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The challenge of enlargement

Commission opinion on Sweden's application for membership

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Foreword

1. The Swedish application for membership is being examined at a time when a number of other accession requests are also on the table. These include applications from three other EFTA countries; Austria, Finland and Switzerland. The Commission has adopted its opinion on the accession request of Austria, and is conducting the work relative to the opinions on the consequences of the accessions of Finland and Switzerland.

2. The question of enlargement was addressed by the European Council during its Lisbon meeting of 26 and 27 June 1992, on the basis of a report[1] presented by the Commission. The European Council on that occasion considered that 'the EEA Agreement had paved the way for opening enlargement negotiations with a view to an early conclusion with EFTA countries seeking membership of the European Union. It invited the institutions to speed up preparatory work needed to ensure rapid progress including the preparation before the European Council in Edinburgh of the Union's general negotiation framework. The official negotiations would be opened immediately after the Treaty on European Union was ratified and the agreement had been achieved on the Delors-II package'.

3. In preparing the present opinion, the Commission has assumed, in line with the conclusions of the European Council in Maastricht in December 1991, that accession will, in accordance with Article O of the Maastricht Treaty, be to a European Union characterized by the establishment of economic and monetary union, ultimately including a single currency; the implementation of a common foreign and security policy, including the eventual framing of a common defence policy, which might in time lead to a common defence; the introduction of a citizenship of the Union and the development of close cooperation in justice and home affairs as well as the strengthening of economic and social cohesion.

4. The European Council in Lisbon also concluded that 'negotiations with the candidate countries would, to the extent possible, be conducted in parallel, while dealing with each candidature on its own merit'. This will be particularly important in the case of the EFTA candidates, not only in respect of the adjustments to the Treaties provided for in Article O, but also because of the numerous similarities in the questions to be addressed in the negotiations.

[1] 'Europe and the challenge of enlargement', Supplement 3/92 — Bull. EC.

Introduction

1. On 1 July 1991, Mr Ingvar Carlsson, the then Swedish Prime Minister, submitted to the Council of the European Communities, on behalf of his government, the application of the Kingdom of Sweden for membership of the European Coal and Steel Community (ECSC), the European Economic Community (EEC) and the European Atomic Energy Community (EAEC).

2. At its meeting of 29 July 1991, the Council decided to set in motion the procedure laid down in Articles 98 of the ECSC Treaty, 237 of the EEC Treaty and 205 of the EAEC Treaty.

3. Following the European Council meeting at Maastricht, on 11 December 1991, the Swedish Prime Minister, Mr Carl Bildt, welcomed the agreement reached by the Heads of State or Government of the Community on the content of the Treaty on European Union, and stated Sweden's willingness to participate actively, as a Member of the Community, in the cooperation in the field of foreign policy and security cooperation, considering that this cooperation will mean that the Community will be able to contribute with reinforced strength and consistency to security, stability and cooperation in the development of the new Europe. The Swedish Prime Minister stated Sweden's aspiration to join as soon as possible the work in view of the creation of the economic and monetary union, which would lay one of the main foundations for positive economic development in the decades ahead. Sweden also welcomed the extension of the cooperation, in the context of the Community, to other new areas of major importance.

4. The Commission has, in this opinion, based itself on the *acquis* of the future European Union. The analysis is focused on those sectors not covered, or only partially covered, by the EEA Agreement. These are the sectors where the impact of accession will be largest and are analysed in the Part One of the present opinion. An additional analysis of specific aspects of these sectors is conducted in Part Two, where also are summarily described the implications of accession on sectors covered by the EEA or where the integration between Sweden and the Community is already very advanced.

5. During the preparation of its opinion, the Commission obtained a wealth of information on Sweden's situation from the Swedish authorities, with which it has remained in close contact, notably through the Swedish Mission to the European Communities in Brussels and the Commission's Delegation in Stockholm.

Part one

General

Relations to date between the Community and Sweden

1. The relations between Sweden and the Community have evolved against the background of Swedish external policy as a whole, both global and regional. Since the Second World War, Sweden has been a full participant in the newly created United Nations system. Within the limits Sweden had set herself as a consequence of her policy of freedom from alliances, she has played an active role in European cooperation both in her immediate vicinity, in the context of the Nordic Council and also in the wider context, participating for instance in the Council of Europe, and, later, in the CSCE.

2. Sweden was a participant in the attempts to create a large free trade area in Europe, in the context of the so-called 'Maudling plan'. When the Treaty of Rome was signed, in 1957, Sweden went on, together with six other European countries, to found the European Free Trade Association (EFTA), in 1960. Sweden continued nevertheless to search for close relations with the Community. In 1961 Sweden requested the opening of negotiations for an Association Agreement to establish closer economic ties. In the event, however, no negotiations were pursued. Later, in 1967 and 1969, Sweden proposed the opening of negotiations for a form of participation in the enlargement of the Community, compatible with her policy of neutrality. Ministerial level contacts were initiated on 10 November 1970, but the initiative ended by evolving in a different direction from that foreseen. When two founding members of the EFTA, the UK and Denmark, joined the Community, free trade agreements were concluded between the Community and the remaining member States of EFTA, including Sweden.

3. These free trade agreements[1] signed in 1972, provided for the progressive abolition, in respect of trade between the parties in industrial goods, of customs duties, quantitative restrictions and all measures of equivalent effect. The agreements, which also provided for rules on State aid and industrial competition and a number of mutual concessions in the agriculture and fisheries fields, created bilateral Joint Committee meetings regularly to administer them.

4. To mark the completion of this process, the Ministers of the Community and of the EFTA countries met in Luxembourg in April 1984 and adopted a declaration laying down the guidelines for the continuation, deepening and extending of cooperation, within the framework of, and beyond, the free trade agreements, with the objective of progressively establishing a dynamic European economic space. This led to efforts to strengthen and consolidate cooperation on a pragmatic basis, following three main principles (known as the 'Interlaken principles'): priority to the Community's own internal integration; preservation of the Community's decision-making autonomy and a satisfactory balance of advantages and obligations. This enabled a number of important achievements, particularly in free circulation of industrial goods.

5. In his investiture speech at the European Parliament in January 1989, President Delors invited the EFTA States to reflect on the possibility of a more structured partnership. Responding to this declaration, in March 1989 in Oslo, the EFTA Heads of Government declared their readiness to explore, together with the Community, ways and means to achieve such partnership, based on the fullest possible realization of free movements of goods, services, capital and persons as well as enhanced cooperation in fields going beyond the internal market programme. Ministers of the Community and

[1] Agreement between the European Economic Community and the Kingdom of Sweden (OJ L 300, 31.12.1972) and Agreement between the Member States of the European Coal and Steel Community and the European Coal and Steel Community, on the one part, and the Kingdom of Sweden, on the other part (OJ L 350, 19.12.1973).

EFTA States decided in December 1989, in a meeting in Brussels, to open negotiations with a view to reaching such a partnership by the same time the single market will be completed on 1 January 1993.

6. This culminated, after nearly two years of complex negotiations, in the signature, in Oporto, on 2 May 1992 of the Agreement creating the European Economic Area. This agreement, signed by the Community and Sweden, together with the other EFTA States, will, once ratified and in force, establish, throughout the territories of the Contracting Parties, the free circulation of goods, persons, services and capital (known as the 'four freedoms') as well as the broadening and strengthening of the cooperation in a number of other areas. In parallel with the EEA Agreement, Sweden has established a Protocol with the Community to facilitate the exchanges of certain agricultural products. Sweden would thus accede to the rights and obligations of membership from a high level of integration where she was already applying a large part of the Community's *acquis*, not only in the field of the 'four freedoms' but also in such areas as social policy, the environment, company law, consumer protection and competition rules. In the field of social policy, for example, there would be little further legislative change necessary in Sweden as a result of accession beyond that required as a result of taking over the *acquis* of the Community in the context of the EEA.

7. While the Community and Sweden were negotiating the EEA Agreement, the world in general and Europe in particular were changing very fast. Full membership of the Community came to be considered in Sweden as no longer incompatible with the Swedish policy of freedom from alliances. Sweden, realizing also the large extent of the Community *acquis* already taken on board, initiated a reflection about the advantages and disadvantages of requesting membership of the Community, as another member of EFTA, Austria, had already done. It was above all the Swedish determination to play an important role in the construction of the new European architecture that led to the presentation of the request. The then Prime Minister, Mr Ingvar Carlsson, indicated this in the course of a speech to the Swedish Parliament on 14 June 1991. Recognizing that the Community was regarded as a major driving force for cooperation and development in Europe, Sweden believed that, as a member, her possibilities of influencing this future cooperation—in political, economic and social terms—would be improved, and that membership would be in Sweden's overall interest. Sweden shared the Community's long-term goals, as formulated in the Treaty of Rome and the Single European Act, and wanted to work for their realization together with the other members of the Community.

The Swedish economy and the Community

1. Achieving economic and monetary union in the Community will require increased convergence of its Member States in the monetary and budgetary spheres, greater cohesion in their economic policy objectives and structures, which will need to be all the more competitive in the face of increased competition.

2. Sweden has a population of eight and a half million. Its per capita GDP is around 20% higher than the Community average, putting it close to that of Germany. Its medium-sized economy is heavily dependent on external trade and is already well integrated with Community markets.[1] Trade relations with the Community will soon be boosted by its becoming part of the European Economic Area. The Swedish economy's increasing involvement with the Community, which is already far advanced, should allow it to apply the entire *acquis communautaire* on the internal market right from its accession. In addition, Sweden's unilateral action in linking the Swedish krona to the ecu in 1991 has brought the country's economy closer, in monetary terms, to the economies of countries in the EMS.

3. Sweden's economic development and its people's standard of living are fundamentally dependent on its ability to position its

[1] See 'External trade', pp. 11 and 16.

economy in the international division of labour. This assumes steps to integrate the Swedish economy further into international markets and at the same time to establish structures to improve its competitiveness. However, the pattern of Swedish economic development has been significantly different from that of Community countries and, what is more, its main industrialized trading partners. Essentially, the economy has traditionally had four major specific features:

(i) a level of social protection and public goods provision which has raised State spending as a percentage of GDP, and with it the burden of taxation and other like charges, to 14 points above the Community average;

(ii) a relatively high degree of regulation and weak domestic competition, particularly in the service sector but also in some manufacturing sectors;

(iii) the priority long given to keeping unemployment under control both in the choice of macroeconomic policies and by means of active employment policies — between 1960 and 1990 unemployment never exceeded 3% of the working population;

(iv) weaker performance on inflation during the 1980s than the Community average, with the gap widening towards the end of the period. In 1992, the level of inflation could, however, fall to close to 3% under the influence of the recession and a reduction in the indirect tax burden.

4. In the 1980s this pattern of development was increasingly challenged. One measure of the crisis is that the Swedish economy is currently experiencing one of the worst recessions among the industrialized countries. Another is Sweden's economic decline relative to its industrialized trading partners. For example, per capita GDP was 30% higher than the Community average in 1970 but is now only 20% higher. Moreover, although during the last upturn between 1985 and 1989 domestic demand rose faster in Sweden than in the Community, GDP growth was only about the same and industrial production rose markedly more slowly than in the Community. This decline in Sweden's competitive position was reflected in a rapid deterioration of its external balances over the period.

The gradual extension of State intervention via public finance and regulatory measures restricting competition evidently reflects a popular Swedish preference for collective action and consumption of public goods. This preference has long gone hand in hand with acceptance of an unusually high level of taxation. After all, the bulk (70%) of public consumption is administered at municipal and regional level. Around half of this expenditure is financed by direct taxation set independently at local level.

None the less, the expansion of public intervention has produced macroeconomic and price mechanism dysfunctions, which have made the Swedish economy less efficient and less flexible and have intensified inflationary pressures. On the one hand, a high level of taxation and social welfare increases the strain on the labour market in periods of expansion. On the other hand, distortions in relative prices tie up resources in sectors protected or favoured by public intervention when they could be used more effectively in sectors geared to international markets.

Sweden's strategy, being introduced gradually since the late 1980s, for eliminating these dysfunctions has been to pursue sustained monetary stability and revive market mechanisms. In its present form, the strategy will involve reducing public spending and taxation as a percentage of GDP. It is seen as important that the objective of the structural reforms (some of which have already been started) should be to eliminate obstacles to allocating resources in the most efficient way possible. In this way, the Swedes' preference for a relatively high level of consumption of public goods can be reconciled with a healthy competitive position and a dynamic economy. Integrating the Swedish economy into first, the internal market and then the Community will none the less increase the effectiveness of the reforms.

5. In 1991 inflation fell substantially to 3%, which is lower than the Community average, from 10% in 1990. This was linked to a fall in demand, a rise in unemployment and a cut in the rate of indirect taxation. This achievement has yet to be confirmed in conditions of economic recovery, but the prospects are indeed good.

6. The new objective set for monetary and exchange rate policy is creating conditions for stability and convergence with the countries in the EMS. It has already gained in credibility. The switch in the first half of the 1980s from a monetary policy based on credit controls to one based on interest rates, similar to that applied in the Community, has given Sweden the instruments it needs for this purpose. The more recent but now almost complete liberalization of capital movements is contributing greatly to achieving this objective, increasing the integration of Sweden's money and capital markets with those of the Community. However, the credibility of monetary policy will have to be increased still more by judicious use of economic policy.

7. The new exchange rate objective links Swedish interest rates and prices more closely to those on the international markets. Consequently, a surge in nominal wages is reflected more quickly in the labour market in a loss of competitiveness and profitability and in higher interest rates. In future, labour market adjustments will depend more on a greater flexibility in nominal wages.

In Sweden, the social partners negotiate wages independently in a highly centralized manner. This model of wage negotiation means that they bear a great responsibility for the macroeconomic consequences of their wage agreements. In the past, the consequences of wage agreements have often been offset by a rise in inflation, which moderates real wages but is ultimately detrimental to competitiveness and optimal resource allocation, and by the absorption of a significant proportion of the working population by means of active employment policies. The new monetary regime is fundamentally at odds with the first of these adjustment mechanisms because it compels the social partners to pay more attention to the twin objectives of stability and full employment. Moreover, the impact of active employment policies is limited both by budgetary constraints and by the fact that their effectiveness decreases as the number of people covered by them rises.

8. For budgetary policy this is certainly a crucial point in time. The budget, which was still in surplus in 1990, is expected to show a deficit of close to 5% of GDP in 1993. Up to now the Swedish Government has given priority to reducing the tax burden, which will fall from around 56% of GDP in 1991 to 51% in 1993 as a result of reforms already undertaken or planned, as well as the effects of a decline in economic activity. Despite reductions in spending (equal to around 2% of GDP) planned in the supplementary bill presented by the government in late April, public spending's share of GDP will probably rise by almost two percentage points between 1991 and 1993. At present, Parliament is examining a number of structural reforms aimed at halting the trend in public spending as part of a medium-term strategy. It should be noted that the Swedish public debt in relation to GDP in recent years has been substantially lower than the average of the Community.[1] Whatever happens, the effort required to reconcile the objectives of reducing taxes and bringing public finances back into equilibrium will be considerable.

9. Since the late 1980s, the Swedish authorities have had to move quickly to introduce a strategy to revitalize the economy. On the one hand, given the specific characteristics of the Swedish economy and its comparative advantages, it had little choice but to opt for closer integration with a Community which was advancing towards the internal market and monetary union. On the other hand, internal tensions and the need to restore competitiveness in the face of increased competition demanded a thorough review of the very functioning of the economy. This review is far from being finished, although important measures have already been taken. A key issue is the redefinition of the public sector. There is political and social pressure to find a balance which will reconcile the specific preferences of the Swedes with the need for efficiency which, alone, will enable the country to preserve in the long term its remarkable achievements, namely a standard of living well above the Community average and low unemployment. Pursuing these objectives with determination will allow Sweden to integrate into the Community without too much difficulty and eventually to make a positive contribution to the achievement of monetary union.

[1] See Graph 21 in the Statistical annex.

10. Sweden's external trade is strongly directed towards Europe and in particular the Community, which accounts for 55% of both its exports and its imports. Sweden's fellow members of EFTA, three of which have applied for membership of the Community, account for 18% of its exports and imports. Central and Eastern Europe now account for some 2.3% of Sweden's external trade.

Sweden's largest export markets outside Europe are the United States (8%) and Japan (2.1%), which also supply 8.5% and 5.1% respectively of its imports.

Despite the modest size of its economy, Sweden ranked fourth as a supplier of the Community in 1991, after the US, Japan and Switzerland, accounting for about 5.1% of imports from outside the Community (ECU 21.9 billion). It was the Community's fifth largest export market after the US, Switzerland, Austria and Japan, taking 5.2% (ECU 25.2 billion) of total EC exports.

Since the late 1980s, Sweden has had a substantial trade surplus with the Community, which amounted to ECU 3.3 billion in 1991.

The pattern of trade between the Community and Sweden is fairly similar in both directions, mainly comprising machinery and manufactured goods. The Community's major imports from Sweden are paper and board (16.3% or ECU 4.1 billion), machinery (16% or ECU 4 billion), vehicles and vehicle accessories (13.2% or ECU 3.3 billion) and electric motors (6% or ECU 1.5 billion). The Community's major exports to Sweden were machinery (18% or ECU 3.9 billion), electric motors (10% or ECU 2.1 billion), vehicles and vehicle accessories (9.5% or ECU 2 billion) and plastics (4.6% or ECU 1 billion).

Impact of accession

Agriculture and forestry

1. Sweden has about 2.8 million ha of arable land and about 0.3 million ha of meadows. Of the arable land, about 1.2 million ha is grain area and 0.9 million ha is pasture and temporary pasture. The remaining area of 0.6 to 0.7 million ha is either used for other crops or it is left fallow. The area of Sweden covered by forest totals 23.4 million ha which is slightly less than 60% of the area of the entire country.[1]

Production of a number of important agricultural products has in recent years exceeded the 100% degree of self-sufficiency. As a result of a major reform of the Swedish agricultural policy, decided in 1990 and implemented from 1 July 1991, the surplus production is expected to be reduced or eliminated. In the livestock sector production has already fallen significantly and earlier surpluses have virtually disappeared. Compared with EC agricultural production, Sweden's production represents 1 to 3% according to the product.

2. Presently, the Swedish system of support to the agricultural sector differs from that of the Community. The Swedish deregulation has meant a shift away from certain traditional policy instruments (e.g. internal market and price regulations and export refunds) which are still an important part of the CAP. Given the overall importance of market and price policy for the CAP, the adaptation of the Swedish policy is necessary. In particular, a reintroduction of the above policy instruments and quota system would be necessary, as well as, in certain sectors, a reduction of the level of producer prices. Since the fruit and vegetable sector in Sweden is not regulated, an adjustment to the CAP will necessitate the adoption of intervention buying and export support for these products.

The level of border protection for some major agricultural products is higher in the EC than in Sweden, although market prices are often lower. Nevertheless, as a general rule, harmonization of the Swedish border protection should not cause major problems.

3. Under present conditions, a Swedish accession to the EC would mean, in terms of consequences for Swedish producers, a downward pressure on prices for some of the main agricultural products. A preliminary study done in Sweden[2] showed that the

[1] A more detailed description of the Swedish agriculture sector is enclosed in Part Two.

[2] Before the CAP reform.

general producer price for cereals in the EC was somewhat lower than the long-term prices expected in Sweden. For most livestock products, a downward pressure on producer prices is expected. Feed costs will, however, also be lower and to some extent compensate for the lower prices of livestock products. In the sugar sector, no dramatic changes are expected as regards producer prices and production. The level of EC direct support for certain feed crops such as peas and beans and for grass seed is generally higher than in Sweden. For lamb and sheepmeat, an accession would mean increased support as well as increased import competition. For horticultural products, an accession is expected to lead to a downward pressure on producer prices. An adaptation by the Swedish farmers to the conditions prevailing on the EC market means that they will be exposed to generally lower producer prices, a reduced support level and more intense competition. As a result of decreasing producer prices and stronger competition, reduced consumer prices as well as a broader variation of food supply can be expected in Sweden.

4. Given the small volume of production of the applicant country compared to the production volume of the Community, no global effects for Community markets have to be expected, especially since Sweden is reducing or has already eliminated its earlier surplus production. However, there is a possibility that regional trade flows between countries directly neighbouring Sweden could be shifted. This would possibly result in the need for regional adaptation.

5. Production patterns and climatic conditions in the south of Sweden are not very different from those prevailing in the northern EC countries, although the low population density and the geographical location may give Swedish agriculture certain specific characteristics. In the north of Sweden, however, the conditions for agriculture are quite different from those in the south. The northern parts of Sweden constitute a special problem given in particular the extremely low density of population, unfavourable climatic conditions, long transport distances and higher production costs. For many different reasons, such as regional development, employment, national security and nature conservation, special support is therefore directed to these regions. The agricultural sector is one of the main beneficiaries of these supports. According to Swedish estimates, the level of support directed to the north of Sweden as a part of the Swedish agriculture policy considerably exceeds the corresponding support levels in the EC. It is anticipated that Sweden would wish to maintain a high level of support in the event of accession. The Community would have to verify, in the course of negotiations, compatibility between such support and the Community's relevant policies and legislation, including State aid policy.

6. The existence in Sweden of a variety of measures in the field of agricultural structures and rural development which are specifically adapted to its own situation makes a direct comparison with EC rural development measures somewhat difficult. However, the adoption of the accompanying measures to the CAP reform enlarged the range of Swedish rural development measures comparable with those of the EC. This applies both to a number of horizontal measures and to the regional development measures.[1] As far as horizontal measures are concerned, two of the main measures do not have equivalents in Sweden: aids for investment in farms and aids for processing and marketing of agricultural and forestry products. The same applies to the early retirement schemes or measures aimed at encouraging accounting on agricultural holdings, launching of mutual assistance, relief and management services, start-up for launching producers' groups. EC aids to young farmers or vocational training aids have comparable equivalents in Sweden. This is also true of the set-aside scheme and the conversion scheme, especially after the CAP reform. Sweden has no geographical definition of less favoured areas on which to base payments per livestock units. Direct payments to farmers were introduced for a transitional period, without any geographical definition. These payments are much higher than the maximum amount available under EC legislation. Concerning the regional development measures, regions in the north of Sweden

[1] The possibility of Community aids is analysed in 'Economic and social cohesion', p. 13.