

Global Vision Perspective

57 Tufton Street, London SW1P 3QL, Tel 020 7233 3121, Fax 020 7222 4388
info@global-vision.net

Britain in a global world?

By Dr Mark Baimbridge, Dr Brian Burkitt
and Professor Philip B Whyman

In the second of two papers for Global Vision, economists Mark Baimbridge, Brian Burkitt and Philip Whyman continue their investigation of alternative approaches to the relationship between Britain and the European Union. Here, they investigate options such as a revitalised EFTA, developing Commonwealth trade, bilateral free trade, and membership of NAFTA, which could all help the UK prosper in the globalised 21st Century by concentrating its energies on developing markets for British goods and services amongst the fastest growing areas of the world.

Introduction

In our previous *Global Vision Perspective - Moored to the Continent?* - we discussed the potential for the UK developing a number of alternative strategies regarding its relationship with the EU. These included a number of options for a much looser relationship which would exclude the UK from the current political integration in Europe. Furthermore, they all presumed our ability to negotiate such an arrangement on favourable terms. While there is no reason to believe the EU would seek to prevent that, it implies the need to have, at least in reserve, the option of threatening withdrawal from the current EU if negotiations prove tricky.

This *Perspective* therefore considers the consequences of a much looser relationship with the EU, including the ultimate option of negotiating a new relationship following the UK's initial withdrawal, and examines the range of potential economic and political consequences.

An independent, global Britain

Rather than withdrawal from the EU being the catastrophe that supporters of greater integration claim it would be, freedom from the restrictions imposed by over-concentration upon the EU could enable Britain to take an independent approach to political and economic issues confronting the nation.

Thereafter, the UK is free to operate any economic policy it wishes (Whyman, *et al.*, 2000). The crucial point is that UK citizens would possess the power to decide how they are governed and how the economy is run, rather than exercising merely a token vote at British General Elections because important decisions concerning fiscal, monetary, exchange rate and trade policy are taken in Brussels and Frankfurt.

The potential arising from renewed economic independence is, not surprisingly, dismissed as illusory by supporters of EU economic integration. They argue that sterling would be prey to speculation, requiring higher interest rates to be maintained. Moreover, they believe that the only way in which the UK can exercise any power in world affairs is as part of the EU. Furthermore, withdrawal may endanger foreign investment in the UK and cause negative reactions from remaining EU members.

These arguments enjoy little factual basis and their predictions are unlikely to be fulfilled if the UK did withdraw from the EU. For instance, after the ERM debacle, it is disingenuous of the supporters of European integration to suggest that sterling would be damaged by floating its exchange rate.

Moreover, the argument that the UK can only exercise any influence on world events only from within the EU is questionable. The UK lost its former world position because of economic problems. If the UK is to regain influence, it must be based upon economic success, which is less likely to be secured within the EU straitjacket of deflationary European Central Bank and Stability and Growth Pact policies.

Indeed, a UK economy growing faster outside the EU with a permanently competitive exchange rate is more attractive to foreign-based companies. They locate productive facilities to enhance their profits through producing output they can sell in the British and European markets, together with utilising the skills and abilities of a well-educated and flexible labour force.

Nor is the idea that withdrawal from the EU would provoke retaliation from current EU 'partners' probable. Apart from EU Commission pressure attempting to persuade the UK to change its mind, most EU countries will not engage in a trade war because their surplus with the UK means that it would hurt them most.

Hence, if the UK could not secure fundamental reform of the EU, or alternatively renegotiate its current commitments bound by EU rules and international treaty, as Minford *et al.* (2005) state it would be in the UK's interest to withdraw from the EU and pursue a set of economic and social policies determined according to national priorities.

However, withdrawal from the EU, if it became necessary, would not be the end of the road. The UK could move forward to not only agree new arrangements with the EU - mirroring the kind of arrangements that Switzerland has in place - but also to develop new trading relationships with other nations.

A revitalised EFTA

This strategy would involve the UK formally withdrawing from the EU and re-joining the European Free Trade Association (EFTA) it helped to found four decades ago. Article 41 of the Convention establishing EFTA states that any country may accede, if it receives the approval of the EFTA Council. Alternatively the Council may negotiate bilateral agreements with individual states subject to the unanimous approval of all member states. The potential offered by EFTA is worth exploring, by establishing trade relationships supplementary to those with the EU member states.

A revitalised EFTA could provide an alternative to the EU as a looser form of co-operation between European nations. It might prove attractive to some political parties and segments of the electorate in the 2004 and 2007 accession countries where significant opposition to European integration was demonstrated in the 2004 elections to the European Parliament (Baimbridge, 2005). This would be in addition to sizeable majorities occurring within Norway, Sweden, Denmark, Iceland and Switzerland who are broadly sceptical towards further European political and economic integration.

Developing Commonwealth trade

The greatest visible sign of economic weakness is the persistence of mass unemployment within EU nations, which is not matched by the North American, Asian 'Tiger' and Latin American areas. Indeed, it is interesting to note that many Commonwealth countries offer potentially faster growing markets than do other EU

member states. Historic links with Commonwealth nations could give the UK a potential advantage in re-establishing trade links with these dynamic economies (West, 1995). They include Singapore, India, Pakistan, Malaysia, New Zealand, Australia, Canada and South Africa. Moreover, the East Asian link is also potentially important as a bridgehead to closer trading links with China.

Estimates indicate that the areas of the world which grew most during the past two decades - namely South and East Asia - will continue to expand more rapidly in the next decade. Additionally, growth potential is expected to result in significantly higher rates amongst most developing/transitional, than amongst the developed, economies. Latin America, Africa and the Middle East join Asia in offering UK companies superior potential for increased export sales than does the EU Single Market.

However, the UK is distracted from taking advantage of such opportunities by the Single Internal Market and the EU's common external tariff. In particular, the latter is an impediment to free trade which encourages other nations to place tariffs upon EU nations' exports, thereby putting UK exporters at a competitive disadvantage against the rest of the world.

Bilateral free trade between EU and UK

Another option for the British government following withdrawal is to seek its replacement with a bilateral trade agreement between the EU and UK.

Since the UK is ill-served by participating in the Common Agricultural Policy and the Common Fisheries Policy, a restriction of free trade with EU nations to industrial and financial goods and services would prove more beneficial. The remaining EFTA countries negotiated such a free trade agreement with the EU in 1972, after the UK, Denmark and Ireland joined the EU.

Such a policy allows the UK to reorientate its economic policy to serve its own needs rather than those of competitor EU countries. The money saved by non-contribution to the EU budget could be used to increase incentives for productive investment within the UK, such as infrastructural and research-based projects that increase long-term competitiveness.

Such a tactic closely resembles Switzerland's current position, which does not haemorrhage its economic vitality, but strengthens the Swiss economy which has maintained relatively low levels of inflation, interest rates and unemployment, together with a significant balance of payments surplus.

Membership of NAFTA

If the UK were to join the North American Free Trade Agreement (NAFTA) comprising the United States of America, Canada and Mexico, it would be required to leave the EU since the latter compels its member states to adopt a common external tariff and

to subscribe to an EU-wide uniform external trade policy. There are, however, a number of compelling reasons why both the US and the UK should actively promote such a development (USITC, 2000; Baimbridge *et al.*, 2004).

Firstly, the UK and US economies are closely intertwined such that further trade liberalisation would result in immediate benefits, in terms of trade creation, for both. Over the last decade, for instance, UK net direct investment in North America was more than double its investment in the EU. This also builds on economic success, because over the past 15 years the US and Canada have created 2 million more jobs than EU countries.

If Britain joins NAFTA, the larger group will help to protect both the US and the UK from whatever outcome emerges from the EU experiment in supranationalism. A more broadly-based NAFTA could counter the impact of either an imploding, or a successfully integrating - but by necessity largely inward-looking - EU, particularly given enlargement.

Moreover, the existing NAFTA countries are already negotiating with EFTA and Chile. If Britain participated in such a grouping, a revamped NAFTA could ultimately be transformed into a global free trade association, based solely upon a commitment to free trade. It would seek no control of member states' trade relations with non-members nor would it possess the motivation to pursue 'ever closer union' that renders the EU unpalatable.

Since its withdrawal from the ERM, the British economy has been convergent, both structurally and cyclically, with North America. Consequently, sterling tracks the US dollar not the euro, whilst its divergence from continental currencies has widened. Such oscillations determine the efficiency of interest rate harmonisation, leading to the conclusion that the American and British economies are more convergent with each other than either is with the eurozone.

In terms of the business cycle, the UK has traditionally possessed a closer relationship with the USA than with EU member states (Bayoumi and Eichengreen, 1993). Furthermore, a noticeable change in both US and UK economies during the past decade has been the remarkable transition in their respective labour markets. The shift towards non-standard contracts, together with the deregulation of the labour market, has increased the ability of both economies to adapt flexibly to industrial restructuring. Moreover, productivity has been rising quickly in both nations, with US productivity growth outstripping average wage growth thereby dampening inflationary pressure from increasing oil prices and property market booms.

Finally, macroeconomic strategy is similar for both countries, with restrained fiscal policy permitting looser monetary policy to facilitate economic growth and increased levels of investment though lower real interest rates. Supply-side policy seeks to reduce taxation to encourage entrepreneurship, together with stimulation of investment in human capital. Consequently, both nations are ranked in the top ten most competitive nations in the world.

Conclusion

One of the most fundamental problems that EU membership has imposed is that too great a proportion of Britain's energies are dedicated towards facilitating convergence with European neighbour economies, rather than concentrating upon the national interest by developing markets for British goods and services amongst the fastest growing areas of the world.

In response to these problematic aspects of membership, this *Perspective* has outlined a number of potential alternative approaches to the relationship between Britain and the EU, including the ultimate option of complete withdrawal. Each should be assessed on the basis of a cost-benefit analysis after an informed public debate.

Crucially, however, these alternatives explode forever the establishment claim that 'there is no alternative' to membership of an increasingly centralised, integrated EU. For the UK, a multiplicity of more attractive potential futures is possible, if the political will exists to pursue them.

References

- Baimbridge (2005), EUphoria to apathy: EP turnout in the new member states; in Lodge, J. (ed.) *The 2004 elections to the European Parliament*, London: Palgrave Macmillan.
- Baimbridge, M., Harrop, J. and Philippidis, G. (2004) *Current economic issues in EU integration*, London: Palgrave Macmillan.
- Bayoumi, T. and Eichengreen, B. (1993) Shocking aspects of European monetary integration; in Torres, F. and Giavazzi, F. (eds.) *Adjustment and growth in the European Monetary Union*, Cambridge University Press: Cambridge.
- Minford, P., Mahabare, V. and Novell, E. (2005), *Should Britain leave the EU? An economic analysis of a troubled relationship*, Cheltenham: Edward Elgar.
- United States International Trade Commission (2000), *The impact on the US economy of including the United Kingdom in a free trade arrangement with the United States, Canada and Mexico*, Investigation No. 332-409, Publication 3339, August.
- West, K. (1995), *Economic Opportunities for Britain and the Commonwealth*, London: Royal Institute for International Affairs.
- Whyman, P., Burkitt, B. and Baimbridge, M. (2000), Economic policy outside EMU: strategies for a global Britain, *Political Quarterly*, 71 (4), 451-462.

Notes on the author:

Dr. Mark Baimbridge (University of Bradford) - his principal areas of research are: monetary integration; the UK-EU relationship; applied microeconomic aspects; political integration. He is the author/editor of: *The impact of the euro* (Macmillan, 2000), *Economic and monetary union in Europe* (Edward Elgar, 2003 & 2005), *Fiscal federalism and European economic integration* (Routledge, 2004), *Current economic issues in EU integration* (Palgrave, 2004), *Implications of the euro* (Routledge, 2006), *Analysing the 1975 referendum: lessons for the future?* (Imprint Academic, 2007) and *Analysing the 1975 referendum: reflections on the 1975 referendum* (Imprint Academic, 2007), together with a number of forthcoming texts: *Britain, the euro and beyond* (Ashgate), *Current issues in EU enlargement* (Palgrave), *EU enlargement: challenges and prospects* (Copenhagen Business School Press), *Social Europe* (Routledge) and a three volume series analysing *The EU at 50* (Palgrave).

Dr. Brian Burkitt (University of Bradford) - his principal research areas are the UK-EU relationship; monetary union; social policy. He wrote two widely quoted reports, *Britain and the European Economic Community: an economic re-appraisal*, and *Britain and the European Economic Community: a political re-appraisal* at the time of the 1975 Referendum on EEC membership. He is also author/editor of: *Trade unions and wages* (Crosby Lockwood Staples, 1975 & 1980), *Trade unions and the economy* (Macmillan, 1979), *Radical political economy* (Harvester Wheatsheaf, 1984), *The political economy of social credit and guild socialism* (Routledge, 1997), *The impact of the euro* (Macmillan, 2000) and *Implications of the euro* (Routledge, 2006).

Professor Philip B. Whyman (University of Central Lancashire) - his research interests include the impact of European integration upon labour markets; fiscal federalism; international monetary developments; the UK's future relationship with the EU. He is the author/editor of: *The impact of the euro* (Macmillan, 2000), *Economic and monetary union in Europe* (Elgar, 2003 & 2005), *Sweden and the 'Third Way'* (Ashgate, 2003), *Fiscal federalism and European economic integration* (Routledge, 2004), *An analysis of the economic democracy reforms in Sweden* (Mellen Press, 2004), *'Third way' economics* (Palgrave, 2005), *Implications of the euro* (Routledge, 2006) and *Analysing the 1975 referendum: lessons for the future?* (Imprint Academic, 2007), together with the forthcoming texts: *Britain, the euro and beyond* (Ashgate) and *Social Europe* (Routledge).

Global Vision is a new campaign group backed by economists and business leaders that argues for a looser British relationship with the EU, based on free trade and mutually beneficial cooperation, whilst opting out of economic and political union. Global Vision believes that this is the right relationship for Britain in the 21st century's rapidly changing world. For more details on Global Vision please visit our website: www.global-vision.net.