You thought we’ve got an EU single market? Think again!

Forget Europe’s constitutional crisis or disputes over enlargement. EU member governments’ failure to complete the single market is the greatest threat argue R. Daniel Kelemen (far left) and Anand Menon

It’s hard to overstate the importance of the single European market. Its creation has been the centre-piece of economic integration for 20 years and has provided the basis for EU expansion into many new policy arenas. These include economic and monetary union (EMU) and EU social and environmental legislation. An extra two and a half million jobs have been created, European firms are more competitive in the global economy and the Union itself is more attractive to foreign investment - all thanks to the single market.

Less than two decades ago, Europe was warned about the grave economic and political risks of failing to complete the market in a seminal 1988 report by Paolo Cecchini, former Commission deputy director for the internal market and industrial affairs. Yet today the EU’s greatest achievement is in real and present danger.

National governments are being increasingly seduced by protectionism, be it Polish or French attempts to protect ‘strategic’ industries from foreign takeovers, or Spanish reluctance to sell its energy giants. They are also becoming more brazen in their defiance of the Commission’s efforts to ensure fair play. Rhetorical support for the single market is being undermined by member states’ actions, with legal and political obligations being ignored. Moreover, Europe’s political leaders appear incapable of recognising the far-reaching consequences of their deeds, which threaten the very heart of the integration process.

Instead, political debate has been distracted by the future of Europe’s constitutional treaty following the French and Dutch rejections of it. While the failure to ratify the treaty delivered a powerful psychological blow, it was less momentous for the future of Europe than most commentators imply. For instance, the text was notably timid over the institutional reforms it proposed to help the EU to cope with further enlargement. And, despite the
warnings of doomsayers, the Union has continued to function remarkably well on the basis of arrangements established by the Nice Treaty. Indeed, significant progress has been made on two ‘pillars’ of EU policy-making – justice and home affairs and the European Security and Defence Policy – and there is no evidence that constitutional gridlock has affected the legislative process in key areas related to the single market.

So, if treaty reform is not the toughest challenge facing the EU, why are problems with the single market process still hidden below Europe’s political radar?

The economic benefits of the Union are often either misunderstood or downplayed deliberatley by national politicians. When was the last time you heard Britain’s Chancellor of the Exchequer, Gordon Brown, attribute any of the credit for Britain’s economic success to its participation in the single market? Yet this political oversight should not blind us to the scale of its actual impact.

This can be measured in terms of aggregate economic activity. EU Gross Domestic Product, for example, is estimated to have been 1.8% higher in 2002 than it would have been without the single market, according to the Commission.

It can also be seen in the major EU policy initiatives that owe their genesis to the single market. EMU itself was launched partly because a single currency promised to enhance market efficiency. Remember the tale of the American who traveled across Europe with $100 and, having changed money in every EU member state, ended up with only $45? National currency regimes
were also rendered unsustainable by the free movement of capital, which was an integral part of the single market.

The single market also provided an intellectual and legal catalyst for the EU to extend its powers into new policy sectors. Many on Europe’s political left argued that the single market, with its neo-liberal bias, would endanger national regulations to protect workers, the environment and public health. But their critique ignored the fact that the creation of the single market was coupled with the establishment of common standards in these areas at the EU level.

Debate continues on the degree to which European rules have or should replace national regulations that were dismantled in the name of free trade. However, it is clear that without single market legislation, there would have been no legal basis for, say, Europe-wide limits on working times or vehicle emissions.

Environmental policy provides a good illustration of how the single market has permitted initiatives in other areas. Member states have proven willing to sign up to ambitious EU greenhouse gas reduction programmes partly because their multilateral nature means that their major trading partners are doing likewise. And stringent targets on car emissions are less painful if, because of the size of the European market, other states apply them as well.

Despite scoring such significance advances during its short existence, the single market must now overcome perhaps its greatest hurdles. These include issues outstanding since its inception in the mid-1980s. When EU member states decided to remove barriers to the free movement of goods, services, capital and labour, they did so in very general terms. Ambiguity was the price of agreement between political leaders as diverse as British Prime Minister Margaret Thatcher and French President François Mitterrand. Some 20 years later, member states are once again trying to sort out the equivocal details, only to discover continued disputes over the appropriate balance between, for example, the state and the market in the service sector.

In the energy sector, meanwhile, European-wide restructuring is being stymied by repeated government interventions to protect national producers from foreign takeovers. Last year, following a bid by the German corporation E.ON for Spanish power company Endesa, Madrid empowered the Spanish electricity and gas regulator to block foreign acquisitions. This legislation was passed despite the Commission informing the Spanish authorities that they were violating single market legislation guaranteeing free movement of capital and freedom of establishment. Indeed, Spain currently faces two infringement proceedings brought by the Commission over its behaviour concerning Endesa.

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Meanwhile, the French government in 2006 sought to engineer a merger between energy giant Suez and state-owned Gaz de France to prevent a feared takeover attempt by Italian utility firm Enel. French Prime Minister Dominique de Villepin reacted angrily to accusations of protectionism, defending a policy of “economic patriotism.” The French approach also included vitriolic and often totally misplaced criticisms of the services directive that contributed to its eventual dilution.

Nor is protectionism the preserve of “old Europe”. New member states have been quick learners, as exemplified by the Polish government’s efforts to prevent mergers between Polish and foreign banks. Member states are in effect throwing down a political gauntlet to the Commission, challenging the very principles of the single market. While remaining rhetorically committed to building the single market, they undermine it by their actions.

The Commission tries to “name and shame” offenders but that policy can only work if targeted countries are concerned about public opprobrium. With national governments increasingly willing to challenge the Commission, it would seem that no one can shame the shameless.

The Commission is unwilling to flex its full legal muscle to enforce single market legislation for fear of a national backlash, which might damage its own legitimacy and even the reputation of the entire EU system. After all, from Amsterdam to Athens and Vienna to Vilnius – even at times from...
within the Commission itself – politicians seem anxious to parade their anti-European credentials in front of domestic audiences. It pays political dividends to blame Brussels.

As well as flouting existing single market rules, EU governments are putting stumbling blocks in the path of new regulations too. Take the failure to agree on a patents directive. And legislation to govern cross-border takeovers is another case in point. After 13 years of Commission proposals, member states finally adopted new takeover rules in 2004, but only on condition that certain “opt outs” were available. Twenty-one countries then opted out of provisions on the legality of certain forms of takeover defenses, while Germany, Denmark, Luxembourg, Poland and the Netherlands opted out of provisions regarding shareholder consultation.

Member states thus appear to be doing their utmost to wriggle out of their own commitments to market integration by exploiting opt outs and derogations or even, in some policy areas, supplanting the traditional legal approach to market regulation with the toothless “open method of coordination”.

Despite the evident and universal benefits of the single market, it would seem that member states are succumbing to short-term incentives to undermine its progress. For example, as the market-making process moves further into sensitive areas such as the reduction of public subsidies and politicians worry about the effect on unemployment, governments are tempted either to maintain subsidies or to blame Brussels for any cuts.

EU institutions were created to overcome such temptations, but member states are making it increasingly difficult for them to succeed. It is clear that public pronouncements from member states in support of the single market are meaningless unless they allow the Commission to fulfill its duty as guardian of the community’s legal framework.

So what, then, are the potential costs of failing to get the single European market back on track? Despite great progress in generating jobs and growth, the single market is still far from complete. Yawning gaps exist in the service sector and there remains a strong and persistent “home bias” in consumption and investment patterns, according to a recent study by the Bruegel think tank.
A recent report by the European Central Bank also pointed to growing restrictions on labour mobility as a source of economic inefficiency and a potential threat to the stability of the euro. Thus greater market efficiency, lower consumer costs and further employment growth all remain goals of an expanded single European market – and all are threatened by a resurgence of “economic patriotism”.

If the economic cost of failure is high, the political costs would be greater still. The single market is the foundation upon which the European project is built. Many of the tasks that the EU now undertakes, and many powers it has assumed, are justified explicitly by the need for the single market to succeed. As political leaders conduct abstract debates about the constitution and enlargement, they ignore the steady erosion of the EU’s foundations at their peril.

What happens when businesses that restructured operations to take advantage of ‘Europe’ start to question the existence of the single market? If we reach that point, then the rationale for economic integration itself might be called into question. And, if people lose faith in the EU’s ability to manage its own single market, where will this mistrust end? When national leaders subvert the single market for short term gain, they are playing a very dangerous game. The Union can survive without a constitution. It cannot live without the single market.

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