year. Politically, he dismissed the idea of a federal Europe, whilst, constitutionally, he stated that EU law would only take precedence in certain areas, claiming that most domestic law would remain unchanged. However, he conceded that entry would involve the surrender of sovereignty, and that, in future, Britain would have to refrain from enacting legislation inconsistent with EU law.

During the debate 37 Labour MPs tabled an amendment opposing the White Paper, arguing that it failed to uphold the conditions laid down by the Annual Conference. Despite a three-line whip, 35 Labour MPs voted against and 51 abstained. However, due to Conservative support, the Labour motion was approved by 488 to 62. Britain's second application was formally submitted in May, without a mandate from the Annual Conference. During this period anti-EU forces established the Labour Committee for the Five Safeguards on the Common Market.

Brown set out Labour's case for entry before EU representatives at a meeting of the Western European Union (WEU) in July 1967. He attempted to reassure the

Six that the fundamental features of the European Union would remain unchanged if Britain joined by declaring that Labour was willing to accept the EU objectives of economic and political union. Critically, only the problematic issue of agriculture was reserved for future negotiations.

The NEC presented a revised policy statement to the 1967 Conference, stating that the party's concerns about entry had been allayed. The Annual Conference endorsed the policy statement by 4.1 million votes to 2 million, whilst a resolution opposed to entry was defeated by 997,000 votes out of 6 million, as was a federalist resolution. However, de Gaulle vetoed Britain's second application in November 1967.

The 1969 Conference endorsed a Parliamentary Report declaring that Labour was committed to entry and was eager to engage in further negotiations. It adopted an NEC policy statement declaring that the result of any negotiations, and the final decision, would be subject to a parliamentary vote. The Annual Conference also carried a resolution containing additional safeguards, on foreign policy, health and the welfare state, which opposed the development of a nuclear-armed federal European Union. Facing the possibility of defeat, Brown accepted the resolution, subject to qualification. He stated that the NEC would accept the resolution on the understanding that the safeguards set out in his WEU speech in July 1967 were included in the resolution. Critically, it should be recalled that the only issue reserved for negotiation in this speech was agriculture; there was no mention of any other safeguards.

Labour published another White Paper in 1970, conceding that the consequences of entry would be even more adverse than the 1967 calculations. Food prices, for example, were expected to rise between 18 and 26 per cent cumulatively over any negotiated transition period, compared to the estimate of 10 to 14 per cent in 1967. Nevertheless, the second leg of Britain's negotiations opened in April, just two months before Labour lost the 1970 General Election. Labour's manifesto declared that it would negotiate from a position of economic strength. However, the manifesto contained the reassurance that if satisfactory terms could not be secured, then Britain could prosper outside the European Union.

The NEC urged the 1970 Conference not to change party policy just because it was in opposition. It subsequently reaffirmed the decision of the 1969 Conference, and rejected a resolution that was opposed to entry by 140,000 votes out of 6 million.

Opposition to entry on Conservative terms (1971)

The Conservatives' principal objective upon gaining office in 1970 was to secure British entry. It published a White Paper in 1971 conceding that food prices would rise and that Britain's contribution to the EU budget would become a burden unless the CAP was reformed. However, it neglected to mention Economic and Monetary Union (EMU), even though the Six had already pledged to create a single currency by 1980. On the issue of sovereignty there was deliberate obfuscation; the White Paper stated that there would be no erosion of national sovereignty.

Labour held a Special Conference on the European Union in July 1971. A resolution pledging that the NEC would produce a definitive resolution on entry, which the party could vote upon at the Annual Conference in October, was carried, whilst an attempt to hold an immediate vote was defeated. Although the Special Conference agreed the suggested procedure and timetable, the NEC pre-empted the Annual Conference by launching a 'no to entry on Tory terms' campaign.

The 1971 Conference endorsed the policy recommended by the NEC, namely *opposition to entry on Conservative terms*, by 5 million votes to 1 million. An amendment in favour of holding a referendum before joining was defeated by 4.2 million votes to 1.9 million, whilst a resolution advocating a United States of Europe was defeated by 3 million votes to 2 million. James Callaghan concluded the debate on behalf of the NEC and pledged that, when elected, Labour would renegotiate the terms. The Parliamentary Labour Party (PLP) followed the Annual Conference by voting to oppose the terms by 159 to 89.

The House of Commons debated a Conservative motion in favour of entry in October 1971. As a result of a secret alliance between the Conservatives and the 69-strong pro-EU wing of the PLP, 356 MPs voted for entry with 244 against in the final division on 28 October. In January 1972 the government signed the Treaty of Accession and published the European Communities Bill. There were 104 divisions during the Bill's passage and, although government majorities fell to single figures several times, not one vote was lost. Using the guillotine measure to expedite its passage, the Bill was passed on 17 October 1972. Britain joined the European Union on 1 January 1973.

Renegotiating the terms (1972–74)

Labour's attacks on the Conservative government following accession focused on the fact that it possessed no mandate for entry, as the British people had not been consulted. During this period Tony Benn launched his campaign for a referendum on entry. In March 1972, following the French decision to hold a referendum, the Shadow Cabinet accepted Benn's proposal by 13 votes to 11. In April the PLP voted 129 to 96 in favour, prompting pro-EU Cabinet members, including Roy Jenkins, to resign.

The 1972 Conference reaffirmed the party's opposition to entry, whilst agreeing a new policy of *renegotiating the terms*. The NEC policy statement listed the six issues upon which Labour would renegotiate: the CAP, the EU budget, powers over fiscal, industrial and regional policy, capital controls, the protection of Commonwealth interests and value-added tax (VAT). The document stated that if renegotiations were successful Labour would put the decision to the people at a general election or referendum. The policy statement was adopted by 3.4 million votes to 1.8 million. A resolution supporting a boycott of EU institutions was carried by 3.3 million votes to 2.8 million, whilst a resolution calling for a future Labour government to withdraw was defeated by only 118,000 votes out of 6 million.

Given the scale of opposition to the European Union within the party, Wilson

was concerned that the 1973 Conference would vote in favour of withdrawal. He wrote in his memoirs: 'I had to lay my leadership on the line, and made it clear that I would resign and face the Party with the election of a new Leader if the NEC recommended Conference to bind us to a policy of withdrawal' (Wilson 1979: 51). His threat was effective. The NEC supported a resolution in favour of a boycott and the holding of a referendum, which was carried by 5.2 million votes to 945,000. However, a resolution advocating withdrawal, followed by the construction of a socialist united Europe, was defeated by 516,000 votes out of 6 million. In December the PLP voted to boycott EU institutions by 140 to 55.

The February 1974 General Election manifesto set out Labour's objectives for the renegotiations: reform of the CAP and EU budget, opposition to EMU, the retention of powers over the British economy, the protection of Commonwealth interests and opposition to VAT harmonisation. Callaghan launched the renegotiations in April. The October 1974 General Election manifesto stated that, within 12 months, a Labour government would give the people the choice, through the ballot box, on whether to retain membership or withdraw.

The NEC supported a resolution at the 1974 Conference insisting upon balance in a future referendum, in terms of finance and media support, between the anti- and pro-EU campaigns. The resolution was carried. However, a second resolution advocating additional safeguards on capital controls, Commonwealth trade, defence, food subsidies, labour movements, parliamentary sovereignty, public ownership, taxation and state aid was also carried, by a majority of 158,000 votes out of nearly 6 million.

Withdrawal (1975)

Following the conclusion of the renegotiations in March 1975 the Cabinet voted by 16 to 7 to accept the revised terms of membership. In Wilson's absence, the Cabinet also agreed to allow ministers to vote against the government. The NEC voted 18 to 11 against the outcome of the renegotiations, prompting Wilson (1979: 106) to threaten resignation again. Policy-wise, the party leadership and the NEC were opposed, whilst the PLP was split. In April a House of Commons motion in favour of staying in the European Union was carried by 396 to 170, mainly due to Conservative support. On the Labour side, 145 MPs voted against, 137 voted for and 33 abstained. The party held another Special Conference in April, where the NEC document in favour of *withdrawal* was adopted by 3.7 million votes to 1.9 million.

During the 1975 Referendum, Britain in Europe led the Yes campaign, while the National Referendum Campaign united opponents of the European Union. The Yes campaign enjoyed a number of critical advantages. It was supported by the government, was backed by most of the business sector, the civil service and the media, and received more money. Labour granted the Yes and No campaigns a total of £125,000 for publicity. However, the Yes campaign managed to raise an additional £1.8 million, whereas the No campaign merely secured an extra £8,610. On 25 June, 67.2 per cent voted Yes and 32.8 per cent voted No. Following the vote the PLP reversed its boycott and sent representatives to the EU institutions.

Reform of the EU (1976–79)

The 1976 Conference debated the NEC policy statement on direct elections to the European Parliament. The document insisted that there was no mandate for direct elections, as it had not been mentioned during the 1975 Referendum. It further argued that the party should oppose such elections because the European Parliament constituted a threat to Westminster. It was carried by a majority of 4 million votes to 2.2 million. The 1976 Conference also endorsed a radical Keynesian programme, termed the Alternative Economic Strategy (AES).

In April 1977 Labour issued a White Paper on alternative electoral systems for European elections. It made no recommendation and agreed to hold a free House of Commons vote. Following a series of divisions, MPs voted by 321 to 222 to reject proportional representation in favour of 78 single-member constituencies. The Cabinet met in July to discuss a policy paper produced by David Owen, which accepted membership, rejected a European federation and supported enlargement. The paper was supported by a majority of the Cabinet.

The 1977 Conference adopted the NEC policy statement, which reaffirmed the party's opposition to supranationalism and re-emphasised the threat posed by the European Union to its industrial strategy. The policy statement reiterated the 1976 Conference decision to seek specific derogations from EU law on energy, regional and social policies, and transport. It pledged to reform the EU aid policy, the CAP and the CFP. It also pledged to oppose direct elections, the EMS, EMU and tax harmonisation, including VAT. A resolution calling for the fundamental reform of the CAP was carried. However, following a plea to maintain party unity, the 1977 Conference rejected two amendments, one of which called for Britain's withdrawal from the CAP. It also rejected a resolution calling for another referendum on membership, and remitted a resolution in favour of amending the 1972 European Communities Act to restore parliamentary supremacy.

In 1978 the European Council reaffirmed its commitment to EMU, launching a new system of monetary coordination: the European Monetary System (EMS) and its Exchange Rate Mechanism (ERM). Callaghan (1987: 493) declared that he 'favoured the general idea as likely to bring more order into the currency markets of Europe and the world'. However, he complained that: 'many people in the Labour Party remained suspicious of what they thought was too close an entanglement with Europe, and this, coupled with my own and the Treasury's belief that sterling was too high to make our entry advantageous' led him to reject ERM entry. In October the NEC rejected the EMS by 16 to 9.

The 1978 Conference rejected withdrawal in favour of a policy of *reform of the European Union*. The Annual Conference carried a resolution calling for the next Labour manifesto to include a commitment to amend the 1972 European Communities Act so as to restore parliamentary sovereignty. The resolution rejected EMU and supported the reform of the European Union. It was carried by 4.85 million votes to 1.64 million.

Callaghan used the leadership veto over policy, so often used by Wilson, to emasculate the policy decisions of the 1978 Conference when drafting the

manifesto for the 1979 General Election. It declared that Labour would seek the fundamental reform of the European Union. It supported enlargement, pledged to reform the CAP and the EU budget, and promised to amend, *if necessary*, the 1972 European Communities Act so as to safeguard parliamentary sovereignty.

Under Benn's leadership the NEC drafted the manifesto for the 1979 European election. Carried by 19 votes to 4, it warned that, in the absence of fundamental EU reform, the party would adopt a policy of withdrawal. In the first direct elections to the European Parliament, three weeks after Labour's general election defeat, Labour gained 17 Members of the European Parliament (MEPs), compared to the Conservatives' 60 MEPs.

Withdrawal (1980–87)

The European policies of the Annual Conference and the party leadership converged under Michael Foot. The 1980 Conference supported a resolution declaring that there had been no progress in reforming the European Union and that Labour should include a policy of *withdrawal* in its next manifesto. The resolution was carried by 5 million votes to 2 million. At the 1981 Conference an attempt to introduce a commitment to hold a referendum before withdrawing was defeated by 5.8 million votes to 1 million. The 1983 General Election manifesto duly included the pledge to withdraw, within the lifetime of one parliament.

The manifesto for the 1984 European election acknowledged that Britain would remain a member of the European Union for the term of the next European Parliament, but pledged that Labour would fight to get the best deal for Britain within it. It called for the fundamental reform of the European Union, opposed the ceding of any additional powers to the European Parliament, rejected the EMS and reserved the option of withdrawal. However, it also included a 10-point action plan that recognised the potential contribution of the European Union to Labour's programme. In the second direct election to the European Parliament, Labour gained 32 MEPs compared to the Conservatives' 45 MEPs.

The European Commission's plan to create a European single market by 1992 served to accelerate the process of European integration. Conservative Prime Minister Margaret Thatcher supported the creation of a single market, believing it would lead to a free market and a free trade area. With Labour opposed, the House of Commons voted by 270 to 153 to incorporate the EU Single European Act into British law.

Labour's 1987 General Election manifesto contained no reference to withdrawal, although it remained official party policy. Instead, it stated that Labour's aim was to work constructively with the European Union to promote economic expansion and combat unemployment.

Pro-membership (1988–)

The attempt to change the party's withdrawal policy began in 1983, following Labour's general election defeat. Once again, Holland was instrumental in

changing the party leadership's position. The Out of Crisis Project, composed of economists and European socialist party representatives, was founded in 1981. The resulting Euro-Keynesian programme, known as the European AES, recommended that member states should pursue a policy of coordinated reflation. Party Leader Neil Kinnock wished to support the project as means of changing the party's perception of the European Union. Holland agreed to help Kinnock by promoting the European AES. He wrote an article for Kinnock, publish in *New Socialist*, the party's journal, briefed the Socialist Campaign Group and the Tribune Group of Labour MPs, obtained the support of John Prescott, ex-leader of the European Parliamentary Labour Group, and joined the NEC International Sub-Committee.

Kinnock was also influenced by John Eatwell, his economic advisor, and by John Smith, the pro-EU Shadow Chancellor. Eatwell believed that 'the collapse of the Bretton Woods System had led to a deflationary bias' and that 'an exchange rate system in Europe was the means of mitigating these deflationary effects'. He also believed that 'the larger scale and scope of European markets could provide a stimulating environment for British industry, particularly the financial services', that is the City of London.[3]

Kinnock later declared that 'the rejection of the withdrawal policy by the voters was clear and absolute'. However, 'because anti-Europeanism was quite deeply rooted in parts of the movement, particularly the trade unions, the change had to be achieved by degrees rather than by a sudden shift'. This was because 'as Labour had already demonstrated, parties were seriously in danger of cracking and then crumbling over the issue of Europe if the matter was not handled with care as well as determination'.[4]

Kinnock's chosen vehicle for changing party policy was the Policy Review, established following Labour's 1987 General Election defeat. Seven policy committees were created, including the Modern World Committee, which was responsible for European policy. Committee member Regan Scott revealed that Kinnock 'packed the committee with pro-Europeans' to achieve his 'new policy of conditional engagement'.[5] The macroeconomic committee considered the economic aspects of Labour's European policy and was chaired by Bryan Gould. He was critical of the City's influence over economic policy, an opponent of the ERM and an ardent defender of the use of the exchange rate as an instrument of policy. However, outmanoeuvred by pro-EU members such as Gordon Brown, John Eatwell and John Edmonds, Gould and his reports were sidelined.

Pro-EU forces, having secured Kinnock's U-turn and marginalised potential opponents, were ready to change party policy. Their opportunity came in 1988 when the European Commission President, Jacques Delors, addressed the Trades Union Congress (TUC). The big trade unions, commanding a majority of Congress votes and attracted to the promise of a 'social Europe', reversed the withdrawal policy of the TUC. Three weeks later they voted to change Labour's policy. The 1988 Conference endorsed the first Policy Review report, which supported EU-wide employment standards plus the coordination of member states' foreign, industrial, regional and social policies. It also carried a resolution

stating that Labour, in conjunction with other parties, should use the European Union to promote democratic socialism. A second resolution calling for a future Labour government to amend the 1972 European Communities Act was remitted. It had taken several years, but the party leadership had finally secured a *pro-membership* policy.

In the post-1988 period, judged in terms of European policy, the Annual Conference has been particularly compliant, consistently supporting the pro-EU position of the party leadership, as shown in Table 2.1. The trend is reflected in the dramatic fall in the number of critical resolutions and amendments submitted to the Annual Conference in the post-1988 period (13) compared to the 1947–87 period (187) (see Table 2.2). It is manifest in the dearth of critical speakers during Annual Conference debates on the European Union: just 10 in the post-1988 period compared to 199 in the 1947–87 period (see Table 2.3). It is also evident in the contrast between the two periods in terms of the party's discourse on European integration, illustrated by Tables 2.4, 2.5, 2.6 and 2.7.The latter point is discussed in more detail below.

Labour entered the 1989 European election on a pro-EU platform, gaining 45 MEPs compared to the Conservatives' 32 MEPs. The 1989 Conference endorsed

Table 2.2 Number of resolutions and amendments on the EU submitted by affiliates to the Labour Party Annual Conference (1947–97)*

Years	*With-drawal from EU*	*Anti-EU*	*Opposition without safeguards, or opposition to (a) EU treaties (b) Terms of entry/membership (c) Specific EU policies*	*Neutral*	*Conditional support for EU*	*Pro-EU*	*Reform of EU*	*Federal-ist*
1947–87**	30	66	91	19	14	29	2	36
1988–97	0	0	13	4	5	37	9	0

Source: Labour Party *Annual Conference Agenda*.

Notes

* Affiliated organisations include constituency Labour parties, socialist societies and trade unions.

** Does not include data for the 1962 Conference, which is not available.

Table 2.3 Number of speakers and their stance on the EU during Labour's Annual Conference debates (1947–2000)

Years	*With-drawal from EU*	*Anti-EU*	*Opposition without safeguards, or opposition to (a) EU treaties (b) Terms of entry/membership (c) Specific EU policies*	*Neutral*	*Conditional support for EU*	*Pro-EU*	*Reform of EU*	*Federal-ist*
1947–87	53	59	87	14	26	80	2	23
1988–2000	0	3	7	1	1	93	2	0

Source: Labour Party *Annual Conference Report*.

Table 2.4 Pro-EU arguments during Labour's Annual Conference debates (1947–87)

Arguments	*Frequency*
• EU provided Britain with a bigger home market	21
• Socialists and trade unionists in the EU wanted Britain to join/stay in	14
• EU was internationalism in action	12
• Entry/membership would raise the British standard of living	10
• EU was a means to control multinational companies	9
• 'Socialism in one country' was impossible	8
• Withdrawal was a dangerous policy (risking the loss of jobs and trade)	7
• Entry/membership would increase economic growth rate in Britain	7
• Britain would lose influence outside the EU	7
• EU enjoyed better wages and working conditions than Britain	6
• EU represented Britain's destiny/future	6
• There was no alternative to the EU; it was inevitable	4
• EU presented an opportunity for socialism	4
• Britain would benefit from EU regional and structural funds	4
• EU provided more aid to developing countries than Britain	4
• EU ensured peace in Europe	5
• EU member states enjoyed higher welfare benefits	5
• Britain was already part of Europe; the key question was what sort of Europe	4
• Treaty of Rome was not opposed to economic planning, nationalisation and state aid	4
• EU helped to contain British nationalism and xenophobia	4
• National sovereignty was an outmoded concept	3
• EU was a fact that needed to be accepted	3
• Commonwealth countries wanted Britain to join the EU/stay in	3
• Markets of the Commonwealth and European Free Trade Association were not sufficient	3
• British home market was not sufficient	2
• EU was not a threat to national sovereignty	2
• EU would enable Britain to gain independence from the United States	2
• EU member states had higher levels of public ownership than Britain	2
• Britain would be poorer outside the EU	2
• Entry/membership would lead to an increase in British exports	2
• Entry membership would benefit the British working class	1

Source: Labour Party *Annual Conference Report*.

Table 2.5 Anti-EU arguments during Labour's Annual Conference debates (1947–87)

Arguments	*Frequency*
• Entry/membership resulted in higher food prices	34
• Common Agricultural Policy was damaging for Britain	33
• Entry/membership worsened Britain's balance of payments and trade deficit problems	33
• EU was capitalist	28
• Pro-EU forces resorted to deceit/propaganda	27
• EU undermined parliamentary democracy	25

Table 2.5 Continued

Arguments	*Frequency*
• EU threatened jobs and policy of full employment	23
• Entry/membership led to an increased in the cost of living/lowered the standard of living	21
• Opponents/sceptics of the EU were not isolationist or 'little Englanders'	17
• British public opinion opposed to entry/membership	17
• Conservative Government had no mandate for entry	16
• Entry/membership resulted in a loss of control/independence	15
• Entry/membership would not benefit the working class	15
• Treaty of Rome provisions for the free movement of capital led to capital flight from Britain following entry	14
• EU membership was a barrier to implementing socialism	14
• Imposition of value-added tax was regressive	14
• EU was opposed to public ownership/state aid	13
• EU membership threatened British agriculture	12
• Britain contributions to the EU Budget were too high	12
• EU would develop into a militaristic/nuclear-armed bloc	12
• Objective of the EU was political union	11
• EU was undemocratic	11
• EU membership damaged Commonwealth trade	10
• Economic and Monetary Union policy was damaging/threatening	10
• Rule by Brussels bureaucrats should be opposed	9
• EU was opposed to economic planning	9
• EU was threat to Britain's regional policy	9
• EU membership contributed to rising inflation in Britain	7
• Treaty of Rome was not negotiable	7
• Common Fisheries Policy was damaging	7
• Treaty of Rome outlawed import and export controls	6
• Entry/membership damaged British industry	6
• EU damaged relations with the European Free Trade Association	6
• EU membership was incompatible with the Alternative Economic Strategy	5
• EU membership would limit a future Labour government's freedom of action	5
• Entry/membership would result in lower economic growth	4
• Britain could stand on its own outside the EU	4
• Europe was wider than the EU	4
• Entry to the EU was irreversible	4
• EU was dominated by cartels/multinational companies	3
• EU was part of the Cold War system	3
• EU was a 'rich man's club'	3
• EU contributed to the post-war division of Europe	3
• Pro-EU case for entry/membership was defeatist	3
• EU was a threat to neutrality	2
• EU was a threat to Britain's foreign policy	2

Source: Labour Party *Annual Conference Report.*

Table 2.6 Pro-EU arguments during Labour's Annual Conference debates (1988–2000)

Arguments	*Frequency*
• Social Chapter would benefit British workers	35
• EU was essential for tackling unemployment across Europe	24
• There was a need to democratise the EU	23
• Enlargement would bring benefits for Britain (including bigger home market)	22
• Economic and Monetary Union would benefit Britain	22
• There was a need to reform the Common Agricultural Policy	15
• Labour had put Britain at the centre/heart of Europe	12
• EU ensured peace in Europe	12
• EU was internationalism in action	11
• EU was important to British exports, jobs and investment	9
• There was a need for a 'People's Europe'	8
• There was a need to strengthen the powers of the European Parliament	8
• EU was an effective means of tackling environmental issues	7
• There was a need for a stronger 'social Europe'	7
• EU was essential for tackling racism and fascism across Europe	6
• Single Market would provide new opportunities for British industry and workers	6
• 'European social model' was preferable to the US model	5
• Globalisation meant that there was no alternative to the EU	5
• Britain would lose influence outside the EU	5
• 'Social dialogue' would help to transform industrial relations in Britain	4
• Labour's debate about Europe was over	3
• Labour was the party of Europe	3
• EU was a means to control transnational corporations	2
• Withdrawal was a dangerous policy (risking the loss of jobs and trade)	2
• Involvement in further European integration was Britain's destiny/future	2
• Britain is part of Europe	2

Source: Labour Party *Annual Conference Report*.

Table 2.7 Anti-EU arguments during Labour's Annual Conference debates (1988–2000)

Arguments	*Frequency*
• Maastricht Convergence Criteria threatened jobs	5
• European Central Bank is undemocratic, deflationary and monetarist	4
• Membership of Economic and Monetary Union involved surrendering power to unelected central bankers	4
• EU needed to solve its democratic deficit	4
• Britain's membership of the Exchange Rate Mechanism was a disaster	4
• Economic and Monetary Union would limit freedom of action for future Labour government	3
• EU membership undermined parliamentary democracy	3

Source: Labour Party *Annual Conference Report*.

the second Policy Review report, which advocated the democratisation of EU decision making whilst supporting enlargement, foreign policy coordination and the Single Market.

The European Commission's three-stage EMU project, agreed in June 1989, was translated into the 1991 Maastricht Treaty. It was originally envisaged that the treaty would include a social chapter. However, the British refused to accept it, leading the other 11 member states to adopt a separate Social Charter. Britain negotiated an opt-out from stage 3 of EMU – membership of a single currency – but participated in the first two stages. Britain duly joined the ERM in October 1990, supported by the Labour leadership and the TUC General Council, plus the Bank of England, the Foreign Office, the Treasury and much of the media.

The 1990 Conference endorsed the third Policy Review report, which supported enlargement and institutional reform. It also carried a resolution recommending membership of EMU and the EMS. The 1991 Conference adopted the final Policy Review report, which highlighted the need to strengthen the supply side of Britain's economy to meet the challenge of the Single Market. It claimed that EMU would reduce business costs and eliminate currency speculation, and suggested that monetary policy cooperation, manifest in the ERM, was both inevitable and desirable. It favoured a London-based European central bank and supported the Social Charter. The Annual Conference also carried a resolution in favour of British membership of the single currency.

The Bill incorporating the Maastricht Treaty into British law was presented to the House of Commons in May 1992. Although MPs were not given the full text of the treaty, only 72 MPs voted against the Bill. However, the Danish No vote in June and the ejection of sterling from the ERM in September represented major setbacks for pro-EU forces, encouraging opponents to embark upon a protracted parliamentary war to stop the Bill. During this period Benn presented his Treaty of Maastricht (Referendum) Bill plus his Commonwealth of Europe Bill as an alternative to the European Union. The Maastricht Bill's parliamentary journey witnessed several rebellions. During the second reading in April 1993 Labour helped the Conservatives to defeat an amendment demanding a referendum on the treaty. The battle culminated in the final reading in May in which the Conservatives secured a 292 to 112 victory, with Labour officially abstaining. However, 65 Labour MPs voted against the treaty and four voted in favour. A further division in July on Labour's amendment to incorporate the Social Chapter produced a 317 draw, with the Speaker casting her vote in favour. The Conservatives then presented a motion to accept the Bill and lost by eight votes. The following day John Major held a confidence vote to overturn the vote of the previous day and the Bill was passed by 39 votes.

Holland resigned from the House of Commons in 1989, followed by Gould in 1992. The former went to work for Delors, whilst the latter, disillusioned with Labour's 'modernisation', retired. Holland produced two reports for Delors which highlighted the need for economic and social cohesion to counterbalance the Single Market and set out the case for a new EU public borrowing instrument to finance the necessary investment. Several European socialist parties supported

Holland's proposals. However, at a European Council meeting in 1996 Prime Minister John Major and German Chancellor Helmut Kohl voted against the principle of EU bonds. When the proposal was tabled again one year later Prime Minister Tony Blair was also opposed, later revealing that he 'had been briefed to argue against any new European financial instruments' (Holland 1997: 26). In 1997 the European Council extended the remit of the European Investment Bank to facilitate the introduction of EU bonds. However, the volume of bonds issued has been lower than Holland recommended; consequently, its macroeconomic impact has been limited.

Between 1990 and 1996 the Annual Conference followed the party leadership line on the European Union. It endorsed NEC policy statements and carried resolutions and amendments which supported the reform of the EU budget, CAP and Common Fisheries Policy, the Single Market, a London-based European central bank, EMU, the ERM and the ratification of the Maastricht Treaty with the Social Chapter. It also supported common policies on defence, foreign affairs, justice and home affairs, enlargement, institutional reform and EU-wide workers' rights. Dissent from this consensus emerged on only two occasions. At the 1992 Conference Benn submitted a resolution demanding a referendum on the Maastricht Treaty. It was defeated, as was a resolution calling for the fundamental revision of the treaty. Opponents of these resolutions insisted that if the treaty fell, Labour would lose the option of reversing the opt-out from the Social Chapter. At the 1995 Conference Austin Mitchell delivered a speech attacking EMU and the European Union more generally.

New Labour's 1997 General Election victory heralded a sea change in Britain's relationship with the European Union, both rhetorically and in terms of policy. Rhetorically, Blair promised to put Britain at the heart of Europe. Policy-wise, where previous governments exercised caution and introduced a measure of reluctance and scepticism in the relationship with the European Union, New Labour pursued an overtly pro-EU agenda.

One of New Labour's first acts was to grant independence to the Bank of England, as required by stage 2 of the Maastricht Treaty. Stage 1 requires member states to abide by the EMU convergence criteria/Stability and Growth Pact (SGP); hence New Labour's decision to freeze public spending in its first two years in office, Chancellor Gordon Brown's 'golden rule' governing public finance and the expansion of the Private Finance Initiative. However, Britain has been repeatedly chastised for breaching, or threatening to breach, the euro rules even though it is not a member of the single currency. New Labour signed the Social Chapter. However, it has delayed or blocked the implementation of several EU directives, including the working time directive, despite the fact that Britons work the longest hours in the European Union.

New Labour supported the 1997 Amsterdam Treaty. In November the House of Commons voted by 392 to 162 to incorporate the treaty into British law, with 31 Labour MPs abstaining. It also supported the 2001 Nice Treaty. A Conservative amendment in the House of Commons in June 2001, calling for a referendum on the Nice Treaty, was defeated by 403 to 150, with 29 Labour MPs abstaining. The

following month the Bill incorporating the treaty into British law was carried by 388 to 151, with 29 Labour MPs abstaining and one MP voting against.

New Labour actively supported the development of the CFSP and secured its objective of EU enlargement in 2004. However, the policy where New Labour's enthusiasm is most evident is that concerning the euro. New Labour's 1997 manifesto set out three preconditions that would have to be satisfied before Britain could join the euro: the Cabinet would have to agree, Parliament would have to vote in favour and the British people would have to say yes in a referendum. In its first term, New Labour's euro policy was ostensibly one of *wait and see*. It decided against joining the first wave of euro members in 1999, and it opted to delay membership until a number of conditions, set out by Brown in October 1997, were met. Five economic tests would have to be passed before any decision was taken: whether there is sustainable convergence between Britain and the eurozone, whether there is sufficient flexibility to cope with economic change, the effect of membership on investment and on the financial services industry, and whether it is good for employment.

Although the official policy in its first term was one of *wait and see*, New Labour's unofficial policy was euro entry. However, the main obstacle to its strategy was public opinion, with a consistent majority opposed to the euro. Consequently, New Labour adopted a policy of *prepare and persuade*, as evidenced by a number of institutional and legislative initiatives, two 'low-intensity' propaganda campaigns aimed at the business sector and the public, and successive interventions by business leaders and EU bureaucrats to augment these campaigns (Mullen and Burkitt 2003). Another obstacle was Rupert Murdoch. Peter Mandelson revealed that New Labour did not attempt a referendum during its first term because Murdoch's media empire would have campaigned against euro entry. Importantly, Mandelson revealed that 'the Cabinet was never consulted; the decision involved only Tony Blair, Gordon Brown, Robin Cook and John Prescott' (Rawnsley 1998).

In June 2003 the Treasury published its assessment of the five economic tests, together with 18 additional documents, and concluded that only one test, the impact on financial services, had been passed. New Labour subsequently set out a road map to euro entry, concluding that several reforms would have to be instituted before Britain could join. These include transforming Britain's fiscal policy, restructuring its housing market and introducing a new inflation index. Other reforms include changing the statute of the ECB, introducing a Bank of England-style symmetrical inflation target, transforming the SGP and increasing labour market flexibility across the European Union. Unofficially, EU reform constitutes the sixth euro test.

There is opposition within the party to the euro. Labour against the Euro was formed in 2002, gaining the support of 37 MPs and 62 councillors, whilst a 2002 survey for ITV found that 27 per cent of Labour MPs were opposed to euro entry. There is also opposition amongst Labour's supporters. An ICM poll in 2002 found that a substantial majority of Labour voters were opposed to euro entry.

New Labour supported the 2002 Convention on the Future of Europe and the resulting European Constitution, which was agreed in June 2004. A Conservative

motion in the House of Commons in March 2004, demanding a referendum on a future European constitution, was defeated by 328 to 212, with 36 Labour MPs abstaining. New Labour argued that there was no need for a referendum; indeed, one minister described the restructuring of the EU treaties as a mere 'tidying up' exercise. However, one month later, following a campaign by the Murdoch press, and another by Vote 2004, which gained the support of 60 Labour MPs, Blair performed a U-turn and agreed to hold a referendum. He also hinted that a second referendum would be held if the first one produced a No vote. It has been alleged that Blair's U-turn, which was not discussed by the Cabinet, was also influenced by Murdoch's threat to withdraw his support from New Labour at the next general election unless he changed his policy.

In April 2004 Labour against a Superstate was formed and claimed the support of over 80 MPs. In June a YouGov poll found that 49 per cent of voters were opposed to the European Constitution, whilst an ICM poll found that almost half of Labour voters would vote against it. Two months later Mandelson was appointed as a European Commissioner, a prime position from which to sell the euro and the European Constitution to a sceptical British public whilst promoting the EU reform agenda. However, despite New Labour's enthusiasm for the euro and the European Constitution, the anti- and pro-EU forces are more evenly balanced, in terms of funds and media support than at the time of the 1975 Referendum. Victory in future referenda is therefore far from assured.

Why did these policy changes occur?

Broadly speaking, Labour's European policy has shifted three times over the post-war period. During the early post-war period Labour was in favour of some form of European integration. It was viewed as a way of avoiding future wars and as a potential vehicle for creating an independent third force between the two Cold War superpowers.

Following the formation of the European Union – on the basis of the 1957 Treaty of Rome which prioritised the free movement of capital and placed restrictions on state aid – many in the Labour Party began to view the European Union as a barrier to the implementation of socialism. Indeed, an analysis of the discourse of Labour Party debates on the European Union between 1947 and 1987 clearly reveals a widespread belief in a *national* socialist strategy (Table 2.5), or at least a critical engagement with it (Table 2.4). Whether it was centre-left support for Keynesian macroeconomics, hard left support for radical Keynesianism in the form of the AES or far left support for the British road to socialism, the left generally believed in the efficacy of national state power to advance socialism. The arguments and language deployed in Labour Party policy documents, resolutions and amendments during this period add further weight to this view.

Following the end of the Cold War and the emergence of the 'globalisation' thesis, whereby nation-states are perceived to be powerless, some sections of the Labour Party have shifted to a pro-EU position. It was argued that national Keynesianism was redundant and that the left faced a stark choice between the

European and US models of capitalism. Those sections have therefore returned to a position of supporting a *European* socialist strategy, as revealed in the radically altered discourse of Labour Party debates on the European Union from 1988 (Tables 2.6 and 2.7).

In addition to these generalisations, a number of specific factors can be advanced to explain the 'tectonic' shift from a pro-European integration position to an anti-EU stance in the 1960s and 1970s:

- the growing influence of the anti-EU Communist Party within the Labour Party;
- the shifting balance of power within the party in favour of the anti-EU left;
- the role of influential individuals such as Tony Benn, the leader of the left who was pro-EU in the mid-1960s and anti-EU from the 1970s, and Stuart Holland, co-architect of the AES.

Similarly, a number of specific factors can be advanced to explain the 'tectonic' shift from an anti-EU position to a pro-EU stance in the 1980s:

- the defeat of anti-EU forces in the 1975 Referendum;
- the shifting position of the party leadership in favour of the European Union – Harold Wilson from 1965 and Neil Kinnock from 1983;
- the subverting of official policy, using procedural devices at the Annual Conference ('qualified acceptance' and the 'three-year rule'), the powers of patronage (Policy Review committee membership) and party loyalty (Harold Wilson's threats of resignation and James Callaghan's veto over the manifesto) to secure a pro-EU policy;
- the defeat of the anti-EU left in the 1983 General Election;
- the perceived redundancy of national Keynesianism, following the 1981–3 'Mitterand experiment' in France and the subsequent demise of the AES;
- the association of Labour Party 'modernisation', under Neil Kinnock, John Smith and Tony Blair, with 'Europeanisation';
- the allure of the 'European social model';
- the 'contamination thesis', whereby the left fears the label of 'little Englander' and thus association with the anti-EU position of the right (Ramsay 1997);
- the end of the Cold War and the perceived defeat of socialism;
- the retreat from Marxist/class analysis of the EU;
- the changes in public opinion, and Labour Party opinion, brought about by pro-EU propaganda campaigns (Mullen and Burkitt 2003, 2005);
- the influence of the United States of America, which supported European integration and British participation in the European Union during the Cold War, and which exerted its influence by covertly supporting elements of the pro-EU left (Wilford 2003);
- the low salience of the European Union as an issue for the general public, which made it easier to change policy.

Conclusion

It is clear that European integration has been contentious for the Labour Party and that the party remains divided on the issue. However, the balance of argument favours those who are sceptical of and/or opposed to the European Union. The socialist case against the European Union, and British participation in further European integration, rests on four principal arguments.

The first argument is the economic and political cost of British membership of the European Union, both historically and in contemporary terms. Although no government has conducted a review of the costs and benefits of membership, Barratt Brown (1974), Burkitt (1974), Holland (1975), Benn (1980), Burkitt *et al.* (1992, 1996, 1997) and Elliott and Atkinson (1998) assessed the economic costs. These included EU budget contributions, the costs of the CAP, the Common Fisheries Policy (CFP) and ERM membership, import penetration and the subsequent loss of manufacturing jobs, the loss of overseas markets and the cumulative trade deficit. Two studies tried to put a figure to these costs. The first, by Jay (1968), estimated the probable economic cost at between £600 and £1,000 million per year. The second, by Podmore and Katz (1998), estimated the combined cost of EU budget contributions, EMU and ERM membership, and the cumulative trade deficit between 1973 and 1997 at £255 billion. This total did not include the costs of the CAP, the CFP, import penetration and subsequent loss of manufacturing jobs, or the loss of markets in the rest of the world. Burkitt (1975), Benn (1980, 1982), Burkitt *et al.* (1992) and Benn and Hood (1993) reviewed the political costs and concluded that the European Union undermined democracy, national sovereignty and Britain's capacity for self-government. More recently, Milne (2004) estimated the current recurring annual net direct cost of membership at 3–5 per cent of gross domestic product.

The second argument is the illusion of the 'European social model' and the false choice between this and the US model of capitalism. Across the European Union, public sectors and welfare systems are being systematically privatised and dismantled by member states as a result of the Single Market, euro and enlargement projects. In short, the European Union is pursuing a neo-liberal rather than a Keynesian project, under which multinational companies (MNCs) are the driving force. Balanyá *et al.* (2000), for example, found a significant relationship between the recommendations of reports produced by European Round Table of Industrialists (ERT), composed of captains of industry from EU-based MNCs, and the policy and treaty output of the European Union. Similarly, Lucas and Hines (2000) highlighted the role of the ERT in the enlargement process. At best, the European Union places considerable constraints on governmental freedom of action, manifest in the euro (SGP) rules for example. At worst, the European Union could overrule and block the implementation of a socialist programme mandated by the British electorate.

The third argument is the difficulty, if not impossibility, of constructing a democratic United States of Europe, modelled on the United States of America, with a supreme parliament, senate, court of justice and federal bank. The

European Union lacks a common culture and language, whilst there is insufficient population movement to create a single, truly European, polity. Furthermore, European parliamentary constituencies are large and therefore remote from voters. Consequently, the public is unlikely to pay the additional, and substantial, EU-wide taxes necessary to fund a federal government. Furthermore, coalition politics and majority voting in an all-powerful parliament could subvert the will of the British people. If the United States of Europe model was a real possibility, a powerful case could be made for the formation of a Europe-wide socialist party to pursue a European socialist strategy. However, this is not the model that is on offer. The European Union is a hybrid of federal and intergovernmental forms that aims to elevate power and decision making away from ordinary people, thus insulating it from democracy. Crucially, the choice of a European Union run by unelected bankers and bureaucrats, or a democratically elected federal European government, has never been offered to the British people.

The fourth, and possibly most compelling, argument is the undemocratic nature of the European Union. Britain's accession to the Treaty of Rome, participation in the Single Market and possible adoption of the euro and European Constitution all involve the surrender of democratic control to the unaccountable Council of Ministers and the unelected European Commission and European Central Bank. As noted by Carey (1995: 18):

> The twentieth century has been characterised by three developments of great political importance: the growth of democracy, the growth of corporate power, and the growth of corporate propaganda as a means of protecting corporate power against democracy.

The historic objective of the Labour Party, however, is to extend democracy at the local, national, European and global levels, not to participate in curtailing it.

The socialist project requires the fundamental reform of the European Union and/or the withdrawal of Britain and others in order to construct a system of voluntary cooperation amongst democratic, independent nation-states. Whether this objective can be achieved is a matter for debate. What is clear, however, is that the long-standing division of the Labour Party over European integration will continue.

Notes

1 An extended version of this chapter, which evaluates the European policies of the Trades Union Congress and the wider British left, can be found at www.andymullen.com.
2 Federalist supporters included Clement Attlee, Fenner Brockway, G.D.H. Cole, Richard Crossman, Michael Foot, Lord Philip Lothian, R.W.G. Mackay, Ian Mikardo, R.H. Tawney and Harold Wilson.
3 Correspondence from John Eatwell, 20 November 2003.
4 Correspondence from Neil Kinnock, 29 January 2003.
5 Interview with Regan Scott on 8 October 2002.

Part I

The economics of a single currency

3 Economic consequences for Britain

Jonathan Michie

Introduction

Europe seems stuck with high levels of unemployment as we enter the twenty-first century, with all the economic and social misery which goes with that. The blame is put alternatively on 'rigid labour markets', a 'too costly welfare state', or new technology – almost anywhere except on government economic policy. Yet the governments of the European Union have been deliberately pursuing deflationary, low-growth, high-unemployment policies, first under the auspices of the Maastricht convergence criteria and now under the post-Single Currency 'Stability Pact'.

The resulting unemployment should come as no surprise. Similar policies were pursued in Britain under the gold standard[1] of the 1920s, with parallel results in terms of deflationary government economic policies and the creation of mass unemployment (Kitson and Michie 1994). It seems that nothing has been learned. The world economy only managed to pull itself out of the Great Depression[2] in the 1930s by abandoning fixed exchange rates, cutting interest rates and boosting growth. Yet when similar policies were advocated prior to 16 September 1992, when Britain was forced out of the ERM against its will by the currency speculators, such policies were denounced as 'anti-European'. But it does our European partners no favours to have our economy in recession, any more than we are currently being helped by our EU partners pursuing restrictive policies.

Unless current European economic policy is reorientated towards the objective of full employment, embracing an active industrial and regional policy, rather than being stuck on the myopic concern with zero inflation, the route forward must once again be based on independent national growth strategies which would not only allow countries to help themselves, but by doing so would help each other. Competitive deflation, not competitive devaluation, was the real 'beggar my neighbour' policy of the 1990s. As the economist Joan Robinson put it: 'Of all bad-neighbourly conduct among trading nations, the worst is to go into a slump' (Robinson 1966).

The ERM

The Exchange Rate Mechanism (ERM) of the European Monetary System (EMS) tried to bring national currencies more or less into line. Britain joined the ERM in

October 1990. The pound was pegged at 2.95 Deutschmarks. This was too high a rate, making goods produced in Britain relatively expensive compared to goods produced elsewhere. This means that market share is lost abroad, but also at home as imports become more competitive against domestically produced goods. The overvalued rate at which the pound was pegged in the ERM therefore caused markets to be lost and production to be cut back, with firms going to the wall and workers being sacked.

Why then was an overvalued exchange rate chosen by the government when they entered the ERM? In part it was for the stated objective of squeezing inflation; what was not stated is the route by which it was hoped it would work, by deliberately making things hard for British firms, thereby forcing them to try to cut costs by turning on their workers, cutting wages and forcing increased work pressures. This is not the first time that governments have allowed the currency to be overvalued in this way. Winston Churchill as Chancellor took Britain back onto the gold standard in the 1920s at an overvalued rate, with Keynes warning at the time, in his pamphlet *The Economic Consequences of Mr Churchill*, of the disastrous likely consequences of this policy, consequences which were to include the General Strike of 1926 (Keynes 1925). Similarly, the first Thatcher recession of 1979–81 was exacerbated by the high exchange rate caused not only by the coming on stream of North Sea oil, increasing the demand from overseas for sterling with which to buy that oil, but also by the high interest rates which followed from the government's monetarist policies. Thatcher's attempts to reduce money supply growth were pursued through increasing interest rates, aimed at reducing the amount people would then want, or be able, to borrow. But the high interest rates also attracted money into the country, pushing up the exchange rate (Michie 1992).

In the inter-war period Britain was indeed forced to abandon the gold standard. And the exchange rate similarly fell after 1981, depreciating nearly 30 per cent by 1986 and helping to fuel the recovery. Likewise, the overvalued rate at which Chancellor Major entered the ERM meant that our membership was always doomed to failure. Yet those who pointed this out at the time were dismissed out of hand. It was said amongst other things that if sterling left the ERM then interest rates would have to rise; this proved false. The leadership of all three major political parties supported continued membership at the overvalued rate. Even if this had been a genuine option, it would have been a disastrous one. But in reality it was not even an option. It was unsustainable. As Bryan Gould has argued, Britain's ERM membership was vitiated by at least three policy mistakes:

> First, we chose a plainly overvalued parity. This was not an accident, but a deliberate attempt to use overvaluation as a means of bearing down on costs and imposing a counter-inflationary discipline. The result, of course, was so to enfeeble our productive economy that the gap between the exchange rate decreed by the ERM and the rate that could be justified by the performance of the real economy widened inexorably and eventually became unsustainable.
>
> Second, the obligations imposed by ERM membership were asymmetrical. The whole burden of staying within the parity bands fell upon the weaker

> economies, who found that, in a vain attempt to maintain short-term competitiveness and to shore up their currencies, they were obliged to try to cut costs through deflationary measures like high interest rates and cuts in public investment. The Germans, on the other hand, whose appreciating D-Mark put constant pressure on the parity bands, recognised no obligation to bring their currency back into line by reflating and cutting interest rates. It was for this reason that the ERM became a deflationary engine. It was no accident that western Europe became the world's unemployment black spot.
>
> Third, the ERM itself changed in nature. It ceased to be a 'crawling peg' arrangement – a sensible means of securing greater exchange rate stability by damping down excessive market volatility. It became instead the essential precondition for and means of the transition to a single currency. As a result, no adjustments could be permitted. The parities had to be set in concrete. Such inflexibility was inevitably shattered into fragments by the sheer force of economic realities and market pressures.
>
> (Gould 1993)

So the problems of the ERM lay deeper than just having joined at the wrong rate. It was a high-unemployment mechanism, because all the pressure was on the weak economies to take action, rather than on the strong ones.[3] And worse, that action was designed more to prop up the currencies of the weak economies than to strengthen those economies' productive potential, which is the only sustainable basis for maintaining a healthy currency. Increased interest rates were ordered. These depress investment plans and leave the economy in question further weakened. Yet it is most likely the weakness of the economy that underlay the weakness of the currency in the first place. So a weak economy produces a weak currency; the ERM then requires the government in question to raise interest rates; and increased interest rates squeeze the country's economy, leaving it still weaker.[4]

The Maastricht Treaty

The three key points of the Maastricht Treaty were as follows:

All power to the central bankers

The Central Bank would be independent,[5] that is independent of any democratic influence, control or accountability. The electorate of Britain and of the European Union would no longer be able to decide on, or even influence, monetary policy. Indeed, such influence would be outlawed. This is fundamentally undemocratic. It is true that the Bank of England was made independent by the Labour Government elected in 1997, but the Chancellor Gordon Brown at least pledged that new mechanisms would ensure that the Bank would nevertheless be accountable (although it is true that at the time of writing the proof of this is yet to be seen).

Price stability

Not only would the central bankers be independent of the electorate, they would be constitutionally prevented from prioritising full employment; their one primary objective would be to achieve and maintain 'price stability' (this is referred to several times; see, for example. Article 3a). Everything else would have to be secondary, 'without prejudice to this objective' (of price stability – same Article). Why, then, did the Treaty's drafters have such a mania for price stability? And should we object to this? The idea of price stability is often presented as preferable to inflation because it would be more stable, in the sense that it would be easier to hold inflation at that zero (or low) rate than it would be to hold inflation stable around a higher rate. But there is no reason why this should be so. The inflation rate is the average of thousands of price movements, some falling, like the price for personal computers at the moment, some stable and some rising. If zero inflation is achieved it would not be because prices were stable, but because these movements happened to cancel each other out on average. And there is no reason why that average rate of inflation should remain static just because it was previously averaging at a value of zero or 1 per cent, rather than say 7 or 8 per cent. At a more practical level, the reason for the Maastricht Treaty's preoccupation with the rate of inflation is because it arose from the deliberations of the Delors Committee (composed largely of bankers) before the European Union's economy slumped into its early 1990s recession. In part, then, Maastricht was just yesteryear's Treaty, focusing on issues of the 1980s when what is needed are policies for expansion and employment. The other problem with the Treaty – and now with the post-Single Currency 'Stability Pact' – is that the goal of stable prices is not to be pursued through positive interventionist measures, such as price controls or the rejuvenating of industry, which might allow cost increases to be absorbed by productivity increases rather than being passed on in higher prices. The way that progressive economic policies can help tackle inflation are set out in detail by Deakin *et al.* (1992), but the key point is that low inflation should be pursued on the basis of a strong economy which can absorb cost increases (see also Michie and Wilkinson 1992, 1993). The Treaty instead limits the economic policy options to the free market pursuit of monetarism, plus rate capping.

National rate capping

Government borrowing in member states is capped at 3 per cent of national income (GDP). Similarly, government debt must be kept below 60 per cent of GDP. If GDP falls – as it did in Britain throughout 1991 and 1992 – this could require debt to be cut in line, which could exacerbate the decline in national income itself. Also, the Maastricht Treaty sets the debt criterion in terms of gross rather than net debt – that is, totally ignoring all assets. This is a very narrow view of the government's balance sheet. In effect, it forbids governments to take account of even their most liquid assets in setting fiscal policy. Selling assets to pay debt (for example, through privatisation) – which in reality leaves the government no better

off, since their assets will have fallen – is seen as an improvement. Indeed, the situation is even worse than this, because under the Maastricht conditions the government's performance is thought to have improved even if it sells off assets for less than they are worth. The amount of money brought in from the sale, however low, is seen as pure gain in reducing gross debt, while the loss of the asset is totally ignored.

Maastricht and the alternatives

On alternatives, first, there is no reason to have any such rules; the United States of America does not put any such rules on its states, and the British Government never used to put such rules on its local authorities until the Conservative governments of the 1980s introduced rate capping. Second, on fiscal redistribution, the MacDougall Report (Commission of the European Communities 1977) suggested that a Community budget equivalent to 7 per cent of GDP would be necessary just to tackle 40 per cent of existing inequalities, yet the budget at present is set at 1.27 per cent; the more ambitious proposal rejected at the 1992 Edinburgh summit was for this to rise to only 1.38 per cent.

There would be something to be said for creating a new superstate, with a single government, fiscal policy, industrial policy and so on. One attraction would be the power to intervene in the economy to force through socially beneficial outcomes. But it is quite dishonest (or else naive) to present Maastricht or the Single Currency as representing anything along these lines. It represents the precise opposite: an attempt to roll back the state on a European scale, to give capital free reign.

It is sometimes argued that the power of the international markets to dictate to nationally elected governments is such that no one country can any longer defend its currency. But this is hardly new. It is true that this power has been boosted in recent years by the free-market, deregulatory policies pursued by governments. But probably the clearest example of such a process, designed to increase the power of multinational capital and financial markets, has been the programme of increased European Community/Union integration. It is quite wrong to interpret this process as a reaction to the increased power of multinational capital. On the contrary, the Single European Market programme[6] and the single currency have shifted the balance away from governments and in favour of private capital.

To respond effectively to the challenges of growth and employment will require the exact opposite of everything that the single currency process represents. The single currency increases the leverage of international markets to behave exactly as they wish, and prevents elected governments from pursuing the policies on which they were elected – unless of course these happen to coincide with the interests of those financial markets. And this is therefore likely to happen: the policies of political parties will become determined less and less in response to people's aspirations and more and more by what is deemed acceptable to the continued undisturbed operation of international financial markets and multinational corporations.

Background to Maastricht

The '1992' process required all member states to abolish exchange controls, thus allowing capital to flow freely across borders. (The Thatcher Government had of course already abolished Britain's exchange controls in 1979.) This, the Commission argued, would increase economic welfare, since the money would be able to travel across frontiers in order to be put to more productive use. Instead the money went into speculation. Only 5 per cent of all capital flows now relates to trade in goods and services, or to money spent on holidays or to any other real activity. The remaining 95 per cent is conducted by foreign exchange dealers trying to second-guess each other to make a speculative profit.

Having proposed and successfully implemented this financial free-for-all, on quite spurious grounds, the European Commission then went on to argue that it was contradictory to maintain separate national currencies – the pound sterling, the franc, the D-Mark and so on. If there were no longer any restrictions on capital moving from one of those countries to the other, it was argued, then individual member states would no longer be able to pursue independent monetary policies; if they lowered interest rates below those operating in the other countries, money would just flow out. So since abolishing exchange controls had removed the member states' ability to pursue their own independent monetary policies, they might as well recognise the fact and go the whole way: abandon their separate currencies and hand monetary and interest rate policy over to a central bank (and thereby also give up any exchange rate policy, since the countries would no longer have separate exchange rates to adjust). An alternative would have been to reintroduce exchange controls.

Instead we got Maastricht, which stipulates that exchange controls be outlawed forever and that a single currency be adopted. Maastricht, by removing any possibility for currency realignment between member states, and by removing any possibility for lowering interest rates below those in other EU countries, would make the ERM permanent and compulsory. It is true that, with no separate currencies, the weakness of one economy would no longer be signalled by a weak currency, yet the lack of a signal would not abolish the structural problem. Instead, the lack of industrial competitiveness of that geographical area would lead to a loss of industry and jobs, leading to a downward slide into relative economic decline. As Wynne Godley has argued:

> It is thus an extraordinary fact about Maastricht that the only new institution to be created is a new independent central bank to run monetary policy. How is the rest of economic policy supposed to be run? How in particular is fiscal policy supposed to be determined? The authors of the Treaty appear to think that provided you have a central bank to conduct monetary policy, fiscal policy and every other aspect of economic policy can be resolved by laying down one or two simple rules, for instance that countries should normally balance their budget. Now I think this is a very impoverished and inadequate proposal, and I am forced to the conclusion that it could only have been made

> by people who think that nothing more is needed. That is, people who follow the new consensus and are prepared to base all their recommendations on the idea that economies are basically self-righting systems. It should be remembered that the Delors Committee, which was the forerunner of Maastricht, was predominantly composed of central bankers; the proposal to place all power in the hands of the central bank should perhaps not be so surprising. . . . we have been down this road before. The need for active fiscal and exchange rate policies in the 1920s came up against the orthodoxy of the day, that public spending would crowd out private investment and that currency adjustments could be effected with a fixed exchange rate system by forcing down domestic wages and prices. Those truths were wrong then and they are wrong today.
>
> (Godley 1993)

The economics of a single currency

There are obvious attractions to having a single currency across countries that have high levels of trade with each other. Equally, even the most ardent supporters of the single currency proposals would admit that there are potential problems; indeed, if it were not the case that there were real difficulties, then surely more countries would by now have tried to tap the benefits by merging their currencies? The more rational supporters of Maastricht will agree that there are costs and potential dangers, but argue that these need not be overwhelming. Thus, for example, individual countries at the moment have single currencies without their weak regions spiralling into decline. So surely a single currency area covering all 25 member states could operate in the same way as individual countries do at present?

There are two key reasons why this is not the case. First, the Maastricht Treaty could have been quite different. It could, for example, have proposed a single currency alongside a democratically accountable central bank (a bank committed to the pursuit of economic development) and allowed national governments to tackle unemployment, and expand public services through government borrowing. Instead of this, Maastricht lays down that the single currency will be administered by central bankers who are accountable to no one and who are committed to trying to reduce inflation to achieve 'stable prices' and to imposing rate capping on EU governments through restrictions in the form of rigid limits on national public expenditure.

The second problem is that the Maastricht Treaty would not provide the sort of economic mechanisms that limit the decline of weak areas within existing 'single currency areas'. Within a single country such as Britain, the government's revenue – in the form of income tax, VAT, company taxes and the like – is collected from all areas of the country. Similarly, the money is spent on health, education, unemployment pay, housing and other welfare benefits and so on in all areas of the country. Now, if one area in particular suffers bad times there is an automatic transfer of resources from all the other areas of the country to that area. This helps prevent the depressed area from falling into a spiral of decline. If this one area hits hard times, then the profits of the companies operating in that area will fall, so they

will pay less profits tax to the central government. If people are made unemployed they will pay no income tax. And those who remain in work may, for example, earn less overtime pay, and so they may also pay less income tax than before. The result is that less money flows from that particular area of the country into the Treasury coffers. And the same process works on the spending side. More people in that area will receive unemployment pay from central government. More money will go to that area in the form of housing benefit, social security and other transfers. So a higher share of national government spending will go to that area of the country. All this happens automatically without the government actively doing anything. It involves no decision making.

This process is referred to as 'fiscal transfers', since it refers to government spending (fiscal policy) and it results in money being transferred automatically from areas that are prospering to areas in economic difficulty. It operates through the tax and benefit system affecting the whole country (the single currency area). No equivalent process would be in operation in Maastricht's new single currency area because the vast bulk of taxation revenue and public spending would remain locked within the existing nation states – the new regions of the European superstate. So the automatic transfer between regions would not take place. The poor would just get poorer. And this in turn would undermine the revenue base from which benefits are funded.

If a country's currency is overvalued and its goods are uncompetitive, both at home and abroad, this will tend to cause bankruptcies and unemployment. This in turn usually forces a devaluation (or depreciation of the currency) to remove the specific problem. With a single currency that possibility will be removed as far as, say, the British economy goes in relation to all the other countries within the single currency, and also possibly with the rest of the world. There is the additional problem that even if the rate we join a single currency at is appropriate, it is likely – assuming Britain's continued relative economic decline (see Kitson and Michie 1996a) – that after a few years a depreciation of Britain's currency against Germany's would be required. But this would no longer be possible. Kaldor (1978) always warned that, in the Common Market, Britain risked becoming the 'Northern Ireland of Europe'. There is no guaranteed 'European' fate which all will enjoy equally, regardless of policies, exchange rates and so on. It is quite possible to become a declining region, locked into a vicious cycle of decline.

Would a single currency avoid balance of payments deficits?

One argument which is sometimes put in favour of a single currency, and which is simply wrong, is that if we had the same currency as France, Germany and the other EU countries, then we would no longer have a balance of payments deficit with them. In fact, however, the deficit would still be there. More money would still be going out of Britain than was coming in. What would change is that this deficit, and this drain, would no longer be recorded. And it would no longer be seen as the duty of the government to do anything about it. So to that extent, the underlying

problem would actually be made worse. This real imbalance in economic activity would have to be balanced by falling relative income and wealth in Britain, a process that would continue until we could no longer afford the imports which were causing the problem. People would be made poorer; jobs would be lost. However, as the economy becomes impoverished, less would be bought from domestic firms as well, so some of these would be forced out of business. We thereby lose any exports those firms may have had, and some of their custom will go not to other domestic firms but to imports. Hence the slide into poverty does not just restrict imports, it also damages exports. And the actual shortfall of exports from imports will not necessarily be made good. It could even deteriorate. In that situation there remains little to prevent the declining region of the single currency area from sliding further into poverty. The one lifeline would be the fiscal transfers that would be missing in this single currency area. Emigration is then all that is left, although even that does not necessarily improve the well-being of those left behind, particularly if it is the well trained who get the job offers elsewhere.[7]

A similar process would operate with what is at present Britain's balance of payments deficit with non-EU states, which would likewise be apparently abolished and become one component of the European Union's balance of payments with the rest of the world, in the same way as, say, Yorkshire's trade is at present subsumed within Britain's balance. This bookkeeping transfer would simply disguise the fact that there was a net outflow of money from what would by then be the British component of the greater Single Currency Area.

Monetary and political union

If the monetary integration of several countries into one is thought desirable, then it should be seen as the final act of economic, industrial, social and political integration. Putting it first threatens to undermine the whole process. Above all, if monetary policy is to be centralised, then so must all the other aspects of government economic policy. Maastricht would in effect do away with all these other aspects, such as any scope for active taxation and public spending policies, leaving the European Union's economy engineless and rudderless.

A single currency could only be considered acceptable within an EU-wide taxation and benefit system, with massively expanded regional transfers from rich to poor parts of the Union to ensure real economic convergence, and with living standards and employment levels moving closer together throughout the Union rather than further apart. The sort of substantial increase in regional policy spending required was ruled out by the December 1992 Edinburgh summit, and any suggestions that there should be an EU-wide tax and benefits system has been totally rejected whenever the subject has been raised. There seems no prospect that the richer countries are prepared to see very substantial income transfers to poorer regions, either in the form of regional policy or through the automatic transfers of a tax and benefit system.

EU policies for jobs

The European Union's December 1993 biannual summit was billed as the one that was to tackle unemployment. Indeed, Delors warned that the Union's unemployment total could be heading for 30 million by the late 1990s if the policies in his December 1993 White Paper were not adopted. Similar sentiments were articulated by the Union's (then) social affairs commissioner, Padraig Flynn, who described the White Paper as a plan for creating 20 million jobs by the end of the decade. At the same time, Mitterrand was calling for a doubling of the Union's spending on infrastructure and growth projects – as was Delors, who was proposing in particular a widening of the programme to include investment in labour-intensive sectors such as housing, as well as the subsidising of borrowing for small and medium-sized enterprises. Even these rather modest proposals were scorned by the German and British governments. Indeed, less than half the £5.6 billion earmarked for recovery projects by the European Investment Bank had been committed by the end of October 1993, with Commission officials blaming the low take-up on the lack of commercially viable investment projects – hardly surprising in a recession – and because companies were failing to provide the matching finance required from the private sector.

While the Delors White Paper (Commission of the European Communities 1993b) was therefore welcome insofar as it went some way towards shifting the focus of policy onto the problem of unemployment, it remained hopelessly compromised by its failure to break from the policy straitjacket within which the Maastricht Treaty had trapped governments.[8]

An additional policy idea from the Commission has been to introduce reductions in employer taxes on unskilled labour in particular. On the general idea of an employment subsidy, expanded public employment would be a more effective method of tackling unemployment, particularly if there are either inflation or balance of payments constraints (Glyn and Rowthorn 1994). The specific idea of a differential subsidy for unskilled work – generally defined in these contexts as low-paid work, which raises a rather separate issue of why skills such as cooking or cleaning tend not to be recognised as skills – risks reducing firms' incentives to improve productivity and upgrade productive techniques (Michie and Wilkinson 1995).

Behind the talk of jobs packages, therefore, lies the longer-term agenda of economic and monetary union. What has been amply demonstrated in the academic and policy literature is that measured against the criteria for being an 'optimum currency area', the present 25 member states (never mind a Union with additional members) falls some way short, and if the process of integration is to proceed, this shortfall would have to be made up – without straining cohesion to breaking point – by active industrial and regional policies to ensure the continual (not just one-off) economic adjustments to so-called 'shocks' and, more generally, to different levels and growth rates of output and productivity.

With talk today of a 'two-speed Europe' – with some member states having adopted the single currency and others not – it is worth recalling that the ill-fated

gold standard did not collapse in one go in the 1930s: some countries attempted to maintain the fixed exchange rate system, thus heralding a two- (or multi-) tier system (see Kitson and Michie 1994). The ones who stuck with the system grew more slowly; those who left first grew fastest. Hence the 'speed' with which countries move towards fixed exchange rate systems should not be confused with the speed at which their economies will grow. In a two-speed Europe the 'slow' lane may be preferable.

Of course, one of the stock responses to any call for growth is to refer to the expansionary policies of the Mitterrand government in 1981 and the subsequent U-turn of 1983. The orthodox interpretation of this experience is that the Keynesian policies were discovered to be unsustainable because of balance of payments and exchange rate constraints and hence had to be abandoned. This is (as argued by Halimi *et al.* 1994) simply false: these difficulties were not learned from the 1981–3 experience in France but were perfectly well understood and stated quite explicitly by, amongst others, the French Socialist Party before taking office. The problems which any government pursuing such expansionary policies would encounter were documented in advance, as were the additional policies which would be necessary to see through the expansion –including the use of trade policies to ensure that imports grew only in line with exports (see Kitson and Michie 1995a, 1995b). The point is that no attempt was, in fact, made to introduce these additional, necessary, policies; the government instead chose the beggar-my-neighbour route of 'competitive disinflation'.

While coordination is preferable (as pointed out by Kalecki in 1932), there are nevertheless viable programmes for raising employment in a single country; indeed, the only way of building support for an EU-level expansion may be through the contagious impact of a successful expansion of employment in one country. Indeed, the 'cooperative' route – of completing the internal market and pursuing economic and monetary union – has tended to increase industrial concentration and exacerbate regional disparities; instead an active industrial policy is needed to ensure the development of industrial activity outside the European core. To consider the nature which such an interventionist strategy to bolster industrial performance might take, it is necessary to draw a distinction between the notion of a developmental state, organised and concerned to promote economic and industrial development, on the one hand, and a regulatory state concentrating on competition policy, on the other,. A broadly conceived industrial strategy (as opposed to just a 'policy') is needed to offset the forces of cumulative causation which otherwise will increase disparities and exacerbate the under-utilisation of resources in backward regions in particular.

Current levels of unemployment are a reflection of the political priorities attached to different objectives of economic policy. The low demand created by monetarist and restrictive economic policies has eroded the potential to produce: plant capacity, management structures, sales organisation, skilled and experienced labour and the number of firms have all settled down at a level consistent with high unemployment. Increased demand is therefore needed, but it would have to be sustained if capacity is to be rebuilt. This is unlikely with an independent European

central bank dedicated to the achievement of price stability. The emphasis has to be shifted towards restoring full employment.

Conclusion

Unemployment in Europe is due to the interrelation between macroeconomic policy, balance of payments constraints and de-industrialisation. The idea of pursuing active macroeconomic and industrial policies has given way to an adherence to monetarism, privatisation and labour market deregulation. Yet the resulting growth in low pay, poverty and unemployment has, ironically, placed an increasing burden on the public purse. At the same time, productive efficiency is harmed by the resulting instability in the labour market – particularly within the increasingly low-paid sectors – and the loss of incentives for producers to upgrade their productive systems. A vicious circle of low-wage, low-productivity, low-investment activity is generated, leading to loss of competitiveness and growing unemployment, with the increasing burdens on the exchequer provoking yet further moves down the recessionary spiral (Michie and Wilkinson 1994, 1995).

An alternative agenda would include, first, pushing for global expansion rather than being the most orthodox, 1920s-style block in the world. Second, there are a series of measures (such as re-establishing exchange controls) which there seems little hope of getting adopted, but, to paraphrase Keynes, just because people won't listen to sense is no excuse for talking nonsense. The fact that such policies would be an improvement on the current state of affairs should still be pointed out. Third, there are things which would appear acceptable to call for even in today's free-market climate, such as keeping the government responsible for monetary policy rather than handing it over to unaccountable central bankers; keeping the government responsible for fiscal policy, i,e. abandoning the Maastricht Treaty's restrictions; keeping the possibility of currency realignments in the event of one member state's output becoming uncompetitive, rather than adopting a single currency; and restoring the right to pursue interventionist industrial policies which are increasingly falling foul of free-market dictats from Brussels. In other words, member states should pursue those industrial, interest rate, exchange rate and fiscal policies that were in force before most of them became outlawed by the Maastricht Treaty.

What is wrong is the free market, laissez-faire character of the process of European integration at present. So the basic point about what needs to be done is that European governments and the European Commission should stop introducing 1920s-style policies and rules; the countries of Europe should then pursue interventionist policies to tackle unemployment etc., and should cooperate internationally over it.

The power of international capitalism to dictate to nationally elected governments is not new, although it is true that it has been boosted in recent years by the free-market, deregulatory policies pursued by governments. Probably the clearest example of such a process, designed to increase the power of multinational capital and financial markets, has been the programme of increased European

Community/Union integration. It is quite wrong to interpret this process as a reaction to the increased power of multinational capital; on the contrary, the Single European Market programme and now the single currency have themselves deliberately shifted the balance away from governments. EMU is at heart a political process that will prevent governments – whether at national or EU level – from pursuing policies to promote economic and social welfare. Such a scenario is no more sustainable now than when it was last in place, namely in the 1920s and 1930s. It is likely to come to the same unpleasant end, with individual countries being eventually forced to take action regardless of the power of international capitalism. But with the European political elite so wedded to the laissez-faire politics of the single currency, any attempt by the population to insist that they should be allowed to express political preferences risks taking ugly nationalistic forms – against the 'internationalism' of the European central bankers and the entire existing political elite.

Notes

1 A country is said to be on the gold standard when its central bank is obliged to give gold in exchange for any of its currency presented.
2 The 'Great Depression' refers to the global recession of 1929–32.
3 More responsibility should have been placed on those countries whose currencies were at the top of the currency range to take action, rather than have the burden falling on those economies already in difficulty. The stronger economies could cut interest rates and boost government spending. As their economies expanded, they would be likely to import more. And as their currency is offered on the foreign exchange markets to pay for those imports, its price against other currencies would tend to decline back towards its central rate.
4 On the importance of creating industrial capacity as a progressive way of overcoming balance of payments and inflation constraints see Michie and Grieve Smith 1996, in particular the chapter by Kitson and Michie (1996b), and also Kitson and Michie 1996a.
5 See for example the 'Protocol on the Statute of the European System of Central Banks and of the European Central Bank' at the end of the *Maastricht Treaty*.
6 The Single European Market (SEM), also known as the Internal Market or simply '1992', consisted of a timetable of 300 measures agreed at the Milan EC summit of 1985 in preparation for 1 January 1993. Also known as the Cockfield plan after Commissioner Cockfield.
7 The argument that balance of payments deficits do not matter, or that they would be eliminated with a single currency, are comprehensively demolished by the contributions in *The Economic Legacy* (Michie 1992) from Brian Reddaway, from Ken Coutts and Wynne Godley, and from John McCombie and Tony Thirlwall.
8 For a full critical assessment of the Delors White Paper, see Grieve Smith (1994).

4 What type of European monetary union?

Malcolm Sawyer and Philip Arestis

Introduction

The creation of a monetary union inevitably involves the use of a single currency for the payment of taxation and that prices, wages etc. are denominated in that currency. Further, a single currency inevitably involves the creation of a single monetary authority (central bank) with the power to set monetary policy. But there is little else that follows inevitably from the creation of a monetary union. There are, though, a host of economic policy and institutional arrangements which surround the euro and its introduction and which would have profound consequences for the effectiveness of the single currency and, more generally, the economic well being of the European Union. In this brief chapter we indicate some of the features of the institutional and policy arrangements surrounding the implementation of the euro and hint at some alternative ones.

One particular and notable feature of the creation of the European Monetary Union is that in effect the only economic institution which has been created at the European level is the European Central Bank (ECB). The creation of other institutions at the European level has been noticeable by their absence. A further feature of the EMU is the constraints which are imposed on national governments in respect of budget deficits and government debt. Specifically, there are limits on budget deficits of 3 per cent of GDP, and failure to meet that requirement could lead to a series of fines depending on the degree to which the deficit exceeds 3 per cent. The Stability and Growth Pact, which has been agreed to govern the operation of the eurozone, details 'escape' clauses which allow a member state that has an excessive deficit to avoid sanction in the event of an economic downturn. Nevertheless, this upper limit of 3 per cent of GDP for budget deficits means that, during the course of the business cycle, budgets may well be in surplus or small deficit (given the large swing in the size of deficits during the business cycle), and national governments will be restrained in responding to recessions.

The Stability and Growth Pact and the Maastricht Treaty (along with the convergence criteria for membership of the euro) reflect a particular neo-liberal agenda. The Maastricht Treaty, which provides the institutional framework for the introduction of the single currency, was signed in late 1991, a time when neo-liberal ideas held sway and political power was generally held by the right.

Neo-liberal ideas still prevail though perhaps are in some decline, as evidenced by the electoral victories of centrist parties in many of the EMU countries. But the neo-liberal agenda has moulded the environment within which the euro will be introduced. The euro (at least for those 12 countries which have signed up) is embedded within an institutional and policy setting which we have elsewhere described as 'new monetarism' (Arestis and Sawyer 1998). It is the implicit argument of this chapter that economic policies reflecting such neo-liberal agenda will not be successful.

This chapter is organised into three main sections. First, the role of the ECB is critically examined. It is argued that the ECB is undemocratic and has been given too narrow a remit. Further, the policy instrument at the disposal of the ECB (that is interest rates) is inadequate for the purpose of controlling inflation (or indeed anything else).

Second, there is a woeful lack of institutions and policies operating at the European level to support the development of a successful European economy. Specifically there is a lack of a European level fiscal policy (or even coordinated fiscal policies across nations) which could be used to smooth fluctuations in economic activity over time.

Third, there is no serious attempt to reduce disparities between regions (in terms of unemployment, employment, income etc.). There has been a specific rejection (at the Nice summit in November 2000) of the development of a European-level social security system.

European Central Bank

The creation of a so-called independent European Central Bank was much in line with the economic doctrine which we have elsewhere (Arestis and Sawyer 1998) described as the 'new monetarism'.[1] The essential features of new monetarism are:

1. Politicians in particular, and the democratic process in general, cannot be trusted with economic policy formulation with a tendency to make decisions which have stimulating short-term effects (reducing unemployment) but which are detrimental in the longer term (notably a rise in inflation). In contrast, experts in the form of central bankers are not subject to political pressures to court short-term popularity and can take a longer-term perspective where it is assumed that there is a conflict between the short term and the long term.
2. Inflation is a monetary phenomenon and can be controlled through monetary policy. The money supply is difficult (or impossible) to control directly, but the central bank can set the key interest rate (the 'repo' rate) to influence monetary conditions, which in turn influence the future rate of inflation.
3. The level of unemployment fluctuates around a supply-side determined equilibrium rate of unemployment, generally labelled the NAIRU (non-accelerating inflation rate of unemployment). The level of the NAIRU may be favourably affected by a 'flexible' labour market, but it is unaffected by the level of aggregate demand or by productive capacity.

4 Fiscal policy is impotent in terms of its impact on real variables and as such it should be subordinate to monetary policy in controlling inflation. It is recognised, though, that the government budget position will fluctuate during the course of the business cycle, but in the context of an essentially passive fiscal policy.

The independent ECB is given the task of using monetary policy to control inflation. Fiscal policy is largely neutered and constrained by the 3 per cent limit on budget deficits with no EU-level fiscal policy.

There are (at least) three basic objections to the manner in which the ECB has been set up. First, there is the essentially undemocratic nature of the ECB in the name of protecting its independence. Article 107 of the amended Treaty of Rome states that:

> When exercising the powers and carrying out the tasks and duties conferred upon them by this Treaty and the Statute of the ESCB, neither the ECB, nor a national central bank, nor any member of their decision making bodies shall seek or take instructions from Community institutions or bodies, from any government of a Member State or from any other body. The Community institutions and bodies and the governments of the Member States undertake to respect this principle and not to seek to influence the members of the decision making bodies of the ECB or of the national central banks in the performance of their tasks.

This precludes influence from say the European Parliament on the decisions of the ECB, even though the ECB is the only European-level economic policy-making body.

Second, the objective given to the ECB when setting monetary policy is the achievement of low inflation. Objectives such as a high level of economic activity, low unemployment or even the external value of the euro are to be considered. If the 'new monetarism' were valid, this would not matter since it is deemed that monetary policy does indeed control inflation, and that the level of unemployment is unaffected by monetary policy. But in the real world, the setting of interest rates has a differential impact across regions and nations, and can have an influence on the exchange rate (and thereby on exports and imports). Differences in inflationary experience and the rate of unemployment across regions and nations make it likely that interest rates will be put up when inflation appears in one part of the European Union even when other regions are not experiencing inflation and when the levels of unemployment are high.

Third, the interest rate is a weak policy instrument to use for the control of inflation. The extent to which interest rates in a single country (or in this case in the European Union) can be varied relative to interest rates in other countries is heavily circumscribed. It is difficult to believe, for example, that real interest rates could be maintained 2 per cent above or below the real rate of interest in the United States of America. Further, the extent to which interest rates can influence the rate

of inflation is small. This means that the eurozone is left with little to counter any upsurge in inflation. At the present time, with inflation subdued, this may not be a serious concern, but any upswing in inflation, whether generated within the European Union or more widespread, would present serious difficulties.

It is imperative that the sole economic policy maker at the European Union level is brought under democratic control, and that the objectives to be pursued by the ECB are broadened to include high levels of employment and economic activity. But this should be done with the recognition that monetary policy is not an effective way of guiding the economy.

Fiscal policies and redistribution

The adoption of a single currency by eurozone countries clearly removes the possibility of variation in the value of their domestic currency. Changes in the exchange rate can allow a country to offset differential shocks and differences in economic performance. It may be questioned how far a country can determine its own exchange rate in the globalised financial markets, though since an exchange rate is the relative value of one currency in terms of another it is rarely the case that one country can completely determine the value of its own currency. It is also the case that exchange rates have been highly volatile since the breakdown of the Bretton Woods system, and that exchange rates have diverged significantly from purchasing power parity (see, for example, Krugman 1989; Rogoff, 1996). Nevertheless, variation in the exchange rate (whether in the context of a fixed or a flexible exchange rate system) does provide an adjustment safety valve to differential shocks and economic performance, even though the safety valve may not always work quickly (in the case of fixed exchange rates) or may often be faulty (in the case of flexible exchange rates).

It is clear that there are few, if any, mechanisms with the Stability and Growth Pact and the single currency for a country or region to adjust to differential shocks and economic performance. The ability of national governments to stabilise their own economies becomes more circumscribed through the requirements of the Stability and Growth Pact and the limits on the size of budget deficits. It is often pointed out that most single-currency zones involve a central or federal government tax and public expenditure programme, which is substantial relative to national GDP, and a government budget, which can run significant deficits.[2] The tax and public expenditure programme generally involves redistribution from richer regions to poorer ones, whether as an automatic consequence of a progressive tax and social security system or as specific acts of policy. The redistribution acts as a stabiliser with negative shocks leading to lower taxation and higher social security payments in the region which is adversely affected. With the removal of exchange rate variations as an adjustment mechanism, it could be expected that economies would adjust to differential shocks and economic performance through a variety of other routes. These would include (in response to a negative shock) declines in economic activity, reductions in living standards and outward migration. There is then a requirement for the development of a larger

EU tax base within a progressive tax system and the use of the tax revenue in a redistributive manner.

The problem of unemployment will be particularly serious in those cases where governments have chosen the wrong exchange rate at entry. An overvalued entry exchange rate will mean an extended period of recession to accommodate its effects, which emanate from the absence of the adjustable exchange rate safety valve. This is accentuated by the virtual absence of fiscal transfers, whether automatic or discretionary, from the relatively rich regions to the relatively poor ones. There is clearly not a tax and social security system operating at the EU level which would make transfers between rich and poor in an automatic manner, and provide an element of fiscal stabilisation. The expenditures on regional aid (structural and cohesion funds) and to a lesser degree agricultural policies do make some transfers from rich to poor, but on a very limited scale. In short, the European budget is neither on a sufficient scale nor of the right design to provide significant interregional insurance in the EMU (Fatas 1998).

The structure of taxation and public expenditure (and the balance between them as reflected in fiscal policy) can redistribute income (depending of course on the degree of progressivity of the tax system and the ways in which public expenditure is allocated) in two particular ways. First, it can in effect redistribute income over time – taxes rise when income rise, fall when income falls. This is the well-known stabilising effect of a progressive tax system. Second, richer regions tend to pay higher levels of tax and (perhaps) receive lower levels of public expenditure. There is a redistribution between regions – some of this redistribution may be a deliberate design of public expenditure and some a by-product of a progressive tax system.

The EU level of public expenditure is restricted to around 1.5 per cent of the GDP of the European Union, and there is a requirement that the EU budget is balanced so that taxation raised through national governments is exactly equal to the level of expenditure. Whilst there is some redistribution (e.g. in the form of regional policy), it is inevitably rather minor, given the size of the overall budget (and also the size of the common agricultural policy within that). The MacDougall Report (1977), written for the European Commission, regarded a EU-level budget of around 7.5 per cent of GDP as necessary to provide adequate stabilising properties.

Fiscal policy at the EU level (whether operated by the European Commission or through the coordination of national fiscal policies) could make a substantial contribution to the effective operation of the single currency. This would be for (at least) three reasons. First, there is no particular reason to think that the level of aggregate demand generated by the private sector will be sufficient to create or to maintain high levels of economic activity. Indeed, currently many of the EU economies suffer from high levels of unemployment and insufficient demand (in part created by the drive for fiscal orthodoxy to fulfil the Maastricht Treaty criteria). There are occasions (such as the USA currently) where private sector demand is high, with low savings and/or high levels of investment, so that the resulting private sector deficit is then matched by a public sector surplus. We may refer to the following national income accounts identity to make the point:

$(I - S) + (X - M) = (T - G)$, where I is investment, S is savings, X is exports, M is imports, T is taxes and G is government expenditure. Positive values on the left-hand side, i.e. net private dissavings and export surplus, are matched by positive on the right-hand side, i.e. budget surplus. But there will be other occasions when private sector demand is low, and there is the requirement for budget deficits to maintain demand.

Second, fiscal policy provides an additional policy instrument (in addition to monetary policy) through which the level and composition of aggregate demand can be influenced. The 'one-club' nature of monetary policy has often been noted, and also the degree to which a uniform policy is applied across diverse economic situations.

Third, the extent of trade between the European Union and the rest of the world is relatively low, particularly as compared with the international trade of the countries which will compose the eurozone, for much of the trade by one EU country is with other EU countries. Fiscal policy (and indeed any policy which leads to demand expansion) may have limited effect domestically as the demand spills abroad. But this is not the case for the European Union, and the impact of fiscal policy on domestic demand and then the level of economic activity can be expected to be substantial.

Disparities

The single European currency will come into being against the background of high levels of unemployment across Europe (9.0 per cent at the time of writing in early 2001) and with enormous disparities: unemployment rates ranging from 2.6 per cent in the Netherlands through to 14.6 per cent in Spain. Average growth of GDP per capita ranges from 1.9 per cent (Austria) to 5.9 per cent (Ireland), i.e. by a factor of 3. These disparities are deep seated and much more than the temporary disparities thrown up by economies at difference stages of the business cycle. These disparities raise many questions: for example, can a monetary union function economically and politically in the face of such disparities? Further, what attempts should be made through economic policies to reduce those disparities? Also lying behind those disparities are considerable differences in the institutions of the national economies such that the economies behave and perform differentially, and such that a single policy measure (for instance, a change in the euro rate of interest) would have quite different effects on the national economies.

The present disparities in regional unemployment levels (and also in labour market participation rates) within the European Union would suggest that even if full employment were achieved in some regions, there would still be very substantial levels of unemployment in many others. In the presence of such disparities in unemployment, the achievement of a low level of unemployment overall (not to mention full employment) would be well-nigh impossible. Inflationary pressures would build up in the fully employed regions even when the less prosperous regions were still suffering from significant levels of unemployment. Interest rates would then rise to dampen down the inflationary pressures in the

prosperous regions without consideration for the continuing unemployment in other regions.

Eichengreen (1997) offered the suggestion that the European Investment Bank (EIB) can borrow off-budget to perform tax-smoothing functions, however, this would exceed the EIB's present remit.[3] Article 198e of the Maastricht Treaty states that:

> The task of the EIB shall be to contribute, by having recourse to the capital market and utilising its own resources, to the balanced and steady development of the common market in the interest of the community.

Whether the functions of the EIB can be enlarged to include stabilisation policy (distribution over time) is extremely questionable. However, it can entail redistribution across countries, and it is specifically this function which should be expanded and strengthened from its present form where assistance is only in the form of loans and guarantees.

Therefore, a further recommendation would be to have a revamped EIB to supplement the activities of the ECB, with the specific objective of enhancing investment activity in those regions where unemployment is acute (Arestis *et al.* 2001). Enhanced investment activity will, thus, aim to reduce the dispersion of unemployment within the framework of reducing unemployment in general. This could be achieved through encouraging long-term investment whenever this is necessary by providing appropriate finance for it.

We suggest an overhaul of the EIB's remit because of the changing environment in which it operates. As highlighted by Honohan (1995), the EIB was established at a time when national capital markets were less developed than at present. Now, however, many lenders of loanable funds compete with the EIB, and in this respect its public policy role is shrinking. Despite this trend, there still remains scope to extend the EIB's public policy role. In particular one area for possible intervention has been identified. The case for a revamped and extended EIB is based on three considerations. First, there is a need for differentiated policies, which will enable the less prosperous regions to catch up with the more prosperous ones; this in turn will enable higher average levels of employment and economic activity. Second, the forces of cumulative causation in the context of a single currency and market will tend to stimulate investment in the more prosperous regions rather than in the less prosperous ones. Third, the high set-up costs of venture capital projects and the disproportionate number of small firms in the EU peripheral areas (which generally experience higher levels of unemployment) provides scope for the provision of subsidies for venture capital activities because costs are mainly independent of the scale of borrowing (Honohan 1995).

Summary and conclusions

A single currency with a central bank as the only policy-making institution would, we argue, be unacceptable. We would also suspect that it is an unstable arrange-

ment. The ECB will be unable to control inflation, and the setting of interest rates will inevitably disadvantage some regions and nations. The transparency of the single currency will be a transparency not only of prices but also of living standards and levels of unemployment. It is an open question as to whether an economy with the degree of diversity (of economic performance and of economic institutions) such as the European Union can operate effectively without policies which recognise those disparities and which seek to mitigate the effects of the disparities and to reduce them over time. Creating a single currency with the only EU-level institution of the ECB and to impose on that single currency a set of policy arrangements which are deflationary in nature are not good omens for the success operation of the European economies. The functioning of a single currency will require the development of federal level policies and institutions.

Notes

1 This 'new monetarism' has, of course, infected 'new Labour', as reflected in the title of our paper 'New Labour, new monetarism' (Arestis and Sawyer 1998).
2 The CFA zone in Francophone West Africa is an exception.
3 The Treaty of Rome created the EIB in 1959. It specifically focused on the financing of infrastructural and other fixed capital formation projects. The scale of its operation has been very small (see Eichengreen 1997).

5 Economic performance and the euro

Janet Bush

Introduction

It is a distinct oddity of the British debate about whether to join the euro that, for a long time, it has been the Right that led the opposition and the Left – or rather the pseudo-Left represented by New Labour and the Liberal Democrats – that has been the warmest advocate of joining. In Sweden, which decisively voted no to the single currency in September 2003, the balance of political opinion was quite different with the Left and the trade union movement swinging opinion against Economic and Monetary Union by highlighting the threat posed to Sweden's cherished tradition of generous social welfare and labour market protection.

The Swedish prognosis was spot on and, finally, with the evidence of four years of privatisation, public spending cuts, concerted attempts to dismantle labour market protection and a deadly combination of tight money and tight budget policies which has strangled growth and exacerbated Europe's dreadful unemployment record, the British Left is beginning to wake up to the true implications of the euro project.

Economic and Monetary Union is a battering ram towards free market economics. For that reason, if political issues of democracy and sovereignty did not override all others for many root-and-branch British Conservatives, the economics ought to be attractive. To outliers such as former Chancellor Kenneth Clarke, it is indeed the hope of a free market Europe that has partly fuelled his euro enthusiasm.

Painfully mindful of the disastrous results of mass unemployment in Germany in the 1930s, Europe has, in the entire post-war period, held out against neo-liberalism and defended a consensual social market model of economic management in defiance of what has become known as the Washington Consensus. However, gradually, a new Brussels consensus started to emerge among Europe's political elites, egged on by multinational business. They were collectively fed up with Europe's relatively sclerotic growth, putting it down to the handicap of 'inflexible' labour markets, overly generous welfare provision and industrial protection. As Professor Christian Watrin of Köln University said to me in the early 1980s: 'What Germany needs is a dose of Thatcherism.'

This theme has appeared repeatedly in the utterances of Europe's new orthodox

priests. Between them, the President of the European Central Bank (ECB), the Vice President and the Chief Economist had, by February 2002, made 14 appearances at the European Parliament's Committee on Economic and Monetary Affairs for the purpose of presenting a report on monetary policy. On 12 occasions the representative of the central bank asserted that further efforts were required to reduce taxation or government spending, or that fiscal stabilisation would otherwise be inappropriate, and on 13 of them reference was made to the desirability of 'structural reform', 'deregulation' or some other expression with a meaning including labour market deregulation.

By early 2003 the ECB's agenda was even clearer. In its *Monthly Bulletin* published at the start of May, the ECB gave warning that free health care in the eurozone would have to be restricted to emergency services only because otherwise the cost would overwhelm European economies. Governments should distinguish between 'essential, privately non-insurable and non-affordable services' and those where 'private financing might be more efficient'. Ageing populations would make state pensions, tax-funded health services and long-term care unaffordable and, it continued, tax rises to meet the extra demands would soon become politically unacceptable.

This report emerged on the day of a key UK parliamentary debate on foundation hospitals, and the link between privatisation of public services and joining the euro was finally rammed home. Gordon Brown's Treasury has so far stood firm against interference by the European Commission in the management of British fiscal policy – the Chancellor has repeatedly made it clear that tax, spending and borrowing decisions remain in his purview, whether it has been in rejecting the Commission's advice in its Broad Economic Guidelines that, to comply with the European Union's Growth and Stability Pact (GSP), Britain would have to cut spending by £10 billion; or in withstanding pressure for a European withholding tax on the City; or in standing firm against attempts to impose VAT on children's books and clothes. However, it is a source of significant dismay that a Labour government in Britain is not only prepared to champion the dismantling of publicly funded services but is, in fact, the main cheerleader for the deregulation agenda in Europe which the euro is catalysing.

The neo-liberal stranglehold on growth

In years gone by Britain's economy was pityingly described as the 'sick man of Europe'. The eurozone now deserves to be known as the 'sick man of the global economy'. In September 2003 the International Monetary Fund again downgraded its forecast for eurozone growth, and its chief economist Kenneth Rogoff, pointedly contrasting the burgeoning recovery in the United States of America (and the United Kingdom), observed: 'For the moment, most Europeans who want to see an economic recovery will have to watch it on TV.'

Neo-liberals, including some in the Blair government, argue that the eurozone's low growth and high unemployment is the result of structural rigidities, most notably in labour markets and in the imposition of high welfare taxes on

employers. If only eurozone governments would scale down the welfare state and introduce an Anglo-Saxon labour market, all would be well.

The real culprit is, however, macroeconomic policy, which has squeezed growth and kept unemployment high for decades now.

Since the oil shocks of the 1970s the European economic establishment has embraced a classic monetarist orthodox approach, centred on bearing down on prices by reining in growth and cutting budget deficits. In the 1970s the Bundesbank reacted with extraordinary zealousness to the threat of higher inflation from rising oil prices, and other central banks followed the German central bank's restrictive policies throughout the 1980s. Inflation came down but so did growth.

The obsession with inflation and disregard of growth continued in the 1990s after the European establishment decided to formalise its commitment to orthodoxy in plans for Economic and Monetary Union, enshrined in the 1992 Maastricht Treaty. Centre stage was a set of convergence criteria, aimed at making it more sustainable for different economies to live with a single interest rate. The criteria were highly conservative, ordering reductions in inflation through swinging cuts in budget deficits and public debt levels for applicant countries. By 1999, when the euro was launched, the orthodox economic establishment was congratulating itself on a cut in EU inflation from an average of 4.9 per cent in 1986–90 to 3.9 per cent in 1991–5. Budget deficits fell sharply. But the result of this restrictive programme was an exponential rise in unemployment. Between 1992 and 1999 national income in the economies that joined EMU rose by only an average of 1.7 per cent a year. From 1994 to late 1998 the average rate of unemployment never dropped below 10 per cent (about twice the rate in the United States over the same period (Figures 5.1 and 5.2)).

Attributing these economic developments substantially to the Maastricht convergence programme may seem controversial, but compare what happened in those European economies that did not set policy to join the euro in the first wave. The United Kingdom, which saw unemployment double between 1990 and 1992

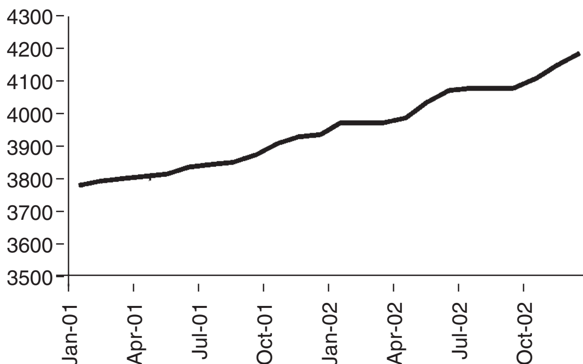

Figure 5.1 German unemployment, January 2001–October 2002 (000s).

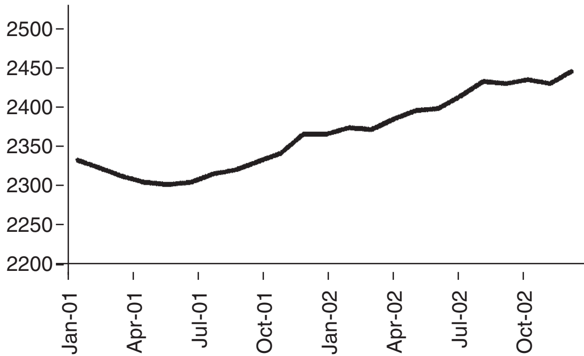

Figure 5.2 French unemployment, January 2001–October 2002 (000s).

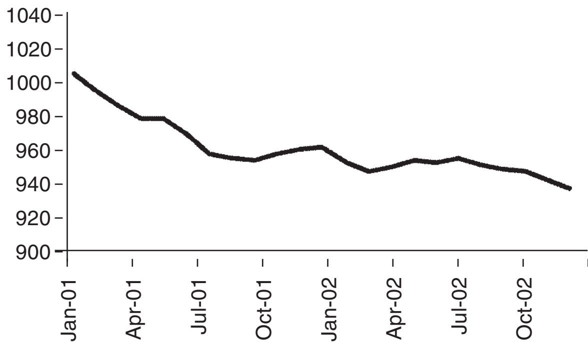

Figure 5.3 UK unemployment, January 2001–October 2002 (000s).

when it briefly locked the pound to European currencies in the Exchange Rate Mechanism, then saw unemployment fall from 9.3 per cent to 6.1 per cent in 1999 (Figure 5.3). Able to pursue monetary and fiscal policies unfettered by Maastricht and then by the discipline of the euro itself, unemployment fell further to 5.1 per cent by the end of 2002. Denmark, which also negotiated an opt-out from the euro, saw unemployment drop from 8.2 per cent to 4.7 per cent at the end of 2002. A measure of how restrictive policies were for euro candidates comes from Brian Burkitt of the University of Bradford, who estimated that, had Britain joined the euro in 1999, it would have had to cut public spending by £42 billion to meet the Treaty's 3 per cent deficit limit.

Inside EMU the squeeze has continued. The European Central Bank was modelled on the Bundesbank, with a sole mandate to bear down on inflation. Unlike the US Federal Reserve, it has no mandate to promote growth and employment and the ECB has been far slower than central banks in the United States or in Britain to cut rates in response to the world slowdown since 2001 (Figure 5.4).

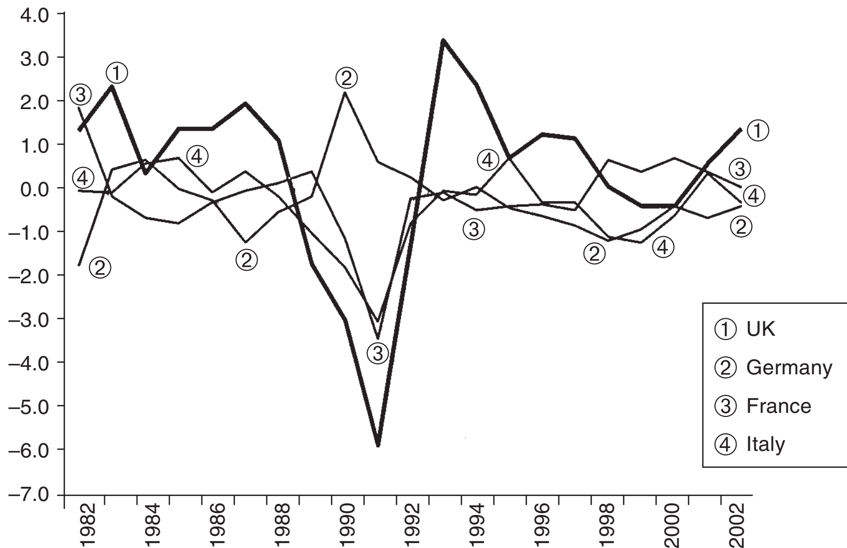

Figure 5.4 Growth rates in the United Kingdom, Germany, France and Italy, 1982–2002 (HM Treasury).

Compounding this ultra-conservatism on interest rates has been the continuing squeeze on public spending in the eurozone under the 3 per cent deficit limit imposed by the Growth and Stability Pact. Even as growth stagnates and unemployment rises, eurozone economies are being obliged to cut spending or raise taxes in order to comply. A counter-cyclical boost to demand, as Keynes classically prescribed, is outlawed. Indeed, the opposite has been occurring – fiscal policy is being tightened even as growth slows.

Public spending cuts and tax rises are being pushed through across the eurozone. At the time of writing (autumn 2003), Italy's 2004 budget plans to include a mixture of revenue-raising measures and spending cuts that would total €16bn–18bn (US$18bn–20bn, £11bn–12.7bn) (*FT*, 11 September). The Netherlands was expected to unveil a €17bn package of cuts in its budget, including a two-year freeze on welfare benefits, civil servants' pay and child benefits, together with higher tobacco prices (*FT*, 15 September). In Germany:

> University funding has been slashed, tuition fees brought in for long-term students, subsidies for housing abolished, urban renewal projects abandoned, charges introduced for school books, kindergarten fees jacked up, 1,450 police jobs axed, swimming pools closed, grants for welfare recipients ended, fountains turned off, arts funding chopped, a freeze imposed on civil-service vacancies, and plans to lop €1 billion off the city's wage bill of €7 billion by 2006 have been approved.
>
> (*Economist*, 19 July)

Outside the euro, Britain, although theoretically bound by the GSP, has escaped such enforced public spending cuts and instead, in the 2003 budget, has been able to raise borrowing, preserve investment plans and boost the economy while it has been relatively weak, the classic Keynesian response to the threat of recession.

Despite a general consensus at the start of 2003 that the rigidity of the Pact was exacerbating the eurozone economic slowdown, the orthodox architects of the rules stayed firm. In March the European Parliament (EP) adopted a resolution in favour of enshrining the Pact into the new EU Constitutional Treaty to avoid any backsliding on fiscal discipline. The EP even stipulated that 'factors such as public investment in services' should not be taken into account in calculating deficits.

Even the International Monetary Fund (IMF), the world's cheerleader of neoliberal economics, takes a more flexible view. In its *World Economic Outlook*, in 2002, it called for further action to bring eurozone deficits down despite evidence of tepid growth. By the spring of 2003 it was so alarmed that it called on the European Union to relax its budget rules. 'Automatic stabilisers should be allowed their full impact, even if that were to lead to a breach of the 3 per cent limit of the Stability Pact in 2003', the *Financial Times* reported in advance of formal publication of the IMF's spring *Outlook*.

Monetarism goes east

Now, with ten new members due to join the European Union in 2004 – and forced to sign up to membership of the euro at some stage as the price of entry – the neoliberalism is being applied also in eastern Europe, which has provided some rare European growth hot spots in recent years. There is the obsession with inflation at the expense of jobs. In March, Tommaso Padoa Schioppa, a member of the ECB Board, told applicant countries that 'they must strive for price stability right from the beginning of the preparation process' and ensure that they institute independence for their central banks, so that the fight against inflation is put at the centre of policy. Applicant countries are also under intense pressure to cut budget deficits, potentially devastating for their already high unemployment levels.

Poland, the largest of the accession countries, is a depressing case study. While unemployment peaked at over 18 per cent in 2002, inflation had fallen to an all-time low of 1.9 per cent as interest rates were kept above 8 per cent. Clearly, the economy has been suffering from a lack of demand, and monetary policy is too restrictive. Two small coalition partners in Poland's left-wing government drafted a controversial bill in 2002 demanding that the independent National Bank of Poland's mandate should be made to include the promotion of employment and growth in addition to ensuring price stability. Poland's president rejected the bill, proposing an alternative measure that would comply with EU requirements for central bank independence.

Low growth has seen Poland's budget deficit soar and, as the country struggles to shape up to meet the Maastricht criteria for euro entry, it is under pressure to cut its deficit – a policy that will only exacerbate Poland's lack of growth and mass unemployment. In 2002 Poland's parliament proposed a programme that would

limit the annual growth of public spending to only 1 per cent in real terms. Days after Hungarians voted overwhelmingly to join the European Union, their prime minister revealed a substantial programme of public-spending cuts, including cuts in health care. In 2002 Hungary's deficit ballooned to 9.4 per cent of GDP. To meet the euro entry criteria, it has to fall to no more than 3 per cent of GDP. There is no escape from a chronic slowdown ahead, led by fiscal retrenchment.

In its end-2000 survey of the region, the European Bank of Reconstruction and Development (EBRD) identified the impossible circle that central and eastern European economies are being forced to square if they are to comply with the membership rules for the European Union and Economic and Monetary Union. It acknowledged that 'rapid growth over a sustained period is necessary for the accession countries to catch up with the EU average for productivity and living standards'. In 2001 the average income per head in the ten accession countries was only 40 per cent of the EU average. However, the EBRD said, 'at the same time they will be subject to the demands of the Stability and Growth Pact and, for those countries striving for early adoption of the euro, the Maastricht criteria'. It noted that the 'looming requirement of a general government budget that is close to balance or in surplus in the medium term further points to the need for early fiscal consolidation in many of the accession candidates'. Fiscal consolidation is economist-speak for cutting budget deficits either through lower public spending or higher taxes.

As in western Europe, eastern Europe is coming under pressure to cut unemployment not through the pursuit of higher growth but through 'free market reform'. Quite simply, workers in high unemployment areas will be expected to see their wages and conditions slashed until they 'price themselves back into the market'. Poland, for example, is planning to make its Labour Code more flexible. In Germany, on the same day as the Institute for Labour Market Research issued its estimate of 7.2 million unemployed, the government announced cuts in unemployment benefit entitlement.

Institutional chaos – the forcing mechanism for political integration

It is not an exaggeration to suggest that macroeconomic policy has been set on maximum squeeze *precisely* because this will engineer a crisis which will be a catalyst towards more flexible markets – the aim of neo-liberals – and, if this reform program fails to live up to expectations (as those who want to force the pace of European political integration quietly hope), radically change the institutional structure of EMU. Romano Prodi, President of the European Commission, came close to admitting this in an interview with the *Financial Times* on 4 December 2001. He said:

> I am sure the euro will oblige us to introduce a new set of economic policy instruments. It is politically impossible to propose that now. But some day there will be a crisis and new instruments will be created.

The argument seems to be that the euro would damage European economies without political change and is therefore a useful forcing mechanism. This is social engineering on a grand scale: Trotsky in Brussels – cause economic chaos and hope for a positive political outcome.

Divergence is actually the norm in currency unions and the disparities in Europe are dramatic compared with those of the United States, making the rigidities of the euro system very worrying indeed. In the United States, unemployment ranges between 2 per cent and 6 per cent. In 2001 Eurostat figures showed a range in unemployment rates in the European Union of 1.2 per cent to 33.3 per cent. In the ten accession countries, the range was similar, between 2 per cent and 32.8 per cent. One quarter of EU regions and nine out of ten of the ten accession countries had GDP below 75 per cent of the EU average. And the average woman in the European Union earns a quarter less than a man. Inflation rates have varied wildly in the eurozone (Figure 5.5).

Convergence is not the answer – no economies or regions ever move in precise lockstep with each other and the mere existence of monetary union, as some of its advocates argue, does not force them so to do. What is needed – and what the US monetary union developed – is increased flexibility in other areas. Professor Robert Mundell who won the Nobel Prize in economics for his paper on 'optimal currency theory' concluded that three ingredients are needed to make a monetary union work: labour mobility, deregulated labour markets and a redistribution mechanism through a federal budget.

In Europe's monetary union, none of these currently exists. Labour mobility in the European Union is 27 times less than in the United States of America, according to the European Commission; moves to make labour markets flexible have foundered in the face of popular European support for a consensual social model; and the eurozone fiscal framework is incapable of playing a rebalancing role.

In well-run economies, monetary and fiscal policies work in harmony. In Britain, even with an independent central bank, an observer from the Treasury sits

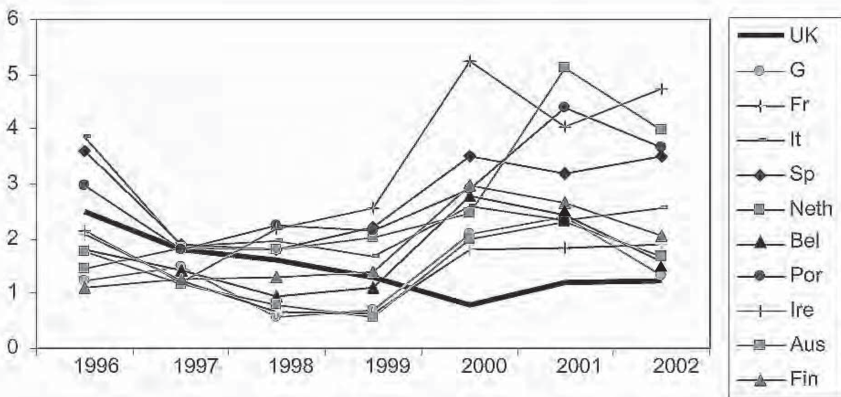

Figure 5.5 UK and eurozone members' inflation, harmonised index of consumer prices (HM Treasury).

in on interest rate meetings. Before the Chancellor unveils his annual budget, private soundings of the Bank of England are taken to ascertain whether the package will impact on interest rates. In the eurozone, such coordination is precluded by a horribly lop-sided institutional set-up. A strictly independent European Central Bank runs monetary policy. But there is no single institution to run fiscal policy for the simple reason that member states were not prepared to give up control of tax, spending and borrowing decisions, described by arch-europhile former chancellor, Kenneth Clarke, as 'the cornerstone of democracy'.

Put bluntly, the ECB could make brilliant judgements in setting the euro interest rate – but, if politicians play fast and loose on the fiscal side, the system will still be unstable. So the Growth and Stability Pact was agreed, limiting governments *at all times* to budgets of 3 per cent of GDP or less or face fines. As is now well known, the GDP, in practice, is unworkable and damaging.

The elemental flaw is that it is not enforceable. The *theory* is that 'peer pressure' and a slap on the wrist from the European Commission would force member states to comply. In practice, smaller countries with less clout have kept to the rules and big countries have flouted them ever more recklessly. The prime minister of France, which has already burst the GDP's limits, is dismissive. He said recently: 'My first duty is employment and not to solve accounting equations and do mathematical problems until some office or other in some country or other is satisfied.'

The second problem is that the GDP requires member states to do exactly the wrong thing when they hit rough economic waters. Instead of temporarily raising borrowing – as Gordon Brown has done in Britain, with the effect that growth is beginning to recover – eurozone members have to cut borrowing and spending and raise taxes. Take the Netherlands. It recorded a GDP contraction of 0.5 per cent in the second quarter. Yet in September it announced public spending cuts to the equivalent of US$12.4 billion. As Romano Prodi, President of the Commission, said of the GDP, it is 'stupid. The Growth and Stability Pact will have to be loosened but what is currently on the agenda is mere tinkering.

EMU's fiscal black hole

Monetary unions do not need marginal fiscal flexibility; they need huge flexibility. This brings us back to Professor Mundell's third condition for a successful currency union – a federal budget to act as an automatic stabiliser. In the United States of America, some 25 per cent of US GDP is available to redistribute resources automatically through the transfer of tax revenues in prospering states to the unemployment benefit in stagnating states. For every $1 fall in a state's GDP, 40 cents will be paid from the federal budget. This is the glue that has kept the US monetary union together.

No such system exists in Europe. The EU budget is 1.27 per cent of EU GDP and half of that goes on agricultural subsidies. This is wholly inadequate and there is no realistic prospect of change because of political opposition to paying a higher proportion of taxation to the European Union. After a Belgian proposal in mid-

2001 of a new EU tax, even the most committed European integrationists were horrified. The Dutch finance minister observed: 'The last time a new tax was launched in the Netherlands it resulted in the Eighty Years War. I am not sure a new tax for the EU would be much better this time.' Post-enlargement, I suspect opposition to paying a higher proportion of taxes direct to the European Union will be even more entrenched as western electorates baulk at their tax euros being used to subsidise relatively poor new entrants.

So, there is a solution to both the problem of fiscal enforcement and redistribution, but it is a political non-starter. The euro needs a single fiscal authority, running a federal budget. In its submission to the Convention on the Future of the European Union, the Commission proposed it be that authority, an 'economic government of Europe'. But the draft EU constitution, in its current form, keeps national vetoes over taxation. Popular political opposition to centralisation of the European Union – most recently expressed in the decisive Swedish 'no' vote to the euro – will ensure this continues to be the case. There is, quite simply, no prospect of a workable fiscal policy in EMU and this leaves the euro in limbo. I suspect that continued low growth, economic instability and political tensions will wreck the system in the years ahead.

Is even a perfect monetary union worth the trouble?

As a postscript to what I believe is a true description of the extraordinary economic and political fault lines in the euro project, let me look finally at whether, intrinsically, it is worth sorting out this mess on economic, rather than political, grounds. The fundamental economic argument of euro advocates is that a single currency is needed to complete and perfect the Single Market. That theory is, in itself, flawed. Bear in mind that the richest state in Asia is Singapore, a small island with no natural resources and with its own currency. The richest country in Europe is Switzerland, which is not even a member of the European Union, let alone the eurozone. The truth is that membership of the Single Market and membership of the euro is a separate matter.

One, even in the view of the European Commission, is far more potentially valuable to its participants than the other. The Commission's Ceccini report in the late 1980s put the gains of belonging to the Single Market at some 4 to 6 per cent of GDP; (a post-mortem on this analysis a couple of years ago admitted that only around 20 per cent of these gains had actually materialised). In 1990 another report by the Commission titled 'One Market, One Currency' concluded that joining the euro would produce a gain of 0.5 to 1.5 per cent of GDP.

It is quite likely that, for Britain, the actual figure would be substantially lower than this. The Commission had a figure of 0.4 per cent for transactions, including lower transaction costs and lower exchange rate volatility. However, this was an estimate for an average EU country and Britain is a larger economy than average and trades less in the European Union than the average. Quite properly, therefore, this component could be reduced to around 0.2 per cent. Then the Commission had a gain of 0.3 per cent from more price certainty and less price discrimination.

This is highly contentious given that increasing use of the Internet means that there is very little lack of transparency in current prices and that we live in a low inflation world. The rest of the Commission's putative gain from membership of the single currency comes from the theoretical extra investment and output generated by the first two components, an effect of some 0.7 per cent. Given the analysis above, let us cut that by half.

So, a credible case can be put for the gains of membership of the euro for the United Kingdom being only around 0.5 per cent of GDP. There continues to be a case for remaining a member of the Single Market, but the case for joining the euro seems laughably trivial compared with giving up control of both monetary and fiscal policy and so taking a substantial step towards a far more centralised, remote political system that, thus far, does not have the consent of the peoples of Europe.

6 The euro

An outsider's perspective

Paul Ormerod

Introduction

In this chapter I want try to look from the perspective of, say, a new or candidate member of the European Union as a whole: one of the countries of eastern Europe which has been struggling to adjust to the concept of a market economy, to the realities of the world economy; or, more generally, one of the countries in South America or East Asia which, whilst not desperately poor, are still a long way behind western Europe in terms of living standards. What does the euro have to offer to countries which have the potential to move towards western European living standards, but which have not yet found the elusive mix of institutional arrangements and incentives which generates such a profusion of wealth?

What might the euro seem like to a poorer country with aspirations to become rich? Many countries are anxious to join the European Union, and we can immediately see why in Table 6.1. This shows the GDP per capita of Greece, Ireland, Portugal and Spain in 1975 and in 2000. The table does not show the raw data, but their per capita GDP *relative to* the rich EU core of France, Germany, Italy and Benelux.

In 1975 these four countries were fairly poor, on the fringe of western Europe. By 2000 they had started to move towards the income levels of the EU core. All countries in the European Union grew in absolute terms between 1975 and 2000, but the 'Fringe Four' of 1975 grew more rapidly.

I cannot resist mentioning that the easiest way to get this data on the web was from the CIA's site. The US government offers speedy access to large amounts of

Table 6.1 Per capita GDP relative to the EU core (%)

	1975	*2000*
Greece	55	65
Ireland	55	90
Portugal	55	65
Spain	70	75

Source: CIA.

data for free – in contrast to European agencies such as Eurostat whose sites tend to be slow to access and who charge for almost everything. In terms of encouraging the use of new technology, there is a lesson here.

But the key point about Table 6.1 is that membership of the European Union has positively benefited its poorer member states. There is a strong incentive for others to join.

Yet the euro cannot have played much of a role in enabling these countries to start catching up with the affluent core in terms of living standards. A simple but very important reason is that the euro did not exist until 1999. The catch-up has happened in part because of the distribution of subsidies from the richer countries, and in part because of the increasing integration of Spain, Portugal and so on with the wider EU market.

Of course, it is argued now that the euro will intensify this process, by reducing transactions costs and promoting price transparency. Whilst this is true, it is much less important than the need to complete the process of implementing the concept of the single market. There are still far too many barriers to trade and competition across the European Union. To give one example: the punitive air fares on most European routes are due to the willingness of the Commission to allow, by one means or another, a succession of massive subsidies to continue to be paid to inefficient national carriers. Another example is the mobile phone, and the failure to establish common standards across the European Union. Energy spent on introducing the euro could have been better spent on removing trade barriers and completing the single market.

The striking feature about the past half-century or so is that a substantial number of countries, principally in Asia, have seen rapid expansions of their living standards – first of all Japan, then countries like South Korea and Singapore, Malaysia and Indonesia and now India. It is precisely those countries which have embraced the concept of globalisation and increasing integration with the rest of the world which have done well. It is states such as Burma, North Korea and Afghanistan, which have cut themselves off, which have gone backwards.

So membership of the European Union offers the benefits of globalisation, of ready access to a huge market. In addition, membership gives a clear badge which certifies credit worthiness and political stability. This enables countries to attract direct investment from overseas. Further, the European Union provides large subsidies to help cushion the shocks which such integration inevitably brings.

But it is not clear what benefits the euro as such, rather than membership of the European Union, brings. Indeed, a case can be made that on balance it hinders rather than helps Europe. Certainly, in the role of a new or candidate member of the European Union, I would be concerned. The emphasis on the euro rather than the single market would make me worry that barriers to the things I produced might not come down as rapidly as I would like. Indeed, this is a far from hypothetical concept, as is shown by the debate on how much mobility of labour will be allowed from the eastern European countries once they are in the European Union.

An immediate concern arises from the wider political economy context, rather than the narrower focus on technical economics. There is legitimate concern about

the impact of globalisation on the democratic process. Large corporations, it is felt, are taking decisions which influence people both much more strongly, and at the same time more remotely, than do elected governments.

Much of this worry is misguided and often seriously misplaced. Nevertheless, there is a sense of unease about the remoteness with which decisions are taken. Unfortunately, the euro brings with it its very own democratic deficit. It is by no means clear that the electorates of western Europe would have gone ahead with the euro project if it had been submitted to referenda. We know that the only country where a vote was permitted recently, Denmark, rejected membership. This was despite the overwhelming support for entry on the part of the political establishment and the media. No other European government dared to put the question before its electorate in the immediate run-up to the introduction of the currency.

New and aspirant members of the European Union in eastern Europe are of course no strangers to the idea of having crucial decisions taken on their behalf by the political elite. But the lack of democratic validation is, I believe, a potentially serious problem for the euro. Across western Europe, we have already seen the growth of parties outside the political mainstream in many of the member states. Discontent with the remoteness of the European Commission appears to be a common feature of the otherwise widely disparate platforms of such parties, some of which are rather disagreeable.

The creation of the euro reinforces centralising tendencies within the European Union. Spain, after all, is not Slovenia, but a strong and powerful economy. But just how much influence does the governor of the Spanish central bank have on decisions taken at the European Central Bank (ECB)? I think we all know the answer. The real danger, I would feel looking from the outside, in joining the European Union and the euro is that my voice would simply not be heard at all. In any adverse circumstances, the euro project would be administered solely in the interests of the EU core.

But even from a French or German perspective, the particular way in which the rules of operation of the ECB have been framed may prove a handicap. The obsession with inflation and the trap of the fiscal stability pact may prevent the ECB from following potentially expansionary policies during any economic downturn.

Countries outside the European Union require not only access to EU markets if they are to eventually prosper, but they require a healthy growth rate in the developed world of which the Union is such a major part. Downturns in the developed world are often reflected in much sharper recessions elsewhere. A squeeze on export earnings in hard currencies can be magnified sharply in the domestic economies of the developing world. For example, in the general world slow-down between 1980 and 1982, the EU 15 grew in real terms by only 1 per cent. But growth in both Argentina and Brazil was sharply negative, at –11 and –8 per cent respectively.

The role of institutions, of the process and rules under which economic agents take decisions is in my view absolutely central to how economies perform. Unfortunately, the rules governing the operation of the ECB have been designed to

fight yesterday's battles. The complete focus on the control of inflation is seriously misplaced. As a result, the prospects for output growth in the European Union, and hence in the developing world, may be affected adversely.

Think back – well, some of us can – to the dark days of 1973. Since the early 1950s inflation rates had been very similar in all western countries. Even in 1973, with huge inflationary pressure from world commodity prices, and at higher absolute levels of inflation, this still obtained. Inflation in most countries was in the range 6–8 per cent, with Italy being somewhat higher at 10 per cent. Following the oil shock, inflation rose sharply everywhere in 1974, reaching over 12 per cent even in Germany. But by 1975 a huge disparity in inflation rates had occurred. In Britain, inflation was 21 per cent, in Italy 16 per cent and in Germany just over 4 per cent.

A great deal of economic policy since then has attempted to deal with these discrepancies, which arose, after a long period of convergence, in a period of only 18 months. Policy makers remain obsessed with this period, which is a most unusual one.

In general, the western economies have seen extremely low rates of inflation. It varies, of course, from year to year, but on average it has been low. Even in the two decades of full employment in the 1950s and 1960s it was only around 3 per cent. With the exceptions of wartime and the unique circumstances following the 1970s, it has usually been even lower. Low inflation is the norm, and the opening years of the twenty-first century are no exception to this rule.

Low inflation exists because of appropriate institutions and structures. These are very complex but can be described very simply. First, the structures of capitalism, to a much higher degree than any other previously or actually existing social and economic system, encourage innovation. Second, there is the existence of competition in the product markets. I do not mean by this the idealised world of perfect competition in economic theory, but we cannot ignore the substantial amount of competition which there is in most product markets. These two factors set the general framework for low inflation.

It is not an accident that the hyperinflations, when inflation reaches millions of per cent, we have seen have only taken place in a restricted set of institutional settings: in siege economies, in wartime and in societies in which the fabric of civil society is extremely strained – Germany in the 1920s, various central European states at the end of the Second World War, Balkan economies in the 1990s are some examples of hyperinflation. All these were societies under massive strain. We could think of some European countries, such as Britain and Italy in the mid-1970s, as very mild examples of this latter phenomenon.

A monetarist might well say that irresponsible monetary policies could prove stronger than these two institutional factors. In a logical sense, this is trivially true. But in practice we never, ever observe a central bank in an orderly, peacetime western society expanding the money supply by one million per cent, even assuming there were enough helicopters in the world to scatter it with. It is much harder to imagine a counter-factual in which this happens than it is to imagine the workers of Britain and Italy being disciplined by monetary policy in 1974.

An implication of this is that detailed, short-term targeting of inflation rates is more or less meaningless. We should decide the kind of inflationary regime we are in – a low one at present – and not worry about year-on-year fluctuations. The ECB should be far more concerned with output growth than with inflation.

The lack of any stable relationship between the growth in demand and inflation in the European Union is shown in Figure 6.1. This plots the annual rate of inflation in the EU 15 against the rate of growth of real GDP over what might be termed the 'transition' period of 1971–94. Inflation rose in the early 1970s, was gradually contained and by the mid-1990s had fallen to under 3 per cent.

The striking feature of the chart is the lack of any recognisable pattern in the relationship between inflation and growth. The picture is the same if the growth in the previous year is used instead. Yet policy makers continue to act as if faster growth leads automatically to higher inflation. In reality, fast growth can coincide with low inflation, the United States of America in the 1990s being but the latest example of this.

It is the misplaced emphasis on containing inflation which is my main concern about the operation of the euro. If this has the effect of restricting output growth in the European Union, the developing world is likely to suffer even more than the Union itself. Far from assisting the rest of the world, the euro may damage it. The potential parallels with the Great Depression of the 1930s and the policies of central bankers are too close for comfort in the present circumstances.

So, overall, if I were a potential EU member I would say that the case for joining remains very strong. But this is because of the access gained to the enormous EU

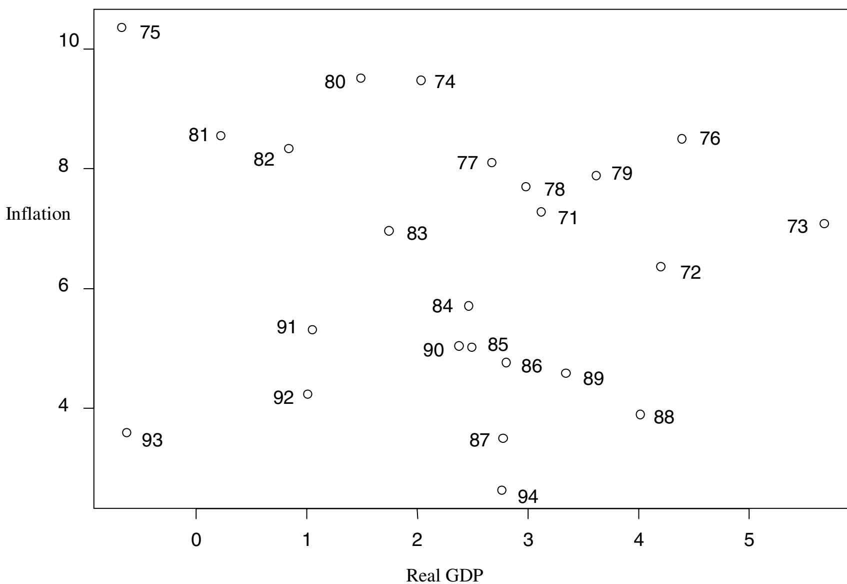

Figure 6.1 Inflation and real GDP growth in the EU15 (%).

market and the increased attractiveness of the country to foreign investment rather than to the elusive benefits of the euro. I would prefer that the member states had focused their energies over the past few years on admitting eastern European states rather than on the euro. I would hope that any economic difficulties which might arise from the euro would not continue to distract them from this. Finally, if I were, say, a South American government, I would certainly be worried about an economic slow-down in Europe, and concerned in particular that the policies of the ECB might exacerbate this, with potentially devastating consequences for my economy.

7 The ECB in theory and practice

Mark Baimbridge

Introduction

The European Central Bank (ECB) is a creation of the Treaty on European Union (TEU), which designed it to be the most independent monetary authority in the world. The ECB's architects sought to insulate it completely from political pressures, both at the national government and at the eurozone level. The position of the ECB under the TEU permits no clear accountability to either national or federal European institutions. It stipulates that the ECB Council's deliberations remain confidential, whilst the only method of questioning the ECB's policies is through periodic reports to the European Parliament. The ECB is the sole body credited with determining the appropriate monetary and exchange rate policy for the entire eurozone and as such its ability to fulfil its stated objectives will be crucial to the eventual success or failure of European Monetary Union (EMU).

The crucial operational features of the ECB are that its sole policy objective is the pursuit of price stability. It is also responsible for defining and implementing the European Union's monetary policy, together with supporting the attainment of general economic objectives. This design format is founded upon both theoretical (Kydland and Prescott 1997; Barro and Gordon 1983; Alesina 1989; Alesina and Grilli 1991) and empirical (Bade and Parkin 1988; Alesina 1988 and 1989; Cukierman 1992; Alesina and Summers 1993) studies whereby the transfer of monetary policy from governments to an independent central bank is likely to result in lower inflation.

Consequently, the paucity of critical analysis of the ability of the ECB to stabilise the eurozone economy, complete with low inflation, full employment, a sustainable balance of payments and good level of economic growth, should be of great concern for all interested in European integration. However, the legal framework, institutional arrangements and emerging operating practices of the ECB are increasingly coming under closer scrutinisation and criticism (Buiter 1999; Howarth and Loedel 2003). This chapter seeks to contribute to this debate through analysing two aspects of the ECB. First, it reviews its theoretical underpinning in terms of the concept of central bank 'independence'. Second, it examines the ECB's philosophy and conduct of monetary policy.

Central bank independence

The apolitical status of the ECB can be examined in greater detail in relation to the concepts of economic and political independence. The latter refers to its decisions not being conditional on the approval of government, whilst the former pertains to its ability to operate monetary policy without government undertaking contrary actions. Table 7.1 illustrates the comparative position in terms of the political, economic and combined indices of national central banks (NCBs), following the adoption of the ECB criteria. The comparative figures are calculated by subtracting the value of the ECB indices from those of the EU member states' central banks. This procedure clearly identifies the German Bundesbank as providing the blueprint for the ECB with no required revisions to its independence characteristics. The central bank of the Netherlands is the only other to fall below the overall mean comparison figure of six, whilst Denmark and Ireland coincide with the average. In contrast, those NCBs requiring the largest institutional reforms to meet the TEU requirements were, in ascending magnitude: Belgium, France, Spain, Britain, Italy, Greece and Portugal. It is interesting to note that this division of EU member states mirrors the established concept of 'core' and periphery groups regarding the formation of the single currency area.

The belief that central banks should be independent from political influence has deep historical roots and featured in the discussions leading to the establishment of many twentieth-century central banks (Toniolo 1988). The historical desire to impose limits upon the government's ability to fund itself through seigniorage is combined with the orthodox contemporary argument that politicians manipulate monetary policy to win elections, resulting in an excessive concentration upon short-term macroeconomic fine-tuning (Swinburne and Castello-Branco 1991). The conceptual case for central bank independence is primarily based on the view

Table 7.1 Comparison of central bank independence of EU member states and the ECB

	Present index of political independence	*Comparison to political independence of ECB*	*Present index of economic independence*	*Comparison to economic independence of ECB*	*Comparison to combined independence of ECB*
Belgium	1	–5	5	–2	–7
Denmark	3	–3	4	–3	–6
France	2	–4	4	–3	–7
Germany	6	0	7	0	0
Greece	2	–4	2	–5	–9
Ireland	3	–3	4	–3	–6
Italy	4	–2	1	–6	–8
Netherlands	6	0	4	–3	–3
Portugal	1	–5	2	–5	–10
Spain	3	–3	3	–4	–7
UK	1	–5	5	–2	–7
Mean	3	–3	4	–3	–6

Source: Baimbridge *et al.* (2004).

that arrangements raising the credibility of monetary policy will increase its effectiveness in pursuit of price stability. Although this view has long been held, only in recent years has the concept of policy credibility been defined and analysed rigorously (Cukierman 1986; Blackburn and Christensen 1989). The establishment of an independent central bank with strong anti-inflationary preferences is seen as a way for the state to bind its hands against the electoral temptation of inducing unanticipated increases in the price level. As commitment increases credibility, orthodox theory predicts that divergences between the central bank's policies and people's expectations will become smaller. It is from this theoretical perspective of monetarism and rational expectations that the ECB was launched.

However, this approach has been challenged. First, if central bank independence increases credibility, it should be associated with greater rigidity in the setting of nominal prices and money wages, reflecting the fact that the bank's promise to keep inflation low is believed. However, studies of OECD countries by Posen (1993, 1998) indicated that neither effect occurs. Indeed independence not merely fails to reduce the cost of disinflation, but rather seems to increase it.

Second, most of the contemporary support for central bank independence stems from a partial and frequently historically naive view of West German experience, whereby any one item that helped to promote rapid post-war German growth, such as the independent Bundesbank, was part of a structural totality defining its role. Accordingly it is unlikely to be effective if transferred by itself to other countries or onto the broader EU stage (Dowd 1989, 1994). It may be more appropriate to reverse the fashionable view; the structural conditions that produced the strength of the German economy, allowing it to grow while maintaining a low inflation rate also enabled it to afford the luxury of an independent central bank concentrating on monetary stability.

Third, the theoretical case for independence is based on two analytical assumptions that have become generally accepted by economists: (i) the vertical long-term Phillips curve, which implies that price stability can be achieved with no long-term cost of unemployment; and (ii) the political business cycle. However, both rest on insecure foundations. The vertical Phillips curve analysis rests upon the concept of a natural rate of unemployment, the frequently changing determinants of which economists remain largely ignorant (Davidson 1998; Karanassou and Snower 1998; Madsen 1998; Nickell 1998; Phelps and Zoega 1998). Moreover, repeated studies indicate that relatively little evidence exists for the occurrence of any systematic political business cycle (Kalecki 1943; Breton 1974; Nordhaus 1975; MacRae 1977; Wagner 1977; Frey 1978; Alesina 1989).

Fourth, the empirical evidence concerning central bank independence and lower-than-average inflation compounds difficulties. The persuasive nature of monetarist ideas led to the widespread conviction that low inflation is an important condition for high and sustained growth. Thus its achievement should be the priority for government economic policy. However, many studies indicate that no significant relationship exists between low inflation and higher rates of growth until double-digit rates of price increase occur, which do retard economic development (Thirlwall and Barton 1971; Brown 1985; Stanners 1993).

Moreover, economic policy objectives should be sufficiently comprehensive as to include the pursuit of multiple policy targets. However, if responsibility for price stability rests solely with an independent central bank, while others remain with government, economic management potentially becomes more difficult due to the separation of monetary and fiscal policy (Blake and Weale 1998). Hence, an advantage of a non-independent central bank is that budgetary and monetary measures can complement each other, forging a coordinated strategy of economic management. Analysis of the role of a central bank confirms that, in a world of external shocks, the case for delegating monetary policy is weak and that a coordinated approach is more likely to achieve the electorate's objectives (Rogoff 1985a, 1985b). Moreover, periods of high inflation have not occurred wholly, or even mainly, due to lax monetary expansion, whilst there is greater international evidence of fiscal, rather than monetary, policy being manipulated for electoral ends (Alesina 1989).

When assessing the impact of central bank independence upon price stability, economists have mostly utilised imputed 'degrees of independence' to evaluate the heterogeneous character of central banks (Mangano 1998). The initial method of imputing degrees of independence, based solely on legislature arrangements, found no relationship between inflation performance and independence (Bodart 1990). The index was refined by subsequent studies, which constructed a measure of central bank independence that reflected both 'political independence' and 'economic independence' (Alesina and Grilli 1991, Grilli *et al.* 1991). The former relates to the ability of the monetary authorities to choose the goals of policy, whilst economic independence is defined by their capacity to choose the instruments with which to pursue policy objectives. The main conclusion from such analyses is that the average rate of inflation, and occasionally its variability, is significantly lower in countries that possess independent central banks.

However, the value of such evidence is problematic, as the authors usually acknowledge, because measurement of 'degrees of independence' possesses serious weaknesses, which cast doubt upon the purported association between central bank independence and the attainment of price stability. The main failings of this approach are (i) that a limited spread of rankings inevitably restricts sensitivity across a wide number of inherently different countries, which raises difficulties concerning the index's analytical usefulness; (ii) that many of the studies cover overlapping time periods, opening up the possibility that they have found a result unique to that particular set of data (Friedman and Schwartz 1991).

Fifth, disregard for non-economic factors that shape fiscal and monetary policy choices is a consistent feature of these studies, illustrated by their assumption that electorates always prefer low inflation to the possible trade-off of higher economic growth and employment (Muscatelli 1998). However, even after analysing the role of political factors, other potential sources of differences in inflation rates are often neglected, such as the position of the government in the political spectrum and various proxies of social consensus (Hansson 1987), the size of the public sector (Alesina 1988) and that lower inflation could result from the presence of 'guest' workers during periods of economic growth (Burdekin and Willett 1991).

Finally, a problematical aspect of this research is the statistical analysis of the link between central bank independence and inflation, with most studies relying upon the plotting of graphs. Furthermore, the manner in which the determined characteristics of central banks are aggregated to produce the overall index of central bank independence is a major area for concern. Consequently, the index is usually constructed through one of a number of alternative methods, none of which is universally valid.

Monetary policy and philosophy

In October 1998 the Governing Council of the ECB announced that a key aspect of monetary policy strategy would be a quantitative definition of price stability. Furthermore, in order to assess risks to price stability, the ECB would make use of two pillars. First, attributing a prominent role to monetary indicators as signalled by the announcement of a quantitative reference value for the growth of a broad monetary aggregate and, second, a comprehensive analysis of a wide range of other economic and financial variables as indicators of price developments (ECB 1998, 1999, 2000, 2001; Issing *et al.* 2001). In relation to the quantitative definition of price stability, the ECB Governing Council initially did not give a precise definition. In order to specify this objective more precisely, the Governing Council announced the quantitative definition of price stability as 'a year-on-year increase in the Harmonised Index of Consumer Prices (HICP) for the euro area of below 2 per cent which was 'to be maintained over the medium term (ECB 1998). Consequently, the ECB (2003) argued that this definition of price stability has been conducive to a firm anchoring of inflation expectations in the euro area at levels compatible with the definition, thereby helping to contain the inflationary effects of the substantial price shocks which have occurred.

While the announcement of a quantitative numerical value for the price stability objective of the ECB was welcomed, there has been criticism regarding specific features of the definition. First, regarding the choice of the price measure, it has been argued that the ECB should put more emphasis on measures of 'core' or 'underlying' inflation, or even specify its objective in terms of a measure of core inflation (Gros *et al.* 2001; Alesina *et al.* 2001). Such measures could help to avoid the risk of monetary policy makers focusing excessively on temporary price fluctuations. Second, it has been argued that the ECB's quantitative definition may be too ambitious given a positive measurement bias in the HICP that could hamper the adjustment process at low levels of inflation (Fitoussi and Creel 2002; De Grauwe 2002). Third, it has been argued that the ECB's definition is imprecise and asymmetric, which may result in it being less effective in anchoring inflation expectations and possibly hindering the clarity of explanations of policy moves (Svensson 2002, 2003; International Monetary Fund 2002). Finally, the choice of the specific quantitative objective requires a balance between the costs of inflation and rationales for small positive inflation rates (Yates 1998; Wynne and Rodriguez-Palenzuela 2002; Coenen 2003; Klaeffling and Lopez-Perez 2003). Unfortunately, such a review of the costs and benefits of moderate inflation does

not allow the optimal rate of inflation to be precisely defined; it indicates the need for an inflation objective embodying a sufficient safety margin against deflation. In response to this criticism the ECB (2003) suggested that inflation objectives above 1 per cent provide sufficient safety margins to ensure against these risks.[1]

In relation to the first pillar, its key characteristic is the announcement of a reference value for the annual growth of M3. Hence, the ECB seeks to communicate the medium-term focus of monetary policy to the public, as it relieves the central bank from responding to short-run fluctuations in financial and other variables (ECB 2003). Furthermore, by signalling continuity of the Bundesbank's strategy, the ESCB hoped to quickly establish credibility (von Hagen and Brückner 2002). However, the role of money and monetary analysis has generated controversy regarding the robustness of the chosen leading indicator's properties with respect to price developments, on the grounds that the correlation between money growth and inflation appears to have declined over time in parallel with restored conditions of price stability (Begg *et al.* 2002). In this context, the necessity for announcing a reference value for money growth has also been queried, together with the usefulness per se of a separate 'money' pillar (Svensson 2003).

In contrast, the second pillar consists of an assessment regarding future price developments (ECB 1998). Initially, it represented the analysis of short-run price developments based on measures of real activity, wage cost, asset prices and fiscal policy indicators, together with indicators of business and consumer confidence (ECB 1999). However, no framework was specified as to how these variables would be used to assess price developments, nor was any guidance given on the relative weight of the variables in such assessments. It is therefore an opaque part to the ESCB's strategy, being void of systematic analysis and being fully discretionary (von Hagen and Brückner 2002). Furthermore, Gaspar *et al.* (2001) suggest that the analysis is now organised in the form of a macroeconomic projection, although the ECB does not provide confidence intervals for its projections (Gali 2001).

Finally, according to the ECB (2003), the two pillars are used in parallel in monetary policy decision making. However, there is no indication of what their relative weights are, thus resulting in an incomprehensible strategy, as Issing *et al.* (2001) partially acknowledge. Although there is nothing that would make the use and revelation of the relative weights of the two pillars impossible, the reason why the ECB has so far denied the public transparency of its strategy is more likely related to the internal decision-making processes (von Hagen and Brückner 2002).

Labour's response to central bank independence

Whether or not Britain has an independent central bank may seem an obscure matter. But it is not. It is crucial to determining whether a Labour government can deliver on a range of policies from the basics of growth and jobs to wider issues of social justice. The cause of central bank independence became a 1990s bandwagon that a great many people scrambled to join. For instance, two former Conservative Chancellors of the Exchequer, Nigel Lawson and Norman Lamont, together with ex-Treasury Chief Sir Peter Middleton, pressed the case for an independent Bank

of England after their respective departures from government. Indeed, for those still clinging on to the remnants of monetarism, they discerned that an independent central bank would be the ideal way of securing the monetarist legacy beyond the 1980s. An independent bank would ensure that monetarists remained in power if not in office, because it would steer the economy by financial indicators to the detriment of the real economy. Hence, they believe that central bank independence would lock monetarism and monetarist priorities into the system regardless of whether Labour came to power.

However, perhaps the greatest catastrophe in this area was the near universal acceptance by Labour politicians and policy advisors of the merits regarding central bank independence. Many were swayed by the number of commentators who wrote favourably on the subject, arguing that this provided the medicine for Britain's economic malaise; others required little convincing, such as pro-EU enthusiasts who happily accepted that as part of the TEU it must be good; whilst a final group were attracted by the idea of being able to impose a high interest rate regime via an independent central bank without having to answer to the public or to the Labour movement for the consequences. Thus, through this unholy alliance the New Labour hierarchy accepted with little question the concept of central bank independence upon gaining power in 1997; one of its first acts was to grant the Bank of England 'operational independence' regarding the setting of interest rates in accordance with an inflation target. However, the Labour Party cannot accept this contemporary swing in opinion if it is to remain true to its fundamental belief in social justice (see Bean 1993; Holtham 1993).

The concept of an independent Bank of England, or an independent ECB, essentially seeks to revert to the principles of the gold standard, under which the level of money wages was compelled through the rate of interest to adjust to the operation of the financial system. Thus structures of social protection become open to undermining by the operation of unaccountable market forces. Independent central banks, national or continental, are currently being advocated as the vehicle to implement this sea change in the class struggle. Socialists, on the other hand, must continue to assert the primacy of democratically accountable control over the money supply, in order that the goals of full employment, rising living standards and distributive justice can be pursued. Otherwise the business and moneyed interests, which control credit flows and determine financial confidence, will exert a silent veto through the 'independent' central bank over the range and character of government action deemed to be 'permissible'. The exercise of such a veto would mean permanent deflation and institutionalised higher unemployment throughout the European Union and the United Kingdom.

Conclusion

The theoretical and empirical evidence surveyed in this chapter suggests that the creation of an independent central bank is a more finely balanced exercise than is frequently portrayed, in particular given national economies which continue to experience varying economic cycles and possess divergent economic structures.

Moreover, the interest rate decisions taken by central banks are amongst the most sensitive actions deployed in a modern economy, influencing growth, living standards, the level of unemployment and the cost of credit and mortgages.

The ECB's problems arise from its lack of democratic accountability, transparency and democratic legitimacy as well as from its arbitrary objectives, questionable economic philosophy and the potential for intermittent conflict with the national governments whose destinies it possesses considerable influence over. An alternative model of a democratically accountable and controlled ECB, operating in coordination with a combination of nationally determined fiscal policies, or a newly established federal authority, would prove a more effective and desirable model for EMU.

Note

1 This is also in line with the practice followed by all of the central banks of the major developed countries that have specified numerical values for their objectives; all have a mid-point above 1 per cent. For example: the Bank of England: 2.5 per cent (RPIX index, approximately 1.75 on average in HICP terms); Sveriges Riksbank: 2±1 per cent (CPI); Norges Bank: 2.5±1 per cent (CPI); Bank of Canada: 1–3 per cent (CPI); Bank of Australia: 1–3 per cent (CPI); Reserve Bank of New Zealand: 1–3 per cent (CPI). The Federal Reserve System and the Bank of Japan have not specified a quantitative definition of their price stability objectives. The Swiss National Bank has adopted a definition of price stability that is equivalent to that of the ECB.

8 The left must wake up – Europe isn't working

Larry Elliott

History, says Tony Blair, is on his side. Back in 1975, Labour turned public opinion around over Europe, and if Harold Wilson could do it then, Blair sees absolutely no reason why he can't do it now.

If nothing else, you have to admire the prime minister's confidence, but he is deluding himself if he thinks the conditions in the mid-1970s are even remotely the same as those today. Wilson had the leaderships of all three parties on his side, together with business and the press. Ironically, however, Wilson's trump card was that he was presiding over one of Europe's most dysfunctional economies.

For those not old enough to remember, 1975 was the year of stagflation – unemployment was rising and inflation hit a post-war peak of 27 per cent. The vote over whether Britain should pull out of the European Economic Community came less than 18 months after the country had been put on a three-day week, and prudent families still kept a healthy stock of candles in case the lights went out.

But it was not just that Britain's performance was so dismal; it was that Europe was doing much better. Germany was Europe's powerhouse, with its recovery symbolised by the spanking new stadium built in Munich for the 1972 Olympics. Voters looked across the Channel and came to the obvious conclusion: Europe worked and Britain didn't. In those circumstances, it was not difficult to persuade the electorate to have second thoughts.

The comparison with 2004 is stark. Back in 1975, Britain was about to get an unwelcome visit from the International Monetary Fund, which insisted on deep and unpopular cuts in public spending as the price of a rescue package. Today it is the eurozone that is the target for the IMF's criticism; it has concerns about Britain's housing market, but says Europe is the one part of the world left untouched by the global recovery. Economic conditions, it says, remain wintry and justify lower interest rates to stimulate growth. When even the IMF is urging cheaper borrowing, you really have got problems.

None of which is to argue that all is wonderful with Britain's economy. Those who point to the whopping trade deficit, the withering of manufacturing and the mountain of consumer debt are right to be concerned that the good times might not last for ever. But the signs are that, for the next couple of years at least, Britain will continue to enjoy faster growth and lower unemployment than the single currency bloc. 'In contrast to the eurozone, macroeconomic performance in the

UK remains strong and the main risk to the outlook is the possibility of an abrupt correction in the housing market', the IMF says. It likes the way the Bank of England has handled interest rates and praises Brown for using higher public spending to underpin growth.

For a nation that has tended to be indifferent, if not downright hostile, to the idea of closer political integration in Europe, all this matters. The idea that Britain risked missing out on a big party happening on the other side of the Channel proved a compelling argument in 1975, but it lacks the same punch today. Indeed, giving extra powers to a Europe that is struggling sits oddly with the government's approach to failing schools and underperforming hospitals.

This problem haunted Blair as he contemplated whether to hold a referendum on the euro, and in the end he decided – almost certainly correctly – that he could not hope to convince voters that joining the single currency was vital for Britain's future prosperity at a time when the eurozone was doing so badly. The same will apply to any campaign on a constitution; the government may find that a generally quite contented public rejects the argument that a Europe of 25 nations requires changes to the relationship with Brussels and will simply ask: 'If it ain't broke, why fix it?'

Of course, those pressing for a yes vote will say that Britain will be broke unless it supports the constitution and (eventually) joins the euro, but the conservatism of the electorate should not be underestimated.

There is an alternative scenario, which is that the prophets of doom are right about Labour's economic 'miracle' being built on sand. Should there be an almighty crash in the property market which pushed the economy into recession and sent unemployment surging back above a million, then it might be possible to deploy the 1975 argument. This would be good news for Kenneth Clarke, Michael Heseltine and other Conservative pro-Europeans, but it would put at jeopardy Blair's chances of winning a third election. In short, the prime minister is in a bit of a fix. If the economy stays strong he stands to win the election, but lose the referendum. If the economy blows up, he wouldn't be in a position to hold a referendum because he will have been kicked out of Downing Street.

Two conclusions can be drawn from the recent spat between Gordon Brown and the European Commission over fiscal policy. The first is that the Stability and Growth Pact is in tatters. The second is that those who should be supporting the demise of this monetarist relic risk being on the wrong side of the argument.

The arguments used to defend the Pact are not new. Sir Geoffrey Howe was fully acquainted with them when in the spring of 1981 he tightened fiscal policy during the depths of Britain's worst post-war recession.

This was monetarism's moment. Howe justified the budget squeeze by arguing that higher deficits would lead to an increase in the money supply. That, according to Milton Friedman's disciples, meant higher inflation. They hailed the chancellor's action as a wise move which yoked together the two central pillars of monetarism: controlling the money supply and balancing the budget. Growth started to pick up shortly afterwards. QED.

Not everybody saw things this way. *The Times* printed a letter signed by 364

members of the great and good of the economics profession. They viewed Mrs Thatcher's ideas as reactionary, deflationary nonsense and warned that tightening fiscal policy in a slump would hold back recovery and that unemployment would continue to rise (as it did, for another five years).

Whatever the rights and wrongs of this argument, by the time of the second big Conservative recession in the early 1990s, both of monetarism's main tenets had been ditched. The money supply was no longer targeted and big budget deficits were amassed. Two bouts of high unemployment put paid to talk of balancing the budget, although one way of saving money was found – cutting capital spending on Britain's infrastructure. The cumulative effect of this neglect – exacerbated by Labour's parsimony in its first term – is now glaringly evident.

Fortunately, since the death of monetarism the United Kingdom has found a better way to achieve healthy public finances. Growth has averaged 3 per cent a year and unemployment has fallen. The result has been that the ratio of public debt to GDP has dropped to about 30 per cent and the budget on current spending was in surplus for over four years. The government decided to exploit this strong fiscal position by pledging to borrow money so that it can double net investment to 1.7 per cent of GDP by 2003–4. Even so, this will only repair a small fraction of the damage caused by years of neglect, taking net investment back to the levels of 1989, Thatcher's last full year in power, and still well below the average for the European Union as a whole.

So what's wrong with ploughing money into the nation's infrastructure, you might ask. Nothing, provided you accept that there are positive returns to be made on investment in capital infrastructure in a country like Britain, which has a very sound fiscal position.

But – of course, there is a but – Mr Prudent's plans are seen as not prudent enough by the European Commission, which views the intention to borrow 1.2 per cent of GDP (£10bn a year in real money) as a breach of the Stability and Growth Pact, which requires member states to keep their budgets in the black. Brown went ballistic when the Commission published its views. The government has a mandate for what it is doing, having fought and won the 2001 General Election on the issue of increasing spending on public services.

Moreover, it is clear that the government's fiscal set-up is far more flexible and appropriate to current economic conditions than the Stability and Growth Pact, underpinned as it is by the same monetarist belief in balanced budgets that gave us the 1981 budget. Britain's fiscal rules distinguish between current and capital spending, and ensure that public finances are sustainable over the economic cycle as a whole. The Pact does neither.

Brown is not the only finance minister to realise that there are serious flaws in the Pact. A meeting of European Union economic and finance ministers last summer agreed a new code of conduct for interpreting the Pact, including the need to take into account the state of the economic cycle, whether the level of public debt is sustainable and the case for higher spending on investment. The Commission, for reasons best known to itself, ignored all this and proceeded to interpret the Pact rigidly when it looked at the state of EU budget deficits.

In Britain's case, there was some justification for concern. The method for calculating whether a country's fiscal policy is entering the danger zone takes account of how volatile the economic cycle is and how responsive the deficit is to changes in growth. Britain has seen gyrations in the economic cycle, and its low marginal tax rates mean that the deficit is sensitive to changes in GDP. As such, the Commission believes that the UK deficit should be 0.5 per cent or lower, just to be on the safe side.

Brown argues that this takes no account of the changes made to UK fiscal policy since 1997, and if implemented would force him either to raise taxes or cut public spending to an unacceptable degree. Balancing the budget would mean reducing the planned deficit by 1.2 per cent of GDP – about £10bn a year. This is the inexorable logic of the Commission's position, despite its attempts to wriggle off the hook.

This is where the fun really begins, because at this point an arcane argument about fiscal policy becomes intertwined with the question of euro entry and the timing of a referendum. The Growth and Stability Pact is dumb economics. It was a 30 per cent devaluation and lower interest rates that prompted recovery in Britain from the slump of the early 1980s, not Howe's monetarist budget. One thing Europe's economy certainly does not need at present is a pro-cyclical fiscal policy. As far as Britain is concerned, dogged support for the Pact is even dumber politics. Root-and-branch reform of the Pact would make it easier, not harder, to convince a sceptical public of the dubious benefits of euro membership.

From Brown's point of view, the prospect of Britain coming under pressure to cut public spending if it joined the single currency is a serious issue. Most Labour supporters would agree; they find it difficult to accept the idea that the national interest would be served by further needless cuts in planned spending on the public infrastructure. Union leaders, particularly those strongly represented in the public sector, are becoming decidedly twitchy.

All this is deeply unhelpful to those who believe that it is the Treasury's job to ignore the dubious economics of monetary union and rubber-stamp an early euro referendum. Opponents of monetary union are supposed to be frothing right-wing xenophobes, not trade unionists and Labour voters anxious about public spending cuts resulting from the application of outdated monetarist dogma. As such, Brown's entirely justified insistence that the Commission back off has been greeted frostily by those who would have been up there on the barricades with the 364 anti-Thatcherites in 1981. They are now in the confused position of trying to draw a distinction between two kinds of spending cuts: Conservative spending cuts (reactionary and bad) and European commission ones (progressive and good).

Scepticism is hard-wired into the left. It is sceptical about the claims made for the private finance initiative. It is sceptical about the government's claims for weapons of mass destruction in Iraq. It is sceptical about trickle-down economics, the need to build over the green belt, GM foods and the World Trade Organisation.

Nobody bats an eyelid at any of this. Scepticism is the beating heart of democracy; it is what informs the approach of a Jeremy Paxman when confronted by a cabinet minister. Scepticism is seen as right and proper in all areas of policy

bar one. That, of course, is Europe, where scepticism is viewed as that most heinous of sins – fraternisation with the swivel-eyed loonies of the right.

This response is futile and daft. Scepticism about the European Union is inevitable and long overdue, particularly on the left. Let's take a few examples. Who among us is not sceptical about the Common Agricultural Policy, which costs every family of four an extra £16 in dearer food bills and stunts the development of poor countries by denying them access to European markets? Aid agencies such as Oxfam have been outspoken in the need for radical reform.

And how about the Common Fisheries Policy? Were not the environmentalists right when they said it would result in the waters of the North Sea being hoovered dry by factory trawlers?

And then there's growth and unemployment. More than a decade ago the Keynesian left in Britain warned that a European central bank with a deflationary mandate would result in weak growth and lengthening dole queues, and they were absolutely correct.

Some of the smaller countries in Europe – Ireland and Finland, for example – have better recent records than the United Kingdom, but overall the performance of the 12-nation eurozone has been dire. It is 12 years since it enjoyed faster growth than Britain, and the result has been a big difference in unemployment: below 5 per cent in the United Kingdom, almost 9 per cent in Euroland. What are we to do in the face of such figures: express scepticism about the claims made for the euro or shut up?

The answer for many on the pro-euro left is that the aid agencies, the greens, the anti-globalisers and the Keynesians should pipe down. Yes, they say, Europe has its faults, but there are good reasons for the left to support it.

These are serious arguments and are worthy of serious consideration. One is that Europe is the only serious bulwark we have against the Americanisation of the globe. A second is that European capitalism is gentler than its rapacious Anglo-Saxon cousin across the Atlantic. A third is that Europe leaves Britain for dead when it comes to roads, railways and the public realm in general. Finally, closer integration has meant that half a century of war has been followed by half a century of peace.

To take the last argument first, the notion that Europe has to move closer together in order to prevent war has always seemed as dubious as the idea that it was all due to the bomb. A more likely explanation is that the nineteenth-century balance of power – which broke down in the first half of the twentieth century – was recreated in a new form by the post-war US–Soviet Union duopoly.

The problem with the first three arguments is that they all rest on the same premise, and that is a strong economy. Political clout is a function of economic clout, and America's lead over Europe has been widening in recent years. Europe's social democracy thrived in an era when the German economy was humming along at 5 per cent a year and France had the lowest unemployment rate in the west; it is an unaffordable luxury when the eurozone is growing by 1 or 2 per cent a year. Gerhard Schroeder and Jacques Chirac know that – which is why they are being forced to embrace flexible labour markets and welfare reform. Those on the

left who think that Europe is a refuge from US-style labour markets are living in cloud-cuckoo-land, because with the ECB and the European Commission eschewing expansionary macroeconomic policies, the only alternative is greater flexibility and supply-side reform.

Predictably enough, this is causing apprehension, prompting the Germans, for example, to save rather than spend, thus leading to even lower levels of growth and even shriller calls for root-and-branch economic reform. And voters are now starting to ask some searching questions, across Europe and not just in Britain.

In the end, there is a simple choice. There can be a left-wing critique: Europe has a strong manufacturing base and an impressive stock of human and physical capital, but needs to grow faster and relocalise power. Or there can be a right-wing critique: it needs a solid dose of Thatcherism to buck its ideas up. The status quo is not an option, because clearly Europe isn't working. Those who pretend it is are in category-one denial.

9 A post-Keynesian strategy for the UK economy

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Introduction

Post-Keynesians argue that the level of output and employment depends upon the interaction between total spending and the economy's capacity to produce. Thus a crucial problem with market capitalism is that it possesses no mechanism that guarantees that output and spending decisions always coincide. Therefore enormous scope exists for government macroeconomic policy to initiate, pursue and implement stabilisation through the budgetary monetary measures. The potential to generate a post-Keynesian strategy will, however, be thwarted if the United Kingdom participates in European Economic and Monetary Union (EMU) within the European Union (EU). Membership requires the separate formulation of money policy from nationally determined fiscal policy, leading to a resultant lack of policy coordination prejudicial to the construction of a post-Keynesian economic framework. The resultant slow-growth, high-unemployment outcome will be further exacerbated by the transfer of monetary policy to a European Central Bank (ECB), whose sole legal objective is the pursuit of price stability. This chapter therefore seeks to develop an alternative post-Keynesian strategy for the United Kingdom based upon a long-term opt-out from the euro. Its fundamentals are achieving a competitive exchange rate, higher investment, a social contract to restrain inflationary pressures via planned redistribution, the reintroduction of exchange control through a transactions tax on dealings unrelated to trade and the pursuit of an active industrial policy to increase the long-run competitiveness of British industry where it already possesses a comparative advantage.

A crucial idea introduced by Keynes (1936) into the corpus of economic thought is that the level of output and employment under market capitalism depends upon interaction between total spending and the economy's capacity to produce. Decisions to produce are made primarily by private profit-making firms; production, the source of employment, takes place only if companies anticipate a market in which goods and services can be sold at a profit. If demand is insufficient, productive capacity will stand idle and people will be without jobs. There is no automatic mechanism which guarantees that output and spending decisions always coincide.

Imbalances between aggregate demand and aggregate supply require active government policy to change either its own or private expenditure through budgetary or monetary instruments. The neoclassical assumption of an automatic tendency towards market clearing is replaced by the necessity for active government intervention in the economy to secure simultaneous internal and external balance in the economy.

Such a Keynesian framework is explicitly receded by the monetarist ideology of the Treaty on European Union (TEU), which laid the basis for EMU. A clear example of its approach is its reliance upon monetary tests of convergence rather than examining real variables of output growth and rates of unemployment. Its convergence criteria include restrictions upon discretionary fiscal policy through the implementation of maximum permitted budget deficits backed by the possibility of levying fines on non-compliant economies. The transfer of monetary and exchange rate policy to an independent ECB, whose sole legally defined objective is to secure stable prices through the use of a single economic policy instrument, a common Euroland interest rate, is at complete variance to a Keynesian approach. The political imperative to comply with this mandarin platform led to the European Union suffering a prolonged period of slow growth and high levels of unemployment.

This chapter highlights the incompatibility between the monetarist model, upon which EMU is constructed, and the possibility of creating an alternative economic strategy grounded in post-Keynesian tradition. Despite the inability of theorists to develop a universal post-Keynesian theoretical model, due in large part to the complexity and dynamic nature of modern economies, it is nevertheless possible to identify a number of important themes that denote the essence of post-Keynesian thought. We also outline the framework within which such an independent post-Keynesian policy could operate.

The TEU: a monetarist document

The TEU provided the foundation upon which EMU was to be constructed (EC Commission 1992). Initially drafted by representatives of Europe's central banks, the TEU established three stages to the introduction of EMU, namely:

- membership of European Exchange Rate Mechanism (ERM);
- evolution of the ERM into a 'hard' system, with no further devaluation nor exchange controls, together with compliance with five convergence criteria prior to entry;
- the establishment of a single currency, with all monetary and exchange rate policy controlled by a single ECB.

The purpose of these stages was to use the ERM to ensure a financial convergence between potential participants as each had to adapt their monetary policies to that of the the strongest economy, Germany, or face higher inflation rates eroding international competitiveness. This element of the strategy worked effectively, as

the variance of inflation rates across ERM member economies narrowed, albeit at the cost of stubbornly high levels of unemployment for many member states. Thus in January 2001 standardised unemployment across the 11 eurozone countries stood at 8.8 per cent compared to 5.1 per cent in the United Kingdom.

The evolution of the ERM depended upon the continued belief of the financial markets in the economic rationale of the ERM project. As soon as this assurance was questioned – when reunification required Germany to operate a tight monetary policy at a time when other ERM members required a relaxation of interest rates to offset impending recession – speculative attacks undermined the validity of a mechanism without exchange controls seeking to 'discipline' participating economies to pursue a monetarist anti-inflationary programme. It has been estimated that the cost for the United Kingdom of its two-year membership of the ERM was approximately £68.2 billion in 1992 prices (equivalent to 11.5 per cent of UK GDP) in terms of lost output plus one and a quarter million more unemployed (Burkitt *et al.* 1996).

Prior to the establishment of the single currency, the TEU required member states to demonstrate their suitability for single currency membership through their attainment of the five Maastricht convergence criteria (MCC). These were:

1. Each country's rate of inflation must be no more then 1.5 per cent above the average of the lowest three inflation rates in the EMS.
2. Its long-term interest rates must be within 2 per cent of the same three countries chosen for the previous condition.
3. It must have been a member of the narrow band of fluctuation of the ERM for at least two years without a realignment.
4. Its budget depict must not be regarded as excessive by the European Council, with 'excessive' defined to be where deficits are greater than 3 per cent of GDP for reasons other than those of a 'temporary' or 'exceptional' nature.
5. Its national debt must not be excessive, defined as being above 60 per cent of GDP and not declining at a 'satisfactory' pace.

The rationale for similarity of inflation performance is clear, interest rates and exchange rate strategies; otherwise the stability of the monetary union may be threatened by the participation of a high-inflation nation which could temporarily lower its headline rate through deflationary monetarist policies that caused its currency to appreciate but could not be sustained in the long run. However, the final two criteria are controversial in terms of their arbitrary maximum rates and restrictions upon discretionary fiscal policy (Baimbridge *et al.* 1999a). Moreover, Article 104c outlined financial sanctions that can be applied to national governments if either variable is above Treaty-specified level. These were subsequently strengthened by the Stability and Growth Pact (SGP), which clarified the excessive deficit procedure of the TEU. Its unprecedented power to fine member states demonstrates the priority given to constraining budget deficits.

Whilst the MCC may be criticised for omitting many of the important tests of convergence outlined in Optimum Currency Area theory (Baimbridge *et al.*

1999a), the majority of member states had the greatest difficulty in meeting even these objectives. Indeed one study found only a 10 per cent compliance rate between 1990 and 1997 (Baimbridge *et al.* 1999a).

The commencement of the third stage of EMU began on 1 January 1999, when all participating currencies were permanently and irrevocably fixed in value, and the sole federal body charged with managing the Euroland economy was created, namely the ECB, sole aim of which is to achieve price stability. Note that Article 3A does not mention any other criteria, such as increased economic growth, maximum employment or the achievement of stipulated welfare targets. Indeed these objectives can only be pursued when they can be achieved 'without prejudice' to price stability (EC Commission 1992). The creation of an independent central bank, independent of democratic control and given a single target of low inflation irrespective of the impact this has upon employment and growth rates, is in complete contrast to a Keynesian approach.

The establishment of a price stability objective for the ECB rests upon the assumption of a natural rate of unemployment, so that structural supply-side problems determine the level of unemployment. Therefore government should concentrate upon ensuring the lowest compatible level of prices. However, there is sizeable body of evidence challenging the existence of a distinct equilibrium level of employment (Davidson 1998; Karanassou and Snower 1998; Madsen 1998; Nickell 1998; Phelps and Zoega 1998). The prevalence of hysteresis, where the level of unemployment is path dependent, provides one analytical challenge to the rationale of ensuring that the ECB is more concerned with developing an anti-inflationary credibility than providing optimum conditions for industrial expansion. Furthermore, no statistically significant evidence exists that independent central banks produce lower inflation (Baimbridge *et al.* 1996b). The ECB is founded upon monetarist principles, which determine its operational objectives and over-concentration upon inflation despite the fact that high interest rates damage investment, thus lowering future produce capacity, employment opportunities and growth potential.

The SGP ensures that this deflationary approach will be maintained once countries have achieving membership of EMU. Permanently maintaining fiscal deficits below 3 per cent of GDP require a more intensive 'reform' of welfare provision than has already occurred. It is no coincidence that speculation concerning the unaffordable nature of current levels of public and final-salary company pensions coincides with the restrictions placed upon government expenditure by the MCC and SGP. Furthermore, maintenance of a budget balance within the SGP limits will require further public sector cuts, as large surpluses are necessary in periods of relatively rapid economic growth to ensure that state finances do not breach the 3 per cent of GDP limit during periods of recession associated with the business cycle (Baimbridge *et al.* 1999a). Therefore self-induced deflation with its associated historically high unemployment in the run-up to the creation of EMU – as EU member states sought to meet the MCC – has continued. Consequently it is no surprise that the initial value of the euro was weak, since Euroland has

continued to experience lower growth rates than indicated by their own output gaps, simply to adhere to these monetarist, anti-welfare targets.

A post-Keynesian alternative

The monetarist bias institutionalised at the core of the EMU project, which will prove difficult to reverse given its centrality to the TEU, is in sharp contrast to the theoretical predictions, and policy prescriptions, which emerge from the broad Keynesian tradition (see Table 9.1).

Table 9.1 A comparison between features of post-Keynesianism and EMU

	Post-Keynesianism	*Neo-liberal EMU*
Macroeconomic assumptions		
Economy tends towards full employment	No, capitalism is inherently unstable	Yes
Demand side		
Aggregate demand level	Vital, but unstable	Important
Aggregate demand management	Essential prerequisite for full employed economy	Not important, no federal instrument to manage demand
Fiscal policy	Main instrument to manage AD	Unimportant, prerogative of nation state
Monetary policy	Supportive to fiscal policy; cheap money to stimulate investment and growth	Uniform interest rate – set to produce price stability
Counter-cyclical	Yes	Limited by MCC and SGP on budget deficits
Status of central bank	Democratically controlled – given multiple objectives	Independent – sole target is price stability
Supply side		
What causes unemployment?	Demand deficiency and supply-side problems	Structural/supply-side factors
Model of unemployment	Hysteresis; tendency towards disequilibrium	Natural rate/NAIRU
Policies to reduce unemployment	Demand management, labour market policies, incomes policy (or wage bargaining coordination) industrial policy (including socialisation investment)	Level and duration of benefits
External balance		
Exchange rate regime	Short-term stability, long-term flexibility	Single currency
How to defeat destabilising speculation?	Capital controls, financial regulation	Large single economy less prone to destabilisation
Globalisation?	National autonomy remains possible	Integrated financial markets; no room for independent monetary policy

Disequilibrium and cumulative causation

The 1990s decade of deflation amongst EU economies was not a simple 'one-off' loss of potential income, but was a long-term process of relative decline fuelled by cumulative causation. The latter term was first used by Myrdal (1957) to convey the reinforcing processes whereby patterns of uneven development may be perpetuated and even accentuated. It constitutes a challenge to orthodox equilibrium theory, which holds that, if divergences in economic phenomenon exist, forces come into play that narrow these differences and ultimately eliminate them. However, in Myrdal's model of cumulative causation, markets reinforce inequality, so that focus on positions of static equilibrium is inappropriate and misleading. The deflationary impact of pursuing the Maastricht convergence criteria lowers current sales and profits, which in turn lead to falling investment, thus reducing demand in the future. By contrast, a post-Keynesian strategy of achieving full employment with growth, prohibited under the monetarism of Maastricht, will fuel an upward spiral of rising income, demand, investment and profitability.

There are many factors operating within capitalism that work towards disequilibrium rather than equilibrium once initial differences in economic and social phenomena arise. It is the process of change that should occupy the centre of analytical attention; this process is not a moving series of equilibrium, but a chain reaction of mutual feedback. The existence of destabilising feedback mechanisms implies that temporary disturbances may involve substantial social and economic consequences, which often gather speed at an ever-accelerating rate. Under cumulative causation, social forces interact with technical, economic and psychological factors, whilst the evolution of the economy depends upon, and is reflected by, the institutional organisation of economic phenomena.

Increasing returns to scale and economic growth

Hardin (1982) related cumulative causation to the existence of increasing returns. The latter jeopardises the existence of standard neoclassical equilibria, but more significantly it creates dynamic tendencies of uneven development. He concluded that 'both comparative success and comparative failure exert self-reinforcing effects', whilst the combination of profit-driven production and investment decisions, free trade and capital mobility produces inherent tendencies towards asymmetrical growth. Growth is perceived to be an endogenous, cumulative process based on increasing returns activities rather than the outcome of exogenously given expansion of factor endowments.

Cumulative causation also depends upon technology gaps, which represent the differences in technical advancement between rival nations, between industries in different countries or between firms in a given industry in one economy. Such gaps imply that technology is not uniform and that technical progress is not instanteously diffused. If these gaps are not simply a function of market failure, technology is more than an endowment and scarcity does not determine the resource allocation process. It is the learned ability to innovate and to imitate

existing commodities and ways of producing, which is the driving force behind higher productivity and competitiveness. The rejection of scarcity and of a crucial role for endowments changes the character of economic policy. In a scarcity-driven world, the state's function is to overcome market failure; in a world of technology gaps, economic policy promotes the innovation process support of research and development, subsidies, demand management and workplace democracy.

Technical change is cumulative and path dependent; it is neither random nor predictable. Agents do not usually share identical knowledge or competence. Moreover, the diffusion of technology requires time; the discontinuity of this diffusion process implies that, even with a steady rate of innovation (itself highly unlikely), technology gaps reinforces the conclusion of cumulative causation theory that convergence is by no means a guaranteed, nor even a frequent, occurrence. Therefore active government economic policy, restricted by the TEU, is essential to achieve an upward spiral of cumulative causation.

Aggregate demand, full employment and output capacity

The inherent instability of capitalist economies requires government intervention to maintain a sufficiently high level of aggregate demand to ensure the full employment of all resources. However, post-Keynesianism emphasises that the level of aggregate demand simultaneously influences the level of capacity utilisation and employment in both the short and the long run. The simulation of investment in the short run will facilitate full employment, but additionally produce additional capacity for an expansion of production in future time periods (Sawyer 1995). In the absence of sufficient future capacity, an economy could be 'too small' to employ all resources and expand at its optimum rate.

Socialisation of investment

A strategy to reduce the natural instability of capitalist economies would focus upon one of the main causes of fluctuations in output, namely entrepreneurial expectations and their resultant impact upon private-sector investment. The maintenance of a sufficiently high level of aggregate demand can contribute towards enhancing expectations of future profitability, whilst simultaneously facilitating a current budget surplus capable of financing a considerable proportion of future investment. However, this strategy leaves the investment function in private hands and therefore dependent upon unstable expectations. Keynes (1936, 1943–44) predicted recurrent problems of market coordination and underutilisation of resources due to a fundamental conflict between industry and finance, where, in a world of uncertainty, the short run behaviour of rentiers tends to prevail in the market for financial securities. The ability of rentiers to impose a constraint on the liquid funds available for the long-term finance of enterprises and their desire for liquidity results in rates of investment that lie below the level necessary to achieve full employment.

Keynes' solution to both these problems was the socialisation of investment.

Only the state could remain impervious to speculative financial gain, and therefore approve sufficient projects 'so as to preserve stability of aggregate investment . . . at the right and appropriate level'. When pressed by fellow economists in 1943 how far he would socialise investment, Keynes replied, 'two-thirds or three-quarters would be indirectly influenced by public and semi public bodies'. Thus full employment could be secured through the establishment of a National Investment Bank (NIB) charged with the strategic regulation of the aggregate flow of investment. This would ensure 'an adequate demand for them, partly by making them available at a rate which would attract a sufficient demand, and partly by stimulating the undertaking of particular investment projects'. More recent proposals of this type have advocated the democratic control of capital formation through pension-fund or employee investment-fund socialism (Burkitt and Whyman 1995). They are only feasible outside the constraints imposed by membership of EMU.

Interrelationship between demand and supply side

The relationship between aggregate demand and aggregate supply is one of the most significant insights to emerge from post-Keynesian thought (Sawyer 1995). Whilst a high level of aggregate demand is a necessary precondition for the full employment of resources, it is insufficient if the economy suffers from supply-side deficiencies. For example, active labour market policy is advocated where skill shortages and labour market bottlenecks threaten to destabilise the economy. Training and educational programmes can match skills to the demand for labour, whilst employment services enhance the efficiency of the search process (Layard *et al.*1991; Meidner 1985; Trehorning 1993). Similarly, incomes policy and/or the coordination of wage bargaining can deliver a superior trade-off between inflation and unemployment compared to decentralized, deregulated bargaining in those economies where trade unions are present.[1] Through internalisation of the costs of imprecise wage levels into the decision-making parameters of all parties to the negotiations, there is an increased likelihood of reaching a compromise between labour and capital over their respective shares of national income, without damaging international competitiveness, growth and employment. Moreover, the degree to which wage bargaining is coordinated is associated with real wage flexibility, because centralised structures provide a more flexible adaptation to market conditions.

UK economic policy outside EMU

The policy imperatives imposed upon the state by cumulative causation and technology gaps are unlikely to be achieved over the whole of the European Union's member states, as they possess different trade cycles, economic structures, histories, languages and cultures. Advanced capitalist economies are inherently unstable; left to themselves, they cannot maintain full employment resources while being marred by inequalities in the distribution of market power, income and wealth. Unfettered market forces via cumulative causation tend to exacerbate these

instabilities and disparities. Considerable scope exists for government involvement in initiating, pursuing and implementing economic policies; on the demand side insufficient aggregate demand and instability of investment are the key problems to resolve, whilst on the supply side, planning of prices and incomes, training, and active industrial measures to direct investment to resolve any balance of payments problems are central. The prospect of a EU-wide strategy to achieve these objectives is remote, although supranational directives may prevent the implementation of effective, national policies.

In order to implement post-Keynesian economic policies, the United Kingdom needs to avoid the uniform monetary policy and the constraints upon budgetary measures imposed by the adoption of a single EU currency. A long-term opt-out will provide the United Kingdom with greater economic flexibility. Therefore, the crucial issue becomes: what frameworks is needed for the formation of macroeconomic policy in an opt-out Britain? The initial stage is a national information campaign to acquaint the public and industry with the opportunities created by, and the dangers averted through, opting out. It should be supported by a detailed strategy for each UK government department, enabling them to identify the trade, financial and investment opportunities arising from the creation of a euro-bloc. For instance, the City of London will be able to trade in eurobonds, whilst British manufacturing and service companies will enjoy competitive advantages from being free of the costs of converting to, and implementing, the euro.

A decision to reject participation in the single currency restores to national government those economic instruments essential to the management of its economy. Therefore, democratic accountability is re-established, because citizens can once again enjoy the opportunity to choose the economic strategy pursued by the government of the day, rather than it being dictated by unelected central bankers. Moreover, governments will be able to develop a balanced economic programme, pursuing the multiple objectives of full employment, rapid economic growth and a sustainable balance of payments as well as low inflation. The opportunities are substantial.

A post-Keynesian economic strategy seeks to achieve both internal and external balance. Internal balance refers to more than the Maastricht target of price stability. Accordingly aggregate demand management could reduce unemployment, whilst a mixture of budgetary and monetary measures, a prices and incomes policy, the re-introduction of credit controls and coordinated national wage bargaining could restrain inflation. Although direct controls are unpopular with orthodox economists, who prefer the supposed allocative efficiency of free markets, the reality of sticky prices within oligopolistic markets creates the potential for governments to increase employment and growth. Moreover, a majority of the world's nations still retain capital controls as part of their economic management, whilst Ireland's recent remarkable growth was facilitated by social contracts with the trade unions.

The post-Keynesian approach stresses a positive role for government action to enhance the competitiveness of UK industry. The analysis by Eltis (2000) of trade flows demonstrates that Britain enjoys a comparative advantage in financial and media services, and in those areas of manufacturing which rely upon a high degree

of scientific innovation, such as telecommunications, pharmaceuticals, aerospace, energy exploration and generation, biochemicals and computer-related activity. The international price structures of these advanced-technology commodities are almost all denominated in US dollars, so that British firms and exports will suffer in EMU should the euro depreciate in value against the dollar. Outside the single currency, the UK government could strengthen the economy's competitiveness by enhancing the production potential of already strong sectors through targeted reductions in corporation tax, research and development, and greater spending upon education.

What about globalisation?

An argument advanced by advocates of EMU is that the degree of economic autonomy for the nation state advocated in this chapter is largely illusory due to globalisation and the international integration of financial markets. To the extent that national economies fail to insulate themselves from international financial markets through exchange controls or 'Tobin taxes', economies became prisoners of the neoclassical assumptions held by the majority of economists.[2] For example, an expansionary fiscal policy is seen by orthodoxy as a prelude to an increase in inflation and a decline in international competitiveness, rather than as a precursor to a higher level of aggregate demand, increased investment in future capacity and therefore the creation of a potentially higher future rate of economic growth. Thus non-orthodox economic policy is penalised by the withdrawal of inward investment, perhaps triggering a currency crisis of a sufficient magnitude to undermine the entire strategy.

An extension of this thesis argues that, due to financial integration, nation states can no longer operate a distinct monetary policy. Interest rates will be set internationally, with a premium equivalent to the degree of the perceived risk of currency devaluation, problems caused by political instability or threats to foreign investment. The argument implies that UK membership of the single currency, together with acceptance of a single Euroland interest rate, will be costless since monetary autonomy no longer exists. Indeed, the greater anti-inflation credibility formerly associated with the Bundesbank, and assumed to pass to its successor, the ECB, should ensure a lower long-term real interest rate than would be possible for an independent nation state.

The effectiveness of devaluation as a means of establishing an international competitive advantage is also dismissed, because the preponderance of subsidiaries of foreign transnational corporations (TNCs) rises as a proportion of the UK manufacturing sector. Subsidiaries of a parent company will not respond to devaluation by allowing their prices to fall, which would imply competing with their own parent company in foreign markets at a lower price. Thus they are more likely to maintain real prices and take higher sterling profits, thereby nullifying the effectiveness of the policy.

In essence, the economic case for participation in EMU rests upon the assertion that the economic effectiveness of the nation state is over, so that only as part of

regional economic blocs can governments reassert the use of traditional economic tools, such as monetary and exchange rate policy. Indeed certain socialist theorists argue that European economic integration can make possible a form of euro-Keynesianism, which can no longer work at national (Holland 1985). However, the contested ratification of the TEU suggest that there will be little appetite for renegotiation, whilst the EU Commission's attacks upon 'expansionary' British and Irish budgetary policy under the auspices pf the GSP indicates that a bias towards deflation remains at the heart of EU economic policy decision making for EMU entry.

The overall implication of the argument is easy to dismiss, as the United Kingdom's recent experience of being ejected from the ERM demonstrates. The resultant 20 per cent devaluation of sterling coincided directly with a resumption of economic growth and a fall in the rate of unemployment, whilst other EU member states that maintained overvalued exchange rates and deflationary Maastricht policies suffered stagnating output and persistently high rates of unemployment. Moreover, although financial integration has, to a certain extent, made an independent monetary policy more difficult, the United Kingdom was able to first loosen and subsequently tighten its policy stance during this period – with predictable results. If its economy were to be protected additionally by exchange controls, the United Kingdom's degree of autonomy would rise accordingly.

Our arguments do not dismiss the reality of a shift towards increasingly globalised trade and financial structures, although it would be more accurate to describe the process as 'triadisation', as the world economy becomes increasingly dominated by three dominant trading groups – the North American Free Trade Agreement (NAFTA), the European Union and an Asian block built around Japan. Many ports of the world, for example almost the entire African continent, play little or no part in these supposedly 'global' markets. Nevertheless, it is true that an explosion in international movements of financial capital, particularly associated with speculation rather than with trade in goods and services, has altered the environment within which national economic strategy is determined. Nevertheless, the majority of countries in the world continue to operate controls on the international movement of capital, whilst the financial destabilisation inflicted upon Mexico, Russia, the ERM and the 'Asian tiger' economies has served to warn world governments of the perils of unregulated capital movements. The policy prescriptions should not come as a surprise, as Keynes outlined it decades ago when the post-war economy was based upon the tight regulation of capital to prevent international economic instability. Therefore the choice is between membership of EMU, becoming increasingly immersed into a neo-liberal, triadised system, or pursing an independent, post-Keynesian strategy protected by a re-regulation of financial capital.

Conclusion

Britain enjoys an effective long-run option concerning its future economic strategy; it can embrace an essentially monetarist EU identity or, if it decides to opt out of the

euro, it can pursue a post-Keynesian policy. The widely held view that Britain possesses 'no alternative' but to participate in European integration is at odds with the facts (Burkitt *et al.* 1996). If Britain is decoupled from the EMU's integrationist momentum, the outcome will be enhanced economic prosperity and restored democratic choice to the British electorate. Indeed, if post-Keynesian insights into the working of the economy in the real world are ever to influence government policy, they are more likely to be effective outside EMU than if the United Kingdom is a prisoner of its neoclassically designed institutions.

Notes

1 There is a large literature on this issue, including: Amoroso and Jespersen (1992); Bruno and Sachs (1985), Cameron (1984); Calmfors and Driffill (1988); Calmfors and Nymoen (1990); Crouch (1985); Henley and Tsakalotos (1995: 186–9); Marshall (1995); McCallum (1983); Rowthorn and Glyn (1990); and Sawyer (1995).

2 'Tobin Taxes' are the name given to taxes levied upon the 90 per cent of foreign exchange transactions unrelated to trade. As some £200 billion daily is currently traded on the London Forex market, such a tax, even at a low 0.5 per cent rate, would yield considerable sums if speculators' behaviour remained unchanged. It could be avoided by moving transactions to offshore havens, but such a strategy is deferred by exempting all currency transactions not undertaken through a registered exchange from legal status. Consequently unpaid, offshore debts would not be backed by the force of law. The removal of the legal support and the low rate of taxation would prevent most speculators from decamping elsewhere.

Part II

Employment and social aspects of EMU

10 The European social model

Myth or reality?

Brian Burkitt

Introduction

Centre-left advocates of the UK's entry into the single currency argue that, despite its obvious deficiencies (e.g. the inefficiency entailed in submitting to a uniform, one-size-fits-all interest rate, given cyclical and structural divergences between member states' economies), the euro should be embraced because it would enable the United Kingdom to enjoy the larger countervailing benefits of participating in the 'European Social Model' (ESM). Much recent work casts doubt as to whether an ESM actually exists – for instance, Kleinman (2002). However, the case for embracing it has been deployed most eloquently and most forcefully by Edmonds (2000), former General Secretary of the General Municipal and Boilermakers' Union (GMB). This chapter queries the very existence of an 'ESM' and establishes that, if it does exist, Edmonds' reasons for participating within it are outdated. Whatever their validity during the Thatcherite 1980s, any centre-left case for joining the euro has become completely redundant in the twenty-first century.

The ESM proposal for closer EU integration

Edmonds asks: How important is it for British trade unionists that the European project succeeds, and how important is it to be close to its centre of power? He answers that it is crucial, because trade unionists identify with the European model of industrial society, combining high levels of productivity with high levels of social protection. The ESM is perceived to bring a little security into people's lives by making it rather difficult to sack workers. When redundancy occurs, the ESM sets the safety net sufficiently high to prevent poverty. Jacques Delors outlined this programme in his speech to the 1988 Trades Union Congress. His message was: put up with the competitive pressures of a single market, whilst the social dimension protects from the worst excesses of market capitalism.

The ESM, according to Edmonds, delivers benefits to working people. It strengthened moves towards equal pay, offered some protection for workers in corporate takeovers, improved health and safety protection, and has given labour a small but increasing influence over the strategies of multinational companies. More importantly, the ESM provides trade unions with a direct involvement in the

design of social legislation. The process of collective dialogue means that the European Trade Union Confederation can negotiate agreements with the employer's organisation (UNICE) that are given binding effect through the European Union.

Edmonds claims that the advantage of joining the single currency in order to bind Britain more tightly into the ESM is compelling. However, he also makes clear that left-of-centre support for entering the euro should be fully conditional on the European Union's commitment to the ESM.

Does an ESM exist?

Underpinning the arguments of Edmonds, and those of left-of-centre europhiles, is the assumption that a distinct, indefinable ESM currently exists. However, the weight of evidence from recent social policy research is that such an assumption is problematic. Most commentators accept that each EU member country possesses a welfare state that grew in size over the twentieth century, but they believe that these welfare states differ significantly from each other and that they can be classified into separate 'clusters'. In the seminal social policy works of the last generation, Esping-Anderson (1996) distinguished different types of welfare state, based on the concept of 'decommodification'. Where markets become universal and hegemonic, workers' material living standards become entirely dependent on the sale of their labour. The development of a welfare state involves a loosening of this commodity status, thereby diminishing financial and psychological insecurity. Decommodification occurs when a good or service is provided as a matter of right, so that a person can maintain a livelihood without reliance on the market.

Esping-Andersen's work generated considerable debate, documented by Arts and Gelissen (2002). It has become accepted that all welfare states decommodify labour but to different degrees. On this basis, four different kinds of welfare state have been identified within the European Union; the social democratic (occurring in Scandinavia – 'the northern model'), the conservative-corporatist (located in France, Germany and the Benelux countries – 'the central model'), the Mediterranean (found in Greece, possibly Italy, Portugal and Spain – 'the southern model') and the uniquely hybrid UK system ('the offshore island model'). To which of these models, does the ESM, so extolled by supporters of British entry into the euro, relate? It might be thought that the social democratic version of Denmark and Sweden, with its explicitly redistributive objectives, would appeal most to democratic socialists. However, the Scandinavian countries were late entrants into the European Union and have exerted little influence upon its central policy goals. Therefore, the ESM model, to which centre-left advocates of the euro aspire, is the conservative-corporatist variant, implemented by the six original signatories to the Treaty of Rome (with the possible exception of Italy). These countries are now a minority within the European Union, but their long-standing and founder status gives them an influence far greater than their numbers would suggest.

The ESM of the original six

The ESM developed in five of the original members contained many discrete national characteristics, but essentially possessed two dimensions:

1 social insurance;
2 labour market regulation.

Contributory social insurance is at the heart of this system. Benefits are mostly financed by contributions from employers and employees, so that social occupational and income differences are reproduced in the pattern of welfare payments. Consequently, unlike in Scandinavia, there is little emphasis on redistribution as an objective of social policy.

Service organisation and delivery tend to be pluralistic, i.e. non-state or parastate organisations predominate in the administration and distribution of insurance funds, and in providing services. They reflect the influence of Catholic social teaching, particularly the principle of 'subsidiarity', which claims that welfare arrangement should be provided by the nation state in the absence of adequate measures at some lower level, be it the family, the local community, the church, occupational groups, businesses or trade unions. There exists a hierarchy of solidarities, the lowest being the most important. Therefore the ESM reflects and supports an organic, hierarchical and integrationist view of society, whereby family, church and occupational forms of welfare are supplemented by the state, but not replaced by it.

Germany is generally taken to be the paradigmatic case of the ESM, where welfare measures are underpinned by the social market economy. The state's general commitment to providing income and employment is complemented by an emphasis upon the obligations of employers, trade unions, families and individuals to support themselves. Redistribution through the ESM is largely horizontal, within occupational and status groups, rather than vertical, from rich to poor. Pensions and welfare benefits reflect income differentials. The short-term unemployed with a full contribution record receive 68 per cent of previous take-home pay. Those not eligible for this comprehensive insurance apply for social assistance, which is means-tested; if the means test is passed, applicants obtain 58 per cent of net pay. A third group, having failed the means test, are dependent on much smaller levels of flat-rate benefit, whilst 15 to 25 per cent of the registered unemployed are currently not in receipt of any benefit.

Although core social insurance is relatively generous by international standards, social assistance is not only heavily means-tested but also carries considerable stigma. Such aspects of the ESM became increasingly important in the 1990s and 2000s, with the rise in unemployment and the growing numbers of those who, due to a lack of attachment to the labour force, did not possess contribution records. These developments led to a rapid increase in social exclusion under the ESM, with the creation of a '2/3 society', from which approximately one-third of citizens are excluded.

New pressures are mounting upon the ESM, but, until Gerhard Schroeder's recent proposed reforms, the response has been to adapt the system of social insurance rather than to pursue radical neo-liberal or democratic socialist changes. Unemployment and pension insurance schemes were relied upon to cover the social costs of unification and of meeting the deflationary Maastricht Convergence Criteria. Moreover, a new compulsory insurance scheme was introduced to finance the costs of long-term care in old age by providing non-means-tested benefits in cash or in kind.

Social insurance has traditionally been underpinned by a corporatist system of industrial relations. In particular, European Works Councils cover companies, whose headquarters or subsidiaries are situated in countries within the eurozone. They provide trade unions with a positive, albeit marginal, role in the industrial relations process.

Problems associated with the ESM

The traditional ESM requires large welfare expenditure backed by public support for a positive state presence in social policy, but tensions exist within the model from a democratic socialist perspective. These are sufficiently serious to undermine centre-left arguments for UK membership of the euro.

The last two decades of the twentieth century witnessed a broad process of increased social differentiation in the ESM member states. Unemployment and social exclusion grew and regional differences intensified, whilst populations became more ethnically diversified. The ESM in France and Germany was based upon a high rate of economic growth; in the words of Ludwig Erhard (1963), 'the best social policy is an effective economic policy'. Over the four decades after the Second World War, the German 'economic miracle', supported by a consensual political system and the 'realpolitik' of the Cold War, delivered both rapidly rising living standards and a generous, socially inclusive ESM. Since 1989 the German social model was confronted with a series of challenges, primarily reunification and the deflationary EU integration process. Economic growth fell, whilst unemployment rose to almost 12 per cent in 1999, before falling to 10.6 per cent in September 2004 (compared to 4.8 per cent in non-eurozone Britain). Consequently, the ESM provides a number of minor micro pension and workplace benefits within a failing macro framework. One of the many problems with the draft EU Constitution is that it leaves intact the existing eurozone system of economics policy, which is failing. Currently 19 million people in the European Union are unemployed.

The European Central Bank (ECB) has consistently pursued monetarist policies, based upon competitive disinflation. Its sole legal objective is the pursuit of price stability. This strategy, aimed at domestic competitiveness, low inflation and the attainment of the Maastricht Fiscal Convergence Criteria, has been adhered to despite the human and political costs of permanently high unemployment plus stagnant living standards for the majority of EU citizens. It is reinforced by the restraints upon budget deficits imposed by the Stability and Growth Pact. The

deflationary Maastricht programme created a differentiated social polity under the ESM where three kinds of citizens exist:

1 the employed in secure jobs, covered by comprehensive insurance schemes and ensuring additional cover from contributions to mutual societies' occupational pensions;
2 those working in less secure jobs without additional schemes to top up benefits;
3 the long-term unemployed, or never employed, dependent on social assistance for a minimum income, who fall through the insurance net.

The whole philosophy of the contemporary ESM is summarised by the statement of the former French Finance Minister Strauss-Khan (2000), which explains why democratic socialists can never accept it:

> No one now contests the free market, but we still need rules and institutions. We say the free market is okay, but it is still not okay for society to be organised only by the market.

This verdict condemns the whole EMU initiative, but can it be embraced, as a wider social project, by democratic socialists?

Conclusion

The traditional ESM is a doomed strategy for the centre-left. It replicates the inequalities of the workplace in retirement, redundancy and sickness. Moreover, the ESM fails completely unless full employment can be ensured because:

1 it becomes more costly to finance with a sizeable pool of people out of work, when demands upon it simultaneously grow;
2 the process of labour market regulation is undermined by large-scale unemployment, because it shifts the balance of power from capital to labour.

The obvious solution to the EMS's unemployment, and hence fiscal, problems is the adoption of an aggressive budgetary and monetary strategy to secure full employment and to promote economic growth. Aggregate demand management, rather than supply-side 'reforms' that impose the costs of structural adjustment upon the most disadvantaged citizens, is the key to creating a future socially inclusive community. However, the ECB's sole legal responsibility to control inflation and the restrictions upon government budgets imposed by the Stability and Growth Pact preclude these solutions, which can only be pursued within a national, democratically accountable framework. The ESM is obsolete and dying, the current 'reforms' to it in France and Germany are actually cutbacks, whilst the European Economic and Monetary Union is based upon deflationist principles and is, therefore, anti-labour. The EU integrationist process is thus one that the British labour movement should avoid.

Fortunately, recent trends indicate that disillusion about the European Union's integrationist momentum is spreading amongst the UK left. In September 2004 a new think tank, The Centre for a Social Europe, was launched to develop the centre-left case for EU reform. Its first publication was titled, *Why the Left Should Reject the Constitution*. With six labour MPs on its advisory board, as well as a representative of the Labour Party National Executive Committee, such movements of opinion will disturb Tony Blair and his europhile support. A similar awareness exists amongst the new wave of union leaders. Thus Bob Crow, the General Secretary of the Rail, Maritime and Transport Union, was greeted by cheers at the 2004 Trades Union Congress when he declared: 'The Constitution will intuitionalise privatisation and the neo-liberal economics that have helped to wreck industries in Britain.' Such a change in opinion from the early 1990s, when to be 'left' was assumed to be 'pro-EU integration', is to be warmly welcomed.

However, this is not a time for complacency. The left must continue its traditional fight for democratic accountability and equality, which under contemporary conditions involves refusing the lesser benefits of the ESM in order to remove the greater threat to progressive policies posed by the draft EU Constitution and by the single currency.

11 Voting no – the euro and Labour voters[1]

Matthew McGregor

"This is what happens when you let women and truckers vote."
(Unnamed European Commission official reacting to the Danish 'no' to the euro, October 2000)

When Labour came to power in 1997, it was on a landslide unprecedented in modern British politics. Although it is hard to believe seven years on, Tony Blair was one of the most trusted and liked politicians the country has ever produced – and respected in other European countries as much as by voters in the United Kingdom. Coming to power on such a wave of popularity, the Blair government has been able to implement almost any policy it saw fit, be it on welfare reform, devolution or the minimum wage. But Tony Blair has failed to come anywhere near implementing one policy he cares about very deeply – the euro.

The euro debate in Britain has been framed by many in the media as a left versus right battle – a straight fight between the little Englanders of the Conservative Party and their media allies and the modern, forward-looking New Labour machine. This thesis explains the position of the most of the newspapers – with the press of the right firmly against the United Kingdom scrapping the pound and the liberal media firmly on the side of joining the euro.

However, this argument has always had one serious flaw – the voters. Labour voters have consistently opposed the United Kingdom's membership of the euro during the period of the current Labour government – and show no sign of changing that stance. Why is it that Labour voters want the United Kingdom to retain the pound? It seems strange that voters who are usually happy to give their vote to Labour politicians, have refused to listen to them on this one particular issue. The Labour government, the Labour Party, the TUC, liberal news outlets and high-profile figures across the left have campaigned hard since 1997 for early membership of the euro, but they failed to persuade their natural core supporters.

In this chapter I will set out the extent to which Labour voters have opposed scrapping the pound, before examining the touchstone policy issues that led to this position, with a particular emphasis on their role in the campaign for public opinion. I will conclude by suggesting that in referenda normal political affiliations become less important to voters, who have genuine choice over a single issue – thus party loyalty is almost totally removed.

The government and the Labour leadership had a firm pro-euro policy going into the General Election in 1997. Before the 2001 General Election, the Labour Party was widely seen as favouring UK membership, and offered a referendum in an attempt to deflect any political damage that stance would have. By 1999 Tony Blair was in a position to make his position clearer than ever. A Downing Street source said at the time: 'Now is the time to start moving off the fence. . . . Business is clamouring for the single currency and Tony will make clear that we are singing from a similar song sheet.'[2]

This level of rhetorical enthusiasm continued through Labour's first term and into the second, despite the lack of any obvious campaigning at a grass-roots level. In 2001 Tony Blair went out of his way to give the impression that a euro referendum would be held within the 2001–5 parliament. Furthermore, it has not only been the government that has been campaigning for Britain to join the euro. The Britain in Europe campaign group, which was launched in 1999 to make the case for euro entry, was labelled a 'front organisation' for the government's euro policy from day one, and was reported as such by the media.[3]

It has been an inescapable fact that the Labour leadership has consistently supported euro membership. But where have the views of grass-roots voters been? Opinion polls have, time after time, shown that Labour voters are against Britain joining the euro. Before the 1997 election, polling by MORI showed that Labour voters erred against the euro[4] and the polls haven't moved since then. Polling for the *Guardian* since the 2001 election has been particularly illuminating. In September 2001 Labour voters opposed EMU participation by 52 per cent to 38 per cent, whilst in June 2002 opinion stood at 48 per cent to 35 per cent against membership, and in June 2003 this opposition had toughened with the polls indicating 53 per cent against with only 28 per cent in favour.[5]

The 'headline' questions used in these polls highlights the views of Labour voters on the general issue of euro membership, but they don't necessarily reflect voter behaviour during an actual referendum. It is fair to say that in the event of a referendum campaign the pressure on Labour's voters to follow their normal party preferences would be intense. Party figures would campaign at the grass-roots and in the media, and identification between opinions on the euro and normal party support would increase. However, track polling from Barclays Capital[6] has highlighted the extent to which Labour supporters would be willing to diverge from the Party on the issue of scrapping the pound. Asked how they would vote in a referendum on the euro *if the government recommended entry*, Labour voters have shown a high level of desire to vote against the party line in a referendum. Since the middle of 2002, polling shows that the number of Labour voters willing to vote against an explicit recommendation from the government hasn't fallen below 35 percent. Those who say that they would reject a government recommendation have outnumbered loyal party supporters three times in the last year.[7]

It isn't just a straight 'yes' or 'no' polling question that shows where the views of Labour voters lie. Polling by ICM in 2002[8] showed that only 3 per cent regarded the euro as a priority – ranking bottom of the 11 issues offered in the questioning. This compared with the NHS (88 percent), education (61 percent) and crime (41

percent). The poll even showed that Labour voters considered cutting red tape a higher priority than joining the euro. So it is clear that Labour voters plan to vote no if a referendum is held in the near future.

The normal processes of decision making, whereby voters tend to share support for policies with the party they support in elections, has clearly broken down. But why would that be? The key answer lies in the fact that working-class voters are much more opposed to the single currency than middle-class voters because the economic effects of joining the euro far outweigh any political considerations.[9] The key issues for Labour voters are jobs, public services and the welfare state. On all three issues, the euro falls down.

On the issue of jobs, the 'yes' campaign and the government have faced a real difficulty in persuading voters that scrapping the pound for the euro would be a good idea, and its not hard to see why – unemployment in the eurozone is almost double that in the United Kingdom. A report for the European Commission highlighted this in its 'Jobs, jobs, jobs' report of November 2003.[10] Of the European Union's member states, the only countries to meet targets for job creation were Sweden, Denmark and the United Kingdom – the three EU15 countries not in the euro. There are, of course, many reasons why the United Kingdom has a good record on employment over the last ten years. To simply say that it is because we are not in the euro would be simplistic. But to discount the deflationary bias of eurozone monetary policy when looking at the economic problems of the countries which have joined the euro would be ridiculous.

Social democrats believe that it is vital for a government to be able to manage the direction of the economy so as to ensure that wealth, power and opportunity are in the hands of the many, not the few. To that end, social democrats think that there are a range of economic tools that the government needs to serve these ends. One of these tools is the ability to set interest rates, but in the euro interest rates are set by the European Central Bank. Despite the popular media perception that ordinary Labour voters are not educated in the ways of the market, focus groups[11] have shown that it hasn't gone unnoticed that the eurozone has one interest rate for the whole area, meaning that many countries have a rate that is wholly inappropriate for their economy. As a report examining the Chancellor's five economic tests, for investment bank UBS Warberg, stated:

> In some countries, interest rates appear to be too low, contributing to above-average rates of inflation, while in others monetary conditions appear to be too tight, contributing to below-average rates of inflation and low rates of economic growth.[12]

Labour voters think that the Labour government has a good economic record, so it shouldn't come as surprise that most of them decline the offer of swapping a successful framework of economic management for one in the eurozone that isn't working. Peter Mandelson touched on this when he made his first speech as an EU Commissioner at the Confederation of British Industry. He said that anti-euro sentiment was an 'unwanted by-product' of the United Kingdom's record on

employment.[13] It may be an unwanted by-product for Peter Mandelson, but it hardly seems like a good reason for Labour voters to change their mind on the euro.

The euro would also attack the foundation upon which the social model is based – security at work. The flexibility that economies need has, in Europe at least, been based on regional and national planning accompanied by fiscal and monetary policy to ensure strong growth. In the euro, these levers are taken away and governments are unable to react quickly and effectively to economic shocks. The only reaction to a sharp downturn of demand in the economy is through flexibility in the labour market – and workers have learnt the hard way that 'flexibility' doesn't usually mean pay rises or more job security. One of the architects of the euro has argued as much. Otmar Issing, the Chief Economist of the European Central Bank has made this case plainly: 'The most obvious [danger to the euro] is the lack of flexibility in the labour market . . . this poses an almost lethal threat to monetary union.'[14] There is a case to suggest that economies will be more successful if labour markets are more flexible, with wages able to fall more easily and companies able to sack staff more quickly. However, it is not a left-wing case, and it is not a case that appeals to working-class people.

During its period in government since 1997 the Labour Party has built its electoral appeal around increasing spending on public services, particularly on education and health. But joining the euro would mean that investment could be put at risk. The rules of the euro, including the Stability and Growth Pact (SGP), were created in a way that imposes a straitjacket on countries during times of economic downturn. The SGP limits members of the euro to running a budget deficit of 3 percent or less year on year. The problem is that when a country faces economic problems and its budget deficit rises, the only recourse is higher taxes or lower public spending. In the short time since the introduction of the euro Portugal, France, Ireland, Greece, Germany and Italy have announced or implemented plans to cut public spending in response to the SGP. Portugal was first in 2002, when the newly elected government of José Manuel Barroso, now the EU Commission President, put in place a severe austerity package in response to the country's breach of the SGP. The package included public spending cuts and VAT tax rises, and the opposition socialists responded to the package saying: 'We cannot afford to sacrifice our future for the sake of blind adherence to a set of quantitative criteria.'[15] In Germany, the country's budget deficit remains stubbornly above the limit allowed and measures to bring it down have included cuts to welfare and public services. Along with a proposal to scrap one of Germany's bank holidays, German Finance Minister Hans Eichel unveiled a plan to impose a €1billion cut on all ministries and freeze public sector pay increases.[16]

It isn't just countries in the eurozone that have had public services threatened. In 2002 the European Commission suggested that the United Kingdom's spending plans could need to be reined-in as if we were members of the euro. The Prime Minister's spokesperson was quick to react, saying: 'The UK has no intention of reducing public spending by £10billion as the Commission seems to imply. . . . As we are outside the single currency we are not subject to its sanctions.'[17] Advocates

of early entry to euro membership have pointed to the fact that many European countries have better public services than the United Kingdom. It is undoubtedly true that countries like France and the Netherlands have good public services. But it hasn't escaped voters' notice that their public services were built up over decades with large-scale investment, the sort of levels of investment that may not be possible in times of economic downturn.

Given that public service investment has formed the backbone of Labour Party campaigning over the last few years, it is hardly surprising that opponents of early UK membership of the euro have highlighted the issue in debates. Ian Davidson of the Labour Against the Euro group of MPs said at its launch that: 'We are neither criticising nor contradicting government policy. We are simply saying that Mr Blair's priority should be public services.'[18] Sir Bill Morris, the then General Secretary of the Transport and General Workers' Union explained the Union's decision to campaign for a 'no' in the event of an early referendum on the euro by saying: "Entry at this particular point would be a major diversion from the policy of the government to increase public expenditure and reform public services.'[19]

It is jobs, public services and welfare that Labour votes are interested in, and it is the jobs, public services and welfare policy spheres that offer the most convincing case for staying out of the euro in its current form. And it isn't just the United Kingdom where this case holds – the evidence from the euro referendum in Sweden in September 2003 is remarkably similar. Exit polls (or *VALU*)[20] from the referendum show that the largest group of 'no' voters were social democrats,[21] and broken down on class, the largest group of 'no' voters was blue-collar staff.[22] Five out of the seven top reasons to vote 'no' (i.e. those reasons cited as being of 'very great importance') were economic reasons, particularly public services and welfare. The evidence from Sweden is all the stronger given that the overwhelming majority of the Social Democratic Party leadership campaigned hard for the 'yes' campaign. One senior Swedish 'no' campaign staffer has described the situation by saying: 'The Party leadership were focused on the political capital to be won in Brussels, and they forgot that our voters care most about everyday issues.'[23]

As in Sweden, the evidence in the United Kingdom points to a significant rejection of the party line by voters who normally support Labour. But despite the fact that so many Labour voters seem willing to buck their normal party preferences and vote 'no' in a referendum on the euro, the usual media reporting of the debate is one of left versus right. Journalists are genuinely interested in stories about left-wing opposition to the euro because it is outside the norm and therefore deemed to be interesting. There is, to some extent, a simple misunderstanding about the nature of referenda in this reporting. Voters are sophisticated enough to understand that voting 'no' in a referendum doesn't mean that the government will change, but reporting of the euro debate still focuses on the views of parties and party political figures. Equally, there is some bias in the media, not least from an unnamed BBC reporter who infamously told a campaign staffer that they favoured joining the euro because, 'we like cappuccinos and we don't like racists'.[24] However, the main cause of the failure to notice and understand the opposition from Labour voters has been the nature of that opposition. To most people who

favour joining the euro, the economics comes second. As Labour voters tend to oppose euro entry on economic, not political, grounds, they don't show up on the media radar.

In the referendum on the north-east assembly in autumn 2004, the 'yes' campaign tried to turn the poll into a Labour versus Tory contest. The 'no' campaign won with 78 per cent of the vote. There are many people in the political world who have not grasped the different nature of referendum politics. When Labour voters cast their ballot in elections, they usually look down the paper in front of them to find the Labour candidate. In a referendum on the euro, they will be looking at a paper that offers them the choice of voting 'yes' or 'no'. It is a simple fact, but one that has vital implications for the campaign.

The party loyalties that voters often feel in elections, because of hugely complex and overlapping factors, are downgraded, if not eradicated, in referenda. Given that in the event of a referendum on joining the single currency, there would be campaigners from the labour movement on both sides of the debate, voters will not face the concerted party effort to bring them to one particular conclusion. That brings voters to a simple choice: vote 'yes' to join a club where unemployment is high, growth is low, and where the tide is turning against the left; vote 'no' to protect the advances the Labour government has won, and keep our ability to continue building our corner of social Europe secure. It's no wonder Labour voters are against the euro.

Labour voters are against joining the euro because it is not in the economic interests of people in this country. They have not changed their mind on this since 1997, and they are not likely to do so in the near future. Despite the popular impression of the euro debate being one which pits left versus right, the different nature of referendum politics mean that Labour voters will buck the Party line if a vote is called. No wonder Tony Blair has gone from a position of seeing the euro as a 'destiny'[25] for the United Kingdom, to saying: 'The argument about the single currency – the position has never changed there; there has got to be a clear case for joining it, and at the moment there isn't.'[26]

Notes

1 I would like to acknowledge the help of Graham Copp in the writing of this chapter.
2 Unnamed Downing Street source, quoted in the *Mirror*, 6 February 1999.
3 There are dozens of examples of this. See, e.g., 'Pro-euro group "a front for labour"', Robert Shrimsley, *Daily Telegraph*, 9 November 1999.
4 MORI poll survey commissioned by the European Movement, August 1996. 12 per cent of Labour voters supported joining the euro in principle with 27 per cent against. Labour voters against in principle and 'generally opposed' versus Labour voters in favour in principle or 'generally in favour' split more evenly – 44–5 against membership.
5 Regular 'euro tracker poll' by ICM for the *Guardian*, http://www.icmresearch.co.uk/reviews/polls-archive.asp. The question ICM used was: 'If there were to be a referendum, would you vote to join the European Single Currency, the euro, or would you vote not to join?'

6 I would like to thank Barclays Capital for providing with me their polling statistics going back several months. Barclays Capital's polling is conducted by MORI.
7 A majority of Labour voters replied that they would reject the euro despite a recommendation from the government in October 2003, August 2004 and September 2004. The figures were tied in June 2004, and the results were within the poll's margin of error in three other months.
8 ICM poll for the 'no' campaign, 27 September 2002. Respondents were asked: 'Which two or three of the following do you think are priorities for the government to address in this parliament?' The options were (in order of popularity): the NHS, crime, education, terrorism, public transport, the economy, environment, social security, income tax, defence, fuel tax, controlling inflation, getting rid of red tape, the euro.
9 Opinion polls have consistently showed stronger opposition to the euro from working-class voters. For example, an ICM poll from September 2002 had opposition to the euro from social classes A and B at 45 per cent, and opposition from social classes D and E at 67 per cent. www.icmresearch.co.uk
10 http://europa.eu.int/comm/employment_social/publications/2004/ke5703265_en.html
11 I am grateful to the no-euro campaign, and the Vote No group for access to records of their focus group research.
12 *Preparations for EMU*, UBS Warburg, October 2002
13 Peter Mandelson, speech to CBI conference, 8 November 2004. For the full text, see http://www.cbi.org.uk/ndbs/press.nsf/0363c1f07c6ca12a8025671c00381cc7/577abfebe84c762880256f4600325c6a?OpenDocument
14 Professor Otmar Issingwas speaking at the 'Forum Dialogue' organised by the Banque central du Luxembourg on 8 February 2000.
15 Luis Nazere, a member of the Socialist Party's national leadership, quoted in 'Austerity measures aim to close the EU gap', *Financial Times*, 7 October 2003.
16 'German package aims to put budget back into line with EU fiscal rules', *Financial Times*, 5 November 2004.
17 Prime Minister's official spokesperson, 31 January 2002.
18 Quoted in 'Put services before euro, say MPs', *Daily Telegraph*, 22 January 2002.
19 'T&G will work for euro no vote', *Guardian*, 5 February 2003.
20 Exit polls conducted by SVT, the state-owned Swedish broadcaster.
21 This figure is for all voters and does not represent proportions. As Social Democrats represent the largest group of voters, the number of Social Democrats voting 'no' was greater than the number of any other party supporter group voting 'no'.
22 Blue-collar workers voted 'no' by 69–29, compared to farmers (65–35). White-collar workers and the self-employed narrowly voted 'yes'.
23 Peter Gustavsson (Director of Organisation for Socialdemokrater Mot EMU – the Social Democrat 'no' campaign) speaking at seminar in Uppsala, January 2004.
24 Quoted in *Sunday Business*, 7 November 2004.
25 In his speech to the Labour Party conference in September 2002 Tony Blair said: 'That's why the euro is not just about our economy but our destiny.'
26 Tony Blair, speaking in a media briefing at Downing Street, 29 November 2004: http://www.number10.gov.uk/output/Page6679.asp

12 What future in the European Union?

Joe Marino

Introduction

Many myths have been spread about the trade union approach to the European Union. To read the messages coming from Congress House and reported in the media, one could be forgiven for believing that the trade union movement was a wholehearted cheerleader for the European Union. This is part and parcel of the old misconception that sees the trade union movement as a monolithic whole. Nothing could be further from the truth. The issue of the European Union divides trade unions and their members as much as it divides all political parties and British society as a whole. There is nothing new, nor is there anything wrong with that. Is it not called democratic debate? Does this not make us stronger than those who would preach unanimity at any price no matter what the cost?

Nor is this division new or never changing. Some individuals change 'sides' as their stances move with what they would call 'events'. One has only to look at the two main parties to see that. Initially the Conservatives were the main champions of EEC membership, pushing it for all it was worth. The labour movements initial stance was one of healthy scepticism, with many in the labour movement campaigning for a 'No' vote in the referendum for EEC entry. True, some of those opponents are now cheerleaders for the European Union, for example Neil Kinnock, an EU Commissioner. And the Tories are a mainly eurosceptic party (without, of course, daring to ask the $64,000 question on continued membership). How times change. Individuals and parties can, of course, change their views. Nothing wrong with that, nor need such changes be a matter for criticism. However, I would argue that the questions that hung over the original membership of the EEC are writ large over the current debate on Britain's future in the European Union.

There is no doubt that a sea change came over the views of many trade unions in relation to the European Union during the period of the Conservative governments of 1979–97. Those governments were so anti-trade union and working class that anything was seen as better. However, even in those halcyon days some of us were warning about greener grass in the next field. At union conference after union conference I remember warning – both internally and externally – that membership of the European Union only looked good because the Tory government was so

bad. What mattered was our own control over our own democracy – and that meant trade union and labour movement democracy not nationalistic claptrap.

The counter-argument was always on the 'benefit' of European Union legislation that was favourable to workers set against the anti-trade union approach of the then Conservative governments. That, we were told, was what made membership of the European Union attractive. I never believed that was a sustainable argument. The brief history of New Labour shows that it is untenable. With Tony Blair bragging about the United Kingdom having the most restrictive labour laws in the developed world, and the New Labour government seeking opt-outs and the watering down of any EU issues that benefit working people and trade unionists – after all we must not upset the CBI must we? – one has to seriously question the future of what has been described as 'social Europe'. Indeed, New Labour is leading the charge to sweep away or, at worst for them, water down any social gains the European Union boasted of in the past.

Several points have now become clear regarding the position of our union in the debate over the future of the European Union:

Club rules

If Britain is to be part of the European Union it is clear that, sooner or later an EU constitution is necessary. In the short term, the issue is not the production of a constitution but what is in it. There is also the longer-term view in relation to control over changes in the constitution. Trade unions know only too well that agreements struck on amalgamation or transfer of engagements are temporary affairs that, in the fullness of time – often much speedier than that – are overtaken by reality.

There is a lot in the proposed 'constitution' that makes sense for a club. The replacement of the rotating presidency by a chair of the council; the reduction of commissioners to one per state, and then restricting that number to two-thirds of member states on a rotation system; increased powers for MEPs (although these go nowhere near far enough for democratic responsibility); a single EU Foreign Ministry etc. All these steps recognise the basic fact that a club must have one set of rules.

Yet at the same time we are asked to believe that other areas of the workings of the European Union will not be part of the constitution; that the so-called red lines have not and will not be breached. Such a claim beggars belief. There can be no guarantee that these areas will remain 'free' from the constitution, and it is naive to think so and dishonest to claim so. Put simply, the European Union cannot work in the long term with differing rules for different member states. Once the economy is centralised all else must and will follow. In such a case the present democratic deficiency will multiply and Britain will, like others, be left at the margins of a Union it cannot influence.

Here the central issue is economic management, and the fact is that the isolation of the European Central Bank from reality – not to mention any kind of democratic control and accountability – is central. There is not space here to argue this case in

detail; others will do that. Yet it is a fact that even pro-European Union economists despair about the role and lack of accountability – not to mention the policies – of the ECB. There can be no green light for the European Union constitution until the ECB is brought under that democratic control. Even the 'independent' Bank of England faces the final political control – its very independence can be reversed by a political decision of the House of Commons. No such sanction is there for the ECB and there is a fundamental flaw in the structure of the European Union. Of course, it can be argued that powerful governments can just ignore the ECB – as Germany and France have done recently. That, of course, begs the question of how long the very structure of the ECB, the single currency and the Union itself can survive unilateralist, individual state decisions. By themselves the actions of the German and French governments show the sham of unity.

Single currency

The same is true of the single currency. We believe that membership of the single currency would be a disaster for Britain and that the issue of the level of joining – at what exact exchange rate – is a red herring. We would be bound by the rules of the euro and our economic independence would be gone for good. All that would be left is tinkering at the edges. Nor is it tenable to suggest that once we join we could then influence events – that boat has already left the harbour. Democratisation of the euro and the ECB is essential – but much harder to achieve once let go. And no one can seriously doubt the democratic deficiency here.

Of equal importance are the so-called budget rules. The Commission president may well hail the recent European Court of Justice ruling that EU governments had acted illegally in ignoring a call to punish France and Germany for violating budget rules, but the fact is they did. And in doing so they highlighted a major failing in those rules. Of equal importance are the inflexibility of the euro rules and the role of the ECB. Even the most ardent supporters of the single currency do not disagree that Gordon Brown's investment plans for the NHS and education would fall foul of these rules. In such inevitable circumstances Britain would have to face the same 'dilemma' faced by Germany and France. Do we heed the euro rules or meet the demands of the British people for investment in health and education? I know my choice – but I doubt that of some British political parties. One has only to look at the mess the Schroeder and Chirac governments are in over the euro/state funding/stability pact issues to see the writing on the wall. Both German and French governments are taking the axe to social provisions, especially pensions, in order to minimise their busting of the euro rules – and, despite those savage cuts, still failing. It seems the only 'positive' in the euro is not having to pay commission on holiday exchange rates – I can live with that if it means making our own decisions on investment in British public services.

The constant bleating that being outside the single currency – indeed outside the European Union – equals job losses is so far off the mark one gets surprised that it is still being made. To quote the 'Labour Euro-Safeguards Campaign Bulletin' of November 2003:

> We constantly have a trade deficit with the other EU countries, currently running at well over £10bn per annum. Nor is Britain dependent on the EU for jobs. The claim that 3m jobs would be lost if we were not in the EU is nonsensical. In fact, Britain's economic performance has been considerably better recently than most other EU Member States, largely because we are not in the euro and thus not bound by the Stability and Growth Pact and the deflationary dictates of the European Central Bank.

It is not a long-term tenable position to support membership of the European Union but oppose the single currency. The issue here is not just timing and the level at which Britain joins the single currency if it stays in the Union. There is also the issue of democratic accountability in relation to the European Central Bank and the need for flexibility in economic management to take account of differing needs in different parts of the single currency area. These issues are far from settled and until they are our view remains one of opposition to single currency membership. As set out above, the weakness shown by the present EU institutions does not bode well for the success of the constitution. If economic sections of EU policy can be ignored, then why not others? And it is not just the German and French governments who claim this right of different treatment.

I have argued that membership of the European Union only looked good to British trade unionists because of the anti-union stance of the Thatcher and Major governments. I remember warning at the time that, should a Labour government wish to pour money into the social fabric of Britain – in particular the NHS and schools – then it could well fall foul of EU rules. Sure enough, as Gordon Brown belatedly began the rebuilding of our neglected public services, the ECB issued its warnings against his spending plans for breaching EU rules. Of course, being outside the single currency the Treasury quite rightly ignored those 'suggestions'. It would, of course, be a different matter if we were strangled by the single currency rules – as France and Germany found. Yet to brush these problems aside by either following the French and German example – unsustainable in even the medium term if the single currency is to survive – or by saying we never will join the single currency unless it is on our own terms is disingenuous. The single currency is the lifeblood of the European Union and, sooner rather than later, all member states will have to join if they want to stay in the club –there can be no dispute about that. The only point of disagreement for pro-Europeans seems to be the level at which we join. Important as that is, it is dishonest to give any other signal. Membership of the European Union must mean at some stage membership of the single currency. Let's at least be honest about that.

Therefore the argument about the democratic deficiency in economic matters is vital but is avoided by those who wish to shove us into the European Union by the back door. As with other aspects of the European Constitution, at the end of the day it is all or nothing.

Diluted membership

The issue of detail is also one that drives our current view on the constitution and on continued membership of the European Union. If a constitution is to be agreed, it must be the same for all member states. That is far from the position of the British government which continues to seek opt-outs of that EU legislation favourable to working people in the United Kingdom. How the government can hope to win a referendum on the constitution whilst it takes such an anti-worker stance beggars belief. And why should we support such a stance that is clearly against the best interests of our members? If the perceived gains of 'social Europe' are to be denied us, what are we in it for? Indeed our conference was clear on one thing: the government need not seek our members' assistance in getting a 'Yes' vote whilst it takes this stance.

Cherry-picking at the constitution is not an option. If that is to be allowed then the constitution itself will be a farce and would not deserve support.

Thus the claim is made by some that trade unions must support the constitution because it embraces the European Charter of Fundamental Rights. This goes right to the heart of the debate for us – because the claim is spurious. How can we campaign for such a laudable aim if, at the same time, the New Labour government is opting out of that same Charter all over the place. This is the problem with the guarantees given to the CBI and other employer organisations. In effect, British workers are being told: here is what the rest of the European Union workforce is getting but we are ensuring they don't apply here in Britain. Vote for a constitution that makes you the poor relations of the Union. What a farce – and one we, at least, are not prepared to take part in.

Resistance to full information and consultation for British workers; opposition to full implementation of the working-time directive; refusal to grant British workers the same rights to defend themselves through the right to take industrial action; the failure to guarantee employment protection rights from day one of employment; the ease with which British workers – one of the least protected workforces in the advanced economic world – can be dismissed . . . The list is endless. Whilst perhaps we should not be surprised by New Labour's anti-worker stand in these areas, it is surely simplistic of them to expect our support for a constitution that leaves British workers as the poor relations of the European Union in any referendum. The question is 'what's in it for us?' And the answer is 'very little'.

It may well be claimed that membership of the European Union creates jobs in the United Kingdom. I don't accept that – at the very least the jury is still out on that question. But what is the use of job creation if, due to the weakest labour protection laws in the advanced economies, those same jobs can be taken away at a mere whim with no comeback or protection?

Conclusion

Our current view was one of opposition to membership of a club that stacks the rules against our members and their families. However, we do believe that

membership of the European Union must mean acceptance of a constriction of some sort; and that any attempt by the UK government to opt out of worker-friendly clauses of the constitution or other EU laws and directives would lead us to campaign for a 'No' vote in any referendum. It would simply not be worth the candle.

Membership of the euro and support for the European constitution are inextricably linked. The Conservatives and their supporters on the right, such as the UKIP, wish to see the European Union as a free market for big business with little or no protection for workers or consumers. Hence, for example, their opposition to strengthening labelling laws or the strict control on GM foods. The Tories' problem is that they cannot take their opposition to current trends in the European Union to its logical conclusion – that of leaving the Union. The UKIP is against anything that smacks of Johnny Foreigner and wants to see Britain return to pre-Elizabethan days when the world was much smaller and we were blissfully ignorant of anywhere past these shores.

Our opposition to the euro must be and is based on more than little-Englander prejudice. This idea that economic super-blocs are the answer is riddled with contradictions that will inevitably burst them apart. Who, outside Washington that is, seriously believes that NAFTA is anything but an economic extension of the pax Americana and a vehicle for the export of US capitalism? From where we stand the current state of the European Union is one inevitably linked to and supporting capital against labour. That becomes more and more apparent as worker protection and social advancement are abandoned in favour of flexible markets. We want no part of that.

13 Hooked to the falling stars

Doug Nicholls

Slow motion *coup d'état*

It has been described as the biggest slow motion *coup d'état* in history. The drive towards one legal and political entity under one constitution, known as the European Union (EU), has reached a crossroads. However, its momentum is fragile. Britain, Denmark, Poland and possibly even France – now that large unions like the CGT and FSU have opposed the Constitution – could upset the apple cart. This is why we really need to be thinking beyond the latest Federal plans and critically re-examine our entire membership of the European Union. The publications of the campaigning organisation Trade Unionists Against the European Union Constitution make a powerful contribution to the debate.

The multinationals and bankers want ultimate power over a superstate in which nations cease to exist. Practically every constituency you care to name, short of the multinationals and gravy train politicians, is opposed to a federal Europe. Any talk of welcoming a stronger European Union as a progressive counterweight to the United States is in fact a spine-chilling acceptance of the growing economic conflict that is brewing between the great blocs based around the dollar, the Deutschmark and the yen. The difference between a Republican US President and an EU President could, as their tensions continue, be no more than that between Pepsi and Coke. Britain's schizophrenic position, one minute obedient servant of Bush, next of Brussels, makes it an increasingly important battleground for the idea of the next century. Will we have comprador governments or national ones? Governments of the people or of the power blocs?

And what would be the consequences of an EU Foreign Minister getting in the way of the United States of America on any issue of substance? Tensions between the European Union and USA are increasing over trade and the world's resources, which is one reason why the European Union desperately wants its centrally controlled foreign policy and armed services. Whatever the political complexion of the USA and the European Union, as competing blocs they are on collision course and will battle it out over the resource war. The USA is also deeply alarmed that the European Union is developing its own independent satellite navigation networks that can break the current US monopoly and have considerable military

applications. Strangely enough, we are in the middle, with a Foreign Office currently doing splits over the Atlantic and the English Channel and never looking at its own people beneath.

Fragments not nations

A more domestic reflection of this huge centralisation of power is the pressure for further regionalisation of Britain. The European Union is a highly centralised, inefficient superstate fragmenting its territories into economic zones with little real power but to beg for handouts from Brussels. With Peter Mandelson there, the European Union becomes a giant Dome, monument to gambling, fraud and poor planning and the Smilesian greed of the billionaires. It cannot even be described as a gentleman's club any more. The traffickers in human life, destroyers of fertile fish stocks and agricultural land, and sharpeners of swords, are not exactly gents. Indeed Mandelson is one of only six Commissioners who can be described as coming from centre-left parties – and remember, under the Constitution the unelected Commissioners have exclusive power to initiate legislation.

These vast developments are not socialist, nor can they be subject to a programme of reform from within by socialists. They represent the very opposite of what trade unionists and socialists wanted after the Second World War. Our forebears' vision was of peacefully coexisting independent nations capable of putting their own people first without the need for mass migrations of labour. Current EU plans represent more what the defeated German generals planned in their immediate post-war document *Winning the Peace*, when they advocated a single government, currency, tax system, foreign policy, industrial and agricultural policy for the entire Continent, with a renewed Drang nach Osten (drive to the east) to incorporate those now joining the European Union.

International solidarity has two sides to it, theirs and ours. The drive to one political legal entity in the European Union is clearly their form of solidarity, the regional arm of globalisation – that is an imperialist bloc. The handlebar moustaches of the competing capitalist nations at the outset of the twentieth century have gone. In exhaustion and desperation, the boardrooms are now huddling together for a final breath of life. The EU Constitution is like their life-support machine; it is not a harbinger of a brave new world. I argue here that the best thing to do is to switch the whole thing off, and I tackle some of the reasons why we should do this and outline the outdated thinking, especially in trade unions, that is holding us back.

Self-determination

Trade unionists have always supported others in their struggles for national independence. In Britain we have been slow to apply this principle to ourselves. You could argue that we haven't had to since 1939. We are used to applauding the heroism of others in liberating themselves from imperial domination, apartheid

and colonialism. It comes as a shock therefore to recognise that now we are being taken over and we have an external power seeking to remove our national powers and democratic structures.

It is more of a problem when the political party most in favour of this takeover is the one originally created to represent trade unions in parliament. Affiliated trade unions, by default, are complicit in a form of political denationalisation on a scale never known before. This does not reflect the views of the majority of trade union members, nor the majority of workers generally. When some trade unions lose themselves in this level of embroilment with an undemocratic process, they become incorporated in what can be a sinister way and act undemocratically themselves; hence the unpleasant recent history of suppression of the EU debate in some unions. The so-called European Social Model encourages this incorporation around the table and the failed policies of partnership, and invites are made to various ETUC-sponsored trade union figures to sit round the tables of the Bildeberg Group and the Round Table of Industrialists. This is a real betrayal of the purpose of trade unions, which are about skill and power at the workplace. Nothing could be further from both than the European Central Bank and the European Commissioners, which run the euro and European Union currently and which would be further empowered under the new Constitution.

The TUC's recent spin and misinformation about the euro and EU Constitution has represented the very shoddiest of thinking in the Labour movement. The TUC's fawning to the European Union has not brought us the goods they promised and there doesn't even seem to be any embarrassment.

For example, the General Council's 2004 report said 'the European Union is a full employment economy'. This doesn't explain why unemployment in the EU zone is double ours at 9 per cent and why at one stage, as the Maastricht criteria struck, unemployment in the European Union was equivalent to the entire populations of Belgium, Denmark and Ireland being out of work. Furthermore, the 2004 report said 'the Constitution gives legislation protecting public services'. It doesn't. The terms of convergence for the euro remain, and the legislation they are in fact proposing opens up the richest prizes – health and education – to privatisation. The Constitution does the opposite of what the TUC said it does.

Often the significant thing about TUC General Council reports is what they leave out. There was no mention of the subsequently agreed General Council statement on manufacturing. Under the EU Constitution we could not have an independent national industrial strategy to rebuild domestic energy supply and factories. Our ability to do so now is very limited within the Amsterdam and Maastricht terms. Even government procurement will have to be subject to even more competition. Imports will continue to flood in, and our historically disastrous balance of payment deficits will continue.

But the General Council was, pre-Congress 2004, most silent on the very biggest issues tied up in the proposed Constitution: the economy and governance. We are the fourth biggest economy in the world. This means that in real terms only 48 per cent of our exported goods and services are with the European Union. But if we look at what we produce and buy and sell as a whole we trade 10 per cent with the

European Union, 11 per cent with the rest of the world and 79 per cent within our own domestic market. As the Chancellor continually warns us, the European Union is still the lowest growth area in the world. Putting all our eggs in the basket in which only 10 per cent of our production is involved could be fatal.

But an economy has to be managed, and the General Council is not getting to the political heart of the matter. Even proponents of the Constitution describe it as the political capstone of the EU federal state. In a federation, nation states lose the basic right of self-government. This is a right that our predecessors and many of our guests as trade unionists to our own conferences and to the TUC Congress this year, have fought in blood for.

Until now independent governments in Europe have been relating through various treaties. But the proposed Constitution is a new instrument of government with power over all member states. Westminster becomes a subsidiary conveyor of laws exclusively initiated by unelected commissioners and subservient to economic policies made by the unelected bankers and invented by Chicago School monetarists.

Trade unions want a third term of a government we elect and help direct. An EU Constitution would not allow this. It would return Thatcherite economics indefinitely. If trade unionists fail to fully explore the fundamental principle and purpose undermining the Constitution they will let us down. The 900 pages of the Constitutional Treaty come down to a simple question: who rules Britain, those we elect, or those who we do not elect? If trade unions are to have a future they must be seen to advocate for democracy the loudest of all.

Much of the slovenly thinking in the trade unions relates to the seductive illusions of European legislation. Without 'Europe' Thatcher would have killed us, goes the argument. The general pragmatism of trade unionists born of continually negotiating between a rock and a hard place, has dulled the sense of what could really be achieved. It has also led to a serious over-egging of the European employment law pudding – and, in fact, many of our substantial problems, such as pensions, detailed below, originate in European employment law. Whether any legislation is good or bad is however entirely secondary. All legislation is temporary in any event. What matters is what you do to make the legislation. If you rely on others to make it because you can't deal with your own bad lawmakers, you are giving up on one of the fundamental rights of democracy and active citizenship. For trade unionists to give up the ghost in this way has been shameful and worrying. It is as if the fundamental trade union principles – that you only get what you fight for and that as soon as you step into the court room you have lost – have been conveniently forgotten.

Pensions and the European Union

Trade unions have, rightly, been quick to condemn the pensions crisis, the huge £57 billion shortfall to meet needs and the closure of final salary schemes, but they have been slow to recognise that the origin of this problem lies in the European Union. Other European nations have not had the tradition of final pension salary

schemes. Pensions, like any other regulation, had to be harmonised in the European Union. But the end of final salary pension schemes has its origins in the restrictions demanded by the Maastricht criteria on public spending.

In stark contrast to the euro countries, Britain has a potential source of finance, which, if utilised in a prudent manner, could act as a springboard to rebuild the country. It has 75 per cent of the European Union's total occupational pension scheme assets, amounting to approximately £750 billion.

This occupational wealth, created by past and present generations of British workers, has been put aside to pay present and future pensions and represents the equivalent of 81 per cent of Britain's GDP. By comparison, occupational pension provision in Germany represents 16.3 per cent of its GDP, with equivalent figures for France at 6.6 per cent, Italy at 2.6 per cent and Belgium at 5.9 per cent.

This perspective has so far not been part of the discussion surrounding pensions, which has largely consisted of articles in the British press panicking about pensions in crisis, but without any context. At the same time, nothing at all has been said in the press about the Occupational Pension Funds Directive, discussed by EU finance ministers. In the words of European Commissioner Frits Bolkstein, the directive will 'mobilise capital in the order of trillions of euros and this will save companies millions in the cost of running employee pension schemes'. It is apparent from this statement that the whole of Britain's pensions capital is under threat. The idea is that our pension assets could be shifted by international companies and placed elsewhere in Europe.

Already, Britain's pension funds hold record levels of overseas stocks and shares. The average fund now has 28 per cent of its assets invested elsewhere, with some funds having as much as 50 per cent. In the meantime, our country is in desperate need of investment. Now the European Union wants to grab the rest by further liberalising national investment rules for pension funds and enabling multinationals to provide unified pension plans for their staff, reducing costs by millions per year. The directive, by enabling a financial institution in one member state to manage company pension schemes in other member states, will simply result in the exit of more capital from this country.

The European Union mask slips again when you look at why the cost of occupational pensions has increased by some 50 per cent over the past eight years. This has not come about by accident or because workers are living a couple of years longer during retirement, but because it has been planned by the Treasury.

In 1995 the Treasury, then run by the Tories, decided that to help meet the EU convergence criteria, the issue of government debt through the UK financial gilt market should cease. At the time, the government said that it was reducing the national debt. What it really meant was that the government was no longer able to help finance its revenues through the issue of new gilts because it would contravene the parameters laid down by the European Union on borrowing. The result was that the supply of new gilts ceased, whilst the financial demand for gilts increased, especially for 15-year and 20-year government gilts, which have always been ideal financial instruments to underpin occupational pensions whilst in payment. This is because people retiring at age 65 tend to go on living for a further 15 to 20 years.

So gilts with a 15- or 20-year term are ideal security to underpin the financial liability of an occupational pension becoming payable over the same period. Unsurprisingly (supply and demand) the price of the remaining gilts issued in the market prior to 1995 have since rocketed, to the extent that the cost of, for example, a subsistence level of pension of £7,500 per annum payable to a male aged 65, now requires at least £100,000 of capital to match the financial liability whilst in payment.

The policy of no longer issuing new government gilts has continued since 1997 and so it is small wonder that the cost of pension final salary guarantees has increased in the manner they have. Evidence of this comes from what is known as the Minimum Funding Requirement (MFR) introduced by the Tories in April 1997 but conceived in 1995 at the time the Treasury decided to dry up the gilt market.

Some sense emerging

Despite the propaganda barrage by the TUC and some unions who have lost their industries because of the European Union, they still seem to see it as the answer to their prayers. Although the TUC, goaded no doubt by the European Trade Union Confederation (ETUC), has sought to avoid this issue, at Congress 2004 a note of concern crept into even the General Council's statement, the effect of which is to open a wide debate in every trade union. The statement reads:

> Congress welcomes proposals for a referendum on the proposed Constitutional treaty for the European Union. At long last a genuine and constructive debate can take place in Britain on the issue. However, it would be inappropriate to take a formal position for or against the Constitutional treaty until unions and the General Council have had the opportunity to consider it in depth and assess its impact on key issues such as the rights of working people to decent work, the national democratic rights of member states, public services and equality.

At the very least, over the coming months we would expect all trade unions to be debating the issue in a calm and collected way and trying to get to the facts of the issue. Accept the EU Constitution and you have to accept the single currency, single tax system, single legal authority and single foreign policy. The British Parliament becomes no more than a cipher, a parish pump administering laws and finances determined by those we do not elect. The unique relationship between the British trade unions and the Labour Party would be totally irrelevant. No British government would have any meaningful authority and would have to listen to Brussels more than the brothers and sisters.

From economic to political subservience

Thatcher sought to destroy the basis of national independence by lifting export controls on capital and running down manufacturing. In particular, energy supply

had to be broken up. We will shortly be dependent almost exclusively on importing foreign-sourced energy from often unstable states, with pipes running across the European Union. We wasted our own gas and oil on paying for unemployment. There has been no let-up in the decline in manufacturing, but it has a new twist. The EU-dominated regional strategies, mean that no country is permitted to produce a balanced range of manufactured products to enhance its independence. Industries are focused in particular zones throughout Europe. This is why we have lost key staple national industries like textiles, clothing and footwear, and ceramics. Britain is not on the European Union's list to have these. The destruction of our agriculture and fisheries is just a foretaste of what is to come to our remaining manufacturing base under a more integrated European Union. You can't be a friend of manufacturing and the European Union; you will have to choose. Nations must be dependent on the market, not self-reliant and productive. All this, of course, has profound implications for environmental policies. Making and consuming as locally as possible becomes almost impossible. At a cultural level, national cultures are reduced to the uniform market in American pulp and Eurotrash.

Once your wealth-creating base becomes foreign owned and skewed to a wider strategy, so your need for a national government capable of planning and enhancing a domestic economy becomes redundant. And that is where we have been taken now. The Constitution replaces national governments. You become governed by those you do not elect.

The lost of democracy is the biggest cost of the EU Constitution, but, regardless, EU membership is leeching our wealth incredibly, and the majority of collective trade union aspirations would be met by saving the money wasted on EU membership. The Nazis who first dreamed in the modern epoch of a single European government were master liars, and much of the pro-EU propaganda here is based on pure lies.

So here are some true economic facts which should encourage us to see we have a prosperous future outside the regardless. Equivalent to about 4 per cent of our Gross Domestic Product is spent on EU membership. That could be redirected here. Every authoritative report has shown that if Britain left the regardless it would have minimal impact on jobs.

The benefits of independence and the agenda of the trade unions in command could be enormous. Not only would there be huge capital reserves to re-invest in manufacturing renewal and public services, there would be an ability to plan our economy for ourselves. An independent energy policy could be envisaged. Industries could be brought back under state control. A plan for creating production across a variety of manufacturing areas could be developed. Government procurement could be exclusively British based. Employment laws could be regulated to fit our circumstances. Taxes and interest rates could be levied to suit our pace of change. The import and export of labour and capital could be regulated also. So much could be done.

It's time for trade unionists to think ahead, leave the European Union and create our own democratic alternative. Such vision will attract members. Continuing

compliance with the status quo will not. The national question has now become dominant in Britain and, no matter who else shares the view, trade unionists should be unashamed in leading the battle for democracy and national independence. The intellectual challenges, particularly for trade unionists, are going to be demanding. They have become used to not thinking big. We are told there is only the American model red in tooth and claw or the softer European model. Used to making the best of two bad options at work, we forget that there is truly a Third Way. If we don't create this, then national chauvinists, the extreme right and others will. Nationalism coupled with socialism can emerge in a creative and positive way; otherwise there will emerge a new form of National Socialism – neither nationalist nor socialist – led by the unelected.

14 A safe European home?

Billy Hayes

Whatever view is taken by the left towards the European Union and the euro, one thing is certain: there is as yet no 'left strategy' in Europe. By this I mean a common path of action which socialists across Europe pursue to achieve the type of hegemony which the neo-liberals have gained in the United States. Instead we see various national 'à la carte' menus pursued in relation to the European Union. Taken together, the various proposals for achieving greater democracy, transparency, accountability, etc., may be considered very good. But where do they lead and how do they reflect key facts of international existence?

In the period 1989–91 capitalism was restored into eastern Europe and the Soviet Union was dismantled. The dominance of the United States of America in the world reasserted itself. The 1990s should have been a period when the left in Europe also reasserted itself. Certainly this was vital if the overwhelming self-confidence of the ruling circles in the USA were to be challenged. Yet in this time the European left has failed in restraining US ambitions to reshape the world in its desired image. Instead the left has found itself compromised by flirtations with neo-liberalism. The prospect of a second term for President Bush ought to force the European left into a period of coherent and united action. A precondition for this is a new debate on the future of the European Union.

The USA and the European Union

It is only in the world context that the future of Europe can be resolved. As a General Secretary of a trade union, I will be delighted if the CWU's problems could simply be solved in negotiations with employers, or with the British government. But I know that the future of, for example, the postal industry, is being defined by GATT negotiations, by European directives on postal liberalisation and by the broader development in the world economy. The practical question is then how to secure the most favourable development of the European Union in the context of contending international forces.

There are two key contending forces to register. First, there is US imperialism which is in an age of remaking an empire, utilising aggressive political and military means. Second, there is the dominant class forces in Europe continuing to use neo-liberalism to achieve an European Union capable of competing with the USA.

What is not sufficiently registered by the left is the fact of US intervention in the

European process – an intervention which is decidedly hostile to the success of the EU project. Divisions on Iraq have sharpened this hostility. For example, it is not simply nostalgia for an independent role in the world that drives the Tories' opposition to the European Union. It's that the Tories favour the USA's role over the European Union. Margaret Thatcher supported the Single European Act. But her government came into conflict on the European Union when it became clear that European ruling circles were driving towards a single market in order to compete more effectively against the USA. Or take the example of the role of the new ascension countries. The division of Europe into 'old and new Europe' by the White House is a slogan for a real policy. The US administration is determined to use its leverage with countries like Poland in order to limit the independence of the European Union from US policy goals.

We can assume that hostility from US ruling circles to the European Union is not an ideological quirk. Rather it is a recognition that the size of the European Union offers not just protection for EU countries against a rampant American economy, but also an attractive poll for developing countries at present in traction, financially and politically, to the US-dominated World Bank, IMF, WTO, etc.

The context of the debate about the euro and the Constitution

Once understood, I believe it is essential to place the frame of US intervention around the debates of the future of the European Union. It is mistaken to assume that all that we require is analysis internal to the Union, let alone a single country. In my view an appreciation of the current discussion relating to both the euro and the proposed European Constitution must demonstrate an awareness of the advance of US imperialism. The urgency of achieving some alternative is hardly academic. One of the decisive reasons for the assault upon Iraq was a decision of Saddam Hussein to transfer the settlement of oil transactions into euros and away from dollars. In the world today the borders between trade wars and real wars are constantly permeable. So let us examine the issue of the euro and the Constitution in this light.

The critique of deepening European integration initiatives (i.e. EMU and the Constitution) from the left tends to centre on the neo-liberal character of its economic policy. Thus:

> In an era of growing global challenges, the EU is attempting to push out-dated 1980s neo-liberal politics. The European Commission is putting pressure on member states to liberalise their labour markets. The Euro zones inflexible rules mean that Governments have privatised public services to balance their budgets. The European Central Bank has short-termist obsession with inflation, rather than creating jobs. As a result the European economies have now suffered years of very high unemployment. The need for change should be clear, but the Constitution commits the EU to the same old policies.
>
> (Centre for a Social Europe 2004: 9)

What is notable about the quote is the absence of contrast. If the European Commission policy had been contrasted to a single national government, we will be able to measure the difference but it is not contrasted for a good reason. There is no national government pursuing a qualitatively better policy. Neo-liberalism is the foundation of European national governments at present. It can hardly be a coincidence then that both a single currency and a Constitution negotiated by these governments are neo-liberal in nature. Moreover, it is not particularly convincing to claim that this contrasts with the policy of the British government.

The fact that the British government is not participating in the euro is apparently the reason why unemployment is less in the United Kingdom than in Europe. Yet, this is not, however, the rationale behind the British government's action. The critique of the European Union by the British government is that it is *insufficiently neo-liberal*. The EU countries have not liberalised their labour markets in a comparable manner to the United Kingdom. Gordon Smith believes the US labour market is a more effective engine for job creation than the European Union. The United Kingdom will adopt the euro once there is a sustainable convergence between the United Kingdom and the eurozone economic cycles. This, the first of the five conditions for entry, will be most practically tested when the single currency demonstrates a positive long-term effect on jobs, the fifth criteria. In other words, for the British government, the single currency can be entirely neutral, or supportive, on job creation. It is the unliberalised character of the labour market, apparently, that is definitely antagonistic to job creation.

This critique demonstrates parallels between the position of the United States of America, the Tories and Gordon Brown. Recently Brown deepened this parallel when he told the CBI Congress that there was the need for a new transatlantic alliance based on 'entrepreneurial flair', which apparently the US economy demonstrates. Clearly Brown's opposition to the euro is generally posed as a short-term piece of pragmatism. But much of the left opposition to the euro operates on an identical premise. That is that there is a demonstrable immediate gain to the UK economy by staying outside.

The difficulty the left faces is not in the immediate period. Brown's policy demonstrates that it is not involvement in a single currently that is decisive. What is decisive is a basis for capital accumulation over an extended period. The US economies extended capital reproduction has been premised on a thoroughly liberalised labour market in the USA, and borrowing capital from the rest of the world to sustain US living standards. The weakness of the US labour movement and the US hegemonic international position makes such a stance viable.

For the European Union to carry out such a policy would require the destruction of the welfare state, massive extension of working hours, etc. The incoherence of Gordon Brown's position is the assumption that comparability with the USA can be achieved in any other manner. Unfortunately, the left critique of the single currency has yet to suggest an alternative in which the extended capital reproduction can be demonstrated. Whilst defending the 'social gains' of the European Union the left has yet to demonstrate what pan-European economic policy can deliver the material basis for sustaining these gains.

Opposition and reform

British trade unions are generally taking a very caution stance on both the single currency and the EU Constitution. I would number the CWU amongst these. We are yet to be persuaded, and have yet to finalise our tactics. But what is finally persuasive must be coherent. Some lines of thought in a British trade union have individual merit, but exactly lack overall coherence. Some trade unions oppose the EU Constitution because of inadequate guarantees of employment rights. Given the contribution that the European Union made to employment law in Britain during the Thatcher/Major years we can understand this preoccupation.

But really does this add up? What if the EU Constitution guaranteed a 'European right to strike' rather than its definition by national law. Would the left then support both EMU and the Constitution with its priority of price stability as the primary economic goal? Surely the failure to overcome the national limits of employment law is not more important than the fact that member state government deficits cannot represent more than 3 per cent of GDP. The latter, of course, has substantial significance for any expansionary welfare programme by a national government.

A European statute on the right to strike does not amount to much in a deflated economy. It must be clear that pressing the particular social employment rights only makes sense with a simultaneous pressure for an expansionary economy. Yet immediately this poses the issue of which economy is to be expanded, a member state economy or that of the European Union.

There is one line which answers this dilemma. At its most abstract track it runs as follows: against EMU and the euro/Constitution and for the United Socialist States of Europe. Such a prospect is very pleasant but also not in view. What such a line suggests is no immediate prospect of power and a long period of isolation. This is chilly indeed. It accepts that neo-liberal forces would hold sway for many years to come. It accepts that the European Union cannot, for any foreseeable time, act as any sort of counter to the new US empire. And it suggests that progressive forces are confined to the margins of the labour movement in Europe.

This cannot be the basis for a left strategy. To suggest that the best that socialists can do at the start of the twenty-first century is to make propaganda is genuinely infantile. A left strategy would outline a course of action which starts from the needs of hundreds of millions of people in Europe and billions across the planet. It must act as a rallying point to those opposing the construction of a new American empire.

The question to be answered rests on the viability of the European Union acting as a coherent block in the world. To establish this we must achieve clarity on the following issues: First, on the outline of an alternative economic policy to neo-liberalism which operates in the member states and the European Union. The argument about EMU and the Constitution must not duck the fact that both replicate the prevailing orthodoxy in at least the most influential member states. The limits of the single currency and the EU Constitution are to be found in Raffarin's reforms, Schroeder's reforms and Blair and Brown's advocacy of

'flexibility'. Supporting or opposing the euro and the EU Constitution changes this not a jot.

Second, a large expansionary economic block is an essential precondition for a 'social Europe'. The left must aim to gain hold of national governments in Europe in order to promote a growth of the national and European economy. Confining ourselves to making propaganda may seem comfortable, but it would be a capitulation to neo-liberalism.

Third, that the combined economic weight of the nation states of Europe offers a sufficient enough basis to carry on a common foreign policy independent of the US government. For the left this is one potential route to improve the bargaining position of developing countries against the US domination of the WTO, IMF, World Bank, etc. The left in Britain should not be a bridge between the USA and Europe. It should aim to be a defender in Europe of the developing countries against the USA.

Finally, a left policy for the European Union will be coherent across the Union and within the member states. This would indicate the tendency towards greater integration and coordination for the member states. 'Enhanced cooperation' is possible from a left, as well as a right perspective. So whether such cooperation is correct depends on whether it assists the struggle and needs of the workers and oppressed.

15 British trade unions and EMU

Natural supporters or conflicting interests?[1]

Philip Whyman

Introduction

The establishment of Economic and Monetary Union (EMU), amongst (currently) 12 European Union (EU) member states, has great significance for European working people and their families. This initiative involves the introduction of a common currency (the euro), with both exchange rate management and monetary policy having been transferred from national to super-national control, exercised by the European Central Bank (ECB). The United Kingdom has to date remained uncommitted to this initiative, preferring to rely upon an opt-out clause, ostensibly until economic cycles coincide and five economic tests indicate that participation is in the national interest. Leading members of the Labour Party and prominent trade union leaders have indicated their personal support for further European integration, despite the consistent hostility of the electorate as reflected in opinion poll data. The current political position, where the majority is committed to further integration whilst the majority of the Conservative Party firmly opposes the deepening of economic integration, is a reversal of the balance of opinion two decades ago.

This 'report' will therefore seek to answer two main questions: first, why the labour movement altered their previous critical stance towards European economic integration and became amongst its staunchest supporters; second, whether this new enthusiasm towards further integration, and particularly membership of EMU, is in the national interest or that of working people.

Evolution of labour movement opinion

The British labour movement was initially opposed to EU membership on the grounds that it was designed to benefit multinational capital at the expense of workers. The free movement of goods and capital enhanced corporate profitability through economies of scale, but also provided transnational capital with the opportunity to threaten national workforces with disinvestment and the relocation of production abroad if wage concessions were not made or strikes abandoned. Furthermore, the free movement of capital undermines government policy autonomy, thereby weakening democratic self-determination and full employment

strategies, thereby potentially reducing the strength of nationally located labour movements (Nairn 1973: 7, 66–73, 147).

The leadership of the Labour Party abandoned this policy in 1974, and successive leaders have become increasingly favourable to further integration, pledging the intention to keep Britain at 'the heart of Europe'. Prime Minister Blair emphasises this policy shift to distinguish 'new' from 'old' Labour Party politics, whilst magnifying differences with an increasingly eurosceptic Conservative Party. Labour MPs have largely adopted the new strategy, with only 16 per cent opposed to EMU entry, despite 29 per cent believing EMU would institutionalise neo-liberal economic policy in Britain and therefore severely constrain the ability of a Labour government to successfully govern the country (Baker *et al.* 1996). The explanation for this apparent contradiction may be found among the 88 per cent of Labour MPs who believe globalisation makes membership of EMU a necessity. Euroscepticism within the labour movement therefore appears to be concentrated amongst the 'old' left, thereby forming a 'declining legacy of Labour's past' with the party's 'centre of gravity . . . shifted decisively in favour of Europe and EMU' (Strange 1997: 15).

The Trades Union Congress (TUC) was more reluctant to abandon its position to EU membership, and only did so after a 1975 national referendum produced two-thirds support for continued membership (Strange 1997: 16). However, it was only a decade of Conservative government, determined to marginalise trade unions politically and undermine their industrial strength through legislation and the toleration of a high level of unemployment, that led to the 1988 TUC Congress enthusiastically greeting the alternative presented by Jacques Delors as a 'social Europe' which embraced labour rights as core elements (Strange 1997). Concern that economic integration may create unemployment, particularly expressed by TGWU and the public sector unions, became more muted over time due to the preference for a 'European' social democratic model rather than an 'American' version of neo-liberalism. Furthermore, this position was reinforced by:

1 Labour movement discipline – the desire to secure the election of a Labour Party government led to self-imposed avoidance of contentious issues.
2 TUC advocacy of European Exchange Rate Mechanism (ERM) membership – the acceptance of the loss of monetary policy sovereignty, dismissal of devaluation as 'anti-worker' due to the usual reduction in living standards, and substitution of low inflation over full employment as the prime goal of government policy all meant that membership of EMU would not imply a significant shift in trade union economic strategy.
3 The European Trades Union Congress (ETUC) securing a commitment from the EU Commission to emphasise employment policy (Monks 2000: 186–7) – this diffused criticism that EMU was simply concerned with financial interests, but unfortunately has done little to resolve the persistence of mass unemployment across most EU member states.
4 EMU being 'part of the European Social Model (ESM) package'.

European Social Model (ESM)

Although an ESM may be more variable in practice, and more comprehensive than the current approach taken in the text, a good basis for definition may be to consider it as a variant of the post-war German 'Social Market Model', whereby a successful, competitive market economy has been counterbalanced by generous welfare provision and labour protection. The rights available to German employees and citizens remain amongst the most extensive of any capitalist economy throughout history (Glasman 1997: 134). The emphasis upon the inclusion of workers and their unions in the working of the economy facilitates an expression of 'voice' rather than 'exit'. This, in turn, leads to cooperation in adapting to change, superior morale resulting in enhanced productivity and lower employee turnover, and, finally, the prevention of low-skill, low-investment competitive alternatives stimulates productive investment and innovation. Moreover, it provides the European social democratic labour movements with an alternative model to the neo-liberal prescription of market superiority to social institutions and the commodification of worker-citizens.

An ESM offers British trade unions the possibility of realising four distinct types of objective. First, it provides a bulwark against the renewal of radical Conservatism intent upon weakening trade unions as part of a pro-market strategy, since EU Directives supersede national legislation and cannot therefore be easily changed. Second, trade unions are incorporated as legitimate social partners and counterpoints to organised business organisations, thereby promoting employee involvement in relevant aspects of working life at both the local and the supernational level. This provides a role for unions to fulfil and thereby justifies continued membership. Third, comprehensive welfare provision promotes income redistribution and labour de-commodification, thereby enhancing trade union power resources. Even the present, minimalist EU social measures have delivered additional protection for British workers, thereby insulating them from 'the worst excesses of laissez-faire capitalism' (Edmonds 2000: 194). Fourth, material support provided by the EU Commission to facilitate social partnership represents fully 13 per cent of ETUC income, in addition to travel subsidies and technical assistance (Abbott 1997: 472). Thus, the ETUC has a direct financial interest in supporting further European integration.

The combination of material support for a beleaguered trade union movement and the possibility of the European Union establishing its distinct variant of an ESM, provided powerful reasons for the union leadership to overlook a degree of scepticism concerning the European integration project and to embrace EMU. Admittedly, the case for joining EMU would appear more compelling had an ESM *actually* been established and not remained an unrealised aspiration. Hence, although the British trade union movement supports EMU membership, for influential members this position remains conditional upon the promotion of an ESM (Edmonds 2000: 198–9).

Contradictions within the trade union case

The stance taken by leading figures in the trade union movement appears to be consistent with their traditional aims and values only as long as certain key assumptions hold. These are: that EMU proves to be an economic success outweighing the costs of transition: and that the unions are correct to believe that the EU Commission will ultimately create an ESM for Euroland which will prove consistent with the requirements of EMU. Unfortunately, there is a considerable body of evidence to cast doubt upon both of these assumptions. Consequently, the trade union case for supporting EMU must be subjected to rigorous evaluation to ascertain which elements are likely to prove unreliable and, therefore, whether the strategy followed by most leading trade union figures is fundamentally flawed.

Economic impact of EMU

The net economic effect of EMU membership is understandably uncertain because it has no historical precedent. Optimists argue that greater exchange rate stability, reduced transaction costs, enhanced competition deriving from price transparency and low real interest rates resulting from a successful anti-inflation strategy pursued by the independent ECB will all combine to provide a virtuous cycle of increased business confidence, trade, investment and growth. Sceptics point to the loss of monetary and exchange rate policy instruments as being likely to increase economic instability amongst countries which are incompletely converged and are therefore more likely to suffer from asymmetric external shocks which the ECB will be incapable of moderating by use of its only policy instrument: interest rates. Furthermore, the ECB may itself represent a second source of instability, as its desire to establish anti-inflation credibility with the financial markets may result in over-tightened monetary policy, resulting in unemployment and a stagnant economy. The rigid convergence rules, reinforced by the Stability and Growth Pact (SGP), oblige participating member states to limit budget deficits to 3 per cent of GDP in all but the deepest recessions, necessitating an approximate 7 per cent in boom periods. These restrictions have already contributed towards a decade of high unemployment and stagnant European growth (Holland 1995).

Responses have ranged from austerity packages, including Germany's largest fiscal entrenchment in post-war economic history (£30 billion, DM70 billion), to the conclusion of tripartite social pacts (i.e. Italy and Portugal) to legitimise fiscal retrenchment (Strange 1997: 13–14; Teague 1998: 119–20). Unlike traditional corporatism, these agreements offer organised labour nothing in terms of enhanced redistribution, but rather promise to *reduce* the social wage in order to meet the convergence rules. However, many trade unions defend them as providing the best strategy to ensure they remain influential actors in a single-currency Europe (Teague 1998: 120). Nevertheless, public sector unions will experience increasing pressure to moderate pay, to maintain international competitiveness and to meet fiscal restrictions, but at the cost of exacerbating pay differentials between public and private sectors. This will ultimately lead to industrial unrest or

recruitment problems – already evident in the British health and education sectors. It is for this reason that those unions with the greatest reservations about EMU are generally to be found in the public sector (Strange 1997: 16–17).

Wage formation – crucial for successful EMU

Pay determination will become increasingly important within EMU to ensure that aggregate wages grow in line with productivity and to facilitate acceleration of industrial restructuring. The difficulty for government, employers and unions, is that there may be a conflict between a *macroeconomic* definition of flexibility of real wages, and a *microeconomic* objective of rapid adaptation to diverse patterns of industrial change. The former may be best achieved through coordinated wage bargaining, where all parties can internalise the inflationary implications of their decisions, whilst a solidaristic wage structure should minimise social conflict and encourage self-restraint in exchange for increased employment opportunities. Indeed, the Netherlands, Germany and Ireland have sought to promote wage bargaining moderation through national or sector-level pay bargaining structures to facilitate the transition to EMU (Teague 1998: 119–20). However, micro-economic objectives may be best advanced via decentralised bargaining and flexible contracts (Pissarides 1997).

An additional consideration derives from Keynes' observation that *relative* wages are at least as significant as real wages when formulating negotiating objectives. Thus, the transparency resulting from a single currency facilitates wage comparisons within the EMU area, stimulating demands for wage equalisation. This strategy may be supported by union confederations in high wage areas, as this will reduce the threat of wage competition undermining their preferential labour market position. However, if attempted in the absence of an equalisation of productivity, this will lead to job losses in the less productive region. The 1989 German reunification occurred at exchange rate parity, whilst considerations for equal citizenship and prevention of large-scale migration led to a considerable increase in former East German wages, despite productivity remaining less than half the western level. Accordingly, gross wages in manufacturing in the east rose to 138 per cent of net value-added, resulting in output falling by 67 per cent in the first year after unification and leading to 25 per cent of the entire labour market losing their jobs (Buechtemann and Schupp 1992: 95–7, 102–4). Hence, the German unification case represents a stark warning of the dangers of mishandling a rapid movement towards EMU.

Europeanisation of industrial relations?

The desire for real wage flexibility within EMU may facilitate the creation of new forms of national labour market coordination between social partners, perhaps on corporatist lines. Pan European TNCs may encourage an embryo European system of industrial relations through the harmonisation of pay and conditions for employees irrespective of the location of production. The European Works

Council (EWC) initiative is considered to further strengthen cooperation and the pooling of information between EU trade unions, potentially leading to euro-bargaining to establish universal minimum standards of training, anti-discrimination practice and promotion procedures (Rhodes 1992: 45).

It is equally possible, however, that the creation of a European labour market may be limited to certain key groups of workers, who possess specific technical and managerial skills, and to particular categories of highly mobile labour, notably managers, construction workers, labourers and young people. In this scenario, the higher incomes that are commanded by key employees may disrupt national labour markets by increasing income inequality or by low-wage countries losing skilled labour to higher-wage member states. Furthermore, while the advent of euro-bargaining could provide new opportunities for trade unions and their members, it could equally fragment unions along supranational company lines, thereby undermining class solidarity. Accordingly, unions risk becoming 'partners . . . of regional capital trying to survive in inter-regional free market competition' rather than 'agents of inter-regional redistribution' (Streeck and Schmitter 1991: 55).

The intensification of international competition may additionally cause companies to focus upon internal rather than national labour markets (Marginson and Sisson 1996: 177–8). Trade unions therefore face marginalisation due to employer preference for company-level 'productivity coalitions' rather than centralised concentration or sectoral bargaining. According to this viewpoint, euro-bargaining is irrelevant to the needs of post-Fordist flexible production (Rhodes 1992: 28). The divergent tensions, threatening to further complicate European industrial relations, are likely to persist into EMU because current arrangements show no clear evidence of converging to a uniform pattern across Euroland (Rhodes 1992: 43–4).

Social policy and labour regulation

The EU Commission proposes that the creation of a 'Social Europe' is sufficient to counterbalance negative features emanating from competition and restructuring stimulated by EMU. Whilst unfair to dismiss such achievements as meaningless, it is nevertheless grossly insufficient for the EU Commission to portray this as a distinct ESM. The high fragmentation of social policy within, and between, EU member states implies that European regulation is only possible for non-contentious issues, issues on which nations share common interests and goals, such as health and safety matters. Otherwise, social protection occurs at the lowest common denominator. Thus, the presentation of the European Union's social dimension as the basis for a social citizenship is premature. It remains little more than an 'eclectic body of employment law' with a 'hollow core' (Leibfried and Pierson 1995). It may have been successful in enticing trade union support for further European integration. Nevertheless, Streeck (1992: 218–19) considers the 'retarded advancement of European-level political rights' and the 'almost complete absence of a European system of industrial citizenship' as indicating that there is little reason to anticipate that these initiatives will prove particularly successful.

Of course, it is possible that the European Union's social dimension may progressively evolve into an ESM. However, this ignores the increasingly vocal neo-liberal critique that 'excessive' welfare expenditure causes 'eurosclerosis' and a decline in economic performance. It is claimed that labour regulation and taxation reduce work incentives and that government borrowing crowds out more productive private investment, whilst social security transfers reduce private saving and therefore the stock of capital. However, the evidence is rather mixed. Welfare expenditure is an automatic stabiliser, whilst labour market policies and social insurance facilitates risk-taking and acceptance of industrial restructuring. Indeed, British Prime Minister Tony Blair has pointedly rejected the 'old social model' in Europe, arguing 'our welfare systems and labour markets will require fundamental reform'.[2] Similarly, the ECB's senior economist, Otmar Issing, blamed the poor performance of the euro on 'the adverse impact of minimum wage and employment protection legislation', which can only be overcome by a 'comprehensive programme of structural reform'.

In practice, this consists in creating what Cerny (1990) describes as a transition from welfare state to '*competition state*', one in which policies are determined by the perceived demands of survival in the global economy. Consequently, it appears paradoxical that British trade union leaders are relying upon the completion of an ESM to provide them with a preferable system of social protection and employee participation in the work process when EU governments are increasingly questioning the future of this very model.

Conclusion

Trade union support for EMU relies upon its association with the establishment of an ESM within the 'New Europe'. However, analysis of this assumption highlights significant contradictory indicators. The economic evidence is balanced over whether membership will deliver any significant dynamic gain, as cost savings are counter-balanced by the deflationary impact of the SGP and ECB. Public expenditure restraints threaten public sector national pay bargaining whilst acerbating differentials between public and private wage growth, thereby fuelling recruitment problems and industrial unrest.

Predicted developments in industrial relations and wage formation hold as many problems as solutions for unions and their members. Trends towards euro-corporatism seem weak, and where they do exist the value to government's lies in the possibility of securing lower real wage growth – hardly a long-term strategy to appeal to union members. The tendency for TNCs to concentrate more closely on internal labour market arrangements than on national wage formation implies that any emergence of euro-bargaining may be company-orientated and undermine class solidarity. Moreover, after two decades of construction, the European Union's social dimension is a poor reflection of an ESM of the type favoured by trade unionists. The acceptance of the neo-liberal critique of welfare states by influential EU actors is inconsistent with the trade union belief in the ultimate creation of a fully fledged 'Social Europe'.

In short, the trade union case for supporting EMU is fatally flawed and its current leadership is basing its support for EMU upon a number of questionable assumptions. A deflationary, neo-liberal Euroland, whose economy is managed by a ECB charged with the sole objective of producing stable prices, is inconsistent with the development of an ESM capable of guaranteeing social citizenship based on generous welfare provision, protection at work and employee input into their working lives. Trade unionists should, therefore, reconsider their strategy of uncritical support in order to calculate the possibility of mobilising sufficient European public opinion behind their vision of a 'Social Europe' to secure a shift in government policy, thereby modifying the constraints imposed by EMU and supporting an extension of social policy, labour regulation and the promotion of full employment. The only other realistic alternatives involve the rejection of EMU and preference for implementing the desired policies in individual nation states, or the uncritical acceptance of EMU and hope for the creation of an ESM, against the balance of the evidence. Neither strategy will appeal to a trade union leadership, which has invested considerable political capital in its current position. Nevertheless, a new strategy is urgently required. The only remaining question is whether the current trade union leadership have the courage and vision to re-examine these issues and develop a new approach to avoid future damage to the movement and its membership.

Notes

1 An earlier version of this paper was published in *Industrial Relations*, 41 (3): 467–76.
2 A. Blair, 'Managing change: a national and international agenda of reform?', speech given at the World Economic Forum, Davos, Switzerland, 28 January 2000.

16 The European social model

Between a rock and a hard place?

Matthew Watson[1]

Introduction

The British debate about European economic integration displays many peculiarities. Prime amongst them, I suggest, is the following. Whilst the party political right in Britain has tended to opt into the debate about integration, albeit primarily as a means to opt out of the institutional arrangements established to guide the integration process, the party political left has increasingly opted into the institutional arrangements having previously opted out of the debate. I attempt to use this chapter, first, to explain the limited nature of left political mobilisation around the preferred form of Economic and Monetary Union (EMU) and, second, to show that the institutional apparatus established at Maastricht to guide the integration process further constrains the political space for viable left strategies.

I focus my discussion around an analysis of the 'European Social Model'. Influenced by repeated Commission assertions that the development of a supranational 'social dimension' would run parallel and be given equal weight to the process of economic integration, the European left has tended to vacate the ostensibly technical economic debate concerning increased market interdependence in favour of the more overtly political debate concerning the 'social dimension'. Yet, as the outcomes of the technical economic debate have been embedded both as Community Law and as everyday member state practice, it has become increasingly clear that they create an institutional apparatus within which the defence of existing national social models has become ever more problematic, and the development of a supranational 'European Social Model' all but impossible.

My conclusions are threefold. First, I argue that it is important to distinguish between the impact on the 'European Social Model' arising from the formalised constraints on policy autonomy introduced alongside the euro, and those arising from changes in the business culture of European firms triggered by the creation of a single capital market. I call the former the macroeconomic impact of EMU and the latter the microeconomic impact of EMU. Second, I argue that the space for viable left political mobilisation within the context of EMU has been narrowed most particularly by the establishment of an active cross-border market in corporate control, which has served to undermine the traditional 'European'

model of corporate governance. As such, I conclude that the microeconomic impact of EMU outweighs the macroeconomic impact. Third, I suggest that the form of corporate governance to which Europe appears to be gravitating is, in many ways, relatively similar to that already in place in Britain. Consequently, such a process is likely to have least effect in Britain.

Market ideology, European institution-building and the macroeconomics of EMU

It is only relatively recently that the extension of the 'European Social Model' has been identified by the left as a means to use European institutions to construct a progressive counterweight to an increasingly pervasive global market ideology (Kenner 2000). Indeed, much of the early discussion of the potential benefits of economic integration, from both left and right, focused on expectations of social gains resulting from an increasing exposure of everyday life to market relations (Gordon and Thirlwall 1989). For many authors, the concepts of integration and marketisation are reasonably interchangeable in the history of ever closer economic union within Europe.

Moreover, if this is true of the *process* of integration, it is even more true of the *debate* which has preceded key moments of that process, and which has focused on the necessary institutional developments for facilitating integration. According to Grahl and Teague (1990), at every stage of accelerated integration, one condition has dominated the debate above all others: to what extent will future institutional arrangements provide enhanced incentives for economic agents to create increased cross-border market interdependencies? As a consequence, the institutional arrangements which have set the parameters for the socio-economic status quo within the European Union have typically been subjected to reform at precisely the point at which their potential to increase the scope of market relations has been exhausted. The ideal of *extending* the 'European Social Model' in order to create a supranational zone in which citizens' rights might take precedence over market ideology may well be an active part of contemporary left political discourse at the EU level. However, the history of European institution-building would suggest that a more pressing reality is the *defence* of existing national social models against the encroachment of market ideology originating from within the European Union itself.

This is not the way in which threats to the 'European Social Model' are usually presented in the popular political discourse of the left. It is more typical for European integration to be promoted as the means through which national social models may be defended, rather than that which they must be defended against. A simple 'Europeanisation' versus 'globalisation' dichotomy tends to prevail, in which global economic integration is identified as a force that serves to undermine existing levels of social protection, and European economic integration is identified as a potentially progressive palliative to such pressures. However, this line of reasoning would seem to owe more to an unquestioning faith in the necessarily progressive nature of European integration than it does to an awareness of the

practical operations of the institutional arrangements in which the integration process is currently embedded. Perhaps most significantly, it allows us to understand little about the way in which the institutions of EMU are likely to exert similar political pressures to those which are more commonly described as 'effects' of globalisation (Hay *et al.* 1999). The Stability Pact, for instance, formally legislates away governments' ability to engage in deficit-financed growth, whilst the persistence of global economic forces is merely assumed to make such a strategy 'inadvisable'.

The left has generally been quick to highlight the negative social consequences of globalisation, but much more reticent in attributing similar consequences to European integration. Yet, it is clear that the decision to pool monetary sovereignty will only be socially costless under certain macroeconomic conditions. Moreover, such conditions are so extreme – perfect synchronisation of business cycles, perfect symmetry in the transmission of monetary policy, perfect flexibility in wage adjustment, perfect mobility of labour (Healey 2000) – as to suggest that they are logical abstractions rather than situations which could ever be expected to arise in practice. In the absence of such conditions, EMU has been buttressed by a number of policing mechanisms designed to prevent internal economic instability from undermining the political sustainability of monetary union.

If we consider the macroeconomic constraints imposed by the European Central Bank and the Stability Pact, the suggestion of Dyson (1999) that the procedures of EMU generate a 'bound Leviathan' may be particularly apt. The intellectual justification for increasingly circumscribing the scope for autonomous policy initiatives with a series of binding commitments is rooted in the economics literature on 'policy credibility' (De Grauwe 1996). Without such commitments, it is assumed that rational market actors would interpret the absence of costless adjustment mechanisms to monetary union as a sign of its inherent political contradictions. Moreover, in acting in line with that interpretation, it is further assumed that by their own actions they would make the prediction of an unworkable EMU come true in practice. As Stanley Fischer suggests, arguments for both an independent European Central Bank and a Stability Pact are drawn from an explicit acknowledgement of a 'second-best' world. In a 'first-best' world of costless adjustment, we could expect that monetary, fiscal and labour market policies would be perfectly coordinated, and that there would be no need for European institutions to impose a series of binding commitments as a substitute for market coordination (Fischer 1996).

There are a number of ironies in this situation. First, EMU has been constructed in elite EU discourse as a 'necessary' condition of successful integration, in that it is only through monetary union that the success of the internal market can be ensured (Gros and Thygesen 1998). In other words, EMU has been identified by Europe's political leaders as the means to embed *further* market rationalities within the European economy. Yet, on the basis of a reading of the 'policy credibility' literature, we could be forgiven for concluding that *existing* market rationalities would render EMU unworkable were it not for the range of institutional procedures which have been introduced alongside the single currency to restrain

certain forms of policy autonomy. Second, the academic literature on EMU contains a number of empirical analyses which attempt to assess which member states may be least disadvantaged by the transition to monetary union because they have appropriate adjustment mechanisms which enable them to minimise the social costs of transition (Garrett 1998). This literature tends to conclude that the existence of encompassing labour market regimes is likely to be the best predictor of an efficient macroeconomic transition to monetary union (Golden 1993; Hall and Franzese 1998; Soskice and Iversen 1998). However, these are the very labour market conditions that EMU's constraining institutional procedures will make it more difficult to reproduce. In general, the macroeconomic stance privileged by EMU is seen as antithetical to the ability to maintain the fiscal base of encompassing labour market regimes (Esping-Andersen 1996; Stephens *et al.* 1999).

With monetary union likely to erode all but the most liberal of labour market regimes, the logic of EMU is for the European Union to accept responsibility for mitigating the adverse social consequences of economic shocks (Begg and Hodson 2000). Yet, it is clear that no such mechanism exists to act as a supranational 'social shock absorber'. As Kenner (2000) suggests, social policy continues to operate very much 'in the Community's "twilight zone"'. Despite all the Commission's recent rhetoric about a supranational 'European Social Model', this has yet to be translated into the world of lived experience. Indeed, whilst the Commission's sympathetic pronouncements on EMU view monetary union as the context within which the construction of a supranational 'European Social Model' becomes possible (Commission of the European Communities 1993a; Ross 1994), its more immediate impact has been to undermine governments' ability to fund progressive social entitlements at the national level.

However, it has to be recognised that the debate about the macroeconomics of EMU is rather more complex than the above analysis may suggest. The social costs of monetary union must be understood in relation to the social costs of viable alternative monetary arrangements. It is clear that such alternatives would also have significant implications for the persistence of European social models, and it would be somewhat misleading to imply that the rejection of EMU would be a necessarily costless exercise.

The most common argument against EMU in the transition to monetary union focused on the desirability of a flexible exchange rate regime within Europe. But, to what extent would this be a costless option? First, it is necessary to note the political costs that would almost certainly have resulted had leaders of the left become open advocates of such a position. To have supported the continued floating of European currencies in opposition to monetary union would have required an acknowledgement that market relations provide the preferred means of macroeconomic adjustment to destabilising shocks. This perhaps goes some way to explain the relative silence of the left in the economic debate on EMU. Market ideology was so pervasive in that debate that the left found itself in the potentially 'no win' situation of either supporting EMU as a means of extending the scope of market rationality within the developing internal market programme, or opposing EMU on the grounds that more suitable market-based solutions to the problem of

economic coordination existed outside the context of monetary union. Either way, it would have been in the position of having to affirm a 'market-enhancing', rather than a 'market-correcting', option.

Second, there are social as well as political costs arising from a flexible exchange rate regime. Whilst EMU seems sure to impose significant social costs through economic restructuring, it is far from obvious that the social costs of the most viable alternative would have been any less pronounced. A flexible exchange rate regime provides an efficient means of economic adjustment only in circumstances in which currency prices reflect nothing more than underlying economic fundamentals. Yet, there is no evidence that this is an appropriate characterisation of the way in which currency markets actually work in practice (Frankel 1996). These markets are now exceptionally liquid, having a daily turnover in excess of US$2 trillion (*The Economist* 2000). Such high levels of liquidity enable market trading to remain profitable, even at prices which bear little correspondence to economic fundamentals. Indeed, much of the activity within the currency markets is now aimed at deliberately driving prices away from their fundamental value; for it is in these moments that market trading is able to deliver substantial gains on the back of self-fulfilling dynamics (Watson 1999).

Exchange rate variability implies significant social costs as it destabilises productive sectors of the economy. As Daniel Gros and Niels Thygesen (1998) suggest, we must therefore hold open the possibility that the relative costs of economic restructuring under monetary union may be lower than under conditions in which productive sectors constantly have to adjust to the destabilising effects of 'momentum trading' within currency markets. 'If the alternative is a prolonged period of exchange rate variability', they argue, 'the benefits [of EMU] could be substantial'.

The welfare effects of the macroeconomics of monetary union are thus somewhat ambiguous. However, it may well be that the welfare effects of the macroeconomics of EMU are less important than those of the microeconomics of EMU. The existing academic literature is heavily weighted towards the former set of concerns, but it is these latter concerns that I will seek to address in the remainder of this chapter.

The microeconomics of EMU and changing forms of corporate governance within Europe

The institutional impact of EMU extends beyond the formal apparatus of the European Central Bank and the Stability Pact and, as such, beyond the constraints which this apparatus places upon government policy. EMU impacts also upon the behavioural traits of economic actors within the private sector and, in particular, firms. The single currency has been introduced on the back of wider changes within the European economy, and these changes have altered the incentives faced by firms to continue to reproduce their existing mode of corporate governance. It is at the microeconomic level that the effects of EMU on the 'European Social Model' are likely to be most pronounced, because national variants of that model

are rooted in distinct types of corporate governance. It is therefore necessary to assess the major structural economic changes which formed part of the transition to monetary union, with a view to understanding their effects on the continued viability of the 'European Social Model' through their effects on European business culture.

Perhaps the most significant change in this respect has been the formal elimination of all internal barriers to financial flows. This has yet to produce a perfectly frictionless capital market at the EU level, as significant transactions costs remain as a continued disincentive to cross-border investment (Watson 2001). Nonetheless, European capital markets are today more integrated than at any previous time, and this has created larger pools of liquidity from which to finance investments in existing companies.

This additional liquidity has had an important influence on existing modes of corporate governance within the European Union. First, it has made it easier to raise large sums of money in a relatively short space of time, and this in turn has created an active market for corporate control at the European level. Second, the fact that financial managers operating within that market are faced with similar profit constraints has led to an increasing homogenisation of firm behaviour with regard to corporate risk. Third, the desire to appear 'takeover proof' in the presence of potentially hostile investors has focused the attention of company executives on internal restructuring designed specifically to maintain buoyancy in share prices. All three of these changes can be traced directly to single capital market legislation, and all three can be argued to be evidence of an emergent business culture somewhat at odds with that which typified the earlier post-war period. Indeed, according to *The Economist* (2000) 'so pronounced is the recent change that one may even question how distinctively "European" the [political economy of] Europe will seem in, say, another five years'. Whilst this is surely to exaggerate both the extent and the nature of current restructuring dynamics, it would be equally misleading to deny significant change in existing modes of corporate governance throughout Europe by virtue of the integration process.

In early 2000 Vodaphone launched a successful hostile takeover bid for the German telecommunications company, Mannesmann. It had used the enhanced liquidity of the European Union's integrated capital markets to raise sufficient short-term capital to buy a controlling stake in Mannesmann against the wishes of the latter's management. This was both the world's largest-ever hostile takeover (demonstrating the potential for structural economic change contained within the single capital market legislation), and also the first ever to succeed in Germany (suggesting, perhaps, a new tolerance of aggressive capital market behaviour). Moreover, this should not be viewed as an isolated incident. In each year since the single market was completed in 1992, the size of the European Union's mergers and acquisitions market has increased. Yet, this is no simple linear expansion; market growth has accelerated markedly since the beginning of stage three of monetary union. Whilst the overall market value of European mergers and acquisitions rose to almost four times its 1992 level in the six years to 1998, in the next year alone it rose to over seven times that level (*The Economist* 2000). A similar

acceleration is visible in the value of hostile takeovers. More than US$400 billion of successful hostile takeovers were conducted in the European Union in 1999, a figure which was over four times that for the rest of the 1990s put together (*The Economist* 2000). From being an inconsequential feature of the European mergers and acquisitions market at the beginning of the 1990s, hostile takeovers accounted for well in excess of 40 per cent of that market in 1999.

The fact that the most significant changes in the European market for corporate control occurred in the year that the single currency was introduced is surely more than merely coincidental. Much of this increase in mergers and acquisitions activity was financed through euro-denominated bond issues (*Financial Times* 2000). In the absence of EMU, this market would quite clearly not have existed. Moreover, in the absence of the additional liquidity created by the prior integration of the European Union's capital markets as part of the transition to EMU, its capacity to have financed such a dramatic increase in mergers and acquisitions would presumably have been more limited.

Arguably the most significant aspect of this increase in mergers and acquisitions activity is the related tendency for the banking sector to be progressively crowded out of the European market for corporate control. This is particularly important, because many comparative political economists have identified closely networked relationships between firms and banks as the defining feature of a distinctively 'European' model of corporate governance (Pollin 1995). These close relationships have tended to allow firms a certain 'breathing space' to adjust to changes in external market conditions. In general, this is an adjustment time which is markedly constrained when the firm is subjected to the constant short-term evaluation of a capital market-based financial system.

If an increasing number of European firms find themselves operating within a market for corporate control more readily typified by capital market-based rather than bank-based financial relations (*The Economist* 2000), this is likely to have significant effects within the European labour market. Existing empirical data indicate that those European countries which have higher exposures to capital market-based corporate governance also have labour markets which adjust more quickly to adverse demand shocks (Barrell *et al.* 1996). To put this somewhat differently, firms operating within bank-based corporate governance systems have found it easier to implement a labour market strategy which acts as a form of social protection in times of economic downturn.

Changes in the market for corporate control would therefore seem to have significant implications for the future viability of the 'European Social Model'. If firms find that they are less able to operate a labour market strategy which also acts as a form of social protection, responsibility for such provision is likely to pass solely into state structures. Should this prove to be the case, it is possible that the microeconomics and the macroeconomics of EMU will combine to form a reinforcing double bind on the 'European Social Model'. For, at the very moment that member states may be required to *increase* their social provision because firms are faced with more exacting labour market pressures due to changes in the market for corporate control (the microeconomic impact of EMU), they may discover

that their ability to reproduce *current* levels of social protection is increasingly constrained by the fiscal criteria of the Stability Pact (the macroeconomic impact of EMU). In such circumstances, it is unclear to what extent the defence of existing national social models is a viable political strategy under conditions of monetary union. Prospects for the creation of a truly supranational 'European Social Model' appear fanciful indeed.

Conclusion

The microeconomic effects of EMU are already an established feature of the context in which all European firms operate. However, the current British debate on euro membership would appear to be almost entirely oblivious to this fact. As a consequence, I suggest that this debate is significantly weakened by two factors:

1. the lack of formal acknowledgement that the microeconomic pressures of EMU are brought to bear on firms irrespective of whether their governments are committed to full participation in the final stage of monetary union; and
2. that they imply a form of corporate governance which is already the established model for firms in Britain.

Even in the highly unlikely circumstances that political conditions changed within the European Union in such a way as to persuade member states to unlock their exchange rates and re-impose their national currencies, this would be no guarantee that governments would be 'freed' from all of the economic constraints of monetary union. The microeconomic impacts of EMU and, in particular, changes in the market for corporate control influenced by the single capital market legislation, are not as closely tied as the macroeconomic impacts of EMU to the physical existence of the euro. Institutional changes which have begun to erode the 'European' model of corporate governance have already become part of the everyday practice of European capitalism and, as the notion of path-dependence suggests, institutional changes are considerably more difficult to undo than they are to initiate in the first place (Pierson 1996). The route back to the past is almost always blocked by the development of new political coalitions with a vested interest in preserving existing institutional arrangements.

In terms of the present discussion, this means that governments currently deciding whether to extend their opt-out from the single currency are not choosing between whether to experience all or none of the impacts of EMU. The formal decision only extends to whether to become a full participant in the macro-economics of monetary union. The microeconomics of monetary union will tend to be experienced irrespective of that decision, because the institutional changes which have created new market-based incentives for firms to reject the traditional 'European' model of corporate governance are already firmly entrenched.

If, as I have suggested in this chapter, it is the microeconomics of EMU that pose the most pronounced threat to the model of corporate governance that under-pinned post-war patterns of social protection within Europe, then the 'European

Social Model' may well be trapped between a rock and a hard place. Whatever the final impact of the euro, welfare-corrosive effects rooted in the microeconomics of EMU are likely to be a persistent feature of the broader European context. In terms of political outcomes, then, the debate currently dominating British politics about the desirability of euro membership may be less significant than the prior debate concerning the institutional arrangements within which the euro would be embedded. On account of its relative silence in that debate, the British left may have contributed to the experience of the social costs of monetary union, irrespective of its final decision of whether to support full participation in the euro. If there is one last irony to be observed in this situation, it is surely that the form of corporate governance to which Europe would seem to be headed is pretty close to that which Britain already has. As such, the microeconomic impact of EMU is likely to have less effect on Britain than elsewhere.

Note

1 Along with his Birmingham colleagues, Colin Hay, Jonathan Hopkin, David Marsh and Daniel Wincott, Matthew Watson holds an ESRC award under the 'One Europe or Several?' programme, entitled 'Globalisation, European integration and the future of the European Social Model' (award number: L213252043). I would like to thank the ESRC for its continued contribution to the funding of my research, and to these colleagues for their helpful suggestions on an earlier draft of this chapter.

Part III

Sovereignty and political determination

17 How the euro threatens the well-being of the planet and its people

Molly Scott Cato

> The decision to join the euro is essentially a political one. The economic consequences are likely to be very negative. If you want the EU to be a superpower, it's essential. If not, then stay out.
>
> (Richard Douthwaite (Green economist))

Introduction – hope to create a green oasis of sanity

The green perspective on the euro shares some common threads with the critique of other radical and left-leaning groups. However, it has certain distinct features. Greens have always been foremost critics of globalisation, arguing instead for an agenda of localisation: local self-reliance and trade subsidiarity (see Hines 2000; Cato 2003). Along with other critics we identify the provenance of the euro with the corporate globalisers, primarily the European Roundtable of Industrialists (ERT). Greens call for a reversal of the process of globalisation for the benefit of people and the planet; for greens, trade has few economic advantages to balance the major environmental costs and global injustice it generates.

The Green Party has been able to lend more balance to the No Campaign against the euro since joining the coalition in 2001. The anti-euro position has been seen as both business dominated and xenophobic, and the green involvement has been able to counter both these unhelpful stereotypes. The No Campaign does have considerable involvement from the business sector, but it tends to be more from the SME sector compared with the corporate domination of the Yes Campaign. The international basis of the green movement, with parties in most countries of the world, also gives the lie to the equation of opposition to the euro with a Little Englander position. The fact that many of the European green parties support the euro, particularly the most politically powerful party in Germany, does not undermine the international image of the green movement.

In the remaining sections of this chapter I explore the source of green concerns about the euro. First, I identify its origin in the corporate world and its close link to the process of globalisation. Second, I explore the constraints of a single currency and the reasons why greens favour a world with more currency diversity. Next, I widen the debate to consider the negative impact of the euro on the south and on

the planet as a whole. Finally, I give a green angle on the criticism of the public spending limits inherent in the Stability and Growth Pact.

Champagne supernova: who wants the single currency?

It is now accepted that the proposal for a single currency for Europe originated with the European Roundtable of Industrialists, a self-selected group of 45 chiefs of European multinationals who have been setting the European agenda for the past 20 years. Table 17.1 shows how for a number of issues the ERT internal agenda became over time the EU agenda. It is no coincidence that the decisions taken by our politicians, avowedly for our benefit, were already on the wish-list of this powerful group of businessmen. The ERT is proud of this level of influence and lists these EU developments as 'achievements' on its self-congratulatory website.

The advantages stemming from euro membership are advantages for multinational corporations. Businesses trading within the United Kingdom – and the majority of employment in the United Kingdom (52.7 per cent of the workforce: Government Small Business Service) is found in businesses with fewer than 500 employees – will see few advantages. For citizens, the best that we are offered is that travel to European countries for holidays will be more convenient. But for the corporations that dominate the globalised economy there will be major advantages. They will see reductions in their menu costs (the costs of exchanging across currency boundaries, and the costs of setting prices in different currency areas as exchange rates change). It will be easier for them to move from country to country at the slightest dip in environmental protection or labour costs. They can also use the interest rate restrictions of the Stability and Growth Pact to reduce employment conditions and wages – exactly the process that is causing the demonstrations, strikes and civil unrest in France and Germany, as explored below. The

Table 17.1 ERT sets the agenda for the EU

Issue	*ERT interest*	*ERT date*	*EU summit discusses*
Single market	'Pressure to complete the single market'	1985	Maastricht Treaty, 1992
Central and eastern Europe	'Europe without borders'; 'management seminars' in Hungary, Poland, Czechoslovakia	1991	Essen Summit, 1995
Single currency	ERT lobbied Madrid summit for single currency and 'named the currency'	1995	Arrangements completed by Luxembourg summit, 1997
Enlargement	'Work started on the enlargement'	1997	Nice Summit, 2000

Sources: Websites of EU Commission (europa.eu.int/comm) and European Roundtable of Industrialists (ert.be); Balanyá *et al.* 2000; Artis and Nixson 2001.

demonstrators identify the threats to their security from 'flexibility', but few have identified the source of that threat as the euro.

European politicians seem to suffer no embarrassment in discussing how the single currency has resulted from corporate pressure. In a 1999 working paper discussing the use of the euro as a parallel currency the authors state that:

> For its part, the corporate sector had started lobbying in favour of unrestricted access to the euro during the transitional period. Its motives for doing so were obvious. Many European-based corporations with production and servicing units scattered in a number of Member States had an interest in stopping the use of the various national sub-units of the euro, and adopting the euro unit itself as their 'base' currency for the whole of their operations: pricing, invoicing, payments, accounting, salaries, tax reporting and payments, and so on. The rewards would be greater transparency and efficiency, time and cost savings.
>
> (European Parliament 1999)

The document continues by pointing out the problems facing the corporations in meeting their need to trade in the same currency throughout the European Union. But they have no need to worry because:

> The national authorities willingly obliged and proceeded – some to a greater extent than others – with the appropriate changes. Consequently, on 1 January 1999, the existing national laws and regulations, instead of imposing the continued and exclusive use of the national currency units, offered the choice between this unit and the euro unit in a wide range of uses.
>
> (European Parliament 1999)

The rest, as they say, is history. It appears that in the field of currency, as in much else, business gets what business wants.

Given the source of the proposal for a single European currency and the destination of any possible benefits, there is no surprise that the public pressure for the United Kingdom to enter the euro comes from exactly this quarter. We have heard a string of corporate executives making dire warnings about the consequences for Britain of remaining outside Euroland. One of the most voluble supporters of the Britain's entry into the euro is Will Hutton, chief executive of the Industrial Society. The chairpersons of two major British corporations – British Telecom and British Airways – are members of the governing council of the Society. Toyota, which has a car assembly plant employing 300 people on Deeside in North Wales, is a foremost example. It has long pressured for the United Kingdom's entry into the eurozone and even went so far as to pre-empt the democratic decision by requesting its UK suppliers to do their business with the company in euros rather than pounds in August 2000. However, in January 2001, as the rest of Europe abandoned its currencies in favour of the euro, Toyota actually increased its investment in Wales and elsewhere in the United Kingdom (information from BBC website).

Corporate pressure for the United Kingdom to join the eurozone is frequently couched in threats to further investment if we were to remain outside. These arguments are disingenuous, since the real reason for the falls in inward investment are the contraction of the global economy and the poor trading conditions in the eurozone, partly as a result of the euro itself. They are undermined by the fact that inward investment is also falling in France where, according to the government inward investment agency, the number of jobs created by inward investment fell by 10 per cent in 2002 compared with 2001. The number of projects fell from 558 to 438. A report by management consultancy Arthur D. Little in 2003 showed that companies are leaving Germany because of the failure of economic growth and the tax regime. They favour two non-eurozone countries: Switzerland and the United Kingdom, with 18 per cent choosing to relocate in the latter. The real reason for corporate lobbying in favour of the single currency has more to do with the downward pressure the single currency exerts on wages and employment conditions, as well as the tight monetary controls it entails, creating a climate of so-called 'flexibility' that is ideal for maximising profits.

Evidence of the close link between globalisation and the euro was to be found in the Chancellor's pronouncement in June 2003 that Britain was not yet ready to join the single currency, which was softened for euro enthusiasts by his up-beat assessment of its potential impact on UK trade (Treasury 2003). Yet the claims about the extent of trade increases were evidence of the vacuity of the econometric models and the paucity of Treasury thinking rather than any proof of a boon from entry into Euroland. The headline figure was an increase in UK trade of between 5 and 50 per cent, for which the woman on the Clapham omnibus might more frankly use the phrase 'I don't have a clue'. Proponents of the euro have pounced on the 50 per cent upper limit as if it were unadulterated good news. But the document informs us that this includes imports and exports, which are likely to be balanced even on an optimistic view, thus underlining that the only definite increase in economic activity will be in the very sectors that are most environmentally damaging, especially transport. The assessment also makes no mention of who are likely competitors within the European Union will be, and ignores the fact that those included when the Union enlarges to 25 members have much lower wage levels than the United Kingdom. Even if such a trade increase were to generate increased cash flow, the distribution of this money is not discussed. In reality the gains are likely to accumulate with the corporations, while the costs, especially the environmental costs, are likely to be borne by the poor here and in developing countries and by the planet (see Cato and Dawe 2003).

Why single currency, not common currency?

There is a glaring anomaly in the public debate about entry into the euro: the arguments are always cited in terms of a 'single currency', whereas all the advantages that are touted could equally be achieved by a common currency. This anomaly looks rather different from the perspective of green economics, which has always argued for diversity in currencies as much else. It is unsurprising, therefore,

that several green commentators on the euro have independently arrived at a position of welcoming the euro but denying the need to face the strictures of having it as a single currency (Cato 2000; Robertson 2002; Boyle 2002).

Robertson (2002) identifies all the usual risks associated with a single currency, such as loss of political control and the inappropriate interest rate. He concludes that we should use the euro alongside the pound and while developing a range of local currencies:

> The role of alternative currencies at the local level, co-existing with the euro in the Eurozone and with national currencies elsewhere, is growing. This points towards the future evolution of a multi-level system of parallel currencies – in tune with the increasingly supra-national and increasingly devolved features of 21st-century society. In addition to its immediate benefits, experience of using the euro as a parallel currency alongside the pound will help to keep the UK at the forefront of monetary advance.

Boyle (2002) identified the inappropriate interest rate as likely to lead to an increasing gap between rich and poor in the eurozone, as it has done in the regions of the United Kingdom. He shares Robertson's conclusion that more diversity of currencies is the sustainable and just response. In his alternative Mansion House speech on behalf of the New Economics Foundation in June 2002, Boyle predicted that there would be 2,000 complementary currencies in the United Kingdom in the next decade, and up to 10,000 in Europe.

There are developments towards creating alternative currencies within the eurozone, especially in Germany (see Kennedy 2003; some of the currencies that are already functioning can be seen at the Moneta website www.monneta.org or at www.appropriate-economics.org). In the United Kingdom, developments such as the Institute for Community Currencies, which is setting up time-based local trading systems in the depressed economy of the valleys of south Wales, is a grassroots response to the failure of the pound to provide sufficient liquidity for a thriving economy. Money is drawn out of the local economy to gain more interest elsewhere, a problem that will only be exacerbated for peripheral economies of the United Kingdom once they are part of the larger eurozone economy (for an explanation of this process, see Ward and Lewis 2002).

For those developing these currencies they have two main functions: dealing with the low level of liquidity in depressed local economies; and creating a geographically limited currency that is protected against global speculation and offers security against the possibility of a collapse in the global financial market. This latter experience is illuminated by the experience of Argentina, which, following the collapse in the value of its currency in 2001, froze citizens' bank accounts to prevent them translating money to safer financial havens overseas. This had a disastrous effect on liquidity in the economy, making economic exchanges impossible. In response the people developed a system of barter clubs, while the local authorities in the different provinces created local currencies to allow them to pay their employees and facilitate economic activity (see Pearson

Figure 17.1 Example of token from an Argentinian barter club.

2003; *Ambito nacional* 2002). The response to a decade-long recession in Japan has been much the same, with work-exchange schemes and local currencies allowing life to thrive outside the damaging global financial system.

What will be the impact on the poor world?

From the view of the corporations, a view shared by our Chancellor, the euro will support globalisation and an increase in international trade, which, it is implied as though it needs no explicit argumentation, will benefit us all. This is dealing with the forecast trade increase in conventional terms. From a green economics perspective, an increase in the volume of trade is not an answer to our problems; quite the reverse it will exacerbate the problems generated by globalisation both for the poor of the world and for the planet itself.

Trade has done little for the poor world. An UNCTAD report in 1997 showed that out of a sample of ten Latin American countries, in nine of them the differential in earnings between skilled and unskilled workers had increased as a result of opening up markets to international trade, and that in most of the countries the real purchasing power of the least skilled workers had actually declined, in several cases by more than 20 per cent. In 1999 a paper from the World Bank reported on data for a sample of 38 countries between 1965 and 1992 to show that opening markets up to trade had reduced the incomes of the poorest 40 per cent of the population while increasing those of the richer groups. Developing countries have spent these 30 years on the economic roller coaster of international trade, because of the dogma from international bodies suggesting that this will end poverty, while at the same time the richest people in these societies have used this international game to increase their own wealth while the poor in the same societies have grown poorer.[1] The overall gains from trade are minimal to the countries producing agricultural products: between 1986 and 1996 Ghana increased its exports of cocoa by nearly 80 per cent but only earned 2 per cent more in return.[2]

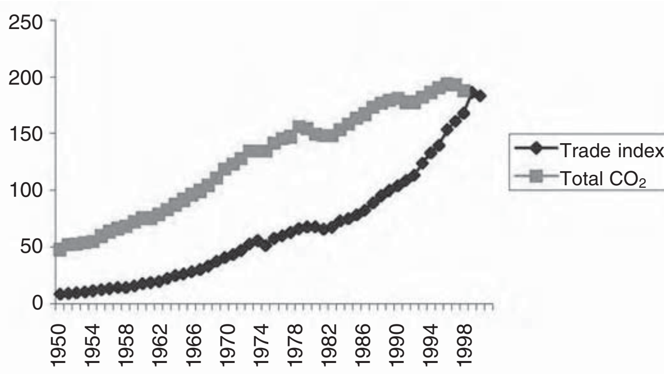

Figure 17.2 Relationship between increase in world trade and global carbon dioxide emission.

Sources: Carbon dioxide data from Oakridge Research Laboratory, California; trade data are from the World Trade Organisation.

Note: The trade figures are calculated as an index based on 1990 = 100 and including agricultural and mining products and manufactures. The CO_2 emissions are for solid, liquid and gas fossil fuels divided by 33 to achieve appropriate scaling.

A report from the New Economics Foundation in 2000 made clear the costs of trade to both the poor world and the planet. OECD data show that carbon dioxide emissions from Indonesia, Malaysia, the Republic of Korea and Thailand while they were positively regarded as Asian Tigers because of their rapid development increased by between 100 and 278 per cent (Simms 2000). Figure 17.2 shows how the increase in total global trade is matched by the increase in carbon dioxide emission.

In the context of our national or continental interest we should also consider the distortionary effects of having national economies based on the world's dominant currency. This has increasingly been the situation for the USA since the Second World War and has been at best a mixed blessing. The use of the dollar for world trade has led to the creation of huge amounts of US dollars, for which the US gains seigniorage. In return it is able to import a practically infinite quantity of foreign goods, enabling the lavish lifestyle of its citizens. The immediate impact of this in terms of obesity and related overconsumption is clear, not to mention the USA's excessive impact on global climate change emissions (around 25 per cent of CO_2 for its 4 per cent of global population). From the economic point of view, living with a huge trade deficit and national debt is fine as long as it lasts. But what about if the bubble bursts?

Being the progenitor of the world's trading currency has certainly offered the United States advantages in the arena of military power, too. Richard Douthwaite argues that the USA's influence in the Far East is, in a broad sense, an exchange of military might for consumer goods. Not only does the possibility of running a huge

deficit enable the purchase of military hardware, leading to the situation where the USA spent as much on arms last year as the next 20 economies combined. It also allows the United States to pull Japan and the East Asian economies into its orbit (China is a rather different case), trading military security for goods that it can never actually pay for.[3] Those who are unconvinced by this case should ask themselves why it is that Argentina with vast natural resources, an area of 1 million square miles and a skilled workforce can be considered bankrupt when carrying only $128bn worth of debt (Palast 2001), while the United States can maintain an external debt of $6 trillion apparently effortlessly, approximately 47 times the size of that of Argentina (figures from US Treasury). Table 17.2 gives figures for external debts and GDP for several of the world's 'problem' economies compared with those of the USA. The trade system as currently structured under dollar domination has increased debts for all developing countries, as illustrated in Figure 17.3.

European bankers looking enviously across the pond have seen the geopolitical strategic advantage of being the world's banker. The USA's increasing unpopularity as its imperialist adventures in the Middle East proceed apace has led several countries to switch from the dollar to the euro for their foreign trade exchanges and their national currency reserves. By the end of last year the share of Russia's foreign exchange reserves consisting of euros had expanded from 10 to 20 per cent, while the dollar share had fallen to below 75 per cent (Fairlamb 2003). Cuba has switched to the euro for international trade, while OPEC is discussing the possibility of denominating world oil prices in dollars.[4] The powerful and growing economies of Russia and China are also working their way around US currency domination: from this year they will be settling their external accounts in rubles and yuan.[5] This role of the euro in a hegemonic power struggle between the two main western trade blocs should not be ignored. It not only threatens certain environmental destruction but probable conflict too.

In apparent ignorance of these threats, the move to develop the euro is supported by some radical commentators, including George Monbiot and Susan George. They see de-dollarisation as an opportunity to push the USA over the brink. This is a short-sighted and highly risky reason for supporting the euro. First, it is based solely on political considerations, ignoring the negative effects of a strong currency on domestic economies and the single interest rate straitjacket. Second,

Table 17.2 Comparison of size of external debt and size of GDP for a range of countries

Country	*GDP ($bn. PPP)*	*External debt ($bn.)*	*Debt/GDP ratio*
Argentina	$476	$154	0.32
Russia	$1,120	$163	0.15
South Korea	$764.6	$764.6	0.18
USA	$1,360	$9,963	0.60

Source: The data are taken from the CIA datafile, apart from the size of the US external debt, which the CIA rather coyly only reports the 1995 figure. The figure used is from the US Treasury website.

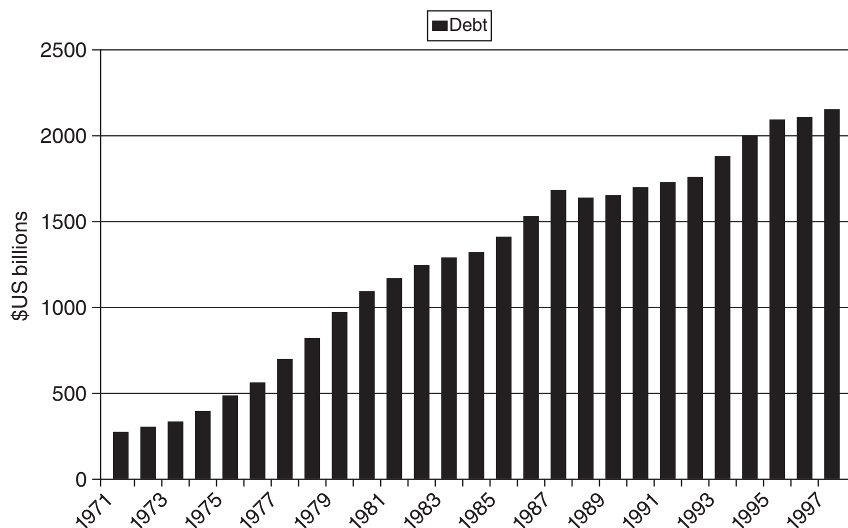

Figure 17.3 External debt of developing countries (1971–97).

Source: Benjamin Holt, Global Policy Forum, New York.

it fails to take account of the almost universally negative consequences of catastrophic economic collapse. Counter-examples are welcome, but within my knowledge base it seems clear that economic disaster is always more likely to result in right-wing authoritarian government than the radical political leaders these commentators would favour.

Pressure on the welfare state in the eurozone

The countries within the eurozone have suffered disastrous consequences since abandoning their domestic currencies. This is the result of two factors: the inflexibility resulting from the imposition of inappropriate interest rates (discussed elsewhere in this book) and the use of that policy to reduce labour standards and public expenditure. The citizens of continental Europe have withstood the ideological pressure towards 'flexibility'; they are now being subject to economic pressure via the euro. The European Social Model is even now being defended by street demonstrations.

Economists could have predicted just these sorts of problems from a single interest rate for 12 diverse economies and many, including most prominently Nobel Prizewinner Joseph Stiglitz, did just that. Exactly these types of problems arose during the period when the pound was pegged to the mark, resulting in Black Wednesday; and in more extreme form during Argentina's financial collapse in 2000. According to Larry Elliott writing in the *Guardian*:

> Argentina in 2001 was like Britain in 1992, when the John Major administration insisted that the pound would remain pegged to the German mark even as unemployment edged towards three million and record numbers of people lost their homes and businesses.

It is the memory of these devastating times that has propelled many small businessmen in Britain to oppose entry into the euro; they cannot forget the experience of laying off good workers because of bad economics.

France, and most strikingly Germany, are in deep recession but the strict rules of the Stability and Growth Pact, administered by bankers rather than politicians, prevents them from taking action. The dangers inherent in this have been identified by Stiglitz:

> There does need to be a commitment to fiscal responsibility. In the long run, governments should run balanced budgets, with surpluses in good years making up for deficits in bad years. But to insist on an arbitrary budgetary position in an economic downturn is to ignore everything we have learned about economics in the past 70 years, risking the well-being of millions who are thrown out of employment.
>
> (Stiglitz 2003)

Whether the determination to stick to inappropriate monetary targets results from bureaucratic lack of imagination or the corporate desire to undermine the social model, it is risking a deep and lengthy recession in Europe's largest economy. Dieter Hundt, head of the German Employer's Federation has said that Germany is in a 'massive recession' (in *Frankfurter Algemeine Zeitung*), with 2003 being the third year with growth barely above zero. In a typical response, Wim Duisenberg, President of the ECB, called for economic reforms in the eurozone in order to spur growth, while maintaining that monetary policy could not help the situation (according to Reuters).

The human costs of policy fossilisation are seen in the huge rise in German unemployment. In May 2003 the German Federal Bureau of Labour admitted that unemployment in Germany might reach 5 million by the winter from its current level of 4.4 million, breaking the previous pre-unification record of 4.8 million. The report, published in *Die Welt* on 30 May, found there were 475,000 more unemployed people than in the same month in 2002.

While the battle between economists, bankers and politicians continues Europe's citizens are suffering hardship and losing rights to employment conditions and social security that they had felt were secure. This is resulting in high levels of strikes and civil unrest. The economic 'reforms' that Schroeder is desperately trying to implement to slim the economy sufficiently to fit into the interest rate straightjacket include relaxing redundancy laws and reducing the length of eligibility for unemployment benefit. *Figaro* reported a demonstration of 10,000 people against these proposals in Berlin in late May. Those who live in the

eurozone must regret the decision by their politicians to give away their power in economic decision making.

Conclusion

For those of us who have worked to oppose the onward march of globalisation, opposition to the euro comes easily. The development of the single European currency fits so neatly into the pattern alongside the North America Free Trade Agreement (NAFTA), which the globalisers won, and the Multilateral Agreement on Investment (MAI), which they lost, that we can easily identify its provenance, its purpose and the need to oppose it. For those who do not share this perspective the whole debate can appear somewhat unreal, since there are very few obvious advantages to joining the system. From the viewpoint of conventional economics, Britain is functioning well with a flexible interest rate regime and ultimate political control over its own economy. Whatever the strength of arguments against the euro coming from the anti-globalisation and green movements, it is the combination of British scepticism and xenophobia that will ensure Tony Blair will never win his referendum.

Notes

1 UNCTAD report on trade (1997), Part Two, chap. IV, sect. B.1; World Bank report: M. Lundberg and L. Squire, 'The simultaneous evolution of growth and inequality', December 1999. Grateful thanks to Richard Douthwaite for both these references.

2 Data from an unpublished report by Nick Robins called 'Taming world trade', cited by Simms, 2000.

3 See R. Douthwaite, 'Defense and the Dollar'. He cites Professor Thomas Barnett of the US Naval War College, as follows:

> We trade little pieces of paper (our currency, in the form of a trade deficit) for Asia's amazing array of products and services. We are smart enough to know this is a patently unfair deal unless we offer something of great value along with those little pieces of paper. That product is a strong US Pacific Fleet, which squares the transaction nicely.

See: 'Asia: The Military-Market Link', The US Naval Institute, January 2002, pp. 53–6; http://www.nwc.navy.mil/newrulesets/AsiaThe Military-MarketLink.htm

4 Saudi Arabia's Prince Muhammad Bin-Turki Bin-Abdallah Bin-Abd-al-Rahman suggested this as a protest against US and Israeli actions in the Middle East according to an article 'Protest by switching oil trade from dollar to euro' published in *Oil and Gas International* (15 April 2002).

5 'Goodbye dollar! Goodbye euro!?', *Pravda*, August 2002. See: http://english.pravda.ru/world/2002/08/22/35049.html

18 EMU and British sovereignty

Brian Burkitt

Introduction

The UK economy is insufficiently integrated with, and too structurally different from, the EMU12 countries to benefit from participation. The United Kingdom suffered heavy losses of jobs and production due to its following an inappropriate monetary policy during membership of the Exchange Rate Mechanism (ERM). All the evidence indicates that a single currency would generate similar consequences, except that having lost an independent pound sterling, there would be no escape. The conclusion is unequivocal; Britain should not join EMU, which is prejudicial to its economic interests. However, the issues raised by the single currency are not simply economic; participation would pose problems for the operation of British democratic self-government. A loss of national independence and a weakening of democracy are profound threats arising from the essential character of EMU.

An analysis of these threats must start with Gordon Brown's statement to the House of Commons on 27 October 1997. Its key passage was:

> It must be clearly recognised that to share a common monetary policy with other states does represent a major pooling of economic sovereignty. There are those who argue that this should be a constitutional bar to participation in a single currency, regardless of the economic benefits it could bring to the people of this country. That is an understandable objection and one argued from principle. But in our view it is wrong. If a single currency would be good for British jobs, business and future prosperity, it is right, in principle, to join. The constitutional issue is a factor in the decision, but is not an overriding one.

That statement was unclear; did it mean that the end of the pound sterling will exert no serious impact upon British self-government or did it mean that the impact would be serious but that the British government is willing to tolerate its effects? As early as February 1970, Enoch Powell, in a speech to the House of Commons, defined the crucial question as 'the issue we are deciding is whether we can and will enter a political unit that deals with major matters of political life affecting the daily lives of people in this country'.

Gordon Brown dismissed this issue without even saying what it was. It is incredible that the permanent and irrevocable loss of self-governance could be treated with such disregard. The principle at stake, which Brown failed to address, is nothing less than the loss of national, democratic self-determination. The question is whether Britain still desires to be a sovereign nation or whether it is driven by its fears of the spurious dangers, fuelled by EU-financed propaganda, of staying out of EMU.

If EMU operates for more than a short period of time, a single currency will be created without a government accountable to an electorate operating it. In the absence of a responsive democratic institution, the workings of the ECB and the committee of finance ministers will, particularly in times of economic stress, be dangerously alien from the public. In such a gap, indifference at best, and extremism at worst, thrives. Any response that strengthened the European Parliament would mean an inevitable growth in its scope and ambitions. Therefore, in joining a single currency, Britain would be participating in a political process for which monetary union was a staging post, i.e. an EMU that survives for more than a few years will underpin a developing European state.

The federalists are trying to build a United States of Europe from the top down. Institutions to manage monetary union have now been constructed, and political institutions to manage these monetary union institutions will follow. Such a process of building a federal union is the opposite of how every other nation has been created. It will be disastrous, because it will deploy exchange and interest rates as weapons of nation building. EMU converts economic into political institutions to build an ever-more integrated European Union, thus distorting their real purpose and function. Moreover, the operation of EMU will lead to calls for further harmonisation of laws and customs, culminating in a single fiscal policy, which will diminish still more Britain's ability to take fundamental decisions in its own interests.

Hence, EMU is not simply, nor even mainly, an economic project. It constitutes a major step towards political integration, transferring power from accountable national institutions to bureaucratic, unelected EU-wide institutions.

Democracy

The parliamentary democracy developed and established in Britain is based upon the sovereignty of the people, who by exercising their vote lend their sovereign powers to MPs, to use on their behalf for the duration of a single parliament; these powers are returned intact to the electorate to whom they belong, to return again to the MPs they elect at each subsequent General Election. Five basic democratic rights emerge from this process, each of which is fundamentally diminished by British membership of the European Union.

First, parliamentary democracy means that every person over 18 is entitled to vote to elect his or her MP to serve in the House of Commons. The consent of the House of Commons is necessary before Parliament can pass any Act laying down new laws or imposing new taxation upon the people. British membership of the

European Union subjects all its citizens to laws and taxes, which their MPs do not enact. Such laws and taxes are implemented by EU institutions that they do not directly elect, and cannot dismiss, through the ballot box.

Second, parliamentary democracy means that MPs, who derive their power directly from the British people, can change any law and any tax by majority vote. British membership of the European Union prevents EU laws and taxes from being changed or repealed by the British Parliament. They can only be altered or abolished by EU bodies not directly elected by the British people.

Third, parliamentary democracy requires that British courts and judges must uphold all laws passed by Parliament. If Parliament changes any law, the courts must enforce the new law because it has been passed by Parliament, which is directly elected by the people. British membership of the European Union forces British courts to uphold and enforce EU laws, which have not been passed by Parliament. Nor can Parliament amend or repeal them, even when they conflict with laws passed by Parliament, since EU law overrides British law.

Fourth, parliamentary democracy means that all British governments, ministers and civil servants under their control can only act within the Laws of Britain. They are accountable to Parliament for all their public actions and, through Parliament, to the electorate as a whole. British membership of the European Union imposes duties and constraints upon British governments not deriving from the British Parliament. Therefore, in discharging these duties, ministers are not accountable to Parliament or to the British citizens who elect them.

Finally, parliamentary democracy is vital because it entrenches the right of the people to elect and dismiss MPs, secures their continuing accountability to the electorate, obliging them to listen to the views of British citizens between as well as during General Elections. It thus offers the possibility of peaceful change through Parliament to meet the voters' needs. British membership of the European Union, by permanently transferring financial and legislative powers to EU institutions not directly elected by the British people, insulates those institutions from the control of British voters. who cannot dismiss them and whose opinions, therefore, need carry no weight with them and whose grievances they cannot be compelled to remedy.

These five rights have protected British citizens from the worst abuses of power by the state, safeguarded them against the excesses of bureaucracy, defended their basic liberties, offered them an opportunity for peaceful change, reduced the risk of civil strife and created a national framework of consent for the law-making process. However, the powers of the British electorate, through their direct representatives in Parliament, to levy taxes, to make laws which the courts must uphold and to control the conduct of public affairs have been substantially ceded to the European Union, whose Commission and Council of Ministers are neither collectively elected nor collectively dismissed by the British people, or by the peoples of the EU countries put together.

Hence, the European Union, through the fundamental character of its institutions and their behaviour, severely curtails the operation of British parliamentary democracy. This process, undermining the rights of the British people, will be accelerated by participation in EMU.

Sovereignty

Such a major change in the operation of the UK constitution carries profound implications for the exercise of national sovereignty. The concept of 'sovereignty' has been much disputed in recent debates, particularly with respect to the relationship between Britain and the European Union. Therefore it is appropriate to analyse its essentials in detail.

Malcolm (1996) defined sovereignty as constitutional independence, i.e. the exercise of plenary and exclusive political authority in a legal order. A sovereign state possesses independent authority, e.g. a small country may be dwarfed by a powerful nation, but so long as it is not legally subordinate to that neighbour, it remains sovereign. Sovereignty rests upon authority rather than power; in a famous opinion on the Austria-German customs union in 1931 Judge Anzilotti declared, 'sovereignty means that the state has over it no other authority than that of international law'. An independent state must possess full competence to act internationally; it acts under its own authority not requiring authorisation from any superior state. If a state is constitutionally independent, it is sovereign; if it is not, it is not. There are no intermediate stages of sovereignty.

The idea of Gordon Brown's that sovereignty (constitutional independence) can be 'pooled' is an evident absurdity. Power can be pooled, but authority cannot. 'Pooling' is a dangerous concept, because it falsely implies that authority can both be retained and given away simultaneously. If the sovereign authority of the United Kingdom is pooled within the European Union, that sovereign authority will cease to exist, because British laws would become subject to a higher authority. So far this has not happened; to date, the United Kingdom has delegated a part of its sovereign authority to some EU bodies on which it is represented. It has also delegated the exercise of important elements of administrative, jurisdictional and legislative authority by treaties and by statutes. The latter were expressions of the UK's authority. The United Kingdom remains sovereign so long as it retains the ability to renounce the treaties and repeal the statutes.

However, the character of delegations to the European Union is different from that involved in any previous treaty signed by Britain. The EU Council of Ministers is a law-creating body, whose laws possess 'direct effect' in Britain, overriding British laws. With uniformity the whole procedure can (in theory) be accommodated within the UK's exercise of its own authority. Majority voting, significantly advanced by the 1997 Amsterdam Treaty, destroys the illusion; whenever the United Kingdom is in a minority, it becomes obvious that is has given away the exercise of legislative authority to a body it cannot control. Article 100 of the Single European Act allows majority voting on measures 'which have as their object the establishment and functioning of the internal market'. If the clause focused solely upon establishment, majority voting would be designed only for achieving a single task. Unfortunately, the inclusion of 'and functioning' ensures that a potentially large sphere of legislative authority has been delegated in a totally open-ended way.

If most (or crucial) areas of jurisdictional and legislative authority become subject to long-term delegation, a situation will arise where the United Kingdom

would cease to resemble a sovereign state. Each time Britain delegates the exercise of its authority to the European Union it does not automatically lose sovereignty, but becomes more likely to do so. Therefore, it comes closer to the moment when its constitution will be remodelled into a subordinate part of a federal European Union. EMU constitutes a major step down this route.

In a federal European Union, sovereignty is not abolished; it transfers to the new EU constitution. If such a federal framework is to be constructed, it requires the underpinning of political authority. It must be at least possible to make citizens think that the federal authority is entitled to rule them; if enough citizens do think so, it will be. To achieve the objective, representative politics on an EU-wide scale is required, i.e. European parties functioning as a single entity across the European Union as the Democratic and Republican parties do in the USA. Such a system operates effectively in an established political democracy, where people share the same customs, language and traditions. Could this kind of politics operate in the European Union? Without a genuine political community, any European constitution will remain an artificial construction. Its political role will not derive from any sense of participation, but from wishful thinking and indifference. Of course, over time people may come to feel part of a genuine EU-wide political community. It could happen, but it would take many generations and involve substantial changes to many aspects of our lives. Therefore, UK membership of EMU (and ultimately of the European Union itself) depends upon whether the British people will accept heartily and willingly the voice of the people of the whole European Union as binding upon them, at first in some, then in more and ultimately in all matters of economic, political and social determination. Closer EU integration cannot be effective in the long-run without creating one electorate, one constituency and one federal EU-wide nation. All supporters of such integration need to answer why such an enormously artificial, disruptive and risky project should be embarked on.

It is frequently claimed that national sovereignty is undermined by globalisation. To a large extent the claim is based upon a confusion between sovereignty (resting on a constitutional independence) and power. However, even within its own terms of reference, the claim is grossly exaggerated. Since 1945 increasingly freer trade, the emergence of transnational corporations and the hugely expanded volume of international capital movements have made the task of national economic management in reconciling full employment, stable prices and rapid growth harder to achieve. These difficulties created political problems, as electorates became frustrated with governments of all persuasions failing to meet their demands. Nevertheless, it remains hard to understand why these developments suggest the need for a closer association between the United Kingdom and other members of the European Union specifically; rather they pose the imperative for worldwide cooperation. The inability of both national governments and regional blocs to control currency realignments led to the G7 meetings (and if Britain devoted the ministerial and civil service time to the G7 that it spends upon the European Union, both it and the world would be more prosperous). It was the G7 rather than the European Union that became the focal point of decision making during the 1998 global financial crises. The European Union has proved similarly ineffectual

in the sphere of environmental protection. Only an international forum can generate effective ecological policy responses. Therefore, those problems that cannot be completely solved at national level require a broader policy implementation framework than the European Union provides.

Moreover, acceptance of the limitations of national strategy often obscures the numerous spheres where the European Union remains effective. Voluntary abandonment of its authority in these spheres is detrimental to the exercise of democratic citizenship rights and to living standards. Those who believe that national economic sovereignty is valueless in the modern world need to explain recent British experience. In the months before September 1992 the requirement to maintain interest rates at the level needed to defend sterling's ERM parity resulted in unemployment rising to three million simultaneously with record levels of bankruptcies and home repossessions. The months afterwards, with four percentage point cuts in base rates and when the pound was devalued by 15 per cent, saw immediate economic recovery. By contrast, France's determination to achieve exchange rate stability with the Deutschmark created stagnation, with unemployment rising to 12 per cent alongside an alarming increase in xenophobia. National economic sovereignty still exists in substantial measure; all that matters is the will to use it.

Thus the United Kingdom can still enjoy the advantage of sovereignty, i.e. constitutional independence, if it resists the embrace of continental integration. British strategy should concentrate upon developing fully national policy instruments, whilst cooperating on a global, rather than a regional, basis on issues beyond national control.

Conclusion

The Maastricht Treaty puts all the emphasis for achieving closer EU integration upon a deflationary single currency. The project was designed to unleash economic demands that would lead to political union. The economic–political imbalance is clear; if the Maastricht Treaty is implemented in full, the European Union will possess a single currency, whilst levying a proportionally smaller EU-wide budget than Boadicea did over pre-Roman Britain! Acceptance of such an absurdity prevents ruling parties from following an independent economic policy. It also creates scope for radical right movements, such as the National Front in France, the Republicans in Germany and the Fascists and the National League in Italy. Therefore it is essential that the United Kingdom retains its freedom of manoeuvre to develop discretionary policies. If artificial federalist rules frustrate this capacity, extremist movements will fill the unnecessary vacuum.

A United States of Europe would be economically disastrous and politically undesirable. It is a tragic error of historic proportions for the European Union to try to bond member countries into one ever-more closely integrated entity. Instead it should extend membership of a looser, free trade grouping to east European nations struggling through their democratic transition. Britain needs to uncouple itself from damaging integrationist trends and seize the tremendous opportunities

open to it as an internationally cooperative yet independent country in an interdependent world, which requires effective international and national policy responses (as opposed to regional ones). Such a major change in the direction of UK strategy, away from current drifting with EU tides, requires determination and far-sighted thinking. The prize, however, is great: no less than the survival of a Britain as a worldwide responsive partner yet also as an independent, economically prosperous, democratically self-governing nation.

Outside EMU, Britain can develop policies for wealth creation, employment generation and welfare improvement, freed from the EMU straitjacket of continent-wide deflation. It is evident that the United Kingdom's future self-interest lies in being outside this artificial, inflexible creation.

19 Euro versus the people

Austin Mitchell MP

Sovereignty, the firm base of the nation state, is the issue which dare not speak its name lying at the heart of Britain's tortured relationship with the European Union. Little discussed and regularly misinterpreted, sovereignty is crucial because the European Union's lurching drive to ever closer union is a struggle over sovereignty between members and a collective building its own, European, sovereignty. This is a zero sum game. The nation state's loss is Europe's gain. What the European Union decides the British people cannot.

The long internal struggle over sovereignty, first who reigns, then who governs, characterised the long rise of democracy. The answers have been the king, parliament, then the people. Now that struggle is between British democracy and Europe, and the point at issue is the degree of sovereignty to be surrendered. Europe grows stronger by taking away the power of peoples and parliaments to decide matters for themselves. That conflict is fought on many fronts, mostly minor, from pounds and ounces, the registration of fishing vessels, or a nation's right to veto, right up to the running of the economy. The euro is the biggest assault so far.

Lawyers distinguish between de facto and *de jure* sovereignty. Traditionalists elevate the argument to a mystical level claiming that EU directives are incompatible with the British constitution, with Magna Carta, the Bill of Rights or the power and responsibilities of the monarch. Euro-enthusiasts, equally mystical, argue that by being pooled sovereignty is magnified. Being a lawyer's term it is much used by the right who put sovereignty at the centre of arguments with the European Union while some on the left, who see the issue in economic terms, argue that it is a delusion in a world of globalisation, multinationals and huge flows of money which means nation states no longer have the power to manage their own destinies.

Such arguments are much used but untrue. Pooling sovereignty is irrelevant. We are minor contributors to EU decisions which bind us more powerfully than our own. We have only 13.9 per cent of the votes in Parliament and 18 per cent of the qualified majority votes on European Councils, which is 82 per cent less than in domestic decisions. Having a dominant influence in the European Union does give a nation power to advance objectives it can't achieve on its own, and the French have been particularly skilful to this end. Yet this isn't extending their sovereignty but exploiting everyone else's for their own purposes.

Globalisation may have gone further than when New York bankers dictated terms to the Labour government in 1931. It certainly means that Britain creates fewer waves in the world. Yet to assume that the fifth largest economy in the world has no control over its own destinies, its interest and exchange rates, or in the management of its own economy, is absurd. The contrast between our own failure to grow as fast as others, our wider social gaps and the poverty of our public sector compared to more advanced economies, as well as our higher inflation (in the past) and lower productivity are our fault, not the world's. A pathetic performance compared with Singapore or Hong Kong may be shaming but is neither inevitable nor the result of impotence before external forces. It merely shows that we have used sovereignty less skilfully.

Constitutional arguments about sovereignty are equally irrelevant. We don't have a constitution. Sovereignty rests with the Crown in Parliament and is indivisible and untransferable. Elements can be loaned but never abdicated, for Parliament cannot bind itself. What one has given, another can take back. In the last analysis the constitution is what governments can get away with. So ultimate power, aka sovereignty, lies with the people. They make the decisions on what government can and can't do. Rather than an abstract entity, sovereignty is living democracy: the people taking their own decisions for themselves. To lose it diminishes democracy.

Yet the decisions of the people, unless taken by referendum vote, are more opaque than a written constitution. Public opinion is malleable, influenced by such irrelevancies as how the economy is doing or are the people tired of the government. We live in an age of bamboozlement which the European Union has turned into a system of government. So judgments are imperfect, manipulable, even perverse, because they are not made by judges or courts, or in one simple, single decision, but by public opinion coming to conclusions slowly, and basing these conclusions on broad feelings not rational assessments. The 'win some, lose some' game which is euro negotiation allows few firm measuring points at which surrender of sovereignty is clear, unambiguous and can't be dodged. The euro is one. What is given up to it is the ability of participating nations to manage their own economies for the purposes of their own people.

Unusually, for Britain, this decision is to be taken by the vote of the people. The great majority, those not swayed by euro enthusiasm or euroscepticism, will find it difficult. Many feel they don't understand the issue, or don't have enough information to make their minds up. Some will be swayed not by the argument but by its presenters, as in 1975 when the hairy men: Tony Benn, Enoch Powell and Jack Jones fought the smooth and respectable such as Wilson and Heath. That will play its part next time. So will the media, who are now divided on the euro because they won't be fooled again after the ERM. Yet most will make their judgement as they do between parties at the election: on the basis of the sedimentated arguments, coupled with instincts about the impact on lives, expectations and well-being of the then state of the economy. The judgeent on whether sacrifices of sovereignty to Europe are acceptable or not, whether it is time to say 'thus far and no further', or even whether to take arms against a sea of troubles and, by opposing, make a

confused situation a bloody mess, will be made gradually, on the basis of 'What's Europe done for me?'

That judgment will be less favourable than those of other European electorates, for Britain's relationship with the European Union has always been more fractious. Original members benefited in the growth phase and have been more prepared to make greater sacrifices of sovereignty because they went in voluntarily, even enthusiastically, shaped the institution to suit their national purposes and got more out of it. The Benelux limpets wanted a rock, the French to be the jockey on the powerful German horse, the Italians to be governed from anywhere but Rome, and the newer recruits, lands of the waving palm, demanded and got a generous flow of the support and subsidy which assuages doubts and buys votes. When the Irish get 3 per cent of their GDP from Europe they are bound to feel a little different to the British who pay for it.

Britain joined not from any enthusiasm for integration but because its political class came to the conclusion that with the empire gone Britain needed a new stage to strut on. In the eyes of leaders whose skills were imperial not economic and who had proved incapable of delivering the same economic growth competitors enjoyed, and modern electorates expect, Britain had failed. Blame is a great national skill in a class-divided country. so, reluctant to blame themselves, the elite blamed the people (lazy), the unions (bolshy), management (incompetent) and the welfare state (spoiling). They wrote off the country and looked to Europe.

Their economic assessments demonstrated just how naive and economically illiterate the elite can be. Europe would offer the stimulating cold shower of competition, which their own public school background told them was the best discipline for naughty boys. It would hitch to the fast moving locomotive of European growth. Both images were as wrong as they were simple minded. Cold showers kill the ailing. Exposure to more powerful and better invested challengers destroys the unready. It was like urging a one-legged man to join a squash club because the showers would make him fit. When he fell over at the game and developed pneumonia his pleas for a reduced subscription were likely to be greeted with an invitation to 'hop off'. Yet the elite never bothered to think the economics through (even if they could have done so) because their real object was to transfer their own unique skills to the bigger European stage. There the natural leadership ability of a class born and trained to rule was certain to be gratefully received. Relegated to Lilliput because the country had proved unworthy of them, Britain's Gullivers wanted a bigger stage.

All this emerged from Harold Macmillan's post-1959 assessment of Britain's prospects. The feeling of national failure deepened when Harold Wilson's Labour government failed to deliver economic growth in one country. So EEC entry became an obsession for Ted Heath's Tories, who had no other major policy. Coming to power in 1970 Heath was ready to accept anything to get in, and much was forced on us by a Common Market Six determined to strengthen themselves at Britain's expense, to punish us for our American leanings and to force us to break our old Imperial relationships. A Common Fisheries Policy, the betrayal of trading partners, the Common Agricultural Policy with its high food prices, and a system of

contributions designed to make us pay over the odds were all swallowed at one grateful gulp.

We entered on unsuitable terms and spent three decades in the Sysyphean labour of trying to roll the stone back up the hill, always lagging in an institution which did not suit us in the way it benefited others. Europe didn't deliver on the promised economic gains which might have made the loss of sovereignty acceptable. Glowing prospects were followed by two decades of the worst economic performance since the Second World War with low, at times negative, growth, mass unemployment, the closure of traditional industries and the failure to develop any new national dynamic, despite being, alone in Europe, oil rich. Much of this was not Europe's fault given the oil shock and Tory monetarism. Yet Britain had taken on a heavy contributions burden, abandoned traditional markets and the advantages of trading our manufactures for cheap food in order to pay Europe's higher prices with a consequent increase in domestic costs.

Manufacturers found it harder to penetrate a large market from a small one. Much easier the other way because of the costs of distribution networks. European manufacturing had the investment, productivity, and economies of scale we lacked. We asked to be clobbered and duly were. Their exports to us grew faster after entry than before. Ours to them went the other way, leading to a gaping trade deficit which was a drain of jobs. As for hitching to growth, that stopped. The striving for monetary union forced France and Italy to deflate to keep their inflation rates down to the low levels Germany achieves through industrial might. This deflation was then prolonged by the monetarist requirements of Maastricht. The damage to Britain from the EEC was not ruinous. God had put oil in the North Sea to show he wasn't a Moslem, but membership meant its benefits were wasted, not used to rebuild for the future. The balance of payments boost went to pay for imports to destroy jobs, the tax benefits went to support unemployment and the investment flows were invested abroad.

This combination of high hopes, disastrous reality, produced a culture of euro lies and half-truths. Failure had to be portrayed as success, damage as benefit. The electorate had to be told that we were doing well in Europe despite the accumulating evidence of industrial failure, loss of our own market and an industrial base shrinking faster than anyone else's. The electorate made its own sullen assessment. Unemployment, industrial decline and economic growth had all got worse. Europe had done us no good. Polls showed a constant majority disliking membership after 1975. They didn't really want to withdraw: that prospect frightened a people losing confidence. But they certainly didn't like it.

Confusion is maximised. The people don't like Europe but no party gives any lead out, nor does any one offer a brave prospect, apart from Liberals believing in 'my Europe right or wrong'. Governments come in proclaiming their desire to work with Europe. They end up alienated and antagonised. Labour proclaimed a new beginning after its 1975 re-negotiation to end up semi-detached. Margaret Thatcher passed the Single European Act and finished with 'No, No, No'. John Major wanted Britain at the heart of Europe but ended up peripheral with a deeply divided party. Tony Blair's naive euro enthusiasm is already losing some of its glitter.

The issue pollutes politics. No British government can be fully enthusiastic or totally hostile. Our 'partners' are suspicious of us, and we of them, resulting in a constant diet of lectures on the need for us to be better Europeans, and constant 'If only' admonitions: if only Britain would learn to love its misery and maximise its surrenders all would be well – even if its government becomes unpopular with its people. So Britain is relegated to Europe's sulky periphery, dragged behind grumbling, claiming euro victories at home but really downgraded in the European Union, constantly saying one thing to European colleagues and another to its own people, and making maximum use of the European Union's Golden PR rule 'all must have victories' at Councils.

Much sovereignty has been conceded with few benefits in return. The people don't rise in protest but few are happy and an angry minority have kept alive the struggle to withdraw. In MORI polls the proportion feeling Britain should get out was 33 per cent in 1975, 71 per cent in 1980, 48 per cent in 1996 and 47 per cent in November 2000. In the early 1990s 55–60 per cent thought EU membership 'a good thing' in the EU euro-barometer polls. The latest figure is 25 per cent, while 44 per cent think the United Kingdom has not benefited from membership. This underlying alienation is a formula not for making the most of membership but for DIY deadlock. Britain can neither move forward nor backward. The euro must be seen in this context. To join it, government must make the European Union acceptable to an alienated electorate. That would require it to swallow a camel after a long diet of dung. All the problems of our messy relationship come together in the euro, the latest and greatest surrender of sovereignty with consequences greater than any before.

The euro is the last stage of a long effort to build unity by monetary means – starting with the snake, which Britain left after a few weeks, and going on to the ERM which Mrs Thatcher resisted for over a decade until urged in by the same interests now promoting the euro: the Labour Party, the TUC and CBI, the Liberals, euro enthusiasts for whom Europe is a religion and almost all the media. The results were disastrous. Britain lost over two million jobs, mostly in manufacturing, and the 1992 debacle drove the nail in the coffin of the Tory government, cost the country £30 billion, alienated the media and ensured that it will be more difficult to convince the British people that another monetary experiment will be beneficial.

The euro is a political instrument for building ever closer union rather than an economic policy. This is openly avowed in Europe. Here the loss of sovereignty has to be denied and membership sold as an economic benefit. There may be such benefits for countries which trade largely with each other, and will do so even more with a common currency. They will be less for one whose trade is divided half and half with the European Union and outside, and less than half of it with Euroland. Membership will force us to trade more with the European Union, but that is trade at a disadvantage, as demonstrated by our large deficit, compared to our trade with the rest of the world.

The euro is political because it builds union from the top down and without consent. The European Union's deep-seated drive for ever closer union comes

from the Commission, the vested interests around it and the European elite. That cannot be achieved by public consent or a federal constitution for electorates won't vote for it, nor from agreement between governments, for haggles and deals result in messy compromises and not a pristine plan. So the only project in town is the piecemeal building Treaty by Treaty, power by power, of a centralised Europe on a French design: mercantilist, interventionist, bossy, centralising and regulatory. Just like France.

The European Union constantly struggles to become something else but is unable to break away from what it is: building a palace on a cowshed. At its heart lies a restless conflict between Commission, Parliament and nation states. They are then further divided by a battle of small versus large, with Britain always nagging behind. Thus the Union proceeds crab-like to unity without consent. The euro is its latest instrument. It needs a central bank to manage it, then a common economic policy and bodies to run that, which need some kind of democratic supervision and a common tax system to ensure fair competition. So bit-by-bit a stronger Union can be put together. This has nothing to do with any economic benefits of the euro. They are minimal and, for Britain, non-existent.

The problems of sovereignty the euro creates are greatest for Britain, the reluctant European. The processes of deceit, already overused to persuade the British to accept other European policies, must go into overdrive to sell it. They will be invoked to a background of alienation and disbelief from an electorate already inoculated against it by the ERM, through a media now bitterly divided on the issue, and against a Conservative party now largely united against the euro by a government almost united on a 'rock solid' maybe, as against the cowardly Tory 'maybe not'.

All this on an issue imposing the biggest loss of sovereignty Britain has so far been asked to face. The euro takes away the two major tools of economic management available to national governments: interest rates and the exchange rate they affect plus, eventually, tax policies too. All these tools have been mishandled in Britain; witness our low growth rate, because of the overwhelming power of Britain's lopsidedly dominant financial sector centred on a City which always prefers dear money and an overvalued exchange rate. In 1997 Finance took power when interest rates were handed to the Bank of England. According to Geoffrey Robinson, Gordon Brown did this not to provide a training run for Europe, but to emulate America's independent Federal Reserve. If so he was misguided. The Fed takes account of growth, employment, the state of the economy and the exchange rate, as well as inflation. The Bank of England, regarded, perhaps rightly, as less competent, was given only one target: inflation at 2.5 per cent.

However misguided, giving control of interest rates to the Bank of England can be reversed. Conceding the same powers to the European Central Bank transfers power more permanently from democracy to plutocracy, from elected politicians to bankers, from London to Frankfurt. National governments are specifically precluded from interfering with the Euro Bank which has to fix one interest rate for all, something the Bank of England hasn't been able to do for this much smaller country.

However incompetent domestic management is accountable in some degree. The electorate throws out a government which fails. Changes are forced by argument, persuasion, riot, protest, strike or demonstration, as urban riots ended Mrs Thatcher's 1981 deflation and petrol stoppages changed Labour's tax policy. Citizens feel that they have influence. They won't in the euro. Unaccountable bankers in Frankfurt can't be thrown out. One interest rate must cover all, whatever damage it does to some.

This is the ultimate abdication of sovereignty. The state of the economy does more to determine election results than anything else, but the instruments which do most to influence it are lost. Labour came in prepared to surrender them. Before the 1997 election Gordon Brown and Tony Blair persuaded themselves that in a globalised financial world with enormous and instant financial flows dwarfing transfers arising from trade, the nation state is outdated and powerless, sovereignty irrelevant and interest and exchange rates incapable of national management. Yet once in office Gordon Brown found that he could manage policy perfectly well and get the growth and stability Labour craved. Instead of fluctuating wildly, sterling it stayed steady, though far too high. It was the euro which was unstable, falling by 20 per cent. The economy continued to grow, generating almost a million jobs, the opposite of Europe. Britain's unemployment rate fell to 4.5 per cent while Europe's stuck around 10 per cent.

Gradually Brown accepted reality. A national government can successfully manage a national economy. He was doing it. He, therefore, decided to postpone a euro entry, which was impossible anyway, so great Britain's overvaluation against European currencies. Would-be members should go in at the rate holding a stable relationship for two years. Anything like Britain's since 1993 would crucify the economy. The exchange rate translates our costs into Europe's prices so an overvaluation of around 30 per cent would have been locked in forever by entry, making the United Kingdom permanently uncompetitive and unprofitable, just like the ERM before it. Thus the entry issue became a case of 'Lord make us virtuous. But not yet.' The advocates of euro membership (the same as those who had urged the ERM) were forced on the defensive as the euro remained low – though whether this was because of inherent design faults, mistrust of Italy, Spain and, more particularly Greece or because of the all-conquering attractions of the dollar was not clear.

Such the failures of the euro's first two years. At its end, America's prospects look uncertain as the trade deficit gapes. In Britain, growth is slowing with interest rates far too high as inflation undershoots the target, and high, too, in historic real terms and compared to Europe. They prop up the pound at a level far too high compared to the low euro. Overvaluation makes it unprofitable to produce anything from cows to cavaliers in this country, transfers production overseas and brings a rise in imports, a fall in exports and a gaping trade deficit. The third big wind-down in a manufacturing base, already shrunk too far to pay the nation's way in the world, is well under way.

Europe's economy, long held back by Maastricht's deflation, benefits from what amounts to a competitive devaluation. So it is growing again, much of this at our

expense, though the rise in the price of British oil exports to them conceals the consequences for the balance of payments.

Divergence is disguised in Britain by the impetus of what is historically a pretty inadequate rate of growth, by new job creation (greater than Europe's) and higher public spending from the 2000 comprehensive spending review. The hardiest manufacturing companies survived the last two great deflations and have been resilient in resisting the third, but others who have kept going by exporting at zero profit, or even at a loss, by cutting investment, research and design, and all the other ingredients of long-term competitiveness, in order to keep market share are vulnerable. These are finite processes. Eventually firms go under, run out of cash or drop out of the game. Recession is inevitable unless the pound falls substantially and the euro rises ditto. If it does, the strong argument against membership – 'if it ain't broke don't fix it' – weakens.

Success in running the economy has weakened Gordon Brown's desire to get into the euro, but its effect on votes is more difficult to measure. Gordon Brown's purposely vague five tests can be fudged and fiddled at will, a process already going on as pundits hail 'convergence' just because the British and European economies are crossing each other, one on the down escalator, the other on the up: governments, even New Labour, will interpret reality opportunistically, but if the growth gap widens the advocates of euro membership will begin to stir. The electorate will be neither as nervous nor as keen to come to a quick decision, but prolonged British recession while Europe grows will undermine the majority against the euro that the polls currently show and add to the resigned feeling that entry is 'inevitable'.

Economics are a question of image as well as reality. The uninformed see a high exchange rate as a plus, a weak one as a minus, measuring the performance of the economy by the cheapness of foreign holidays. Thus if the euro rises because the dollar is less attractive, even if this weakens European growth, it will build European confidence and give another argument to euro worshippers. A decline in the pound, welcome to those who want to save manufacturing, will boost British production but undermine pride – all perverse but confusing to the electorate, and likely to muddy the economic argument.

The strong economic case against the euro confuses a diffident electorate. Experience, such an effective teacher in respect of the general consequences of the European Union, gives more difficult lessons here. People will be baffled by assertion and counter-claim and as soon as the argument is forced back from the mystic and from sovereignty onto exchange rate issues it is difficult to make on the doorstep.

All this was illustrated in a BBC programme on 18 February 2005 giving the referendum process a trial run in *Referendum Street* where pro- and anti-euro teams laboured to persuade 50 households in a north London street over two days. The end result gave confidence to those who feel the electorate can be persuaded to a 'Yes' vote for a 65 per cent to 35 per cent majority against the euro was changed over two days of intensive canvassing and persuasion into a majority of 58 per cent to 42 per cent.

The BBC experiment was, predictably, loaded to the euro. Yet it also showed that euro enthusiasts have more scope for rosy scenarios, sometimes called lies, by confidently projecting it as the provider of jobs, low interest rates, economic growth, stability and collective strength, and all necessary to avoid the terror of being alone in the world. All this was accepted by electors, particularly women, who were dutiful about orthodoxies and nervous about Britain's prospects, even as the British economy was doing well. Antis were forced onto the defensive and into difficult economic explanations in which left and right, devaluers and advocates of strong sterling, stay-ins and come-outs, took different views. Unity comes easier to the vacuous and those for whom the European Union is a religion.

The political argument of euro opponents did not play well. The sovereignty argument about running our economy for our purposes does not strike chords with those who had little faith in Britain's ability to do that and even less faith in its politicians. There was a middle-class distaste for assertive nationalism, dismissed as lower-class ignorance, and a feeling that Europe is idealism, therefore respectable. It is easier to sell the euro on the basis of idealism, working together, destiny in Europe etc., even though all this is mobilised to justify a leap in the economic dark and a huge risk. Similarly the other strong case that the euro is promoted by the same people and interests, and on the same grounds, as the ERM membership which proved so disastrous in increasing unemployment and prolonging recession are all too long ago. Everything before 1997 is ancient history. The past is another country.

Which creates the sceptics' dilemma: If our political arguments against what is a political instrument don't play, then the debate falls back into the economic arena. There people are bemused, baffled and lack the knowledge and confidence to make their own decisions. Here the wording of the ballot becomes important. The BBC's was loaded to the euro – as will be the wording in the actual poll – since people were asked whether they would replace the pound with the euro. No qualifications about when, in what circumstances, on what conditions or at what exchange rate. All that will be left to the government to decide on the basis of five tests which are eminently fudgeable and which say nothing about jobs in manufacturing, the sector of the economy most affected by exchange rate changes. They also ignore the need for financial redistribution to compensate areas which suffer from the single currency because they are less competitive, a problem certain to affect Britain's manufacturing regions, the industrial north and the Midlands.

Most important of all, the tests say nothing at all about the central problem: the exchange rate at which Britain enters. We went into the ERM at too high a rate, yet the pound is now higher still against the euro. Though it doesn't stop them blaming every problem on our failure to join the euro, the more sensible euro enthusiasts accept that Britain couldn't go in at this level of overvaluation, or anything like it, because the exchange rate translates our costs into European prices. Today's would set high costs and uncompetitiveness in concrete and require massive cuts in wage, living standards and public spending to even try to compete.

Neither government nor euro supporters have any proposals for getting the pound down, while the market seems little inclined to do so. Indeed, it never will by

the necessary amount because it would require a long period of low interest rates and sustained competitiveness. Britain's Financial Interest, which always wants high interest rates and a strong currency, will strongly oppose that and the need to lower the exchange rate to join will be difficult to explain to the electorate. The Maastricht requirement is to go in at a relativity in the ERM maintained for two years to show that it is sustainable. It would be extraordinary if a government which has passively watched the overvalued pound inflict massive damage on manufacturing, steel, cars, engineering and textiles, and lost nearly half a million manufacturing jobs in the third industrial shrinkage in 20 years, suddenly started actively managing the pound down to join the euro. It could do so for either purpose. It won't.

All this will be compounded in the actual referendum by the weight of euro propaganda and money, the nature of choice between the smooth men (pro), the hairy ones (against). The euro argument will again concentrate on creating fear of being alone, outside, out of the club, or unheeded, creating a strong possibility that a nervous electorate, confused about the economics, and dutifully disposed to orthodoxy and government advice, will opt for what it sees as safety.

Such a result could take Britain into the euro at an uncompetitive exchange rate on the worst possible terms. The price of sovereignty is educating the nation into what it's about and how to use it but the British have never even bothered to even think about either. Governments who have never seen the national self-interest clearly haven't exploited independence to pursue it. Indeed, it was because we couldn't do this that we went into the Common Market in the first place.

For Euroland, particularly the hard core who want to become an exclusive club within the union, Britain's entry to the euro would turn the key. For the British it locks us in a final subjection to Europe and relegation to the European Union's offshore, poor, plangent periphery, lacking the subsidies the others get. Our trading role with the wider world will be undermined, to force us to trade more with the European Union, where we sell at a disadvantage demonstrated by the sustained, never closing deficit. We would lose the ability to run our economy for our purposes or take the decisions which determine jobs, welfare, taxes and prospects. Today these decisions may be misguided but they are taken by national authorities for national purposes, authorities who must bear British interests in mind. In the euro there can be no such feeling. The result must be alienation, and the pursuit of selfish self-interest, for there will be no role for the national interest. What price then sermons about pay, greed, the 'unacceptable face of capitalism' or sectional selfishness? They're the only game in euro-town. Apart from learning German.

The euro is the end, not only of national independence, but effectively of the nation state, the only institution fallible humanity has found to improve the lot of the people and ensure that the processes of improvement are accountable. Britain has not managed these processes as successfully as competitors. It has lost an empire and not gained a role either in a Europe which doesn't suit it or as an independent player. It has missed out on the rapid economic growth which has made other countries richer, better, more contented and more powerful. Its

political elite has shown neither the same economic competence nor the same dedication to the national interest. It has neither grasped, nor really wanted, the opportunities open to an independent player, putting national interest first. It has always shown too great a willingness to live beyond its means and shoulders excessive burdens, whether in Defence or in the disproportionate costs of EU membership.

Such mistakes are ours, not imposed from outside by another system dedicated to other interests and making different mistakes. Democracies do make mistakes but making our own is of the essence because those who make them are accountable, and open to influence, protest and ultimately change. People are loyal to, and identify with, the nation state because it belongs to them. All else is plutocracy. Like the euro. Thus the questions facing the people in the referendum are simple: What kind of Britain do you want? A power or a province? Who should run it? Us or them? Exactly the questions the British don't like to face up to.

20 The establishment of a Commonwealth of Europe

The Rt Hon Tony Benn

Introduction[1]

Tony Benn, who was elected to Parliament in 1950 and served as a minister in several Labour governments, is one of those rarities in politics and life generally. Benn's experience of holding government office, and the process of ageing, resulted in him becoming more rather than less radical over time. Likewise, on the issue of European integration, he broke the mould. While many on the left shifted from an anti-European Union (EU) position towards a more favourable stance, particularly during the 1970s and 1980s, Benn moved the other way, becoming one of the most vociferous critics of the European Union on the left. I will briefly trace this journey, highlighting Benn's economic and political arguments against the European Union, thus setting the scene for his contribution to this book.

In the early 1960s Benn was favourable to the concept of European integration:

> The idea of Britain joining the Common Market is emotionally very attractive. To throw open our windows to new influences, to help shape the destiny of a new community, even to merge our sovereignty in a wider unit – these offer an exciting prospect.

However, he recognised that the reality of the European Union was rather different.

> The Treaty of Rome which entrenches laissez-faire as its philosophy and chooses bureaucracy as its administrative method will stultify effective national economic planning without creating the necessary supranational planning mechanisms for growth and social justice under democratic control.'
>
> (Benn 1963: 64)

In the mid-1960s Benn began to question his stance, becoming more disposed to entry, viewing it as a means of arresting Britain's decline and containing the growing power of multinational companies. One example at a practical level was his support for a European Technology Community as part of the solution to Britain's failed economic policy.

> Defence, colour television, Concorde, rocket development – these are all the issues raising economic considerations that reveal this country's inability to stay in the big league. We just can't afford it. The real choice is, do we go in with Europe or do we become an American satellite?

In reality, he lamented:

> The choice lies between Britain as an island and a US protectorate, or Britain as a full member of the Six, followed by a wider European federation. I was always against the Common Market, but the reality of our isolation is being borne in on me all the time.
>
> (Benn 1988: 204)

Britain joined the European Union in January 1973, following a parliamentary vote in October 1972. Benn, however, supported the principle that the people should decide, arguing that the Conservatives possessed no democratic mandate to take Britain in. He first suggested the idea of referendum on entry at a meeting of the Labour Party National Executive Committee in October 1969. In March 1972, following a determined campaign, the Shadow Cabinet accepted Benn's referendum proposal; the Parliamentary Labour Party accepted it in April of the same year. At a Cabinet meeting in July 1974 Benn announced his intention to campaign against British membership of the European Union.

During the Cabinet debate on Labour's renegotiation of the terms of EU membership in March 1975, Benn highlighted what he saw as the critical issue, that of 'whether the Community was to be a supranational structure or a community of sovereign states'. For Benn 'sovereignty means democracy, in the sense of power to make your own laws'. Commenting on the report containing the results of the renegotiation, Benn stated:

> This is the most important constitution document ever put before a Labour Cabinet. Our whole political history is contained in this paper. It recommends a reversal of hundreds of years of history, which have progressively widened the power of the people over their governors. Now great chunks are to be handed to the European Commission. I can think of no body of men outside the Kremlin who have so much power without a shred of accountability for what they do.
>
> (Benn 1990: 342–3)

Benn duly played a leading role in the No campaign during the 1975 Referendum.

Benn's experience as a minister reinforced his opposition to the European Union. He increasingly saw the European Union as a capitalist bureaucracy with a growing democratic deficit that aspired to superpower status. As Secretary of State for Industry, Benn later learnt that the Foreign Office had cleared his Industry Bill with the European Commission before it was even published. As Secretary of State for Energy, which involved attending meetings of the Council of Ministers, Benn noted that the latter:

> is really a parliament because it is a legislative body, but it poses as a cabinet. I felt, as a Minister and an elected representative, that I was among a tiny group of fellow Ministers, all burdened down with briefs prepared by officials to submit to the European Commission, also made up of officials. The political impulse has been completely overcome and the system is so cumbersome and so secret that there is no real feeling of being engaged in a democratic process at all.
>
> (Benn 1990: 408)

He complained that 'not a single working person or the needs of working people are brought near this centre of power'.

Despite the Yes vote in the 1975 Referendum, Benn continued to campaign against the European Union, persuading the 1980 Labour Party Conference to adopt a manifesto commitment to withdraw from the European Union, a pledge which was included in Labour's 1983 General Election Manifesto. However, the process of European integration accelerated with the adoption of the Single European Act (1986), and the treaties of Maastricht (1992), Amsterdam (1997) and Nice (2001), prompting Benn (1996) to devise a practical alternative to the European Union:

> We should be seeking a better framework within which European co-operation can be made both effective and durable, recognising that the treaties of Rome and Maastricht, far from ending nationalism, have actually encouraged it by their centralised and undemocratic structures. The alternative is not for any country to withdraw into isolation, but to begin to construct a Commonwealth of Europe that would allow all the forty seven countries on our continent to harmonise their policies by consent, expressed through their own parliaments. …Unless we move towards a looser, wider Europe, the present Union could disintegrate under the control of unelected Commissioners and bankers.
>
> (Benn 1996)

The Commonwealth of Europe Bill, reproduced below, was submitted to the House of Commons in June 1992.

Commonwealth of Europe Bill

Whereas it would be in the interests of the people of the United Kingdom to co-operate closely with the people in all the other countries in the continent of Europe for the welfare of all, and

Whereas the European Community set up under the Treaty of Rome has conferred too much political power on the Commission, which is not elected, nor can it be removed by democratic means, and

Whereas the Community laws, which take precedence over the domestic laws of member states, are made by the Council of Ministers, in secret, without requiring the prior consent of the elected parliaments of member states, and

Whereas the proposals for an economic, monetary and political union contained in the Treaty of Maastricht would necessarily undermine still further the democratic accountability of those with power to those over whom that power would be exercised, and

Whereas the effect of this would be to weaken the rights of the peoples of Europe to determine the policies of those in power, and

Whereas the long-term effect of these changes could be to lead to apathy, or the recrudescence of the worst form of nationalism, and

Whereas great new opportunities now exist for the creation of a wider European system, based upon the progressive harmonization of interests between the fully self-governing states in the continent;

Now therefore be it enacted, and it is hereby enacted by the Queen's Most Excellent Majesty, by and with the advice and consent of the Lords Spiritual and Temporal, and Commons, in this present Parliament assembled, and by the authority of the same, as follows:

1 Within six months of the passing of this Act, Her Majesty's Government shall summon a Conference in London of the governments of all the European States listed in the Schedule to this Act, to be held not less than six months thereafter, to discuss the establishment of a Commonwealth of Europe, to which all nations in Europe should invited to adhere.
2 At the Conference referred to in section 1 above, the draft of a Treaty of London, in the form set out in the Schedule to this Act, shall be presented to the Conference for discussion, amendments and subsequent ratification by the processes that apply for that purpose in each of the nations wring to participate.
3 Notwithstanding section 2 of the European Communities Act 1972, all legislation that has been enacted, or may be enacted by the United Kingdom Parliament shall, from the passing of this Act, have precedence over any laws, directives or regulations of the European Community.
4 There shall be paid out of money provided by Parliament any expenses of any Minister under this Act.
5 This Act may be cited as the Commonwealth of Europe Act 1992

Schedule

The Treaty of London for the establishment of a Commonwealth of Europe (Preamble)

The duly elected representatives of the following nations peoples of Europe:

Albania	Denmark	Latvia	San Marino
Andorra	Eire	Liechtenstein	Slovenia
Armenia	Estonia	Lithuania	Spain
Austria	Finland	Luxembourg	Sweden
Azerbaijan	France	Malta	The Swiss Confederation
Belgium	Georgia	Moldavia	Tajikistan
Belorussia	Germany	Monaco	Turkey
Bosnia-Herzegovina	Greece	The Netherlands	Turkmenistan
Bulgaria	Hungary	Norway	Ukraine
Croatia	Iceland	Poland	United Kingdom
Cyprus	Italy	Portugal	Uzbekistan
Czechoslovakia	Kazakhstan	Romania	Vatican City State
	Kyrgyzstan	Russia	

Determined to lay the foundation of an ever-closer association of the peoples of Europe for the common welfare of them all;

Accepting that this association must be based upon the maintenance of mutual respect for the fully self-governing status of all the signatories of this Treaty;

Resolved to work for the fullest degree of co-operation between the governments here represented in all matters that concern the continent as a whole, and its relations with the rest of the world community;

Committed to uphold the Charter of the United Nations and its decisions, and to the promotion of peace, democracy, disarmament and development and the maintenance and extension of Human Rights as specified in the United Nations Declaration of Human Rights;

Believing that the rich and diverse cultural, political, economic, religious and institutional identity of Member States must be preserved inviolate if peace and progress are to be achieved;

Resolved to work for these ends with good-will and in a spirit of tolerance and understanding

Have decided, at our meeting London, to create a Commonwealth of Europe, to which all entitled Nations may adhere, and which shall be in accordance with the following provisions:

Article 1 By this Treaty, the High Contracting Parties establish amongst themselves a Commonwealth of European Nations.

Article 2 The Commonwealth of Europe shall assume the task of working, by common consent, for the harmonious and peaceful development of all Member States, and the welfare of all the people living in them, and of the continent as a whole.

Article 3 The tasks entrusted to the Commonwealth shall be carried out by the following institutions: The Assembly, The Council of Ministers, The Court of Justice, The Human Rights Commission, The Secretariat. Each institution shall act strictly within the limits of the powers conferred upon it by this Treaty.

Article 4 Member States shall undertake to promote appropriate measures, whether general or particular, to win support from their own parliaments to secure fulfilment of the obligations arising out of this Treaty, or resulting from recommendations made by the institutions of the Commonwealth.

Article 5 Member States shall in cooperation with the institutions of the Commonwealth, seek to use their best efforts to harmonise their policies.

Article 6 The institutions of the Commonwealth shall take no action that would prejudice the interests of any Member State, or its fully self-governing status.

Article 7 Any independent Nation whose frontiers lie partly, or wholly within the Continent of Europe shall be eligible to join the Commonwealth, the subject only to the consent of a majority of the Members of the Assembly.

Article 8 Any Member State shall be free to leave, after giving twelve months' notice to the Secretariat.

Article 9 The Assembly may suspend the membership of any Member State by a simple majority vote, and may extend, or lift, that suspension at any time.

Article 10 This Treaty shall remain in force for an indefinite period, unless a majority of the Assembly, and of the Council of Ministers, recommend that it be terminated.

Article 11 This Treaty shall come into force when it has been ratified by the National Parliaments of a majority of the Nations whose representatives have signed it, and when a majority of the peoples of those Nations have approved it by a simple majority in referenda in their respective countries.

The institutions

Article 12 The Assembly
The Assembly shall be composed of a maximum of five hundred Members, and of men and women in equal numbers; and the representation of each Member State shall reflect the proportion which its population represents of the total population of Member States; save that in calculating such representation fractions shall be disregarded, provided always that a Member State shall have at least two representatives.

It shall be elected for a four year term, on the basis of an electoral system to be chosen by each Member State, provided that there shall be a single polling day within three months of the coming into force of this Treaty.

It shall meet in public and have the responsibility for determining the policy of the Commonwealth as a whole, subject to the limitations set down the Preamble to this Treaty.

It shall elect its own presiding officer each year, may determine its own procedure and shall have power to establish its own Committees.

Its Members shall be paid out of the national budgets of the Member States, as determined by each of them severally.

Its functions shall include the drafting of Conventions on any matter the Assembly deems to be necessary, which shall then be transmitted to the Council of Ministers and all Member States for ratification.

Article 13 The Council of Ministers

The Council of Ministers shall be composed of one representative from the government of each Member State.

It shall meet in public, unless, by a majority, it decides that it is in the interest of the Commonwealth, as a whole, that certain matters should be discussed privately, and it shall publish all the decisions which it has en, as soon as practicable.

Thereafter, it shall consider recommendations of the Assembly, and shall make recommendations to the governments of Member States.

The Council shall be charged with the task of actively seeking to harmonize the policies of all the nations of the Commonwealth on any issue, which concerns the continent as a whole, including the following matters:

Economic and industrial
Food and Agriculture
Energy
Trade
Political
Social
Environmental
International policy
Defence and disarmament
Development

Article 14 The Court of Justice

A Court of Justice shall be established, composed of judges nominated by each Member State, and confirmed by the Assembly, who shall serve unless they are removed by a two-thirds majority of the Assembly.

The Court shall be responsible for the interpretation of the constitution of the Commonwealth, and for adjudicating on matters referred to it by the Council or the Assembly.

Article 15 The Human Rights Commission

The Assembly shall elect, at the beginning of each term, from amongst its own Members, a Human Rights Commission, composed of persons from each Member State who shall serve for the duration of that term.

That Commission, guided by the Charter of Right set out below, shall have the authority to examine and report on any matter which it deems to involve human rights throughout the Commonwealth, or any matter referred to it by the Assembly, the Council or the Secretariat, and all its reports shall be published.

The Council, the Assembly and any Member State whose practices have been examined by the Commission shall consider and publish their response to such recommendations as may be made by the Commission.

Article 16 The Secretariat

There shall be a Secretary-General of the Commonwealth, elected by the Assembly at the beginning of its term, who shall serve for four years, and who shall have responsibility for the administration of the Commonwealth, reporting jointly to the Council and the Assembly.

The Secretariat shall consist of a number of deputy Secretaries-General who shall be nominated by the Secretary-General and confirmed by the Assembly and by a full-time staff for whom the Secretary-General shall be responsible.

The Secretary-General, or his deputies, shall attend all meetings of the Council of Ministers and the Assembly, may make recommendations to those bodies, and shall implement decisions taken by the institutions of the Commonwealth.

The costs of administration of the Commonwealth shall be met by moneys provided by the Member States through an equitable tax system levied within each state for that purpose.

Article 17 The Rights of Member States

Nothing in this Treaty shall infringe the absolute legal rights of Member States to take such action, within their own jurisdiction, which they believe to be necessary, using such powers as they possess.

The government of each Member State shall, subject to the consent of its parliament, implement any Convention or Treaty to which it has roe a signatory on its own initiative or on the initiative of the Commonwealth.

Article 18 Rights of the Peoples of the Commonwealth

The rights of the peoples of the Commonwealth to elect or remove their own governments, and as a result, to repeal or amend their own domestic legislation or to follow such policies as may have been determined by their own parliaments and governments, shall be entrenched in this Treaty.

Article 19 Domestic jurisdiction of Courts of Member States

Nothing in this Treaty shall in any wry limit the powers of the Courts of

Member States to apply the domestic laws of their own states in accordance with their own constitutional arrangements.

Article 20 Ratification and amendment of the Treaty
This Treaty be ratified by a referendum to be held in each Member State, and may be amended, on the recommendation of a majority of Council of Ministers and the Assembly, subject to the approval of all the Member States by a popular vote in a referendum in each Member State.

Annexe – The Charter of Rights

1 All citizens shall be entitled to enjoy, and to campaign for, universal democratic and enforceable rights, both individual and collective, enshrined in law, adhered to in practice and respected by society, as a precondition of self-government and the achievement of full political, social and economic emancipation within a civilized society.

2 Every citizen shall have the following political rights:

- to freedom of speech;
- to freedom of assembly and of association for the purpose of expressing an opinion, without interference from the State;
- to organize for common political, social or economic ends;
- to practise, or not to practise, any or all religions;
- to vote in all elections, participate in all electoral processes and institutions, and to contest ail elections;
- to privacy and the protection of personal information and correspondence from surveillance or interference;
- to information about public, political, social or economic affairs;
- to freedom of movement, unhindered by arbitrary interference, and to be given asylum from political, social or economic oppression; and
- to conscientious objection to service in the armed forces.

3 Every citizen shall have the following legal rights:

- to personal freedom from arbitrary arrest, detention or harassment;
- to a fair and impartial hearing by a jury of the citizen's peers if accused of any unlawful activity, and to equal treatment before the law and equal access to legal representation;
- to be presumed innocent until proved guilty, to be informed of all charges laid and the evidence in support of them, and the right to silence in court;
- to freedom from torture or cruel and degrading treatment, and from capital punishment;
- to legal advice and services, free at the point of use; and
- to equal treatment before the law, and in the community, without discrimination, and regardless of race, sex or sexual preference, colour, religious or political conviction or disability.

4 Every citizen shall have the following social rights:

- to adequate and warm housing and comfortable living conditions;
- to rest, recreation and leisure, to a limitation of working hours and to holidays;
- to enjoy access to literature, music, the arts and cultural activities;
- to good health care and preventive medicine, free at the moment of need;
- to lifelong and free educational provision;
- to dignity and care in retirement;
- in the case of women, to control of their own fertility and reproduction;
- to free and equal access to child care;
- to cheap, effective and equitable means of transportation;
- to a healthy, sustainable, accessible and attractive environment and to clean water and air;
- to media free from government or commercial domination; and
- to full access to personal information held by any public authority, subject only to a restriction order signed by a Minister and reported to Parliament.

5 Every citizen shall have the following economic rights:

- to useful work at a fair wage that provides an income sufficient to maintain a decent standard of living.

Conclusion

In an attempt to grant the British people the right to accept or reject the Maastricht Treaty, and to open up the debate about the European Union, Benn submitted his Treaty of Maastricht (Referendum) Bill to the House of Commons in September 1992. At the Labour Party Conference later that month, he submitted a resolution in favour of a referendum, which was defeated. Nevertheless, Benn continued his campaign for a Commonwealth of Europe throughout the 1990s.

Although Benn left Parliament in 2001 to devote more time to politics, his case against the European Union has never been more important. The proposed European Constitution, agreed in 2004, will further centralise power at the European level. However, the promised referendum on whether Britain should accept or reject the Constitutional Treaty, expected in 2006, presents the left with an ideal opportunity to rediscover Benn's proposed Commonwealth of Europe and to campaign for such an alternative before it is too late.

Note

1 The introduction and conclusion for this chapter were contributed by Andy Mullen.

21 Fighting against federalism

Rt Hon the Lord Shore of Stepney PC

Introduction

The problem that Europe in general and the euro in particular poses for Prime Minister Tony Blair and his Chancellor Gordon Brown can be simply stated: both men are genuine europhiles, eager to carry forward the whole process of European integration in foreign and defence as well as in domestic policies, keen to bury the pound sterling in the single currency as they see Britain's future as above all centred in the European Union (EU) and quite undeterred by the accelerating progress being made towards transforming the European Union into a fledged United States of Europe.

Both men want, if not a Federal Europe, then something very close to it indeed. Their problem is that they dare not admit it. Their deep commitment to all things European and their longing to be 'at the heart' of Europe, is the 'love that dare not speak its name'. They dare not admit it because, while they rightly assume that the majority of their fellow countrymen are well disposed towards their continental neighbours, they do not and will not accept that Britain, with its separate history, its separate institutions, its parliamentary democracy and its worldwide interest and connection, should be stripped of the powers of self-government and transformed from an independent state into a province of the United States of Europe.

British political leaders are not dishonourable men. Moreover, obvious falsehoods are, in a democracy, sooner or late exposed, with serious loss of public trust in public men. So, the Prime Minister and the Chancellor in their public statements, along with virtually all closet Federalists in UK public life, do their best to dodge the central question: isn't the creation of a United States of Europe now the main objective of the European Union? And isn't the euro simply one of the main means of achieving it?

Deception and self-deception

Were dodging not impossible, like so many of their predecessors they engage not in direct deceit but in self-deception. People around them, overwhelmingly europhiles themselves, whether they are drawn from the FCO or from the appointed advisers in the Number 10 Policy Unit, understand the government's problem very

well and use all their sophisticated skills and word play to give them credence and support. In what is now almost a separate branch and art of politics, they have created their own euro-speak vocabulary: 'pooling' sovereignty, subsidiarity, tax 'coordination' etc.

The Labour Party's approach was worked out years ago in Opposition and thrived during the period of latter-day Neil Kinnock and John Smith just as much as in the period of our present Prime Minister. Just how far self-deception can go was revealed in the Labour Party's 1997 General Election manifesto in this statement 'our vision of Europe is of an alliance of independent nations choosing to co-operate to achieve goals they cannot achieve alone. We oppose a European Federal Superstate.' And for those who don't read manifestos, Tony Blair broadcast the same message through the columns of the *Sun* in these words: 'New Labour will have no truck with the European Superstate' and 'if there are those in Europe who want a Federal Superstate, we would refuse to go along'.

Little was said than about the single currency, except for the low keyed 'we are not opposed, provided it is in the United Kingdom's interest' and the same basic approach was fully deployed by Chancellor Gordon Brown in his definitive statement in November 1997 of Britain's policy. The essence of what he had to say was that the issue was essentially one of economic judgment and that Britain would join provided that five tests of national economic self-interest were met. Yes, there were some constitutional and political considerations but these were in no way of a character that should be allowed to influence the decision to join.

This pragmatic and low keyed approach seemed at first to be working well. The Amsterdam Treaty of June 1997 posed no major problems for the new government and the British Presidency in the first half of 1998, while embarrassingly short of any serious achievements, avoided the great row. Indeed the single currency, the euro, was formally adopted by 11 states of what we now call Euroland on 2 May 1998 at the meeting of ECOFIN with a benign UK Chancellor in the Chair. Chancellor Kohl of Germany, in particular, well understood the political problem of the British government and along with his close colleague, President Chirac of France, understated rather than overstated the immense political significance of the single currency, leaving the triumphalist noises to be made by the Commission's Yves de Silguy and Jacques Santer.

Moreover, the whole strategy of downplaying the significance of the single currency, denying its real meaning and political significance, and asserting that we would join, but only if it didn't threaten Britain's economic interests, had this added attraction: it played very well in the party political battle, both before and after the 1997 General Election. Labour's apparently no-nonsense, straight-forward and friendly approach to our European neighbours contrasted vividly with the increasingly hostile, muddled and obviously divided approach of the Major government and of William Hague's post-election Opposition Conservative Party. Labour's spin doctors were convinced, not without some reason, that the deep divisions within the conservative Party on the issue was politically and electorally damaging to the Major government and was perhaps the crucial factor in Labour's electoral success. The spin doctors took the same view about the

damage caused by division and open dissent within the Labour Party. Much effort, art and skilled media manipulation was deployed to stifle and conceal the continuing Labour debate about Europe and the single currency.

The strategy and approach seemed to be working. But the trouble remained as virtually all the opinion polls showed that the British public remained stubbornly hostile to the single currency. Furthermore, that stubbornness was undoubtedly strengthen as the grass roots level by the vigorous campaigning of the *Sun* and *Daily Mail* newspapers and by the clear editorial eurosceptic tilt of *The Times* and the *Telegraph*, very influential broadsheets read by virtually the whole British political class.

The truth will out

But the crucial input that now threatens to wreck the whole New Labour approach to the euro has come, not surprisingly, from Euroland itself. Chancellor Kohl lost the German General Election in the autumn of 1998 and the successor government under Chancellor Schroeder, with former Finance Minister Lafontaine and his Foreign Minister Fischer, have felt free to openly state both the real significance of the single currency, emphasising its political importance for European integration and stating, in unambiguous terms, the over-riding purpose of accelerating the process of creating a European State. There were audible sighs of relief in Downing Street when Lafontaine unexpectedly resigned. But his successor, Hans Eichel, a far less flamboyant personality, is if anything an even more committed federalist than his predecessor. In an article in January 2000, Eichel wrote 'we will now strive towards political unification . . . EMU will not be enough . . . why do we still need national armies? One European army is enough.'

Equally and embarrassingly clear was Foreign Minister Fischer's statement to the Strasbourg Parliament on 12 January 2000: 'For the first time in the history of the European integration process . . . an important part of national sovereignty, to wit monetary sovereignty, has passed over to a European institution . . . the introduction of a common currency is not primarily an economic, but rather a sovereign and thus eminently political act.'

And, if that was not enough, in his 26 November 1998 speech he said, 'transforming a European Union into a single state with one army, one constitution and one foreign policy is the critical challenge of the age'. The former Finance Minister, Lafontaine, had made his views crystal clear and indeed reminded his fellow countrymen and his European colleagues that 'the United States of Europe has been the aim of the Social Democratic Party all along'.

Not only have none of the 12 states in Euroland dissociated themselves from these remarks, they have added greatly to their strength. Thus former Prime Minister Gonzalez, speaking shortly after the decision of the 12 to join the euro asserted that 'the single currency is the greatest abandonment of sovereignty since the foundation of the European Community . . . we need this United Europe . . . we must never forget the euro is an instrument for this project'. The voice of Belgium, in the person of its then Prime Minister Jean Luc Dehaene claimed that 'monetary

union is the motor of European integration'. The Italian Finance Minister Carlo Ciampi is scarcely less forthcoming when he says, 'I don't think we will have a Federal Government, but something between a Federal State and a Federation of States'.

And it isn't just the European politicians who have loosened their tongues and spoken the truth. Hans Tietmeyer, President of the Bundesbank, strongly believes that the 'European currency will lead to member nations transferring their sovereignty over financial and wage policies as well as in monetary affairs. It is an illusion to think that states can hold on to their autonomy over taxation policies.' And no less a person than the (then) President of the European Central Bank, Wim Duisenberg, publicly asserted, 'the process of monetary union goes hand-in-hand, with political integration and ultimately political union'.

Our European partners have indeed blown the gaff! If that wasn't enough, at the centre of the agenda of the German Presidency, which began on 1 January 1999, were placed the two dreaded items of tax harmonisation and the financing of the European Union, including the large and much resented British rebate. They remain on the agenda.

Getting desperate

So what is the British government now to do? Labour is criticised by their natural allies, Lord Jenkins, Paddy Ashdown, Michael Heseltine, Ken Clarke *et al.* for not being courageous enough, for not openly declaring their commitment to join the single currency. They are faced with a still hostile British public and a Europe now dominated by social democrat governments openly proclaiming not only their hostility to alleged 'unfair' British tax and other advantages but also their profound disagreement with the deflationary provisions written in to the Maastricht Treaty, the very provisions which Mr Gordon Brown, in particular, has totally embraced and accepted. The government's increasingly desperate response has come in three instalments. First, a massive attack on the media, endangering the support that the Murdoch press has in the past given to New Labour, accusing them of hysteria on the subject of tax harmonisation and a new public relations strategy of by-passing the national press and other media channels.

The second and more important reaction was of course the Prime Minister's statement in the House of Commons on 23 February 2000 when, in Paddy Ashdown's words, he 'crossed the Rubicon' and publicly committed himself and the government to joining the euro, just as soon as the economic tests which nobody takes seriously have been met. The launch of a National Changeover Plan backed with millions of pounds of new expenditure, is allegedly to prepare British firms and financial institutions, government departments and consumers for the adoption of the euro. In reality it is aimed at something much more, to convince the British people that the euro is coming, whatever they might wish, and to demonstrate to our European partners that we really do intend to ditch the pound, that we really are, unreservedly 'good Europeans' and that we do genuinely wish to be at 'the heart of Europe'.

The third and most recent government initiative was its attempt to bury the unpopular euro issue in the larger issue of membership of the European Union itself. Both at the Labour Party Conference in Bournemouth and again at the launch of the 'Britain in Europe' campaign, with the Prime Minister openly in alliance with Heseltine, Clark and Kennedy, the claim was made that to oppose the adoption of the euro was to join a 'conveyor belt to withdrawal'. Some of those who do oppose the single currency also wish to leave the European Union. But the great majority of those determined to keep the pound are also in favour of staying in.

The crucial issue is not the alleged 'conveyor belt to withdrawal' but the far more dangerous 'conveyor belt, via the euro, to total immersion' in Europe, to the creation of the European State. To this, the Prime Minister has virtually nothing to say except: 'I do not dismiss the constitutional or political issues. They are real.'

But what those constitutional and political issues were was not stated. Instead the Prime Minister went on, 'monetary union is a big step of integration, but so were the Single European Act and the European Union itself'.

The goal is political union

Yes, Prime Minister, these were important treaties. But there is a big difference between them and the single currency proposals, and the Prime Minister not only knows it but has articulated it with precision on many occasions. The single currency and Economic and Monetary Union are not just another incremental step but a massive leap forward for political union. As its proponents and opponents alike agree, the single currency decision is the most important that Britain and its people will have taken in the whole period since the Second World War.

Why? Because at one and the same time, it destroys the capacity of any future UK government to use the power of the state to guide, influence and control the economy and, at the same time, gives precisely these powers to unelected European institutions in Frankfurt and Brussels. Moreover as the advocates and architects of EMU and the single currency well know, it cannot work without the further fiscal, economic and political integration of the member states. There is not a responsible governmental voice anywhere in the European Union that would deny it. If British ministers are deaf to the voices of their European political colleagues, they can scarcely fail to hear these words from Wim Duisenberg, the President of the newly created European Central Bank: 'EMU is and always was meant to be a stepping stone on the way to a United Europe.'

The genie is out of the bottle. The appalling 'F' word, Federalism, is in the public domain and the United States of Europe, with Britain in it has become indissolubly linked to the issue of the euro itself. The argument cannot be avoided; the issues can no longer be hidden or concealed.

The referendum of course will take place. The government is too strongly committed to that to now renounce it. But, when the British people are asked whether they agree to give up the pound sterling and joint the euro currency, as Prime Minister Blair and the europhiles in all parties will recommend, they will

know they are also being asked to give up their independence as a sovereign state and to abandon parliamentary government and rule by men and women whom they elect as MPs. Henceforth they will merge themselves, along with their currency, into a vast new European State whose institutions – the Commission in Brussels, the European Central Bank in Frankfurt, the Judges of the European Court of Justice in Luxembourg and the European Parliament in Strasbourg – they may occasionally influence but can never control and, except for 87 MEPs out of a total of 626, have no power to elect.

22 Rediscovering progressive economic policy outside EMU

Philip Whyman, Brian Burkitt and Mark Baimbridge

Introduction

As the previous chapters within this edited collection demonstrate, participation in the European Union (EU) single currency will place a straitjacket upon UK macroeconomic policy and sovereignty, thereby increasing the difficulty of pursuing its national interest. The model for Economic and Monetary Union (EMU) designed by representatives from Europe's central banks, and ratified by all member states in the form of the Treaty on European Union (TEU) in 1993, seeks to impose a particular institutional framework which restricts the flexibility of action of individual countries in order to enable economic policy to be determined, or at least coordinated, from the centre. Many economists (see, for instance, Jamieson 1998; Michie 1999; Minford 1999; Ormerod 1999b) argue that greater autonomy for individual nation states, under the principle of subsidiarity, might provide a more stable economic environment in which to pursue further cooperation between countries. However, largely due to the political desire to tie members more closely together, EMU seeks to progressively replace economic autonomy for a nation state by the requirement to coordinate its economic strategy with the EU norm, or else be subject to sanctions levied by the EU Commission (Pennant-Rea *et al.* 1997).

Hence, EMU is an essentially political strategy based upon false economic assumptions of cyclical and structural convergence. The national interest of the United Kingdom requires the implementation of a long-run opt-out from EMU, given that its participation is neither inevitable nor desirable. The central issue therefore becomes, what framework is needed for the formation of macroeconomic policy in a Britain outside the single currency on a permanent basis? An initial stage is a national information campaign to acquaint the public and industry with the factual consequences, the opportunities created and the dangers averted by opting out. It should be supported by a detailed strategy for each British government department, to enable them to identify the trade, financial and investment opportunities arising from the creation of a euro-bloc. For instance, the City of London will gain opportunities to trade in eurobonds, whilst British manufacturing and service companies will enjoy competitive advantages from being free of the costs of converting to, and implementing, the euro. However, this should only be

seen as merely an initial phase. It is vital for those advancing a progressive left critique of Britain's role within European integration to develop positive alternatives. It is this 'vision' of the future policy implications and general economic strategies that would be ultimately instrumental in persuading people to reject the straitjacket of EMU. Hence, this final chapter seeks to move the debate forward to discuss two broad potential policy strategies for the United Kingdom outside EMU and also re-emphasise the importance of retaining control over the exchange rate.

Positive alternatives to EMU participation

A decision to reject participation in the single currency would restore to national government those economic instruments essential to the management of its economy. Governments will be able to devise different economic programmes and, once endorsed by the electorate, will possess the means by which to pursue their chosen objectives. Democracy will, therefore, be restored, so that citizens can once again enjoy the opportunity to choose the economic strategy pursued by the government of the day, rather than it being dictated by unelected, unaccountable central bankers based in Frankfurt. Moreover, governments will be able to pursue a more balanced economic programme, pursuing the multiple objectives of full employment, high economic growth and a sustainable balance of payments as well as low inflation. The opportunities are substantial. To illustrate the broad range of different policies that could be enacted, this chapter will outline two alternative economic strategies that could be pursued, once a nation is freed from the restrictive grip of the ECB and the requirements of the TEU. Additionally, we discuss the development of an exchange rate policy that is critical to the successful implementation of the outlined options for macroeconomic policy. The intention is to demonstrate, not only that national economic management is still feasible despite the arguments of supporters of the single currency, but also that it is preferable to transferring the main levers of macroeconomic policy into the hands of the ECB, which is incapable of using them consistently in the best interests of all member states simultaneously.

Tight monetary policy – low interest rate strategy

The first potential economic strategy seeks to follow the framework established by Alan Greenspan and the US Federal Reserve Bank, whereby national monetary authorities (whether in the hands of an independent or democratically controlled central bank) seek a higher long-term growth rate by providing a favourable climate for industrial expansion through low inflation and hence reduced long-term interest rates. Fiscal policy is used to support the more dominant monetary policy by restraining inflationary pressures, thereby reinforcing the low interest rate objective. The globalisation of financial markets prevents governments from 'persuading' financial institutions to finance public sector borrowing at less than the market rate. Consequently, the higher the level of public sector borrowing on the international money markets, the higher the price for that borrowing in terms

of long-term interest rates. This approach assumes crowding-out in the financial markets due to limited resources for lending to prospective borrowers, because, were banks to create money simply to meet the additional demand for funds so that the supply of loanable funds was relatively elastic, interest rates would be unaffected. However, the strategy seeks to reduce government expenditure in order to reduce borrowing and hence interest rates.

In 'hard' versions of this strategy, the government endeavours to maintain a high value for the currency in order to squeeze inflation further. The objective is comparatively easy to accomplish if the country enjoys a trade surplus, because the pressure on its exchange rate is upwards due to the country's competitive position, assuming the absence of speculative motives to counter this fundamental relationship. However, since the United Kingdom typically suffers from a current account trade deficit, a rise in short-term interest rates is needed to attract sufficient short-term capital investment into UK securities to counterbalance trade-related downward pressures on the currency, thus maintaining a high value for sterling. However, these developments will impact upon long-term interest rates and thus conflict with the fundamental goal of the strategy. Nevertheless, there is no reason why sterling should not prove to be a stronger currency than the euro, particularly due to the participation of high-inflation southern European member states and an ECB forced to balance economic policy between conflicting needs (Baimbridge *et al.* 1999a; Weber 1991b). The ECB will require time to establish its anti-inflation credibility and to demonstrate that it can ensure the long-term stability of EMU.[1] Moreover, unemployment remains the greatest economic problem for Europe to solve; 13 of the 15 governments currently in power were elected on a left-of-centre pledge to create jobs, so that it is only a matter of time before the ECB comes under renewed pressure to loosen monetary policy. The departure of German Finance Minister Lafontaine may have indicated an early victory for supporters of the independent ECB and the restrictive Maastricht rules, but it does not indicate which viewpoint will ultimately prove the stronger.

'Keynesian' strategy

A second distinctive economic strategy involves the more active use of fiscal as well as monetary policy in order to pursue both internal and external balance for the economy. Internal balance refers to more than just low inflation, but also to low unemployment and to high rates of economic growth. Accordingly, a mixture of demand-side reflation and supply-side labour market policies, particularly measures encouraging retraining and labour mobility, could reduce unemployment. Thus, the net stimulative effect is targeted upon specific sectors of the economy which most require assistance, rather than raising aggregate demand per se and creating inflationary bottlenecks. Economic growth could be facilitated by the maintenance of a competitive exchange rate through managed floating, perhaps based upon a trade-weighted basket of currencies, together with tax incentives for firms which increase productive investment. A mixture of fiscal and monetary policy could restrain inflation; if this proved difficult to achieve, rather than abandon the other

internal objectives, governments could enact additional measures to restrain inflationary pressures. These might include the temporary reintroduction of credit controls, an incomes policy (tax-based or otherwise) or coordinated national bargaining. Although currently unpopular amongst economists who prefer the allocative efficiency of free markets, the reality of sticky wages and prices, due to oligopolistic markets as much as the existence of trade unions, gives rise to the possibility of market failure resulting in persistently high unemployment and slower-than-trend output growth. In this case, government intervention is justified to achieve a superior outcome. It is a fact that the majority of the world's nations still retain exchange controls to assist them to manage their economies, whilst Ireland's remarkable recent growth rates have been facilitated by 'social contracts' with trade unions to prevent wage pressures undermining its competitive position. Finally, external balance can be achieved through the provision of a competitive exchange rate, although structural problems in export sectors may require supplementary supply-side measures to improve product quality and reliability and to encourage a shift of resources to provide goods and services in growing rather than stagnant markets.

The 'Keynesian' strategy is notably different from the first approach due to its positive role for government action in wider areas of economic activity. Accordingly, an approach of this nature would probably be accompanied by an industrial policy designed to enhance the long-run competitiveness of UK industry. An analysis of trade flows indicates that Britain enjoys a comparative advantage in financial and media services, and in those areas of manufacturing which rely upon a high degree of scientific innovation, such as telecommunications, pharmaceuticals, aerospace, energy exploration and generation, biochemicals and computer-related activity.[2] In contrast, Britain is less competitive in lower value-added manufactures, most notably in engineering and metalworking sectors. Outside EMU, the UK government could strive to strengthen its competitive position by enhancing the productive potential of already strong sectors through *targeted* reductions in corporation tax, research and development, tax credits, and greater spending upon education. Innovative research undertaken by universities and publicly funded research centres requires prioritisation in terms of the allocation of government resources if higher growth is to be forthcoming. Labour market programmes designed to re-equip workers for the requirements of industries with a competitive advantage ensure that their maximum growth potential is not undermined by the lack of a skilled workforce, whilst facilitating the shift of resources to more productive uses. The promotion of firms based in the United Kingdom has the further advantage that it will substantially improve the balance of payments position in the long run, whilst ensuring that the majority of the improvements in living standards and profitability remain in the UK economy and are not repatriated abroad by transnational corporations. Moreover, the trend towards foreign-owned plants demanding ever-increasing 'sweeteners' to retain production in existing plants raises the possibility that providing inexpensive finance or development grants to UK-based firms might prove a cheaper alternative that generates an improved long-term growth reward.

Exchange rate policy

Over a period the desired objectives of exchange rate policy are short-term stability and long-term flexibility. The dangers to avoid are long-term fixity and short-term volatility. The only way of achieving these goals is a system that permits long-run change whilst avoiding violent short-run fluctuations. Various policies are available to secure this end, but membership of the euro prevents them being implemented by establishing a permanent fixity which imposes deflation upon less competitive national economies. Deflation does not reduce relative prices automatically; it does so by creating unemployment and stifling the future prospects for economic growth.

The exchange rate between two currencies is a price like any other. Its movement enables the two economies to achieve trade and payments balance. If one country's exchange rate is overvalued (i.e. if a unit of its currency is worth too many units of the other currency), its exports become more expensive in the foreign currency, while imports become cheaper in its own currency. Therefore export volumes tend to decline and import volumes to increase, so that eventually the trade balance moves into deficit and unemployment rises. Conversely, when a country lowers its exchange rate, exports became cheaper and expand, while imports are constricted. The trade balance usually improves[3] but at some contemporary sacrifice of real income due to higher internal prices.

The correct level for the exchange rate at any one time is that which enables an economy to combine full employment of productive resources simultaneously with approximate balance of payments equilibrium. A higher exchange rate generates overseas deficits and unemployment; a lower one leads to the build up of excessive foreign currency reserves and domestic inflation. However, it has been emphasised that this 'correct' exchange rate varies in value over time (Jay 1990). The variety of influences affecting economic performance (trade balances, productivity, price movements, discoveries of natural resources etc.) combines to ensure that the 'correct' value of the exchange rate alters with the years. Therefore a country needs to retain its ability to adjust the external value of its currency. To fix it irrevocably forever, as compelled by EMU membership, is no less foolish than attempting to maintain in perpetuity the rate of income tax or the price of oil. The endeavour to do so generates economic inefficiency, usually in the form of accelerating inflation or a rise in unemployment.

Consequently, Britain's optimal strategy is to retain the national policy instruments required to increase its competitiveness in a socially acceptable manner. It is essential that the United Kingdom retains control over its interest rate, uses Bank of England intervention to smooth speculative fluctuations, encourages worldwide cooperation (through the G8) between central banks and aims for the maximum long-term exchange rate flexibility combined with the maximum practical short-term stability. Under such a regime, the exchange rate fulfils its role as facilitator of greater growth, higher living standards and full employment, without becoming an end in itself.

There is always a rate of exchange that enables each country to employ its

productive resources fully. In an ever-changing environment, the rate frequently alters to secure simultaneous full employment and trade balance. Therefore, when formulating British economic policy outside EMU, any suggestion that the pound should 'shadow' the euro must be rebutted. Such targeting makes domestic objectives harder to achieve; in any case the pound moves more closely with the US dollar than with any European currency. Over the past two decades the pound's fluctuations left it almost unchanged against the dollar. Today sterling is just 4.5 per cent below its average value in 1977, whilst lying very close to its average value for the last 20 years as a whole. More recently, the pound has been relatively stable against the dollar even in terms of short- run fluctuations; since leaving the ERM in September 1992, the pound never moved outside a 13 per cent band between $1.50 and $1.70. By contrast, its value against the Deutschmark oscillated considerably, over a range of 35 per cent during the same period.

Misplaced criticism

Supporters of EMU argue that the degree of economic autonomy for the nation state outlined here is illusory, because globalisation and the integration of financial markets will not allow differences in economic policy to persist. Therefore the United Kingdom might as well join the single currency. Indeed, many left-of-centre supporters of economic and monetary integration profess the belief that only as part of a new 'Euroland' can governments become sufficiently powerful to operate a form of euro-Keynesianism without financial markets causing terminal destabilisation via a currency crisis. However, both viewpoints are overstated. For example, the experience of the UK economy between 1990 and 1992 demonstrated that being tied into a fixed exchange rate system at an uncompetitively high rate leads to a fall in output and a rise in unemployment.[4] However, departure from the ERM and the subsequent 20 per cent depreciation in sterling resulted in the resumption of economic growth, which facilitated a fall in unemployment to levels last experienced two-and-a-half decades earlier. Thus arguments that economic policy autonomy is impossible because of financial market integration are wrong, because the United Kingdom's strategy and performance were significantly different from all other EU member states during this period; that is why it was so comparatively successful. Devaluation gave UK firms a much needed increase in competitiveness, which was not instantly lost due to inflation, as new classical theorists claim, but instead provided government with a freedom of manoeuvre that could have resulted in the adoption of either strategy outlined in this chapter or a multiplicity of alternatives.

A second argument for EMU membership is the suggestion that the United Kingdom's European partners would engage in some form of trade protection, which would deny British firms access to the single internal market and therefore cause considerable damage to its economy, should the United Kingdom remain outside the euro on a long-term basis. The argument is implausible. First, the United Kingdom has suffered a substantial trade deficit with the rest of the European Union since accession in 1973. Therefore, in the event of a trade war,

our EU 'partners' would lose the most. Second, any such protectionist measures would fall foul of the Treaty of Rome, the Single European Act, the TEU and the World Trade Organization's regulations. All are international treaties, binding their signatories to respect reciprocity of trade.

Another argument favouring membership of the single currency is that frequently associated with Tony Blair, namely that it will provide the United Kingdom with additional political influence over the future development of the European Union. Independence, according to the argument, equals powerlessness.[5] However, the claim is spurious. Whilst the participants in the single currency may opt to discuss their common economic policy apart from other EU member states, there is no legal mechanism for any other decisions to be taken in this way. Thus the United Kingdom cannot be marginalised simply due to its non-participation in the single currency. Moreover, its position would be strengthened further by consultation and cooperation with other EU member states who have exercised their opt-out (Denmark and Sweden) or been deemed too divergent for immediate membership (Greece). Further enlargement of the European Union will increase the number of member countries incapable or unwilling to sacrifice other policy objectives for conformity to EMU's 'one size fits all' policies. When such uniform monetary measures create areas of high structural unemployment, as they inevitably will, it is essential for opt-out nations to possess a collectively pre-agreed strategy of vetoing any plan to provide EU-wide aid to those areas. Problems created by the euro's operations should not be the responsibility of non-participants, but should be wholly financed by those embracing the single currency. Additionally, because *all* historical monetary unions not based upon political union have collapsed amidst substantial economic difficulties, these non-members would be wise to encourage the European Union to formulate a contingency plan for the re-establishment of individual currencies if (or when) the demise of the euro occurs.

In reality, Britain enjoys an effective long-run choice concerning its future strategy; it can embrace an essentially European identity or, if it decides to opt out of the euro, it can pursue a global strategy. By remaining outside EMU, the United Kingdom would avoid its damaging consequences. Moreover, the advantages of free trade within the European Union and the imposition of a common external tariff on outside imports have become progressively smaller since 1973, as restrictions on trade have been steadily diminished worldwide. Under the auspices of the General Agreement on Tariffs and Trade (GATT) and its successor, the World Trade Organization (WTO), the average tariff on industrial goods between developed countries has been reduced to just 3.8 per cent. As the millennium approaches, the industrialised nations are closer to the free trade ideal than they have ever been. In this gradually emerging new world economy, access to the EU single internal market for UK business is assured.

Britain need not fear that a long-term disengagement with movements towards further EU integration will lead to a powerless isolation. Britain is a member of the G8 industrial nations; its economy ranks as the fifth largest in the world and the third largest in the European Union. It is a member of the World Bank and the International Monetary Fund. It possesses a seat on the United Nations Security

Council and remains the head of the Commonwealth, whose potential for expanded trade has recently been grossly neglected (West 1995; Burkitt *et al.* 1996). Moreover, Britain enjoys a substantial portfolio of overseas assets and investments, and attracts the highest level of inward investment in the European Union. It is the world's second largest financial centre and global investor. It has more companies in the world's top 500 than any other EU country. The United Kingdom is well placed to be one of the most dynamic and innovative global economies (Taylor 1995).

Among Britain's greatest assets, underpinning its global economic effectiveness, is the English language. More than 1,400 million people live in officially English-speaking countries. One in five of the world's population speaks English. By next year, more than a billion will be learning it. It is the main language of books, newspapers, international business, academic conferences, science, technology, diplomacy and the Internet. Of all electronically stored information, 80 per cent is in English.

The widely held view that Britain has 'no alternative' but to participate in European integration is at odds with the facts. Instead a range of possible alternatives exists. Britain could remain an EU member and secure, under WTO rules, free trading arrangements with the EMU-zone through a series of mutually beneficial, bilateral agreements. It could explore the possibility of a closer relationship with the North American Free Trade Association, as recently suggested by Canadian opposition leaders. Now that formal negotiations have been launched to establish a free trade pact between Canada and the European Free Trade Association (Norway, Switzerland, Iceland and Liechtenstein), the United Kingdom could follow the same procedure. Above all, it should intensify its trading and investment links with the Commonwealth and the nations of the Pacific Rim. In these ways Britain would be able to pursue its true contemporary role of global trader and investor, while at the same time retaining its scope for a largely autonomous economic and social policy, such as the two possible strategies detailed above. Furthermore, outside the single currency, the choice between and among such strategies would be taken through the democratic process.

Conclusion

The design of a macroeconomic framework for a complex advanced economy depends upon a multiplicity of diverse factors, including recognition of its unique industrial structure, monetary and fiscal policy transmission mechanisms, the practice of wage formation, propensity for owner-occupation, national savings rates and technological progress. A combination of differences in consumer tastes, political choices, natural resources and centres of competitive excellence, together with the actions of institutions established to implement economic and social policy, necessitates differences in economic policy between nations. For example, the labour market operates very differently in the USA, where non-collective bargaining is the rule, than in Sweden, where trade union representation is close to saturation at 90 per cent density, irrespective of whether their fiscal or monetary

authorities followed a similar strategy. Moreover, exchange rate regimes tend to have a greater impact upon smaller, export-orientated nations than upon their larger neighbours, where only a relatively small proportion of GDP is traded. Consequently, it is extremely difficult for one international economic authority to replace national macroeconomic management by one common interest or exchange rate. This is not a particular design fault of the Maastricht version of EMU, although its preoccupation with stable prices will likely result in a larger dose of deflation across the Continent than would be the case if the ECB was charged with a more balanced agenda. It is simply that many economies of EU member states are too divergent cyclically and structurally from their neighbours for any claim of prior convergence to be convincing and, without such evidence, a common economic strategy is unlikely to be simultaneously in their individual interests.

In view of such fundamental weakness at the heart of the EMU project, the decision to reject participation retains for national government the economic instruments vital to successful macroeconomic management. Exchange rates can fulfil their function of equalising the demand and supply for a currency by the variation of its price, thereby preventing a basic uncompetitive imbalance from causing mass unemployment and falling standards of living. Fiscal policy, freed from the twin restrictions of the MCC and the Stability and Growth Pact, can smooth cyclical fluctuations, avoiding periodic unemployment that wastes productive resources and generates associated human misery. The purpose of monetary policy is, then, to prevent unstable boom and slump conditions in housing and financial markets, whilst seeking to ensure a low interest rate for investors in productive capital. Supply-side policies, including selective labour market programmes and investment in the economy's physical and IT superstructure, do not require a rejection of the single currency to be applied, although the benefit of a macroeconomic structure tailored to the needs of the economy would provide a more fertile environment for their implementation. Thus, rather than being weakened by the refusal to be dominated by an EMU agenda, which will often conflict with the interests of its economy, the United Kingdom would both be stronger and possess a superior ability to adapt to changing international market conditions. In the process democratic choice would be enhanced, rather than withdrawing the ability of citizens to influence the policies pursued by the ECB nominally on their behalf. Furthermore, it might encourage the United Kingdom to end its undue preoccupation with events in a small corner of the European continent at the expense of a vigorous attempt to meet the growing demands of emergent markets across the globe.

In view of the overwhelming evidence supporting the maintenance of national self-determination of economic policy, two factors remain to provide the momentum towards EMU participation. The first relates to the determination of a small political elite, together with the representatives of multinational corporations, to complete the European integration project; the former perhaps seek the increased influence a 'United States of Europe' would play in world events, whereas the latter desire to evade national regulatory regimes and thereby enhance profits. However,

these small elites are neither representative of the wider British electorate, nor even of the majority of business. Indeed, two of the three main UK business organisations, the Institute of Directors and Small Business Federation oppose EMU entry, whilst only the Confederation of British Industry, the group which tends to reflect the interests of large corporations, supports UK membership of single currency despite its membership being deeply split on the issue. In a democracy, governments should act in the interests of all the people, which requires the rejection of abandoning national economic policy.

The second factor undermining the vigorous assertion of national independence is the fear of failure. The notion of the United Kingdom as a declining nation has long sapped its resolve to follow its own interests and has caused many to prefer safety in 'Fortress Europe', with economic policy dictated by outside 'experts'. Yet, as illustrated in this chapter, this is a dangerous illusion which will further weaken the UK economy, which remains the fifth largest in the world and possesses the significant potential for accelerated growth if freed from the restrictions imposed by the EMU integrationist process. Fear is the enemy of innovation and change, yet great is the prize in terms of enhanced economic prosperity and restoring democratic choice to the British electorate.

Notes

1 Kydland and Prescott (1977) argue that rules or pre-commitment are more relevant when the monetary and fiscal authorities enjoy a reputation for discipline and consistency over time, whereas discretionary policy is more appropriate when such credibility is lacking.
2 It is worth noting that the international price structures of many of these key products are denominated in US dollars. Moreover, the euro is likely to have a more volatile medium-term relationship with the US dollar than sterling has experienced since the UK's withdrawal from the ERM in September 1992.
3 The converse occasionally occurs, if import and export volumes do not change sufficiently to offset the price movements; the Marshall–Lerner condition states that the trade balance will improve when the sum of the elasticities of demand for exports and imports exceeds unity.
4 One estimate, made by Burkitt *et al.* (1996), concluded that the UK's two-year membership of the ERM cost an estimated £68.2 billion in 1992 prices (equivalent to 11.5 per cent of UK GDP), in terms of lost output, and one-and-a-quarter million more unemployed.
5 A related, but separate, argument that the United Kingdom will lose its world influence if it remains outside EMU is the direct opposite of the truth. If subsumed into EMU, the United Kingdom will be seen as a duplicate mouthpiece for EU interests and there will be pressure for the European Union to replace British, German and French individual participation on international bodies including the UN, IMF and G8. A distinct British influence over world events will, under such circumstances, be far smaller.

Glossary

Amsterdam Treaty The Amsterdam Treaty of 1997 introduced a number of institutional reforms, incorporated the CFSP and Social Chapter into the European Union, and introduced the concept of variable geometry.

Asymmetric and symmetric external shocks External shocks refer to the impact upon the domestic economy generated by activities beyond the control of the UK authorities, for example a sudden rise in oil prices or change in global demand for raw materials. If an external shock has a similar effect upon a given group of countries, it is said to be a *symmetric* shock, since the policy response will be largely the same for all countries. *Asymmetric* shocks, alternatively, refer to those changes in the external environment which have significantly different effects upon different countries, requiring very different policy responses by each country in order to respond effectively.

Bundesbank German central bank – equivalent to the Bank of England, although operating with greater independence from government.

Common Agricultural Policy (CAP) EU agricultural support scheme which accounted for a majority of the EU budget until 1997. The protection of EU food producers has led to food prices in EU countries rising significantly higher than world prices.

Common Fisheries Policy (CFP) Under the Treaty of Rome, fish and fish products are considered as agricultural products. Consequently, the CFP is based on the same principles as the CAP.

Common Foreign and Security Policy (CPSP) The CFSP was one of the intergovernmental pillars of the Maastricht Treaty, subsequently incorporated into the European Union by the Amsterdam Treaty. The CFSP (which incorporates the Common European Security and Defence Policy) has resulted in a new EU security doctrine, EU police missions in Bosnia, EU-led military operations in the Congo and Macedonia, a European Defence Force, a European Armaments Agency, and an independent EU military planning unit.

Cyclical and structural convergence Economic convergence refers to potential EMU participants becoming economically similar prior to membership. Cyclical convergence occurs when the business cycles of boom and recession become increasingly similar amongst participating economies, so that a recession in the UK would occur approximately at the same time as a comparable slowdown in Germany, rather than one or two years in advance as at present. Similarly, structural convergence refers to changes in the industrial and financial structure of the participating economies which have the effect of ensuring similar reactions to external forces over the long term.

Deflation/Reflation Deflation may be defined as a reduction in economic activity in the

economy which is associated with a sustained fall in inflation, output and employment. Reflation refers to an increase in economic activity which stimulates output, employment and inflation in varying degrees.

Devaluation/revaluation/overvaluation Devaluation refers to a reduction in the value of a given currency relative to others, whilst revaluation concerns an increase in the exchange rate. For example, when the exchange rate on a given day was £1 equals $1.67, if the value of sterling increased so that £1 could now buy $2 worth of goods, the value of the pound would be said to have appreciated, whereas if the value fell to $1.5, sterling would be said to have fallen in value or devalued. Overvaluation refers to the circumstance where the value of sterling is so high that British exporters find it difficult to compete and could lead to a trade deficit where more is imported than exported. An overvaluation could lead to recession as export companies reduce output and lay off workers. This then may spread to the remainder of the economy.

Direct elections The European Assembly, composed of nominated national parliamentarians, was transformed into the European Parliament in 1979 as a result of elections by direct universal suffrage across the European Union.

Economic and Monetary Union (EMU) The European Council accepted Delors' EMU plan in June 1989. Following an intergovernmental council on economic union and another on political union, the Maastricht Treaty was agreed in December 1991. The treaty set out the three stages of EMU, detailed the convergence criteria for EMU, granted the ECJ the power to fine member states, expanded the European Parliament's powers, provided for EU citizenship, established the statute of the European Central Bank and extended EU competence into new policy areas. As a matter of definition, monetary union occurs when exchange rates are *permanently and irrevocably* fixed and may therefore precede the introduction of a single currency. However, the two terms are generally used interchangeably. Economic union involves a further transfer of macroeconomic policy to the federal level – particularly monetary policy but typically also coordination of fiscal policy within prescribed limits.

European Central Bank (ECB) Superseded national central banks in those EU nations participating in EMU. Based in Frankfurt, the ECB is in sole charge of exchange rate and monetary policy for all EMU countries, setting one common interest rate which will apply irrespective of the particular needs of individual countries at any period of time. Its sole policy goal is to achieve price stability and there is no similar responsibility to assist employment creation or economic growth. Policy conflict between the ECB and the wider economic responsibilities of individual governments is difficult to resolve since the ECB is beyond the control of both member states and the EU Commission.

European Company Statute (ECS) Still under discussion, this would enable companies to register at EU, rather than national, level.

European Constitution The Convention on the Future of Europe was established in 2002 and produced a draft EU constitution in 2003. However, disagreement over the European Council voting system, the mutual defence clause, economic, defence and foreign policies, the size of the European Commission, Britain's budget rebate and the status of God in the constitution proved insurmountable. For the first time, the intergovernmental council held in 2003 was a failure. However, following further negotiations, a European Constitution was agreed in 2004. It grants the European Union a legal identity, reforms EU decision making, creates the posts of EU Foreign Minister and President and extends majority voting to 30 new policy areas.

European Council This is the executive of the European Union, composed of heads of state or government of member states.

European Monetary Institute (EMI) The forerunner of the European Central Bank (ECB).

European System of Central Banks (ESCB) The central banks of all member states participating in EMU act as subsidiaries of the ECB, implementing its policies.

European Union (EU) Formally the European Community (EC) and Common Market. The change of name occurred after ratification of the Maastricht Treaty and signified a changed relationship between the 12 (now 25) participating nation states (called member states in EU terminology), from a loose trading community to a federal state with one currency and one central bank, with discussion of parallel moves towards political union.

European Works Councils (EWCs) Originating from an EU Directive, EWCs are to be established in large multinational European companies based in one or more member states, in order to encourage consultation with, and between, workers from all productive units.

Euro-X Committee A committee of those member states participating in EMU whose discussions may include market-sensitive preferences for interest and exchange rates.

Excessive Deficit Procedure (EDP) The EDP is a feature of the Maastricht Treaty, whereby a budget deficit is deemed excessive if it exceeds 3 per cent of GDP, and if government debt exceeds 60 per cent of GDP.

Exchange Rate Mechanism (ERM) Introduced as part of the European Monetary System in 1979 as a means of minimising currency fluctuations. Each currency is allowed to fluctuate against the others by an agreed margin around a set of bilateral central rates. If the currency approached its top or bottom limit, then national central banks intervened to bring the currencies back into line.

Fiscal federalism Involves a redistribution of resources from more successful to weaker regions of a federal state or, in the case of the single currency, between regions or member states participating in EMU. In practice, fiscal federalism acts in a similar manner to regional transfers in a nation state, whereby it seeks to stabilise the entire EMU by reducing inflationary pressure in booming areas and kick-starting recoveries in depressed areas through a transfer of tax revenue from the former into public expenditure (or a tax cut) in the latter. Fiscal federalism may, therefore, assist macroeconomic management, particularly due to the existence of regional spill-overs or externalities, thereby preventing individual regions from going it alone. It may also aid social cohesion by acting as an inter-regional public insurance scheme, preventing unlucky areas from bearing a disproportionate financial burden.

Fiscal policy Refers to the interaction between government expenditure and taxation. Under EMU, fiscal policy will remain under the control of national economic authorities, although constrained by the Maastricht Convergence Criteria (MCC) and the Stability and Growth Pact (SGP) rules.

G7 An informal grouping of seven of the largest industrialised economies (USA, Canada, Germany, France, UK, Australia and Japan). Russia has occasionally been invited to participate in recent summits, giving rise to G8.

Gilts A gilt is a promise by the government to pay interest on a loan which it has raised from the capital markets, with the loan becoming fully repayable at the end of an agreed period, i.e. gilt-edged security.

Gold Standard A currency arrangement whereby the central bank is obliged to give a fixed amount of gold in exchange for its currency. If a number of countries all fix their currencies relative to gold, they must, by definition, fix their exchange rates amongst themselves. The Gold Standard that existed between the majority of industrialised

economies during the 30 years or so before the First World War, imposed certain rules upon participating economies, the most important of which was a distaste for debasing the currency by devaluing. Moreover, a participating nation that experienced a balance of payments deficit would have to take corrective deflationary action, thus preferring external over internal balance. The increased international volatility caused by war conditions terminated the system, and its replication in 1925 was disastrous for the United Kingdom as it occurred upon pre-First World War parities which no longer represented the economic balance between nations.

Gross Domestic Product (GDP)/Gross National Product (GNP) These are two methods of measuring the value of the total flow of goods and services produced by an economy over a specified period of time – usually a year. The difference between the two is that GNP equals GDP *plus* net income earned by domestic residents from overseas investments.

Intergovernmentalism This refers to institutional arrangements and decision-making procedures that allow governments to cooperate in specific areas while retaining their sovereignty.

International Monetary Fund (IMF) Established in 1944, by 2004 it possessed 184 members. It is intended to encourage international cooperation in monetary matters and the removal of foreign exchange restrictions. Members are required to contribute a quota calculated upon the basis of GDP, and this fund can then be utilised to help members over temporary balance of payments difficulties, although usually in parallel with adopting corrective economic policies, such as domestic deflation and devaluation, which are intended to stimulate exports and reduce imports.

Lisbon Agenda The Lisbon Summit in March 2000 set a new strategic goal for the European Union: to become the most competitive and dynamic knowledge-based economy in the world, generating 15 million jobs by 2010. The strategy, based on economic reform through increased competition and on social reform through the modernisation of the European social model, identified the construction of a single financial market, full implementation of the Single Market, and welfare state reform as its key instruments.

Maastricht Convergence Criteria (MCC) Established by the Treaty on the European Union (Maastricht Treaty) to ensure economic convergence amongst potential participants prior to their entry to EMU, there are five criteria which each country must achieve before they are permitted to participate in the single currency. They are: (i) each country's rate of inflation must be no more than 1.5 per cent above the average of the lowest three inflation rates in the EMS; (ii) its long-term interest rates must be within 2 per cent of the same three countries chosen for the previous condition; (iii) it must have been a member of the narrow band of fluctuation of the ERM for at least two years without a realignment; (iv) its budget deficit must not be regarded as excessive by the European Council, with excessive defined to be where deficits are greater than 3 per cent of GDP for reasons other than those of a temporary or exceptional nature; (v) its national debt must not be excessive, defined as where it is above 60 per cent of GDP and is not declining at a satisfactory pace.

Monetary policy Typically concerned with the level of interest rates, the availability of credit, banking regulations and the control of the money supply by the central bank. Under EMU, monetary policy will be transferred from national authorities to the ECB.

Nice Treaty The Nice Treaty of 2001 reformed EU decision making, extended qualified majority voting to 27 new policy areas and provided for enhanced cooperation and thus for the development of a two-speed Europe.

Nominal and real wage rigidity Nominal wages refer to money wages, whereas real wages refer to the purchasing power of those wages. Thus, a 3 per cent rise in nominal wages during a period of 2 per cent inflation produces a 1 per cent rise in real wages. Wage rigidity refers to a situation where wages are observed not to be perfectly flexible in response to a change in economic circumstances, for example if wages should fail to fall sufficiently to price people back into work during a recession.

Non-accelerating inflation rate of unemployment (NAIRU) NAIRU is the rate of unemployment, whether it is 1 per cent or 8 per cent, where inflation remains stable. The importance of this measure is that, if unemployment falls below its NAIRU rate, inflation will accelerate, whilst if above the NAIRU, inflation will fall.

Optimum currency area (OCA) theory This theory is utilised by economists to identify those factors which indicate the *optimum* size of a currency arrangement. Consequently, the theory proposes that objective tests can be employed to decide whether it is in the common interests of, for example, Ireland and Italy, or France and Germany, that they should join together in EMU, or whether it is to their mutual advantage to retain separate currencies and monetary systems. Similarly, the theory could be used to identify whether *regions*, rather than countries, should form a currency union. Thus, the south-east of England may have more in common with certain wealthy regions of Germany and France than either Wales or Northern Ireland, and in theory it may make economic sense to form a currency arrangement accordingly. In practice, however, whilst nation states remain the principal form of government for the majority of the world's population, OCA theory will be concerned in deciding where monetary integration should and should not be formed between groups of countries.

Organisation of Economic Co-operation and Development (OECD) The rich nations' club, based in Paris, famous for economic research and forecasting.

Qualified acceptance This is a procedural device used by the Labour leadership to neuter Annual Conference policy decisions.

Qualified Majority Voting (QMV) A method of voting used in the Council of Ministers, whereby votes are allocated to member states according to the size of their population, and a certain number of assenting votes is required for a measure to be adopted.

Remitted Remitting is a procedural device, whereby the mover of a motion/resolution at the Annual Conference is requested to pass it to the executive committee for consideration. If the mover refuses, the executive committee usually asked the Annual Conference to reject it.

Schuman Plan Proposed the integration of Europe's coal and steel industries, which led to the European Coal and Steel Community (ECSC).

Single European Act (SEA) The 1986 Single European Act introduced the single internal market, but also extended qualified majority voting within the Council of Ministers and further committed the European Union to 'the objective of the progressive realisation of European and Monetary Union'.

Single European Market (SEM)/Single Internal Market (SIM) Resulting from the 1986 Single European Act, the Single Market refers to the removal of trade, capital and physical barriers across Europe, supposedly achieved by 1 January 1993, which allows free competition across the entire EU market. Britain argued that the creation of a European single market could be achieved through a non-legal agreement with implementation proceeding on the basis on unanimity, thus preserving the national veto. However, the British proposal was defeated and an intergovernmental conference was convened to revise the founding treaties of the European Union. The price for the

creation of the Single Market was the Single European Act of 1986, which extended qualified majority voting to 12 new policy areas, whilst committing its signatories to EMU.

The Six In 1951, the original members of the European Union – Belgium, France, Italy, Luxembourg, the Netherlands and West Germany, known as the Six – proceeded to establish the European Coal and Steel Community.

Social Charter/Social Chapter The Social Charter (actually the 1989 Charter on the Fundamental Social Rights of Workers) was agreed as a separate social protocol and was signed by 11 member states during the Maastricht Treaty negotiations. It was subsequently incorporated into the European Union, as a Social Chapter of the Amsterdam Treaty.

Social Dialogue A decision-making process whereby the social partners (representing employers and labour) agree new social policy legislation.

Stability and Growth Pact (SGP) Proposed by Germany to avoid excessive fiscal profligacy by individual member states within EMU, the SGP limits budget deficits to 3 per cent of GDP (as with the MCC prior to membership). If this limit is ignored, and the country is not in recession (defined as GDP falling by 0.75 per cent), fines of between 0.2 and 0.5 per cent of GDP will be levied by the EU financial authorities. The Stability and Growth Pact additionally suggests that budget deficits be limited to 1 per cent of GDP in the long term, thus increasing fiscal tightening.

Supranationalism This is government by institutions operating over and above nation states.

Three-year rule This is a procedural device created to avoid the reaffirmation of a policy for three years following its adoption by Labour's Annual Conference.

Variable geometry/Two-speed Europe This allows member states to proceed towards integration at differential rates.

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