

STUDENTS BRIEF

SCOTLAND'S RELATIONSHIP WITH THE EUROPEAN ECONOMIC COMMUNITY (EEC)

By Neil Fraser

In 1973 the United Kingdom joined the European Economic Community (see Box 1) and, despite continuing protests from certain groups, has remained a member. As a region of the UK much of Scotland's relationship with the EEC has to be viewed in a British context. However as a peripheral region of both the UK and the EEC, certain aspects of membership have particularly important effects on Scotland. While much of the impetus to form the Community arose for political reasons, the principal features are all based on economics.

The central characteristic of the EEC is the customs union and this provides the foundation for other policies designed to create a common market. Two conditions must be fulfilled in a customs union;

- (i) Members do not charge any customs duties or restrict the quantity of goods traded with each other.
- (ii) A common external customs tariff is applied to countries outwith the union

Much progress has been made in achieving these conditions, although they have yet to be fully attained. Anyone who has travelled within the Community will know that crossing borders still involves going through customs. However, such checks are now minimal and the remaining obstacles to wholly free trade at least allow travellers to buy duty-free tobacco, wine, spirits and perfume! Despite the remaining anomalies, it is claimed that the creation of a customs union has greatly stimulated trade between Community members.

Certainly official British statistics support this view. The value of British exports to the EEC grew by 224% between 1975 and 1980, while trade to other areas increased by only 103%. Statistics of Scottish trade are not produced by the government as we are included in the British figures. However, an independent organisation, the Scottish Council Research Institute, has surveyed Scottish firms to establish who their principal trading partners are. Table 1 shows that the EEC has grown in importance as an export market.

TABLE 1 DESTINATION OF SCOTTISH EXPORTS (PER CENT)

Year	EEC	North America	Other
1974	30.1	16.7	53.2
1977	38.2	13.6	48.2
1980	40.4	12.4	47.2

Source: Scottish Council Research Institute

While the EEC has grown in importance as an export market, we now also import more goods from Community countries. The trade gap has, however, been narrowing with the deficit for Britain's Community trade equalling £165m in 1980 compared with £2,536m in 1975. Certainly the size of the Community economy provides fruitful markets, and while many economists and politicians applaud these trends, some regret the shift away from our traditional trading partners in North American and Commonwealth countries. However not everyone believes that increased trade is beneficial. Cheap imports have penetrated some markets previously supplied by British producers and EEC membership prevents Britain from introducing import controls. Some politicians and economists see import controls as a necessary step to rebuild British industry.

Box 1 The European Economic Community.

The European Economic Community (EEC) was formed by the Treaty of Rome in 1958. Initially there were six members - West Germany, France, Italy, Belgium, Netherlands, and Luxembourg. In 1973 they were joined by the United Kingdom, the Republic of Ireland and Denmark. Greece joined in 1981 and negotiations are currently under way regarding the entry of Spain and Portugal. The economies of these countries vary considerably and certain features are outlined below.

	Population 1979 (m)	Gross Domestic Product 1980 (1975 prices \$b)	Unemployment* % Dec. 1981
Belgium	10.2	70.0	12.9
Luxembourg	0.4	2.6	1.3
Denmark	5.1	43.2	9.5
France	53.2	397.0	8.9
West Germany	61.4	501.4	6.5
Greece	9.4	25.5	1.8
Ireland	3.4	9.6	11.5
Netherlands	14.0	94.2	9.1
Italy	56.9	232.0	9.6
UK	55.9	249.8	11.3
EEC	269.9	1625.3	9.0

*The unemployment figures are compiled in different ways and are not directly comparable.

Source: Financial Times and EEC Statistics Office

The Community also engages in a number of other activities outwith the economic sphere. There are a number of institutions such as the European Parliament and European Court of Justice which now influence our administrative and legal affairs. The ten EEC countries are also trying to develop a common approach to various international issues like Poland and the Middle East. For some the EEC is seen an important counterweight to the USA and Soviet Union, while others feel the Common Market infringes on our own national sovereignty and political processes.

Linked to the growth of trade with Europe is the increased attractiveness of Scotland as a location to investors from outwith the Community. Regional assistance, low labour costs and lack of customs barriers are strong inducements to firms seeking a base within Europe. Several American firms have stated that access to European markets has been an important factor in their decision to locate in Scotland.

The Community Budget

The European Economic Community has a wide range of activities within which it operates and has developed policies in agriculture, industrial and regional support, social matters, energy and research. Consequently the Community spends large sums of money and must raise the necessary revenue from its members. The Community Budget has caused much controversy with the UK in particular, arguing that it pays a disproportionately high share.

In 1981 the EEC spent £10.6 billion and the breakdown of expenditure is shown in Table 2. It is estimated that EEC membership cost Britain £127m net in 1981, a significant reduction from the 1980 figure of £1billion.

Table 2 Composition of EEC Expenditure 1981

	%
Agriculture	67.4
Regional	10.2
Social	3.5
Research, Energy, Industry, Transport	1.6
Refunds and Reserves	7.9
Development Cooperation and non-member countries	4.0
Administration & Miscellaneous	5.4
TOTAL	100

Source: Directory of the European Commission

Despite Britain's severe economic problems and lower standards of living than many other EEC members, the structure of the budget has led to Britain being a major contributor. The controversy centres around the vast sums spent on agricultural policy which the UK benefits little from. Similarly, despite Scotland's poor economic performance it is likely that a net contribution is made to the EEC budget. While precise figures are not available, an estimate made by the Fraser of Allander Institute suggests that in 1978 Scotland paid £34m more into the budget than was received. Scotland does relatively better than some other regions of the UK as we are eligible for more forms of regional assistance. Political negotiations are continuing in an attempt to rectify Britain's budget problems but without fundamental reform disproportionate sums will continue to be paid throughout the 1980's.

The Common Agriculture Policy forms the centerpiece of the Community budget and is the cause of much intra-Community arguments. The justification for the policy is that it provides essential stability to food supplies and as such is a valuable insurance in an unpredictable world. The policy is based on a system of price support. When market prices on specified agricultural products fall below a certain agreed rate, the Community will intervene to buy the produce at the agreed price or refund to the farmer the difference between the actual and agreed prices. Coupled to this is a system of exchange rates known as 'green rates'. Because of fluctuations in the value of European currencies, green rates were introduced to provide fixed values to the producer when exporting and thereby provide an element of stability. Critics of the scheme argue that it is excessively bureaucratic and expensive and that farmers benefit at the expense of consumers. In addition, price support has stimulated production above market demand resulting in overproduction and the creation of 'lakes' and 'mountains' of certain products. While the faults of the CAP are widely recognised the Community cannot agree on a more suitable system. Indeed some countries have argued that alternative policies would have even greater faults and that the Common Agricultural Policy should be maintained.

The reduction of regional inequalities is an important aim of the EEC but the task is difficult given the diversity of economic activity, people and climate in the regions of Europe. Regional problems may be classified under two categories: agricultural and industrial. Scotland suffers from both with the Central Belt displaying a decline in traditional industrial activity, while the Highlands and Islands display under employment in agriculture and high outward migration (some oil-affected areas excepted). While the principal responsibility for regional problems rests with individual countries, the Community has developed a number of policies and acted to coordinate the various national schemes. Table 3 outlines the allocations made to Scotland from EEC sources since Britain joined the Community.

The European Regional Development Fund (ERDF) set up in 1975 is the principal instrument of regional policy within the Community. The Fund provides grants to industrial project and to infrastructure projects. The industrial grants are paid to projects which are economically sound, already receive State regional aid schemes and either help to create at least ten new jobs or preserve ten existing jobs. Recent Scottish beneficiaries have been whisky distillers and manufacturers of data processing equipment. Infrastructure investment such as roads, sewerage and harbours can attract a grant of up to 30% of the total outlay. This is paid on projects carried out by public authorities, in particular the Regional and District Councils. These expenditures cannot, however, be viewed as a net addition to the package of incentives offered by the UK government. The ERDF payments are made to the Treasury who then pass them on to industry and local authorities but consequently reduce grants funded by British regional policy. Even although this practice is common throughout Europe, it nevertheless detracts from the potency of the scheme.

The European Social Fund (ESF) is mainly intended to assist the operation of the labour market through training schemes and by assisting mobility. Scotland has benefited in respect of particular projects and also through the general assistance given by the fund to bodies such as the Manpower Services Commission which operates throughout the UK. The European Coal and Steel Community (ECSC) gives grants and loans mainly to schemes involving these industries. Since both of these industries have a substantial presence in Scotland we have received a relatively large share of the assistance available. The European Investment Bank (EIB) finances up to 50%

Table 3 Identified Financial Allocations From EEC Sources in Respect of Projects in Scotland £million

	European Regional Development Fund	European Agriculture Guidance & Guarantee Fund (FEOGA)	European Social Fund ¹	European Investment Bank: Loans ²
1973	-	1.91	5.4	-
1974	-	2.233	5.4	24.8
1975	9.852	2.964	8.5	96.9
1976	14.607	8.285	8.5	66.2
1977	13.928	7.821	15.1	103.
1978	24.826	9.25	14.85	63.4
1979	37.133	5.759	29.0	62.8
1980 (to Nov)	21.360	4.636	5.23	70.5

¹The figures given are estimates of the Scottish share of UK payments.

²Figures refer to specific Scottish projects. There have also been a number of loans for UK projects where the share of expenditure in Scotland cannot be identified with any precision.

Source: Scottish Economic Bulletin, No 22, Spring 1981

of the cost of investment at preferential rates of interest on a wide range of projects, the loans normally maturing between 7 and 12 years. Large schemes such as the Hunterston terminal and the Meggat reservoir have benefited from these loans. It must be remembered that they are loans not grants, and that they have to be repaid. Therefore the current benefit of these loans is the differential between the interest which was actually paid and that which would have been paid on the UK capital market on all outstanding loans. Finally, the European Agricultural Guidance and Guarantee Fund (FEOGA) provides grants, through a number of different schemes, to Scottish agriculture. These range from special assistance for hillfarmers to financial inducements to reduce milk production.

The above expenditure of programmes of the European Community must, of course, be financed. EEC revenue is derived from three principal sources:

(1) Agricultural Levies - these are raised from 'third country' agricultural exports to the Community e.g. New Zealand lamb or American wheat. The sums raised in this manner are unpredictable. The amount depends on the common threshold prices, world market prices and currency fluctuations.

- (2) Customs Duties - all of these are payable to the Community. These are dependent on the structure of tariffs and the real and nominal growth in imports.
- (3) VAT Contributions - Up to 1% of each countries' VAT revenues are paid to the EEC. This is the most flexible source of finance as the rate can be adjusted to compensate for shortfalls in revenue from duties and levies.

There are ongoing discussions as to how the growing EEC budget should be financed, particularly as the VAT contributions are close to the 1% limit. Radical changes are unlikely given the difficulties surrounding negotiations between ten countries with separate interests.

The European Monetary System (EMS)

The movement towards a full customs union and the growing importance of the Community budget have initiated moves towards a monetary union. In its most extreme form monetary union would result in a single European currency with centralized economic decision-making. Such a possibility is unlikely in the foreseeable future with each member keen to retain their own currency. However given the interdependence of the Community, a system has developed in an attempt to harmonize financial and monetary activities.

This is known as the European Monetary System which is designed to reduce exchange fluctuations between Community members. The EMS is an exchange rate mechanism where each currency must trade within fixed but adjustable rates. If any country has problems remaining within the agreed bands, support will be given by the Central Banks of the other participants. It is felt that this reduces uncertainty in trade and payments within the Community and provides a framework for closer economic policy coordination. However Britain is not yet a member of the system despite the fact that all other countries have participated since its inception in March 1979. The official reason for this is that membership of the system is incompatible with the governments domestic monetary policy and that when the supply of money and thence inflation is brought under control, it will be possible to join the system.

Fishing and the EEC

The Community has, for a number of years, been trying to develop a Common Fisheries Policy (CFP). This has met with limited success and the deliberations have met with much antagonism from Scottish fishermen. The fishing industry in Scotland employs around 17,000 people and its influence dominates certain communities and regions. This influence is both direct through catching and indirect through processing, retailing, boat-building etc. Compared to the rest of UK, Scotland relies heavily on fishing and accounted for 51% of landings by value in 1980. The fishing industry has, however, contracted in recent years. As most of this decline has occurred since Britain joined the Community many fishermen feel that this is more than a coincidence.

The foundation for a CFP was laid in 1970 when a regulation was passed requiring equal access to all fishing grounds under the jurisdiction of the member countries. On entering the Community the UK was given special conditions with all waters within a six mile limit and some within a twelve mile limit exclusive to British fishermen. On 1 Jan 1977 the EEC created the European Economic Zone which set 200 mile fishing limits in the North Sea and North Atlantic. This restriction regulated other countries but did not affect the rights of vessels from other EEC countries to fish in UK waters. The special conditions negotiated by Britain expire at the end of 1982 and disputes continue regarding future access to British waters. The British fishermen want to restrict access to UK waters, as they contain about two-thirds of the total catch available in EEC waters. The fishing industry argue that the UK should be allocated at least 45% of the total allowable catches, whereas Commission proposals would give only 31% to the UK. Clearly the outcome will have important influences on Scotland and in particular the small communities heavily dependent on fishing.

Conclusions

As can be seen from this Brief the activities of the European Economic Community affect the Scottish economy in many ways. The question as to whether or not Scotland is better or worse off as a consequence is difficult to answer. Certainly the budgetary arrangements do not result in the massive inflow of cash some politicians claim. Similarly, most fishermen feel that open access to British waters is a direct threat to their livelihood. On the other hand, many businessmen have found the European market very profitable and have been able to maintain or expand their workforce as a consequence. Employment has also been created by incoming companies who see Scotland as the ideal location for a European base. To draw up a balance sheet is impossible, while the non-economic activities and influences of the Community add further difficulties in assessing the full costs and benefits of membership. Personal interests and the nature of an individual's employment are therefore the most likely determinants of whether or not someone is for or against continued membership of the EEC.

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The serious newspapers and the Economist all regularly examine issues related to the EEC. Govt. publications such as British Business, Scottish Economic Bulletin etc give statistics regarding trade developments and budgetary issues. This Commentary regularly reports and comments on issues related to the EEC.

European Communities Commission publish a series of Background Reports on various issues regarding development in the EEC.