Introduction

The European Community is in the grip of a severe recession which is likely to continue at least until the mid-1980s. There is already high unemployment in all member-countries and the numbers out of work will go on increasing for some years to come. New jobs have not been created on anything like the scale required to provide for the exceptionally large generation of young people born in the 1960s, let alone the rising proportion of women who would like to work if jobs were available.

The recession has been pervasive in its effects. It has not only depressed income and output but also productivity, government revenue and both public and private spending. Its causes are widely supposed to be mainly or wholly internal to the Community. It is claimed that market mechanisms have failed or have been impaired by too much government intervention and that this has led to inflation and reduced the potential for growth.

The main message of this *Review* is that recession in the Community was initiated not by internal problems but by external forces. It is mainly the result of world-wide scarcity of energy and increases in the price of oil. These have reduced growth not only in Europe but in the non-OPEC world as a whole. The maintenance of growth in the face of these energy problems would have required the acceptance of high borrowing (the inescapable counterpart of OPEC surpluses) and of high oil prices (the potential means of forcing a reduction in reliance on oil). It would also have required conscious and co-ordinated government action to enforce energy saving and the rapid development of new supplies.

Instead governments, especially in the Community, have responded to the increased cost of fuel imports by deflating domestic expenditure. This has held down demand for oil by curbing economic growth. The price of oil has not yet risen high enough to stimulate really effective action to alleviate the energy constraint, though it has been high enough to cause considerable pain, especially in developing countries unable to finance essential energy imports. The world is unable to buy significantly more oil from OPEC yet is unable to sustain general economic recovery without it.

The Community has been hit in several ways. It has not only had to face increased costs of oil imports but it has also suffered from slow growth of export markets (because of recession in other oil-importing areas) and from increased competition from oil-hungry parts of the world, notably Japan and the USA. The Community as a whole is too important in the world economy to escape global constraints and recession has spread throughout the Community as internal as well as external markets have slumped.

The Community's official institutions and member-governments have not grasped the real nature of the problem. Most member-countries are subjected to restrictive fiscal and monetary policies. The general aim is to force industrial restructuring through greater exposure to market pressures in the hope that the Community could climb out of recession by wresting markets back from producers in other parts of the world. This is a mistaken strategy. Fiscal and monetary restriction do not cure energy scarcity but merely conceal it by holding back growth – the worst conceivable way of saving energy. Nor can the Community hope to overcome its own recession at the expense of the rest of the world. It already takes such a large share of world markets for industrial exports that the scope for further increase is very limited. An export-led recovery is only conceivable if there is faster economic growth in the world as a whole.

Yet the consequences of continued slow growth for employment, for the provision of social services and for the standard of life generally are so serious as in our view to be unacceptable. The so-called 'zero growth' strategy does not offer a viable way of alleviating unemployment and of accommodating the needs of under-privileged groups and weaker countries and regions within the Community. The general aim has to be one of renewed growth – possibly a different pattern of growth from before and certainly achieved in a way which benefits rather than harms the rest of the world – but growth nonetheless.

The changes required to achieve this aim can be stated quite easily. They are:

(a) acceptance of further increases in the world price of oil, combined with maximum effort to save energy and develop new supplies not only in Europe but throughout the world;

(b) large-scale borrowing to finance deficits which are the necessary counterpart of OPEC surpluses for as long as the world needs OPEC oil more than OPEC needs imports from the rest of the world;
(c) increased aid and trade preferences to low-income non-oil producing countries hard-hit by the high price of oil;
(d) recognition on the part of the Community that its surplus on trade in manufactures has to be sufficient, with borrowing, to finance oil imports but, at the same time, not too oppressive to others in a similar position. This depends on (a), (b), and (c) being satisfied as well as on the competitive performance of member-countries in manufacturing *per se;*
(e) re-distribution of growth within the Community *via* changes in shares of markets for manufactures, possibly reinforced by financial transfers, to ensure those countries and regions most in need of growth are able to achieve and sustain it.

It is very hard to see how these necessary changes can be brought about. Effective common policies depend on agreement between member-countries and active support for their implementation. In principle the Community could pursue a strong energy policy and create the financial institutions to ensure sufficient external borrowing, distributed between member-countries in accordance with need. It would then be in a position to try to negotiate solutions with other blocs to what are after all world-wide problems. There is no sign as yet of agreement within the Community on such policies. The interests and perceptions of member-countries differ and such differences are rendered more serious by the lack of effective internal mechanisms for redistribution between member-countries.

What can any one member-government do on its own account? Presumably it could enforce greater energy saving in its own country. Some at least could increase their deficits. Actions of this kind would afford relief but much of the benefit would flow to other member countries. To retain more advantage, a single country might engineer a devaluation of its currency or steal a march on other members by favouring its own industries in international competition in various surreptitious ways. But there are strict limits to how far governments are likely to go on either front under present rules, given the possible reaction of other member-governments and the inflationary repercussions of falls in the exchange rate. Individually, member-governments can ease problems in their own countries but they cannot obtain any full economic recovery.

The UK is a special case. Although it is the one member-country which is a net exporter of oil it has the worst recession and the most severe unemployment. Much of this is due to government policy which through deflation of demand and monetary restriction has ensured a high exchange rate for sterling at the cost of industrial collapse. Whereas the oil deficits of other members have helped to create a sense of urgency, the UK has been lulled by its oil into an acceptance of industrial decline. Reversal of fiscal and monetary restriction would alleviate recession in the UK but would draw in industrial imports from other member countries as well as from outside the Community on a very large scale. This is why the Community's common market rules are an important subject for debate in the UK. Any proposed solution to the UK's predicament has to face up to the problem of how severe deindustrialisation can be reversed in a country which is exposed to intense external competition.

Outline of the Review

The purpose of this *Review* is to clarify the problems which beset the Community and to draw attention to changes which need to be brought about by whatever means, whether by joint or unilateral action, to generate economic recovery in its member countries.

Chapter 1 surveys what has happened to the Community's economy in recent years. It shows how growth has slowed down since 1973 and how this, in combination with demographic changes, has led to rising unemployment in all member-countries as well as to sluggish growth of real income and acute financial problems for governments.

Chapter 2 demonstrates how recession in Europe and much of the rest of the world has been caused by energy problems and increases in the price of oil. It argues that energy problems are the critical constraint on recovery in the world as a whole and shows that little has so far been achieved in the way of energy saving and development of new supplies to alleviate this constraint.

Chapter 3 examines the constraints restricting growth in the Community in particular. It argues that, while countries in Europe are potentially able to finance the increased cost of fuel imports by improving their trade performance especially in manufacturing, Europe as a whole is so large a part of the world economy and its share of world export markets so high that in practice the direct effects on Europe of the high oil price are inevitably reinforced by recession elsewhere. Europe cannot evade global constraints.

Chapter 4 examines how growth has slowed down in individual member-countries of the Community and how their trading performance, both in relation to each other and in relation to the rest of the world, has contributed to the slow-down.

Chapter 5 considers broad policies for tackling problems identified in earlier chapters and suggests ways of avoiding prolonged recession, with all its consequences, in the Community.

The Statistical Appendix provides the historical accounts for the Community and its member countries from which many of the figures in the text and tables have been drawn.