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# EUROPEAN UNION AND THE CHALLENGES OF GLOBALIZATION

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## **Good news and not so good news: EU in search of itself**

One may say that the European Union is a success story: it is growing and in 2004 it witnessed the most significant enlargement in its history up to now – 10 new countries have become members; two other new countries – Romania and Bulgaria – are ready to join the Union and they will most probably access the community by January 1, 2007; after some difficulties, during the autumn of 2005, the accession negotiation with Turkey has started. At the same time, in many booklets and in the articles of some hasty journalists the European Union is presented as the largest economic block in the world as result of an arithmetic operation of adding the surface, the size of population and the GDP of the member countries. Despite the hardships encountered by the Constitutional Treaty, many people speak about a European Constitution and about political union as things that already exist or are anyway well within reach.

Beyond these positive and encouraging facts the European Union seems to be confronted with a weakness with no self-evident cause, with an erosion of its future position: quite often the future seems to be a menace for the European Union. Some examples may substantiate this statement. Thus, the much debated Lisbon Agenda which boasted with pride at the beginning of 2000 that by the end of the decade the European Union will become the most competitive area in the world has proven to be a failure with no hope of redress – the economic growth is very low or even close to zero in the main economies like France, Germany or Italy; the unemployment reached in 2005 19 million and during the time span of a decade the ratio employed/retired will drop from 4 to 1 to only 2 to 1; demography is also a difficult problem to solve and determines for the European Union social and financial problems which can only deepen in the years and decades to come; from a technological point of view the European Union is lagging behind USA and Japan; so far as consumer goods are concerned the competition from China and more recently India, as well as from some other countries seems to be without solution and raise again the specter of protectionism in the world trade arena.

The two aspects mentioned above lead to the idea that at present the mood of the European Union is characterized by dualism and the balance seems to be condemned to instability in the long run. The cause responsible for this situation is globalization which substantially changes the rules of the game: in a nutshell, in the globalized context the new technologies enable that everything can be produced everywhere and everybody can compete with everybody. For the moment, EU seems ill prepared to live with this reality.

In fact, in the globalized economy EU seems to be sandwiched: the lower layer is represented by countries like China, India and other emerging economies which can not be competed in case of standard consumer goods; the upper layer is represented by USA,

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Japan and other innovative competitors which are well ahead EU in case of high technology products and services.

### **EU, globalization and protectionism**

As result of this situation the old world hierarchies were destroyed and some examples can be suggestive:

- in the past 20 years the Chinese economy has grown every year by an average of 9 % and the Indian economy by 6 %. The European Union massively exports on these markets but the imports increase faster. The economies of the European Union which rely more on services are less affected than the ones which rely on industrial activities.<sup>1</sup>

- after 1992 the world trade has increased in annual rhythms of more than 8 % and it witnessed the emergence of new trade giants. Thus, 20 years ago only 10 % of the manufactured goods were made in developing countries. Much different from this situation, in 2020 only China and India will make 50 % of the manufactured goods of the world. In 2004 the weight of China in world trade with manufactured goods exceeded that of Japan. Other data of interest: the annual shoes production of the European Union with 25 member countries is produced by China in 6 days; in 2010 the funds allocated to research in China will exceed those of the EU under the circumstances in which in the past years the research investments of China grew by 20 % every year. At the same time the Indian universities produce about 250 thousand engineers every year.

All these global developments have determined in the EU-15 numerous fears and generated sometimes a rejection reaction or a tendency of isolation. In the EU – 15 the reactions were directed towards all potential competitors, even against member countries. Under stress companies and politicians have had the tendency to look back to the nation state as a sort of shelter of last resort. Some examples are again of help: in 2005 France and Denmark have rejected by referendum the project of the Constitutional Treaty because that seemed to open even more the national entities within EU and place decision levers more outside nation states; also in 2005 France and Germany rejected the plans for liberalization of the services for fear of an invasion from the low wage workers from Central and Eastern Europe; the representatives of the textile industries from France, Spain and Italy have requested with ardor the re-instatement of the textile quotas for the imports from China, when a decade ago the representatives of the developed countries envisaged the elimination of these quotas by January 1, 2005.

More interesting and even more worrisome, France has started to take position even against the free movement of capital by rejecting the possibility that PepsiCo could take over Danone and by announcing an unimaginable thing – the preparation of a list of 10 strategic sectors which they intend to protect against the possibility of acquisition by foreign investors.<sup>2</sup>

During the spring of 2006 this protectionist attitude emerged also in the field of energy. And this time the reaction of some Western European countries was against the

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<sup>1</sup> Liam Halligan, "The UK failed the globalization challenge", The Telegraph, 12 September 2005.

<sup>2</sup> Graham Bowley, News Analysis: Globalization drives a wedge into EU, International Herald Tribune, 23 October, 2005.

intention of Russian companies to take over energy companies in EU countries. But this time, the negotiation EU position is not so strong because Western countries do need Russian energy. And Russians do have other options for selling their energy to big consumers like China or USA. This situation makes again EU countries learn about globalization the hard way.

### **Can EU change its paradigm?**

Such reactions like those mentioned above do not have to be over-estimated. The European Union has anyway a number of ace cards which can be used in order to respond to the challenges of globalization: the existence of the economic and monetary union, the new approaches resulting from the reform of the Lisbon Agenda, the existence of the largest trade block in the world. These ace cards cannot be transformed into real advantages but by a concerted action from the part of all member countries. And also by a much more pragmatic approach than up to now in the design and implementation of EU policies.

The main problem is for all practical purposes a change of paradigm. The combination of free trade regime within Europe and protectionism in relation with the rest of the world has worked successfully as long as Europe could dictate the terms of trade. In the current stage of globalization this combination could no longer work. The interests of the European Union prevents the further application of this paradigm. If we only refer to the experience of 2005, what would be the sense for the European Union to block the textile imports from China worth 100 million Euro when it receives from China orders for Airbus planes for about 3 billion Euro ?

The problems of the European Union does not refer in any way to putting into question its existence. It is rather a problem which refers to direction, purpose, sense<sup>1</sup>. Questions like this are asked: Which is the sense of the European project ? Where is the European Union heading to ? Which is the current role of the European Union ?

Another thing which is clearly needed by the European Union is a better communication with the citizens of the member countries. The main message to be sent across would be that: „ Globalization is not something that China imposes on us but something created by us. People must be informed that globalization is our policy.”<sup>2</sup> The need to improve the communication with citizens results also from the fact that if 20 years ago about two thirds of citizens agreed on their country membership to the EU, in 2005 this percentage was of only 50 %.

The paradigm of history as a continuous improvement has to be changed. The paradigm of a future which is not necessarily better but which is necessarily different has to be presented to all EU citizens, young or old. But who has the courage to tell the EU – 15 citizens this truth ?

In order to respond to these challenges the leaders of the EU member countries have met at Hampton Court in October 2005 for debating the hottest problem of the moment: how to maintain what was achieved in 60 years, starting 1945, against the challenges such

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<sup>1</sup> Douglas Alexander, Europe in a Global Age, The Foreign Policy Centre 49 Chalton Street London NW1 1HY United Kingdom, 2005.

<sup>2</sup> Gunter Verheugen, vice president of the European Commission, June 2005

as the growing competition from the part of China and India, the increase of energy prices and the increase of the age of European population<sup>1</sup>.

The analysis of the historical evolution of European countries and of the European Union itself indicates a number of characteristics which requires specific solutions for Europe. The European model by which we mean the elements common for all European countries is a model based on the social market economy. The public sector is much more present in Europe than in the USA or in Asia and this fact is accompanied by a tradition of three party dialogue including government, patronates and trade unions. It is clear that European solutions cannot be found outside this frame of reference.

The problems facing EU in the context of globalization are structural and they are mainly the following<sup>2</sup>:

- low levels of employment and persistent high levels of unemployment;
- weaknesses of the education and research system. It is estimated that two thirds of the differences in the living standards between the USA and the EU are due to differences in productivity. In this context France proposed to the European Investment Bank to provide 10 billion Euro until 2013 for research and innovation projects<sup>3</sup>;
- the barriers for entering and exiting the labor market are too high compared to the situation in other parts of the globe;
- the gaps between the rich and poor is considerable both within member countries and among these countries.

If the aspects mentioned above refer mostly to the internal causes of the difficulties in competitiveness of the European Union, there are also other causes which are outside the Union:

- the globalization of the financial markets and the increase of the volume of foreign direct investment flows. These developments allowed for the rapid economic growth of other areas of the globe which became strong competitors;
- the opening of the markets and the communication technologies favored the economic growth in new areas of the globe;
- the differences in the labor costs favored the development of the countries with low costs. From this point of view the European Union cannot compete but by increase of productivity and stimulation of innovation;
- the increase of the world demand for energy correlated with a rigid offer raise problems in the long run. In 25 years the European Union will import 90 % of its energy needs. This fact will require more efforts for the increase of energy efficiency and for the development of new energy sources. The European Union should, among other measures, to secure a coordination of its policies in the field of energy given the fact that up to now many major actions, such as the relations in the field of energy with the Russian

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<sup>1</sup> Timothy Garton Ash, Europe needs 'experimental lab' for success, The Asahi Shimbun, 11/09/2005.

<sup>2</sup> Commission Of The European Communities, European values in the globalised world, Communication From The Commission To The European Parliament, The Council, The European Economic And Social Committee And The Committee Of The Regions, COM(2005) 525 final, Brussels, 20.10.2005

<sup>3</sup> Radio Free Europe, EU: Bloc Tackles Thorny Issue Of Globalization Thursday, 27 October 2005.

Federation, has taken place at a bilateral level with the participation of France, Germany, Italy or Great Britain.

### **The need for a long term, large scale partnership in Europe**

The dimension of the problems mentioned above due to their global sphere of content and due to the fact that they will persist for many decades to come require large scale solutions which will imply at the same time the institutions of the European Union, the governments and the European citizens.

At an individual level these solutions will imply a new attitude towards labor, and at the level of social systems these will have to imply of a new attitude towards people.

In order to face the challenges of globalization the European Union will have to finalize what it already began and to add new dimensions of its programmes:

- EU will have to complete the single market with the dimensions regarding services, telecommunications, energy, financial services;
- EU will have to further liberalize its markets and to secure the observance of competition rules;
- EU will have to encourage the entrepreneurs and the companies by means of flexible and dynamic market rules;
- EU will have to improve the quality of business environment;
- EU will have to advocate for the opening of other markets for products made in the EU;
- EU will have to improve the European economic governance and the coordination of the social and economic policies.

Beyond all these options the European Union will have probably to give up some of its extravagances which now erode its position in the global competition. Examples are easy to be found: the European Parliament keeps commuting between two buildings in Brussels and Strasbourg at an annual cost of 200 million Euro. It is not surprising that there were proposals that envisaged the re-allocation of the modern buildings in Strasbourg and the amounts related to this commuting for the scientific research, an area where the European Union has many things to recover. To make things worse, in April 2006 it was just revealed that the European taxpayers paid for many years more than 2 million Euro per year in excess than normal renting rates for the European Parliament premises.

### **EU, globalization and enlargement: can EU manage diversity ?**

Because globalization is an all pervasive phenomenon, it can be also found in the EU enlargement towards Central and Eastern Europe. From an economic point of view enlargement can be seen as a solution for improving the chances of EU in the global competition. For one thing, the enlargement helps Western Europe companies to lower costs. For another, enlargement brings to the same Western European countries markets and economies of scale.

It is very simple to look at the trade balances with the EU of all Central and Eastern European countries after 1990 to see that the old trade theories are still valid: if countries with different levels of development are doing trade, the more developed ones record

excedents just because the prices of goods and services with higher value added grow faster than prices of goods and services with lower value added. In this context the EU15 exports to new member states have risen from 56% in 1993 to 62% in 2005 while imports from new member states have risen by from 5% to 13% in the same period.

The European Commission said at the beginning of May 2006 in a report on the economic impact of the Union's biggest expansion ever that the EU's 2004 enlargement has proven an "economic success" for both the new and the old member states.

The report stated that this enlargement of the EU acted as a catalyst for economic dynamism and modernisation, helping all 25 countries face the challenges of globalisation. In the words of EU Economic and Monetary Affairs Commissioner Joaquin Almunia: "The re-unification of Europe is not only a huge political achievement it is also an economic success,". "We all win as the citizens in the new member states see their standards of living increasing. We win because companies in the EU take advantage of new business opportunities, become more efficient and, therefore, more competitive on the world scene. The enlargement is helping the EU cope better with the new world economic order."<sup>1</sup>

Despite these positive things that stimulated and supported the enlargement towards Central and Eastern Europe, EU is confronted with some problems due to enlargement. And these problems are just smaller scale versions of the problems determined by globalization. The most important one is diversity. Diversity has been present from the very beginning: the six founding countries were not identical. But they were indeed similar. The enlargement of 2004 brought with it an unprecedented diversity: levels of development, culture, history, the centrally planned economy experience, to mention just some of them. The forthcoming enlargement of 2007 with Romania and Bulgaria will only amplify this diversity. And then the Western Balkans will continue to amplify diversity.

For the moment EU has no operational concept for dealing with that diversity. In recent times EU has been compared with a "voluntary empire", meaning by that an empire in which new countries and territories are added because they want to, not because they are compelled to. In our opinion this name has a lot of truth in it, but it needs and adequate system of institutions and rules in order to become functional.

An example will be useful: in 2006 Romania has had a GDP level of about 30 % of EU-25 average. At such a level Romania is a developing country which needs development policies specific for a developing country. But for the moment there is no Directorate General for developing countries in Brussels and the adoption of the *acquis* in the sense of overall implementation of the same rules in Germany and in Romania might, just might, be as efficient as the IMF standard recommendations for Latin American countries.

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<sup>1</sup> Commission says 2004 EU enlargement an "economic success", EurActiv - 04/05/06; EUROPA, AFP, AFX, AP, EUobserver, EUpolitix, Finfacts - 03/05/06.

## **Towards an EU with variable geometry?**

Is there a solution for that ? In our opinion that solution would be accepting and managing diversity. This is easier said than done but from a logical perspective this management of diversity would imply an EU with variable geometry. That would imply a core zone of common rules and institutions including areas like trade, capital flows, labor, partially environment.

Beyond that area of common denominator rules and institutions would be just a dynamic world of associations of those member countries willing and able. Such an approach is not a setback from the present state of play in the EU. It does not mean in any way that EU is disintegrating. It just mean that those countries (or even regions) with common interests and levels of development can move forward faster implementing solutions adequate to their situation. If others find those solutions useful for them at a later stage they can join also. If some of the initial members of a group of further integration decide at a certain point in time to step back they would be able to do so according to certain procedures. And all could be done having a permanent set of common denominator rules and institutions that are permanently maintained. In time, this set of common denominator rules and institutions can be enlarged according to the new realities of every period.

Such an approach would be based on the idea that in the EU of today and tomorrow diversity will be the rule and not the exception. This approach would try to capitalize diversity instead of regarding it as an exception. Countries in the new EU do have different levels of development, different social patterns, different values based on different historical experience. The new idea proposed here is not to regard this situation as an obstacle to further EU integration, but rather to determine a new approach to EU integration. European countries can do a lot of things together accepting they are different and using their differences instead of trying to be as similar as possible.