European Economic Integration I

Lecture 3

7 October 2024

Objectives of Lecture

1. Defining Economic Integration
2. Explaining Different Stages of Economic Integration
3. Inspecting Key Stages in European Economic Integration
4. Determining the Role of Treaties in Deepening EU Economic Integration

Economic Integration

Economic integration refers to the process by which

- countries or regions reduce barriers to trade and investment
- increase economic cooperation
- leading to a greater interdependence of their economies.

Economic Integration

The theory of economic integration proposed by Bela Balassa provides a systematic framework for analyzing the gradual stages through which nations can evolve in their economic collaboration.

1. Preferential Trade Agreement (PTA)
2. Free Trade Area (FTA)
3. Custom Union
4. Common Market
5. Economic Union

1) Preferential Trade Agreement (PTA):

- **Definition:** A PTA is an international treaty with restrictive membership and including any articles that
  - (i) apply only to its members and
  - (ii) aim to secure or increase their respective market access

- In this initial stage, countries reduce tariffs on certain goods traded among themselves while maintaining higher tariffs on imports from non-member countries.

- This step aims to enhance trade relationships without fully committing to more extensive integration.

- *Example*: US and Nepal Trade Preferences (30.12.2016 - 01.12.2025)

2) Free Trade Area (FTA):

- **Definition:** A Free trade Area (FTA) is an agreement between two or more countries
  - (i) where the countries agree on certain obligations that affect trade in goods and services
  - (ii) and protections for investors and intellectual property rights.
- Countries eliminate tariffs and other trade barriers on goods and services
- Each member retains its own external tariffs against non-member countries.
- This stage increases market access and competition but does not involve coordinated external trade policies.

2) Free Trade Area (FTA):

- *Advantageous*: Increased efficiency in trade can lead to lower prices for consumers and greater variety in products
- *Disadvantageous*: The lack of a common external tariff may complicate trade relations with non-members.
- *Example*: The North American Free Trade Agreement (NAFTA) (Canada, Mexico, US)

Economic Integration

3) Custom Union:

- **Definition:** Customs unions are groups of countries that
  - (i) apply one common system of procedures, rules and tariffs for imports, exports and transiting goods
  - (ii) countries participating in customs unions share common trade policies.

- A customs union combines the features of an FTA with a common external tariff (CET) on imports from non-member countries

- It eliminates internal tariffs and establishes uniform external tariffs

3) Custom Union:

- *Advantageous*: A customs union reduces trade barriers and enhances economic cooperation, allowing for more efficient allocation of resources.
- *Disadvantageous*: it may limit the flexibility of individual countries to set their own external trade policies
- *Example*: Southern Common Market (MERCOSUR) (Argentina, Bolivia, Brazil, Paraguay and Uruguay)

4) Common (Single) Market:

- **Definition:** Common Markets refer to an area without internal frontiers where
  - (i) the free movement of factors of production is ensured
  - (ii) common policies on product regulation is established.
- A common market extends beyond a customs union by allowing not only tariff-free trade and a common external tariff but also the free movement of goods, services, labor, and capital among member countries.

4) Common (Single) Market:

- *Advantageous:* A common market allows for the free movement of goods, services, capital, and labor across member states

- *Disadvantageous:* This stage necessitates not only the removal of tariffs but also the harmonization of regulations and policies to facilitate easier movement of resources.

- *Example:* The European Economic Area (EEA).

5) Economic Union

- **Definition:** An economic union denotes a higher level of economic integration that
  - (i) goes beyond a common market
  - (ii) wherein member states agree to harmonize their economic policies, including monetary, fiscal, and regulatory frameworks
- The most advanced stage, an economic union combines a common market with unified economic policies, including coordinated fiscal and monetary policies
- This often leads to the establishment of a common currency and deeper political integration among member states.

5) Economic Union:

- *Advantageous:* trade creation, increasing employment and efficiency, potentially adopting common currency, boosting competitiveness, and strengthening political ties
- *Disadvantageous:* It requires harmonization of a wide range of policies, including taxation and social regulations.
- *Example:* European Economic and Monetary Union

1) European Coal and Steel Community:

- The governments of the six European countries (France, Germany, Italy, Belgium, the Netherlands, and Luxembourg) opened negotiations and on 18 April 1951 signed the Treaty of Paris, creating the European Coal and Steel Community (ECSC).
- It was allowed to reduce tariff barriers, abolish subsidies, fix prices, and raise money by imposing levies on steel and coal production.
- The ECSC was notable for being the first supranational organization to which European governments had transferred significant powers

European Integration: Stages

2) European Economic Community:

- A new round of negotiations led to the signing in March 1957 of the two Treaties of Rome,
  - (i) one creating the European Economic Community (EEC)
  - (ii) and the other creating the European Atomic Energy Community (Euratom)
- both of which came into existence in January 1958.

European Integration: Stages

2) European Economic Community:

- The EEC Treaty committed the six to the creation of a common market within 12 years (end of 1968) by removing all restrictions on the internal movement of people, money and services;
- the setting of a common external tariff for goods coming into the EEC;
- and the development of common agricultural, trade and transport policies.

European Integration: Stages

2) European Economic Community:

- Although the 12-year deadline for the creation of a common market was not met,
- internal tariffs fell quickly enough to allow the Six to agree a common external tariff in July 1968, and to declare an industrial customs union.

3) Custom Union:

- An effort had been made by Community leaders in 1969–70 to pave the way to economic and monetary union (EMU) by controlling fluctuations in the value of their currencies.
- However, this collapsed when the United States
  - (i) wrestling with national debt problems arising in part from the costs of the war in Vietnam
  - (ii) signaled the end of the Bretton Woods system of fixed exchange rates by ending the convertibility of the US dollar with gold and placing a surcharge on imports.

European Integration: Stages

3) Custom Union:

- In 1979, a new initiative was launched in the form of the European Monetary System (EMS), based on an Exchange Rate Mechanism (ERM) that was again designed to control fluctuations in exchange rates

- European Commission president Jacques Delors took EMU a step further in 1989 with the elaboration of a three-stage plan aimed at fixing exchange rates in preparation for a single currency.

European Integration: Stages

4) European Single Market:

- The first major treaty changes since the Treaty of Rome came into force in July 1987 with the goal of completing all requirements for the single market by 31 December 1992.

- This would be achieved by removing all remaining barriers to the free movement of
  - people, money, goods and services,
  - including customs and passport controls at internal borders,
  - different levels of indirect taxation, and conflicting standards, laws and qualifications.

4) European Single Market:

- By 1986 the EEC had become known simply as the European Community (EC).
- Its 12 member states had a combined population of 322 million and accounted for just over one-fifth of all world trade.
- The EC had its own administrative structure and an independent body of law, and its citizens had direct (but limited) representation through the European Parliament.

European Integration: Stages

4) European Single Market: *The Changes brought by the Single European Act*

1. Internal passport and customs controls were eased or lifted
2. Banks and companies could do business throughout the Community
3. Qualified EC residents faced few restrictions on living, working, banking, and accessing pensions in any member country
4. EC competition policy was enhanced, breaking down monopolies in electricity and telecommunication sectors.
5. Community institutions were assigned responsibilities for new areas like the environment, research and development, and regional policy.

European Integration: Stages

4) European Single Market: *The Changes brought by the Single European Act*

6. Meetings of heads of government were granted legal status, and new powers were given to the Council of Ministers and the European Parliament.
7. It established economic and monetary union as an EC objective and promoted 'cohesion' to reduce the gap between richer and poorer regions.
8. It granted legal status to European Political Cooperation, enabling member states to coordinate more closely on foreign, defense, and security issues.
9. It granted new powers to the European Court of Justice and established a Court of First Instance to handle specific cases and reduce its workload.

European Integration: Stages

5) European Economic and Monetary Union:

- In 1990, a decision was made to draft the Maastricht Treaty, which was agreed upon at the European Council summit in December 1991 and signed in February 1992.
- The Maastricht Treaty established the framework for the European Economic and Monetary Union (EMU), aiming to create a single currency and a coordinated monetary policy among EU member states

European Integration: Stages

5) European Economic and Monetary union: *The Changes brought by the Maastricht Treaty*

1. To reach a political compromise, the Maastricht Treaty established three 'pillars' under the new label 'European Union': the first pillar was the European Community, while the second and third pillars focused on intergovernmental cooperation in Common Foreign and Security Policy (CFSP) and justice and home affairs.
2. The Jack Delors three-stage plan for monetary union was confirmed.
3. EU responsibility was extended into new policy areas such as consumer protection, public health policy, transport, education and social policy.

European Integration: Stages

5) European Economic and Monetary union: *The Changes brought by the Maastricht Treaty*

4. European citizens received new rights, including the ability to live in any EU country and to vote or run in local and European elections.
5. Greater intergovernmental cooperation on immigration and asylum was established, Europol was created to combat organized crime and drug trafficking, and regional funds for poorer EU states were increased.
6. The European Parliament was granted new powers, including a codecision procedure requiring a third reading for certain legislation before adoption by the Council of Ministers.

European Integration: Stages

5) European Economic and Monetary Union: *Copenhagen Criteria*

At its June 1993 meeting in Copenhagen, the European Council established the Copenhagen conditions, a formal set of requirements for EU membership that an applicant state must:

1. be democratic, with respect for human rights and the rule of law
2. have a viable free market economy and the ability to respond to market forces within the EU
3. be able to take on the obligations of the acquis communautaire (the body of laws and policies already adopted by the EU).

5) European Economic and Monetary Union: *Delors 3-stages Plan*

The Delors three-stage plan for monetary union consists of:

1. **Stage 1:** Free movement of capital and the establishment of a European Monetary Institute to prepare for monetary integration.
2. **Stage 2:** Establishment of a European Central Bank and the convergence of member states' economic policies, leading to the adoption of the euro.
3. **Stage 3:** Full implementation of a single currency (the euro) and the coordination of monetary policies among member states.

European Integration: Stages

The significance of Single European Act

- The essential purpose of the Single European Act (SEA) was to remove the remaining barriers to trade among the partner countries within the customs union established in 1958.

- Discriminatory regulations and taxation on foreign firms that make them less able to compete against domestic firms, customs and other border controls that increase cross-border transport costs and closed or restrictive bidding for public contracts.

The significance of Single European Act

- The SEA identified three areas of constraints that needed attention by EC competition policy:
  1. physical barriers, such as customs and border controls;
  2. technical barriers, such as product safety rules, public procurement policies, and limits on types of labor and capital flows;
  3. fiscal barriers, such as different tax rates and laws.
- Differences in taxation are at the heart of fiscal barriers. By treaty, each member state of the European Union is required to adopt a system of value-added taxation.

Enlargement of EU Member States

EU Member States Enlargement Timeline

Year	New Members	Total Members
1957	Belgium, France, Germany (West), Italy, Luxembourg, Netherlands	6
1973	Denmark, Ireland, United Kingdom	9
1981	Greece	10
1986	Portugal, Spain	12
1995	Austria, Finland, Sweden	15
2004	Cyprus, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovakia, Slovenia	25
2007	Bulgaria, Romania	27
2013	Croatia	28

Source: European Commission

Major EU Treaties and Milestones (Part 1)

Timeline of Major EU Treaties and Milestones

Year Signed	Year in Force	Name	Main Effects
1951	1952	Treaty of Paris	Created the European Coal and Steel Community. Expired 2002.
1957	1958	Treaties of Rome	Established the European Economic Community and the European Atomic Energy Community.
1968	1968	Customs Union	Established a customs union among member states, removing tariffs and allowing free trade (not a treaty).
1986	1987	Single European Act	Set the goal of completing the single market within five years.
1992	1993	Treaty on European Union (Maastricht)	Cleared the way for economic and monetary union, creating three pillars under the new EU.

Source: European Union

Major EU Treaties and Milestones (Part 2)

Timeline of Major EU Treaties and Milestones

Year Signed	Year in Force	Name	Main Effects
1997	1999	Treaty of Amsterdam	Introduced organizational changes and expanded EU policy responsibilities.
1999	1999	Emergence of the Euro	Launched the Euro as a common currency; established the European Central Bank.
2002	2002	Euro in Circulation	Euro banknotes and coins were introduced, replacing national currencies in many member states.
2001	2003	Treaty of Nice	Addressed unfinished business from the Amsterdam Treaty.
2004	-	Failed Treaty on the European Constitution	Intended to replace and consolidate all existing treaties, introducing significant institutional changes.
2007	2009	Treaty of Lisbon	Implemented most changes intended by the constitutional treaty.

Source: European Union