

Where's the 'clear and unambiguous' evidence that Britain would benefit ?

In the second of his series of articles on the Chancellor's 'Famous Five' economic tests Anthony Scholefield examines the implications of tests two and three

TEST 2

If problems emerge is there sufficient flexibility to deal with them?

This really two questions rolled into one:

Is there sufficient flexibility in the UK economy? Is there sufficient flexibility in the euro zone economy?

The 1997 Treasury Assessment does give a reasonably fair and detailed assessment of the flexibility of the U.K. economy.

However, it falls down badly in its analysis of the flexibility of the euro zone. The analysis is derisively sketchy.

Chapter 2.7 says: 'Governments across Europe are introducing structural reforms to make their labour markets more successful at adapting to economic change.'

Chapter 2.25: 'We need to work further to ensure the EU economy as a whole is able to create jobs and respond to structural change as needed.'

In practice there is no evidence that major EU governments are introducing structural reforms. Germany and France are both hobbled by electoral considerations this year and, in Italy, labour reform proposals have led to the assassination of the labour reform adviser to the government, followed by a general strike in April 2002.

As put by the Labour Euro Safeguards campaign in March 2002:

"The single biggest problem, buttressed by the Growth and Stability Pact with all its baleful consequences, is the power of the European Central Bank. This institution, modelled on the former Bundesbank, is secretive, virtually immune to democratic pressure, and obsessed - in line with its

remit under the Maastricht Treaty - with keeping inflation down to between 0 per cent and 2 per cent; if necessarily at the expense of all other economic objectives. The deflationary conditions thus generated, with low investment and high levels of both unemployment and taxation, much of which is used to finance the cost of having so many people out of work, are just the opposite to those conducive to the restructuring which most of the EU economies badly need."

TEST 3

Would joining EMU create better conditions for firms making long-term decisions to invest in Britain?

This contains a remarkably confused paragraph 3.8:

"Some studies have looked more specifically at the implications of exchange rate volatility for domestic and foreign direct investment. The conclusion tends to be that aggregate investment is higher under fixed rate exchange rate regimes. Furthermore, within flexible exchange rate regimes, increased exchange rate volatility tends to reduce investment, although the evidence is not conclusive. However, it has to be recognized that flexible exchange rates can help ameliorate the impact of certain kinds of shock. Fixed exchange rates do not, by themselves, guarantee a more favourable environment for businesses. And there can be benefits from exchange rate adjustments when economic cycles are out of line."

How U.S. investors, who are overwhelmingly the largest foreign investors in the U.K., will react to this may only be guessed at.

However, they can work out that the assertion in paragraph 3.15: 'there

would be a credibility gain for the U.K. from joining EMU' is a meaningless remark since the U.K. would abandon control over its monetary policy on joining the single currency.

Perhaps they might find it easier to unravel the assertions in chapters 3.26: "Recently inward investment has risen to record levels at a time when many investors are already assuming that the U.K. will opt out of the first move."

And Chapter 3.27: "Over the long term, if the U.K. remained outside a successful EMU there is the opposite danger that inward investment decisions at the margin would move against the U.K. as companies look increasingly favourably on the euro area."

'Clear and unambiguous' it most certainly is not.

The facts on inward investment are that, despite a fall in investment worldwide in 2001, investment in the UK fell less than most and, according to UNCTAD at \$72 billion it remained significantly larger than France's \$38 billion and Germany's \$25 billion combined.

Indeed, *Invest UK's* Chief Executive, William Pedder, in March 2002 stated the following: "*The UK attracts more inward investment than any other country in Europe. It has maintained its leading position because of underlying stability in the economy, its low tax base, lack of bureaucracy and high productivity. UNCTAD's World Investment Report 2002 confirms the UK's standing.*"

Not a mention of the benefits of the euro, nor does William Pedder attribute any advantage to the benefits of EU membership.