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EUROPEAN COMMUNITY MEMBERSHIP AS A POLICY CONSTRAINT:

THE CASE OF SPAIN

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Introduction

In this paper it is argued that the Spain's membership of the European Community (EC) since 1986 has limited the government's room to manoeuvre in central aspects of economic policy. It is further argued that these constraints, although the consequence of a decision (i.e. to enter the EC) freely taken, are nonetheless as rigid as any other set of constraints within which a national government operates. It is not argued that the Spanish case is necessarily applicable to all EC governments, although it is probably does apply in some degree to most; nor is it argued that the Spanish case is unique although there may be factors present in the Spanish case that make the constraints imposed by the EC more of a necessary evil in the Spanish case than in many other EC countries. Membership of the EC is not, of course, only about constraints: if it was, it might be a much less attractive place to be than it is. It is also about opportunities: the scope for broadening trade links, attracting investment, and playing a more significant role in West European politics are factors that balance the restrictive nature of EC membership. Nonetheless, it is argued in this paper that the constraints are more important for the domestic policy makers than the opportunities, if only because the constraints are perceived as the most productive context within which the opportunities can be delivered.

These constraints can be seen most effectively at work in the economic arena: trade, industrial development, unemployment, regional policy and social welfare. The underlying assumption is that economic sacrifices are the necessary backcloth against which political social and economic change can be most efficiently delivered. As we shall see later, public opinion tacitly supports the dichotomy between short term adversity and long term benefits, as it does between economic and political goals. Membership of the EC is clearly perceived as providing a new forum within which national policies are fashioned, not vice versa.

The impact of EC membership

Accession to the EC gave Spain virtually unrestricted access to a market that was fifteen times larger than its own. At the same time, its own highly protected market was now to be progressively exposed to imports from the rest of the EC. Up until EC entry imports had been curbed by quotas, by rates of taxation that effectively discriminated against imports, and by customs duties that were, on average, higher than in the rest of Western Europe. By 1989 almost 40 per cent of the difference between the Common External Tariff and the Spanish tariff level had been removed, and the discrepancy will have been totally removed by the end of the transition period in 1992. The introduction of VAT in 1986 automatically led to the abolition of turnover and border taxes that had hitherto favoured exports over imports.

The phased removal of tariffs has had an immediate and generally unfavourable effect on Spain's trade with the rest of the EC. As can be seen from Table 1, Spain's trade deficit with its EC partners has increased steadily since entry. There has also been trade diversion towards imports from the EC. The share of EC imports in total Spanish imports has risen from 50 per cent before accession to more than 66 per cent in 1989. Grain and other basic foodstuffs, for example, have traditionally been imported from the United States and Latin America, but the Common Agricultural Policy has necessitated the raising of tariffs on imports from those countries. In the case of food imports, Spain has had to raise tariffs to the level of the CET, with the result that whereas in 1985 78 per cent of Spain's food imports came from outside the EC, by 1989 only 55 per cent did. The share of food imports from the EC has doubled while the share from third countries has fallen. In food products, therefore, there are trade diversion effects that mean that Spain is importing food from more expensive suppliers.

Spain's rapid rise in imports is explained partly by the lowering of tariffs and partly by the increasing capital investment much of which is imported. The rise in the 'real' value of the peseta also explains the rise in imports which appear 'cheaper' than home-produced goods.

A study carried out for the Commission (1990) reveals the extent to which the removal of tariffs has weakened Spanish manufacturing competivity. As mentioned above, the removal of a high degree of protectionism of the Spanish economy has resulted in a serious worsening of the trade balance in manufactured products. The Commission study shows that those few industries which actually improved their export-import ratios after the reduction of tariffs (e.g. photographic processing, jewellery, aerospace equipment) were relatively unimportant in terms of employment. The overall picture is not very encouraging: only 12 out of 40 industries surveyed were judged to have a good trade performance after entry, but these 12 are less important in terms of value added and employment than those firms whose performance has become weaker (Commission 1990).

The European Monetary System

Spain has always had a liberal policy on capital flows into the country. Since EC entry in 1986, the peseta has appreciated in value as a result of inflows of investment capital and structural funds from the EC itself. Net transfers between the EC and Spain have risen from a shortfall of -8.4 bn dollars to a surplus of 162.6 bn dollars in 1989 (OECD 1990: 60). Investment in the Spanish economy nearly doubled in the first five years of EC membership; and a greater percentage comes from other EC countries than previously: up from 38.4 per cent of all foreign investment in 1984-5 to 52.0 per cent in 1986-9. The capital inflows have can be attributed partly to the reduced political risks since EC entry, partly to the liberalisation of employment law, and partly to the prospects for the Single Market in 1993. These prospects have encouraged other EC countries, and the United States, to invest in Spain rather than outside the EC since the rate of return on capital remains high in Spain. Nearly half the inward investment is in manufacturing and mining (42 per cent) but the financial sector (37 per cent) is an important runner-up.

In June 1989 the Spanish Government decided to enter the ERM with a fluctuation band of 6 per cent. The decision was taken on political rather than economic grounds, highlighting the government's commitment to Europe at the end of its first EC presidency. The result of this move was to add to the upward pressure on the peseta as investment in the Spanish economy became less vulnerable to exchange rate movements. To counteract the upward push of the peseta (it has been the strongest currency in the ERM since joining it) the Government has had to intervene to support the DM, and interest rate differentials between the peseta and all other ERM currencies have been reduced. The interest rate differential between the DM and the peseta, for example, fell from 8 per cent in June 1989 to 6.6 per cent in June 1990.

The conclusion of some kind of pact between the unions and the employers with the aim of promoting competitiveness, creating jobs, and reducing inflation. The Spanish Government knows that, in order to survive in the SEM, its inflation rate will have to converge downwards towards the EC average of 3.9 per cent (in 1990). If incomes cannot be moderated by government action, the constraints imposed by the peseta's position in the ERM, the main burden of adjustment will have to be borne by budgetary policy. In either case, the Government has very restricted room for manoeuvre; and its policies are essentially reactive within the EC context. Monetary policy has had topursue a twin objective internal demand restraint in the new era of exchange-rate stability, High interst rates plus the unlikelihood of a peserta depreciation have encouraged large inflows of of foreign investment. As exchange controls are progressively liberalised, the situation has become more acute, and as reforms of the whole financial system take place, monetary policy instruments become less effective.

Regional Development

The severity of Spain's regional problems is recognised by the fcat that most of Spain's territory (76 per cent) is designated as an Objective 1 region by the European Community. Objective 1 regions are defined as those having a per capita GDP that is less than 75 per cent of the Community average. Spain's Objective 1 regions are characterised generally by low productivity, demographic imbalances (regarding the age profile of the population), inadequate infrastructure, relatively high unemployment, water shortages and low levels of technological research. Among problems peculiar to specific regions, it is worth mentioning geographical isolation in the case of the Canary Islands, depopulation in Extremadura, weak economic growth in both Galicia and inland Andalusia, and problems of industrial conversion in the case of Asturias.

The Community's Support Framework 1989-93 for Spain sets the parameters within which the Community will be willing to make grants available to the Spanish Government for regional development. The Framework itself constitutes a constraint on Government planning because it requires certain levels of expenditure by the Spanish Government to 'trigger' the EC contribution (since in all cases the Community only part-funds projects). Thus the priorities of the Commission provide the fulcrum around which Spanish national regional policy is focussed. The key problem identified by the Commission is the lack of communications infrastructure, 'This underendowment is the result of the fact that, in recent years, the ratio of of public expenditure to GDP in Spain has been below the Community average' (Commission 1989:10). In other words, the Spanish

Government needs to spend more on motorways and railroads. The Plan General de Carreteras (general Highway Plan) runs until the end of 1991. When preparing the next plan, the Spanish Government will need to bear in mind the Commission's priorities in this sector. Likewise a plan recently approved by the Commission for the development of Spanish fishing ports must be coordinated with ERDF measures for these ports over the next few years. For highways the Spanish Government is contributing 821m ecus and the EC 1231m ecus in the period 1989-93; for ports the contributions are equal, 41 mecus from each.

The interface between the Commission's priorities for regional development and those of the Spanish Government is embodied in the Monitoring Committee which oversees the implementation of the regional development strategy in the period under review. The Monitoring Committee's functions are to coordinate all structural operations implemented by the regional and central authorities in Spain as well as the grant and loan instruments of the Communities, and to harmonise them with other Community policies, with a view to achieving the strategic objectives of the Community's support framework. The membership of the Monitoring Committee encompasses the Commission, the EIB, and Spanish representatives, the latter being drawn, as appropriate, from local and regional as well as national levels of administration.

Direct foreign investment

As suggested above, one apparently beneficial effect of Spain's entry to the EC has been an upsurge in direct foreign investment. However, an increasing proportion of this investment has been oriented towards financial projects rather than the industrial sector. In 1982, only 8 per cent of direct foreign investment went towards financial services, while by 1988 this had risen to 43 per cent; while, at the same time the mining and chemical sector, the metal product sector and 'other manufacturing' all saw their share of direct foreign investment fall. Nevertheless, the amount of foreign investment has gone some way towards redressing the negative trade balance apparent since Spanish accession in 1986. This is true even despite the fact that the bulk of investment goes towards the services sector, and sometimes towards rather speculative projects, rather than manufacturing. The upsurge in direct investment can be attributed to a number of factors of which the following may be the most important. First, advantage is being taken of a relatively low-wage economy during the transitional period (to 1992) which is witnessing the progressve dismantling of trade barriers. Second, Spain's domestic market can be exploited as the fastest growing market in the EC. Thirdly, the lowering of trade barriers on both intra-EC and extra EC-imports has lowered the cost of manufacturing inputs for Spanish industry. Fourthly, investors can take advantage of the different types of government aid offered to attract foreign investment, especially in the new technologies and in the less developed regions of Spain. All these factors are likely to remain relevant up to 1992, and therefore it is reasonable to expect foreign investment to continue at a high rate until at least then. Thereafter, however, it seems likely that all four factors will prove less compelling since they represent, in a sense, 'one-off' circumstances connected to the period of adjustment for the Spanish economy in the EC. Direct foreign investment can, potentially, make Spanish industry more competitive, but whether it does depends partly on the focus of such investment, and partly on government policies that are pursued.

The Spanish Government has played a fairly vigorous role in the modernisation of the country's industrial base. In the early 1980s, traditional industries like steel, shipbuilding and textiles, had to be restructured in the face of increased competition from the NICs. More recently, the government has played a part in stimulating the new technologies, especially electronics, and in 1988 a national research and development programme was launched which mirrored a similar plan launched by the EC. Privatisation, sometimes with the help of foreign multinationals, has been part of the government's strategy of encouraging greater efficiency in export-oriented industries.

What effect will all this have on Spain's ability to compete in the Single Market after 1992 ? If labour cost advantages are maintained, and technology enables higher levels of productivity to be achieved, Spain will do well in ceramics, footwear, textiles, wines, and motor vehicles. The outlook for industries where foreign owned firms dominate the Spanish domestic market, and where international competition is keen (e.g. aerospace, computers, office automation equipment, and telecommunications) the outlook is much less bright.

Some theoretical reflections

In 1983, an article in the Journal of Common Market Studies (Bulmer 1983) argued that EC policy-making could be understood only if the domestic policies of member states was given due attention, and that this varied considerably, not only between states but also over time, as internal party political balances shifted and the government itself was subjected to the fluctuating attentions of pressure groups. This article was not alone. It was part of a wider re-evaluation of the role of national political systems in the EC policy-making system. In the same year, another writer (Taylor 1983) questioned whether European integration was likely to proceed much further, and several years earlier Wallace Wallace and Webb (1977) had begun to see the constraints of the domestic political arena on EC policy-making. While conceding that the EC had increasingly come to impinge on the domestic processes of the member states and 'to bite into fairly sensitive areas of policy', it was still the case that the EC constituted only a small part of each national government's preoccupations:

> Inevitably, therefore, the pull of the domestic political system continues to counter the drift towards Community compromise. Governments are still the victims of their own national contexts, in terms of political traditions, administrative style and economic ideologies. All of these factors condition the interpretation they give to any policy proposals emanating from Brussels, and determine the framework within which they formulate their goals in Community negotiations. The responses of the nine member states to the Communities have thus been assymetrical, in that each reflects the idiosyncracies of its national context (Wallace, Wallace and Webb 1977:46).

It was exactly this line of thinking that conditioned a study of West Germany and the European Community published ten years later (Bulmer and Paterson 1987). There, the authors concluded that there was 'little value in examining a member state's European policy in isolation from its other policies. European policy is conditioned by much the same set of factors which shape domestic policy. Many of the same actors are involved in policy formulation..'.(Bulmer and Paterson 1987:3). Leaving aside the question of whether EC policy ought to be distinguished conceptually from either foreign or domestic policy (surely its uniqueness lies in its abridgement of the two), the West German case may well be <u>sui generis</u>. Clearly, Bulmer and Paterson demonstrated that factors peculiar to West Germany's political system moulded the making of its EC policy: the independence of ministries; the defence of agricultural interests; the federal division between the Lander and Bonn; and the special importance of European Political Cooperation to a country that was timid about raising its head too far above the parapet of international acceptability. For historical and sound economic reasons, West Germany has broadly supported the integrative mechanisms of the Community. But does the national policy-making perspective apply equally to all EC members? And is it the only important determinant ?

To take the second question first, it seems clear that the revival of the momentum towards European integration in the second half of the 1980s was partly, at least, stimulated by exogenous factors in the world economy even though these factors may have manifested themselves in the domestic economic needs of the Community's three most important actors (the UK, West Germany and France). This argument is made by Sandholtz and Zysman (1989) and has now been incorporated into the revised versions of neofunctional integration theory (e.g.Keohane and Hoffman 1990). These latter writers argue that 'spillover' takes place when national governments wish it to do so. This is not to concede the primacy of national contexts in EC decision-making but rather to suggest that governments may more frquently use the EC level of policy-making to achieve national objectives.

Returning to the question of how important the national setting may be for EC policy-making, it may be possible to argue that that it varies considerably according to (1) the weight of the member-state in the EC, (2) the structure of the state's political system (how centralised?) and (3) the issue involved. West Germany may be a special case partly because it has been a 'penetrated' political system in the sense of being abnormally exposed to external events and pressures, and possessing a party system whose tensions were almost a mirror image of the Cold War polarities beyond its boundaries. Moreover, West Germany was never a fully-fledged state in the way other members of the EC have been (even if in the case of Luxembourg the sovereignty was largely nominal). It was a rump-state, created by outsiders, for the benefit of outsiders, and having origins that owed nothing to consensus or a spontaneous expression of popular will. Added to this, West Germany had everything to gain by participating in, and enthusiastically supporting the EC: the economic success of the West Germany economy was built on the back of an 'extended domestic market'. The health of West Germany and the health of the EC became inseparable. As Bulmer and Paterson themselves put it 'In some ways the Federal Republic and European integration are like twins: neither can remember an existence independent of the other. In both economic and political terms the fate of one has a major impact on the other' (Bulmer and Paterson 1987:15).

When we look at Spain the contrast is almost complete. Firstly, as we have seen, it would be difficult to argue that Spain has benefited, or is likely to benefit very much, in an economic sense from EC membership. Secondly, although Spain has its own policy style, it would be difficult to argue that this influences Spain's EC policy very much. Thirdly, Spain has not succeeded in getting very many of its policy proposals accepted by the rest of the EC. Fourthly, although it is possible to see distinct political advantages accruing to the democratic consensus within Spain, these are achieved at an economic price, and involve a considerable loss of independence of action for Spanish governments. Fifthly, many legislative proposals emanating from the Commission (most notably those stemming from acceptance of the Social Charter, and most recently the suggestion that tobacco advertising should be banned throughout the EC), seem particularly problematic for the Spanish Government. In many policy areas, the EC 'system' constrains Spanish policy-makers, and dictates the course of events. It has to said, also, that the Spanish government has not been able to control, and has not wanted to control, the extent to which the Spanish economy is effectively dominated by multinational enterprises, mobile capital, foreign banks, speculative investment and increasingly centripetal forces in the context of a crystallising Single Market.

These latter pressures may create greater intra-national divergences between regions than exist at present. As all restrictions on investment flows are removed after 1992, the flow of investment to north east Spain will increase. Spain's participation in the EC involves it in two converging processes: international integration and, to some extent, intra-national disintegration. A recent study of regional polcy in Spain (Villaverde Castro:1990) concludes that Spanish (and

EC) regional policy has failed to make any inroads into the divergences that exist between the regions of Spain. The propensity of some autonomous regions (eg Catalonia) to open up offices in Madrid to lobby the Commission is a reflection of a belief that Spain's national representation will not give some regions a fair deal, notwithstanding the recent addition of regional representatives in the Spanish permanent delegation in Brussels (Goni 1991).

The experience of EC membership has not been particularly advantageous to Spain so far. Public opinion recognises this by making a distinction between the economic and political effects, seeing the former as disadvantageous, at least in the short term, while the political effects, are seen as sufficiently beneficial to outweigh the economic costs now, and in the longer term. In short, it is difficult to argue that the national policy-making context in Spain, or Spanish priorities, have any real effect on decisions reached at Community level. While these influences may have been, and may still be, important in the case of Germany, it is doubtful if countries with less economic muscle in the EC can colour the complexion of EC decision-making processes. More importantly, all EC members in the 1990s are becoming more exposed to a variety of pressures operating at different levels: regional, national, transnational, supranational, and international. The interplay of these pressures, which is likely to become more evenly balanced in the wake of Treaty revisions, the entrenchment of the subsidiarity principle, and any redefinition of the relationship between the EC institutions, renders the notion of European integration being determined and shaped by predominantly national forces, increasingly obsolete.

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TABLE 1

Spain's trade balance: 1982-1989
(mill$)

1982	1983	1984	1985	1986	1987	1988	1989	YEAR
30579	27463	26939	27740	33164	46234	57573	67777	IMPORT
21321	19874	22660	23550	26714	33399	39570	43221	EXPORT
-9258	-7589	-4279	-4190	-6450	-12835	-18003	-24556	BALANCE