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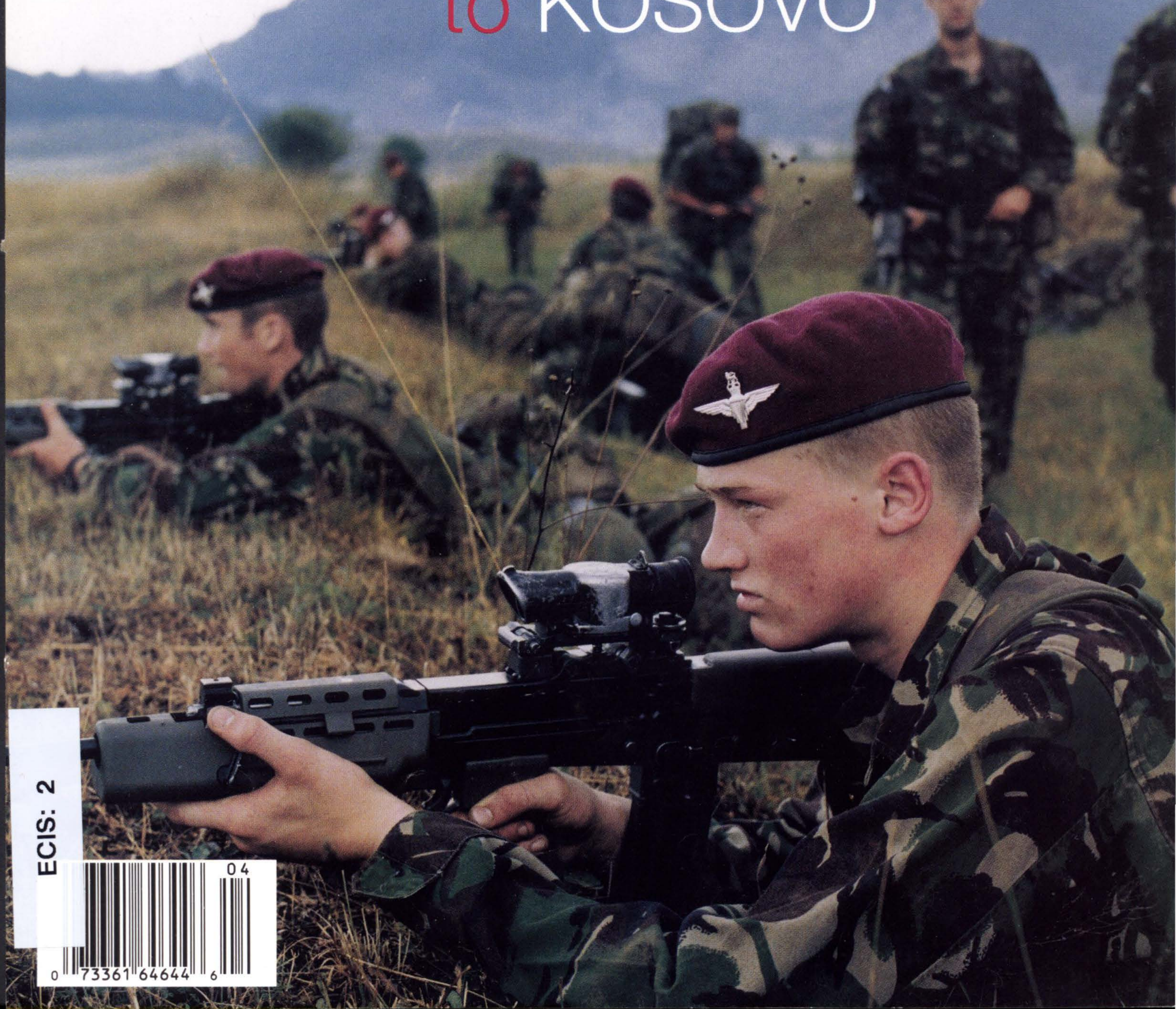

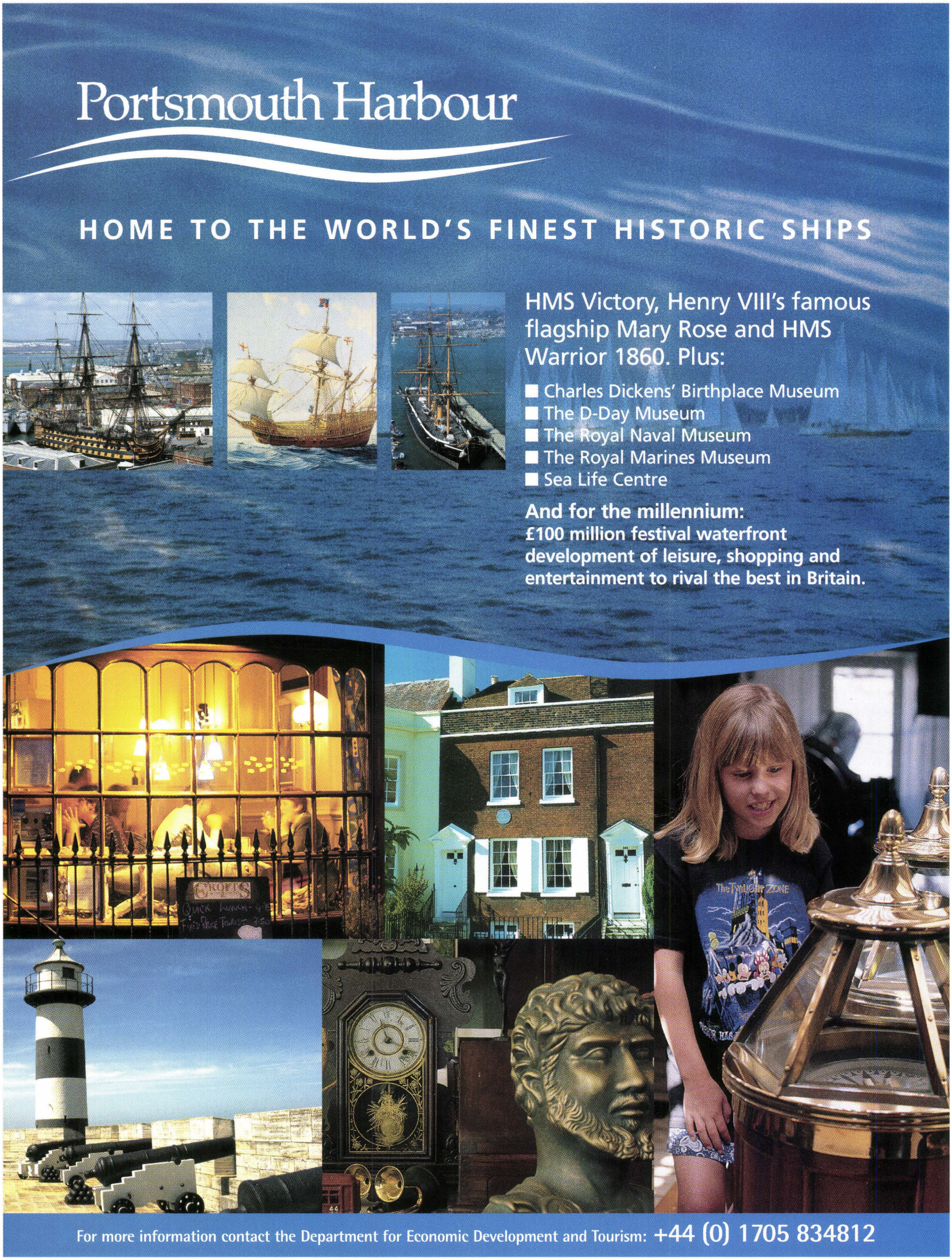
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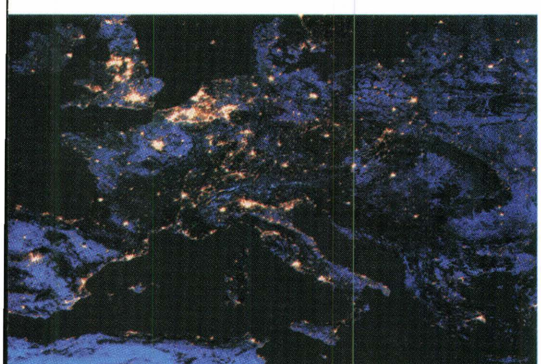
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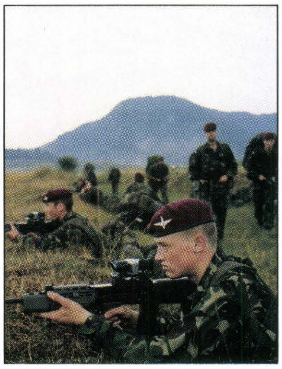
Letter from the Editor

As NATO celebrates its fiftieth birthday with a large celebration in Washington, DC at the end of this month, it faces a number of new missions including the ongoing one in Bosnia and a new and dangerous one in Kosovo.

Martin Walker, reporting from Brussels, presents an in-depth profile of NATO. He looks at NATO's origins, its cold war years, and its future in the new century. Calling NATO "the most successful military alliance in history," Walker goes on to state, "NATO was the shield behind which the European Economic Community could form."



On the cover: UK paratroopers participated in joint exercises that brought together troops from fourteen NATO countries in Albania last summer.

Our profile on NATO begins a new series, "Europe in the New Century," focusing on key organizations and profiling their past, present, and future. Next month, we look at the European Parliament.

Speaking of the European Parliament, Europe's democratically elected forum has just spoken with a loud voice in the case of the independent body of wise men who found the European Commission negligent in many areas. The entire European Commission resigned last month causing a crisis in Brussels. The fifteen leaders of the EU nations swiftly decided to nominate former Italian prime minister Romano Prodi as the new European Commission president.

A new era has now begun in Brussels—an era of accountability to the people of Europe. Hopefully, it will be an era in which the new commissioners will be more in touch with the day-to-day lives of citizens across the European Union. A remote bureaucracy in Brussels will no longer be tolerated. And it seems certain that the new Commission will work hard to be clean and aboveboard in all of its work.

EUROPE presents an overview of the European Council meeting held in Berlin last month under the German presidency to solve outstanding problems under Agenda 2000.

This month, we present a special report on the "Changing Face of the United Kingdom." David Lennon, writing from London, analyzes why Prime Minister Tony Blair continues to enjoy widespread popularity and political support. Meanwhile, the United Kingdom, itself, is undergoing revolutionary changes. *EUROPE* profiles the possibility of a "less united" UK, as upcoming votes in Wales and Scotland will determine their respective futures. London has long held the lofty position of Europe's financial capital. However, can "the City" continue as the continent's financial center if the UK remains outside Euroland?

In our monthly Euro Notes column, Lionel Barber discusses what the recent resignation of Germany's controversial finance minister, Oskar Lafontaine, means for the euro's future.

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WALES

Offering the BEST BUSINESS CLIMATE IN EUROPE

For a country that represents only 5 percent of the UK population, Wales has established itself as an impressive over-achiever when it comes to attracting inward investment. Over the last decade, it has scooped around 20 percent of international direct investment to the UK, proving itself as one of the best business climates in Europe.

Once thought of as being dominated by heavy industries that were largely in decline, Wales has transformed itself into a highly successful base for international and indigenous businesses, offering a modern, dynamic and diversified environment. Since 1983, almost $20 billion of international investment has been attracted to Wales and has led to 175,000 jobs being created or safeguarded.

Among the world class companies already located in Wales are Dow Chemical, Ford, General Electric, Sharp and Sony. Such big names have spearheaded the rapid growth in sectors like electronics, automotive engineering, aerospace and financial services. In addition, many international companies have shown their ongoing commitment to Wales by making significant reinvestments. Ford, for example, has announced eight investments totaling just under $2 billion and both Sony and Kimberly Clark have expanded eight times, reinvesting almost $500 million and over $200 million respectively.

All areas of Wales are proving attractive to international investors, but the prize catch of 1998 was reeled in by Cardiff Bay. Bank One, one of the biggest issuers of Visa and MasterCard in the US, chose the Welsh capital for its European headquarters. The 1,000,000 square foot base now being built on the Millennium Waterfront will create 1,000 new jobs, a substantial boost to the city's prosperity.

Another new American arrival in Wales is California-based International Rectifier – manufacturer of electronic and motion power modules – which is to build a state-of-the-art production facility in Swansea, South West Wales, creating 500 jobs. In all, Wales plays host to around 380 international companies, drawn to the region by several factors, including the efficiency of an established and modern infrastructure, excellent communications and the availability of a skilled, adaptable and committed workforce.

Its high-speed road, rail, sea and air links make Wales a prime gateway to the European market. The skill, reliability and flexibility of the Welsh workforce has raised manufacturing productivity in Wales to 12.9 per cent above the UK average. The Welsh have one of the best industrial records in Europe, with 15 per cent fewer days lost (per 1,000 employees) than the UK average and 69 per cent fewer than the EU average.

International companies are also attracted by the high level of "after sales" support offered by the Welsh Development Agency (WDA). Conceived as a single point of contact for inward investors, the WDA is continually developing further opportunities for networking, sourcing and joint venturing activities, through programs such as its internationally acclaimed Supplier Development Program *Source Wales*.

Another extremely successful concept is the *Team Wales* approach, which ensures that public bodies such as the WDA, the Welsh Office, local authorities, the Training and Enterprise Councils (TEC's) and the private sector work together to meet the needs of incoming businesses.

In the future, international inward investment will remain a vitally important factor in helping Wales maintain the track record it has set in the last ten years as Europe's best business location.

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EYE ON THE EU

Profiling Personalities and Developments Within the European Union

NEW REPORT LOOKS AT HELPING EASTERN ECONOMIES

Lars Anell served for several years as Sweden's ambassador to the EU and was a leading figure in his country's membership negotiations, which led to Swedish accession in 1995. Since then he has been senior vice-president of Volvo, largely responsible for the car and truck company's trade and investment in Eastern Europe and the countries of the former Soviet Union.

As such, he has had intimate experience with both the successes and the failures in the development of western economic links with the former communist countries. He was thus an ideal choice when the Brussels-based think tank, the Center for European Policy Studies (CEPS) was seeking a chairman for its working party on trade and investment in an enlarging Europe.

The working party has now produced a report, "Removing Obstacles to a Deeper Economic Integration in the Broad European Trade Area," and in March Anell presented it to the press. While acknowledging that a great deal had been achieved, notably in Poland, Hungary, and the Baltic states, he said that the overall development of trade and investment had been disappointing, particularly in Russia and other members of the Commonwealth of Independent States (CIS).

The working party's principal conclusion, drawn from the experience of an array of companies deeply engaged in trade and investment in the larger Europe, is that there remains much that European governments could do to stimulate trade and investment *within* the framework of existing trade agreements. It lists a series of steps that EU governments and the EU itself could take and other actions that Eastern European and CIS governments could take.

One problem requiring urgent action is to speed up customs clearance and increase the efficiency of customs procedures. The cost of border delays constitutes a serious constraint upon trade. Delays of up to three days to cross the border into Poland and six days to enter Russia are a commonplace experience.

An even more serious constraint is the lack of transparency and stability concerning property rights in the eastern countries. Cross-border business activity, the report suggests, is dampened by the unpredictability of the legal framework regarding trade and investment and also by frequently changing laws and regulations affecting other areas of business activity such as taxation, accountancy and certification, and product standards.

The excessive complexities of rules-of-origin that control the tariff-free entry of products from the CEECs (countries of Eastern and Central Europe) are a serious barrier to trade, Anell argues. He suggests that all the CEECs should collectively consider adopting the EU's common external tariff (CET) in advance of their achieving membership. Such an action would remove the need for rules-of-origin for the majority of products traded between the CEECs and the EU and among the CEECs themselves. Furthermore, it would make it easier for all of them to increase their exports to the European Union.

Adoption of the CET is recommended not just for those candidate countries currently negotiating membership, but also for those whose applications have been deferred. The potential benefit to them of stabilizing their external tariffs would be considerable, the authors claim, and it should reduce the risk of their being discriminated against by foreign investors.

One problem requiring urgent action is to speed up customs clearance and increase the efficiency of customs procedures.

Anell and his colleagues are critical of the EU for its readiness to apply anti-dumping measures against the CEECs. As they progressively adopt EU competition rules, the EU should desist from launching anti-dumping investigations, but it should deal with complaints under normal EU competition policy. In the meantime, the EU should take steps to penalize EU companies that made 'frivolous' requests for anti-dumping investigations. These investigations, according to a recent OECD study, could cost firms responding to such actions as much as 10 percent of their total export revenue.

Accelerating the harmonization of technical standards and certification procedures, extending the EU's single market into the candidate countries, and enhancing the general business infrastructure are all important ingredients of the working party's recommended strategy. It is also suggested that the fifteen different national export credit guarantee agencies within the EU should be replaced by a single export credit agency.

In several contexts, the working party draws a sharp distinction between the CEECs and the CIS. It pours cold water on proposals for Russia and other CIS members to form free trade associations with the EU. Their level of external protection is currently so high, the working party argues, that a free trade agreement would not be in their interest. Only when they have liberalized their external trade to a far greater extent would increased integration with the EU make sense for them.

Overall, the report's recommendations, if adopted, should prove highly beneficial both to the EU and its eastern neighbors. It is very much to be hoped that they are taken to heart by the governments concerned.

—Dick Leonard

LAFONTAINE'S DEPARTURE SHAPES EURO OUTLOOK

The resignation of Oskar Lafontaine, Germany's mercurial finance minister, will go down as a seismic event in the history of the euro. His abrupt departure restores a measure of predictability to German politics. It also holds out the prospect of a change in the balance of power in Europe in favor of the economic "modernizers" led by Tony Blair of the United Kingdom. Lafontaine's exit also removes a thorn from the side of Wim Duisenberg, president of the European Central Bank, who had left no doubt about his abhorrence toward the Saarlander's brand of Keynesian economics.

Some of the issues raised so bluntly by Lafontaine needed raising. Many believe the ECB should be more transparent in its decision-making and more attentive to the broader macroeconomic climate. Europe's sluggish growth does reflect inadequate demand rather than merely structural weaknesses, such as inflexible labor markets and a burdensome welfare state.

Yet, the stridency of Lafontaine's campaign damaged the confidence of German industry and the credibility of the euro in foreign exchange markets. Lafontaine's attempt to "bounce" the European Central Bank into lowering interest rates and to adopt exchange rate target zones to manage the movement of the euro, dollar, and yen also backfired.

In political terms, Lafontaine's departure offers Chancellor Schröder a fresh start with his Red-Green coalition. It also offers him an opportunity to mend fences with an increasingly disillusioned German business establishment, many of whose leaders expressed pain and outrage toward the Bonn government's plans for the closing of long-cherished corporate tax loopholes without compensating tax breaks.

Since the September general election victory, Schröder's government had shown itself to be split in two fundamental ways. First, there was the Red-Green division between the Social Democrats and the Greens, the junior coalition partner. Second, there was the split inside the Social Democrats between the modernizers led by Schröder, a former governor of Lower Saxony, and the traditional socialists led by Lafontaine.

Schröder never expected he would find himself governing with the Greens. He thought he would be leading a grand coalition with the CDU, the center-right Christian Democrat party, which would dilute Lafontaine's influence. Now his goal of combining the reform of Germany's creaking welfare state and galvanizing the sluggish Germany economy has a chance of success.

Schröder calls this middle course *die neue Mitte* (the new middle), and it bears more than a passing resemblance to Blair's much-touted "third way." Both leaders are seeking to combine US-style rewards and incentives for enterprise with a spirit of fairness and compassion.

It is hard to underestimate the impact of Lafontaine's departure in European terms. Take the example of the EU's secretive monetary committee (now renamed the Economic and Financial Committee). This powerful grouping—comprised of national treasury officials and central bankers—is the critical forum preparing the formulation of macroeconomic policy in the eleven member states of the euro zone.

In the run-up to the launch of the single currency, the key German official was first Horst Köhler (now head of the London-based European Bank for Reconstruction and Development) and then Jürgen Stark, (now at the Bundesbank). Both were fiscal hard-liners. With the SPD-Green victory, Heiner Flassbeck, deputy to Lafontaine and a born-again Keynesian, occupied the post.

Insiders say Flassbeck's presence transformed the macroeconomic debate inside the Economic and Financial Committee. One likens the discussions to the period in 1981-83 when the new Socialist government under French President François Mitterrand sought to pursue "Socialism in one country"—that is, until Jacques Delors arrived as finance minister and pursued a policy of monetary and exchange rate stability.

Now Flassbeck looks set to leave his post at the end of the German presidency of the European Union at the end of June. The sudden switch to economic orthodoxy, which took place in France in the early 1980s, has been sandwiched into five turbulent months in Germany in 1999.

The French government is relieved. Dominique Strauss-Kahn, the French finance minister, is likely to emerge with his position enhanced in Europe. Already dubbed "the thinking man's Socialist," Strauss-Kahn is a resourceful figure who has maintained the respect of the Left in France while winning the confidence of the markets.

He has grasped better than Lafontaine that a public assault on the ECB is no more than a suicide mission. He believes it is better to offer the central bankers a bargain: a modest easing of monetary policy as a reward for a modest tightening of fiscal policy. To borrow from his own slick formulation, Europe should not be following "Reagan-Volcker" (fiscal expansion and tight money) but "Clinton-Greenspan" (fiscal responsibility coupled with a reasonably relaxed monetary policy).

Strauss-Kahn's bet is that the ECB will run a reasonable monetary policy if national governments deliver on their promises to run tight budgets and a degree of structural economic reform. Whether implicit or explicit, this is the "grand bargain" that will determine the success of monetary union in the coming months.

—Lionel Barber

RADIO WAVES

Computers are threatening to become the telephones, televisions, and VCRs of the future. They have already improved on radios as several hundred stations have hooked up to the World Wide Web and allowed listeners half a world away to tune in. Formats and play lists run the gamut—all news, alternative rock, rap, and classical. The BBC and two Web directories make it easy to sort though several dozen radio stations for those interested in listening in on Europe.

The BBC offers hourly updates on the top stories at its news radio site (**news.bbc.co.uk**). The five-minute broadcast focuses on international events and national news in the United Kingdom. Its World Service site (**www.bbc.co.uk/worldservice**) handles the features, sports, and business programming. Listeners can hear a live call-in show on politics, follow London's stock market, or hear the results of a recent cricket match. A portion of the site is also available in Spanish.

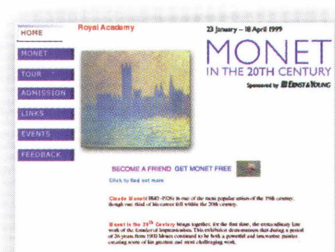
Live Radio Francaises en Direct provides links to several dozen radio stations in France and the francophone world (**www.comfm.com/sites/rdirect/fr.html**). France Info is a source for news twenty-four hours a day, seven days a week. Le Mouv' and Fun Radio are stations popular with French youths. They play pop and rap music in English and French. France Inter Football has live coverage of soccer games. American news broadcast to Africa can be picked up on Voice of America. And Radio Notre Dame offers religious programming affiliated with the Roman Catholic Church. Reflections, prayers, and stories of saints' lives are interspersed with secular music from the likes of the Beatles. Web visitors can go directly to the audio link to any of the stations or can connect with an individual station's Web site.

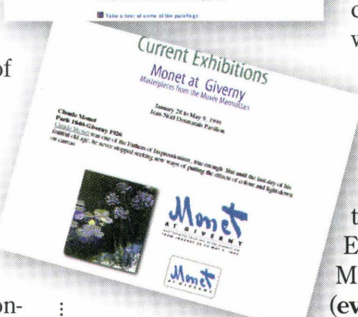
The best sampling of live radio broadcasts from across Europe can be found on Real Audio Europe (**engr.uark.edu/~kaw/europe.html**). Most of the stations feature popular music, although a few, such as Berlin's 93 FM and Flash 96.1 FM in Greece, offer newscasts. The site, which also includes US radio stations, has not been updated in the past year, so some of the links are dead. The quality of the connections (which are made using RealAudio software, which can be downloaded free from **www.realaudio.com**) depends on the speed of modem, the speakers, and the amount of traffic the site is receiving. Recent visits found initial static followed by consistent stereo sound at most sites. Software updates also promise to improve on the sound. With the ability of jumping from a station a few miles away to one across the Atlantic, it makes little sense to bother with a radio dial.

MAD FOR MONET

One of the hottest tickets now in London is to an exhibition of the later works of painter Claude Monet. The grand-scale *Monet in the 20th Century* is about to close its doors at the Royal Academy of Arts following an immensely popular stop at the Boston Museum of Fine Arts. Coincidentally, another Monet show is making the rounds in the US and Canada. Last fall the Portland (Oregon) Art Museum kicked off *Monet at Giverny: Masterpieces From the Museé Marmottan*, a smaller exhibit currently in Montreal and traveling to San Diego and Phoenix, Ariz., before it closes in January 2000. Both focus mostly on the years at Giverny and the famous water lilies. Three of the museums have used the Web to promote the exhibitions and allow more fans of the impressionist icon to explore some of the scenes that inspired him.

The Royal Academy (**www.royalacademy.org.uk/monet/default.htm**) has included eleven of the eighty paintings in the *20th Century* show on its Web site. The paintings illustrate the progression from the height of his impressionist work in 1900 to the more abstract period close to his death in 1926. Viewers can click on the paintings for a larger view and can find out more details of Monet's life in a biography and a chronology of his professional achievements.





The Boston Museum of Fine Arts, in conjunction with underwriter Fleet-Bank, gets a bit more creative in promoting the exhibit. Explore Monet's World (**events/fleet.com**) is a series of pages that follow the artist's travels to London and Venice as well as his home life at Giverny, France. Much of the virtual tour is text that explains how and why Monet painted a series on the

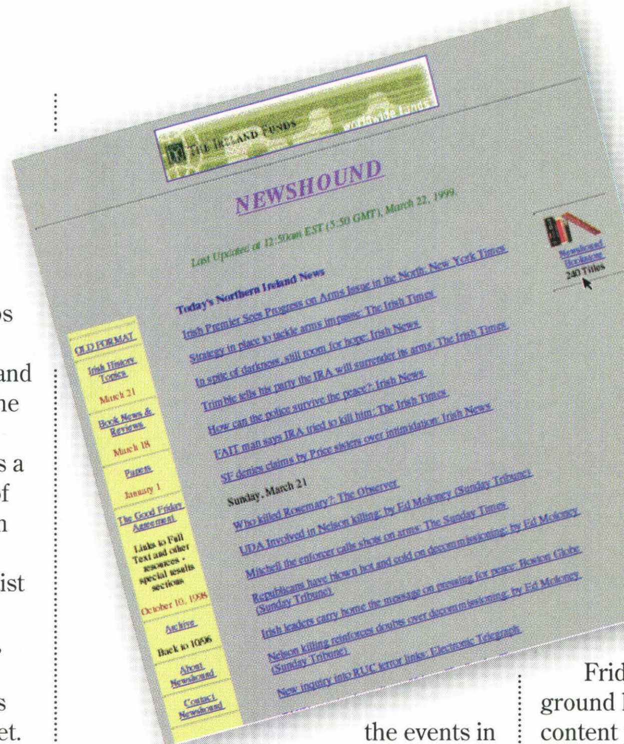
House of Parliament in London or Venice's Grand Canal. Four paintings are incorporated into the site, and visitors can enlarge them, get background information, play two games, or send virtual postcards of the works. A section on Giverny features a map of the property with blurbs about various ponds, gardens, and studios. One of the most fascinating parts of the site is a short video clip of Monet painting in his garden. The footage of the artist with his white beard, white suit, straw hat, and palette in hand, is touted as the only known film of Monet.

One of the most fascinating parts of the site is a short video clip of Monet painting in his garden.

The Montreal Museum of Fine Arts includes several photographs of Monet's garden on its Giverny virtual tour (**www.mbam.qc.ca/en_cours/a-monet.html**). Viewers are invited to move a tiny image of the artist along the pathways of both the flower garden and water garden. He stops along the way to reveal a photo of the Japanese bridge or a cluster of water lilies, a piece of art depicting the scene or a detail of life in Giverny. Some of the photos are from Monet's day. Others are part of a recent series the Montreal museum assigned to a prominent local photographer, who captured the four seasons at Giverny. This exhibit as well as the *20th Century* collection highlights the beauty that kept Monet painting at the lush grounds in his later years. A look at the three museums' Web sites will certainly inspire at least a few art lovers to brave the crowds before the paintings return to their respective homes.

SITE OF THE MONTH: NEWSHOUND

A year after the British and Irish hammered out the Good Friday Agreement to end the violence in Northern Ireland, conflicts between the two sides still feature prominently in the media or at least some of the media. For those who don't want to keep tabs on several overseas newspapers to get a balanced story, a Web site called Newshound (**www.nuzhound.com**) provides a daily update on the events in Ulster with articles from newspapers in Europe and the United States.



The site itself has very little original content. It is mostly a series of links to other news gathering organizations. A log of daily articles on Northern Ireland connects to such on-line media outlets as the BBC, *Irish Times*, *Belfast Telegraph*, and the *New York Times*. The site also tracks Irish history sites and on-line reviews of books on the Irish troubles. Visitors seeking to e-mail letters to the editor will find addresses for several dozen international newspapers. One section of the site explains the Good Friday accords and provides background leading up to it, some of which is content provided by News-hound. Lastly, the site allows visitors to go back as far as October 1996 to see what journalists were writing about Northern Ireland.

—*Christina Barron*

On a Ro

BY DAVID LENNON

Tony Blair rides high in the polls.

Life is pretty good for middle class people in the United Kingdom today. "You have never had it so good," the famous remark of the late premier Harold Macmillan in the 1960s could well be repeated today by Prime Minister Tony Blair who identifies the middle class as his natural constituency.

Tony Blair is hugely popular. Recent opinion polls put the ruling Labor Party twenty-six points ahead of the opposition, twice its 1997 election lead. The economy has sustained good growth; falling interest rates are making housing more affordable; and more money is destined for health and education.

The government is also delivering on its promised radical constitutional changes this year. In May, Scotland and Wales vote for their own parliament and assembly, and by year's end, the hereditary lords will be well on the way to being stripped of their right to vote in the House of Lords. These moves will forever alter the way the UK is governed. (See story on page 11.)

The Labor government has easily survived the enforced resignation of some ministers for improprieties. The prime minister defused the crises by reiterating the message that his government should be judged by real achievements and not on "gossip."

Of course, not everything in the garden is rosy. Some economists fear a recession; the Northern Ireland peace process has been looking very shaky, as the constructive ambiguity of the Good Friday agreement is tested; and many traditional Labor supporters were unhappy with the way London supported Washington in bombing Iraq.

After almost two years in office, the government is poised between promised delivery and the actual results of its actions. Given the time it takes measures to work their way through the economy, it is clear that the government is timing their delivery to ensure that the benefits are evident by the time of the next general election.

If it really is "the economy, stupid," then Chancellor of the Exchequer Gordon Brown was deemed by the *Financial Times* to "have done many things right in managing the economy." The *FT* also asserts that "government finances are now in good shape."

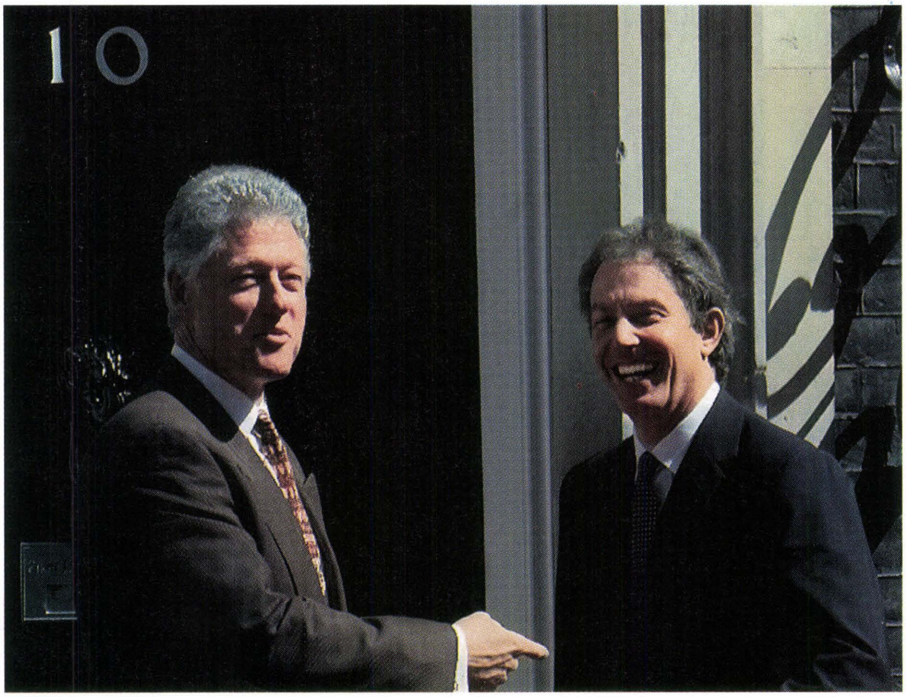
The Institute for Fiscal Studies reported that the government is on course to meet its borrowing and spending targets, even if the economy "flirts with recession." GDP was set to decline in the first half of the year, it said, putting the economy into a technical recession, although growth would rebound in the second half and reach 0.4 percent for 1999 as a whole. The Treasury still believes it can achieve its target of one percent growth this year.

Blair stood by President Clinton from the outset of the Lewinsky affair, and the UK was the only country to join with the US in its renewed military attacks on Iraq.

Brown believes that the series of interest rate cuts by the Bank of England, five in as many months for a current rate of 5.5 percent (at press time), will help the UK economy escape a recession this year.

Analysts are making educated guesses that interest rates will fall to 4 percent and lower over the next two years. This decline will bring UK interest rates closer to those of the euro countries, useful in preparing for possible British entry into the single currency. However, the euro remains an issue that is a domestic minefield yet to be negotiated.

The government is also carefully finessing other changes it introduces, as demonstrated in the new Employment Relations Bill. This legislation proposes a raft of measures to reinforce the role of trade unions and give workers new rights. The changes, however, are far from radical, nor do they reverse the union-crushing legislation of Margaret Thatcher. To do so would have alienated Labor's supporters in big business.



Relations with the US have rarely been better. Blair stood by Clinton from the outset of the Lewinsky affair, and the UK was the only country to join with the US in its renewed military attacks on Iraq, despite the reservations of every other EU member.

This decision reinforced the historical suspicion in Europe that London is a cat's-paw for Washington. While Blair still has credit with his European colleagues, his claim that London alone can speak for Europe in Washington and for the US in Paris, Bonn, or Brussels is wearing thin.

The Atlantic alliance is reinforced by the heavy investment of UK companies in the US—the United Kingdom is the single largest investor—as highlighted by the recent BP and Amoco merger as well as the joint venture between British Aerospace and General Electric Company's defense division.

In domestic politics, the government is fortunate in having a Conservative opposition that does not seem to know who it wants to woo and, indeed, does not even seem to know just what type of party it wants to be.

It is not as though the government has not had its problems. Ministers forced to resign over poor judgement in personal affairs are normally great targets for opposition parties. But the reality is that "whenever voters get irritated by the government, they take a quick look at the Tories, and instantly recoil into the arms of New Labor," as political commentator Andrew Rawnsley rather cruelly but accurately noted.

Tory leader William Hague, faring dismally in the polls, decided to embrace the Republican Party's "caring conservatism" and local empowerment. Conservative officials see Texas Governor George W. Bush as the best US model for their own revival. Tory strategists have been heavily influenced by new Republican thinking that traditional economic issues will no longer win elections for the Right.

This year, one radical proposal that has been embraced across the political spectrum is the government's plan to reform the House of Lords, ending the right of hereditary peers to sit in the upper house. There is little opposition as the popular view of the House of Lords is of a retirement home for out-of-touch, conservative geriatrics.

Blair is as brilliant as President Clinton at showmanship and quotable sincerity. He has been marketed as a good man and continually tries to look and sound like a caring man. The question, however, remains whether he will be able to deliver for the poorer strata of society over the next couple of years in the way he has already delivered for the middle class. Ⓔ

David Lennon is EUROPE*'s London correspondent.*

A Less United Kingdom?

Scottish and Welsh votes will shape the future.

BY DAVID LENNON

The people of Scotland and Wales will go to the polls on May 6 to elect a parliament and an assembly as part of a radical overhaul of the way the United Kingdom is governed. Along with the decision to strip hereditary peers of the right to vote in the House of Lords, this year will see an unprecedented constitutional transformation that may make the kingdom less united.

The British government is creating regional governments in the UK, bringing it into line with the rest of Europe. Northern Ireland is to have its own assembly, and after Scotland and Wales, the English regions may be offered greater local government powers.

The Labor Party promised in its election manifesto that it would offer the people of Scotland and Wales the opportunity to administer their own affairs, rather than have them dictated from the distant UK Parliament in Westminster.

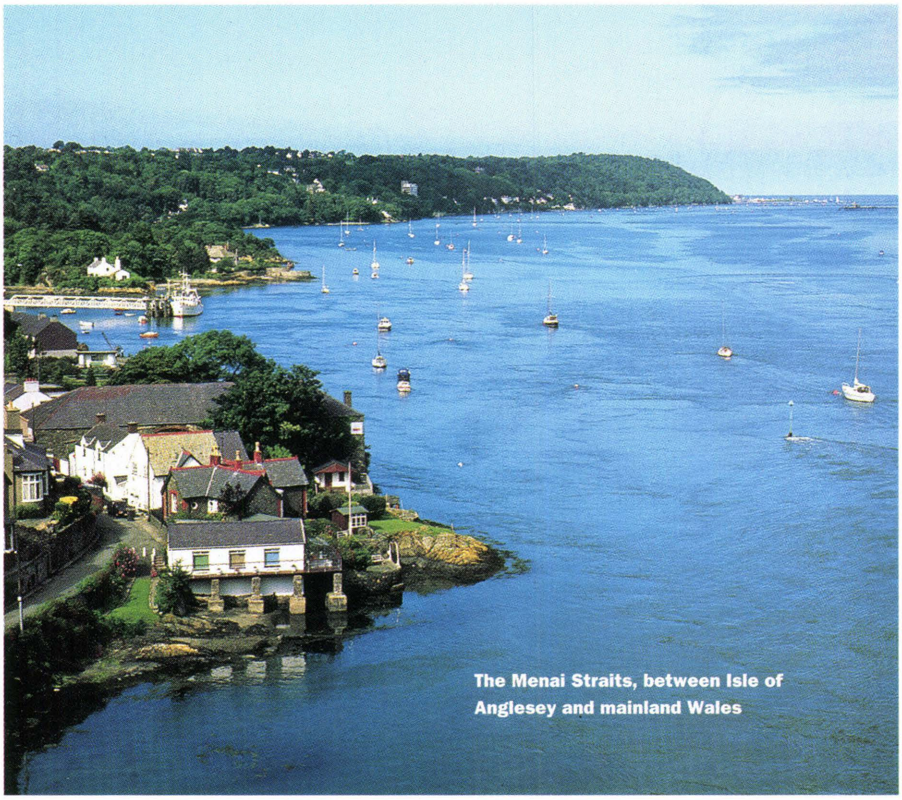
Donald Dewar (right), the UK's Scottish secretary, campaigning in advance of the May elections that will determine how Scotland will be governed.

"Devolution is not an optional extra to the modernization of the UK, nor is it a panacea. It is an essential part of transforming the way we govern ourselves," explains Ron Davies, the former Welsh secretary.

The opposition Conservative Party said that it was deeply concerned that this is the first move toward the dissolution of the United Kingdom. But at the same time, it has accepted that devolution is now irreversible.

Scottish National Party leader Alex Salmond sees devolution for Scotland as simply a stepping stone on the path to Scottish independence after 300 years of rule from London and said that he expected it to come about in his lifetime. The SNP is aiming at transforming the United Kingdom, though Salmond adds buoyantly, "We cannot pretend the history of the last 300 years has not existed. I will go a very long way to work together with the government in London, and we will stay very good chums."

The Scottish Secretary Donald Dewar, the man tipped to become the first prime minister of Scotland if the



The Menai Straits, between Isle of Anglesey and mainland Wales

Labor Party wins enough seats to form a government, says, "This is a real shakeup of our constitution."

The government in London hopes that granting limited regional powers to a parliament in Edinburgh will silence those voices calling for Scottish independence. But opinion polls early this year indicated that the SNP is running neck-and-neck with Labor and, in some polls, even ahead of Labor.

A recent discussion with various Scottish people revealed an enthusiasm for the new parliament but no expectation that this would lead to independence. "We will still be a part of the United Kingdom," said Joyce Magennis from Dundee. A Labor Party candidate for local government, Joyce's expectation is that a Labor-Liberal Democrats coalition will lead the new parliament, but she admits she could be surprised by the performance of the SNP.

A big question is how an independent or even a quasi-independent ministate to the north of England or in Wales would manage its economy. The SNP's Salmond cites Ireland as an example of how the economies of smaller European states have fared better in the past twenty years than larger ones.

While he admits that Scotland's current tax base would not support existing levels of public spending, he believes that any lost subsidy from England could be made up for in moderately higher taxes.

Above all, he believes that the settling of what he calls "the national question" would unleash an entrepreneurial drive so far absent from the Scottish economy. Also a slight improvement in oil prices would cover any shortfall.

The Welsh have shown only lukewarm enthusiasm for the concept of devolution. The vote in favor of creating the new assembly was skimpy, indeed. It is hard to gauge to what extent this is because the assembly will only have secondary legislative powers and no say over taxation and revenue raising.

Some Welsh people appear indifferent to this monumental change. Indeed, Ken Patterson from Cardiff fretted that the changes might mean that he would be forced to learn Welsh, a language of which he claimed, in a lilting Welsh accent, to know not a word. Hard to believe given that all Welsh road signs are bilingual.

Reinventing England

"To be an Englishman is to belong to the most exclusive club there is," wrote American humorist Ogden Nash earlier this century. How true today as constitutional changes leave the English as the only citizens of the United Kingdom without their own national parliament or assembly.

Devolution may require a reexamination of the whole concept of the United Kingdom, from the monarchy to the very concept of Britain, says Scottish National Party leader Alex Salmond. He believes the English will have to drop their ambiguous relationship with Britishness and reinvent English nationalism.

"This government has not shown the slightest curiosity" as to how to frame the relationship between England and the other constituent members of the UK post-devolution, complain some right-wing commentators.

Tory opposition members have been heard to murmur that it may be time to consider an English parliament. They fear the slow evolution of regional institutions foreseen by Labor may not be adequate to deal with the consequences for England of Scottish and Welsh devolution.

"The government is committed to extend the principles of devolution to the English regions as well as to Scotland, Wales, and Northern Ireland, where there is popular demand," says the Department of Environment, Transport, and the Regions, which now speaks for England.

Who guards the interests of England once the others have their own parliament and assembly? "The interests of England continue to be fully covered by the existing machinery of government," says the department.

"England that was wont to conquer others," said King Richard II in other circumstances, "hath made a shameful conquest of itself." I wonder what he would have made of the situation today?

—David Lennon

One reason cited for the cool reception of the plan is that the Welsh national party, Plaid Cymru, had not had anything like the success of the SNP in tapping into historical nationalism.

According to Ron Davies, "Devolution is not a single defining event but a process. The assembly will change and adapt over the years. It will grow in confidence and status. Its power will increase, and it will become the respected forum and authoritative voice of our country."

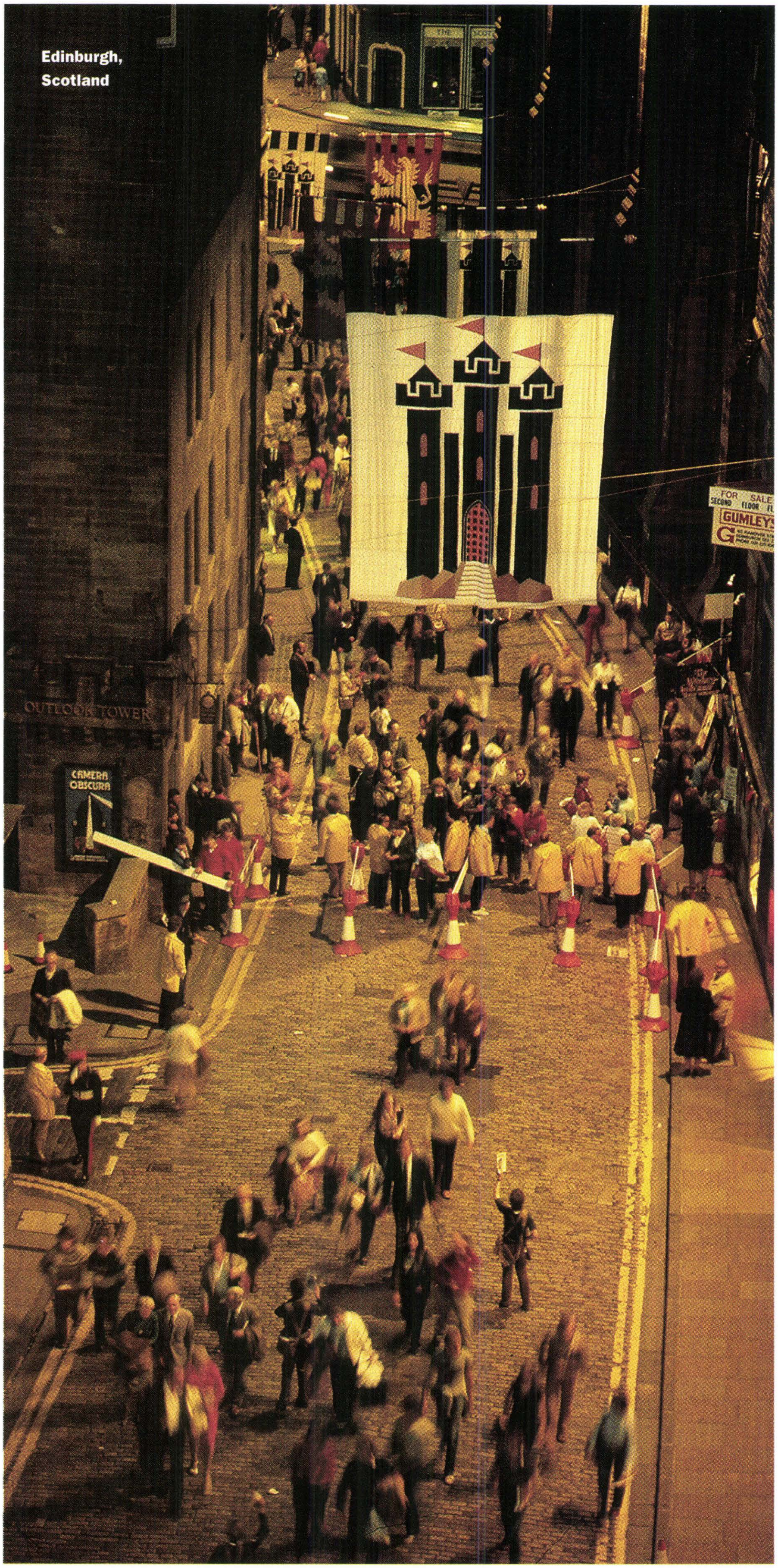
Prime Minister Tony Blair has been making regular visits to Wales to build up support for the assembly and also to try to ensure that the fractious local Labor Party endorses his candidate as potential first minister for Wales.

The government in London hopes that granting limited regional powers to a parliament in Edinburgh will silence those voices calling for Scottish independence.

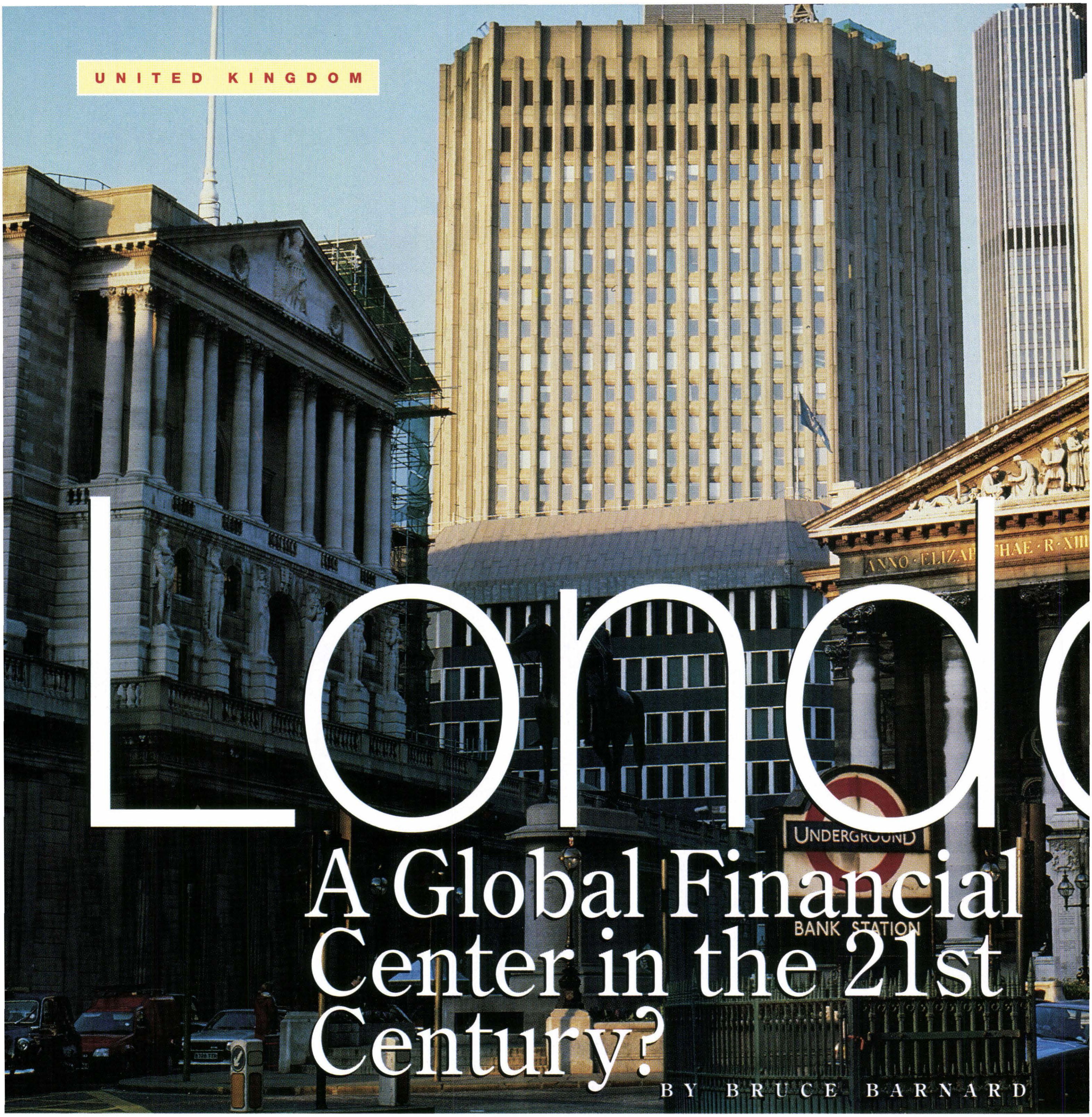
One reason why it is so important for Blair to have his own person heading the Wales assembly is because of fears about how the nationalists in Scotland will fare in the election there. If the SNP do spectacularly well, their fervent nationalism may spread to Wales. If this happens, the whole devolution project could pass from being a controlled exercise in devolution of powers into an event that inflames local patriotism and leads to a genuine breakup of the United Kingdom.

One approach the government is planning to defuse this threat is to establish a joint ministerial committee that will work out of Number 10 Downing Street. The committee would draft concordats to establish common UK-wide policies and to ensure that civil service appointments in Scotland and Wales are made in London, not Edinburgh or Cardiff.

What will happen? No one knows, but certainly this country, or these countries, are undergoing a constitutional revolution unparalleled since the days of Oliver Cromwell. Ⓔ



Edinburgh, Scotland



Lond

A Global Financial Center in the 21st Century?

BY BRUCE BARNARD

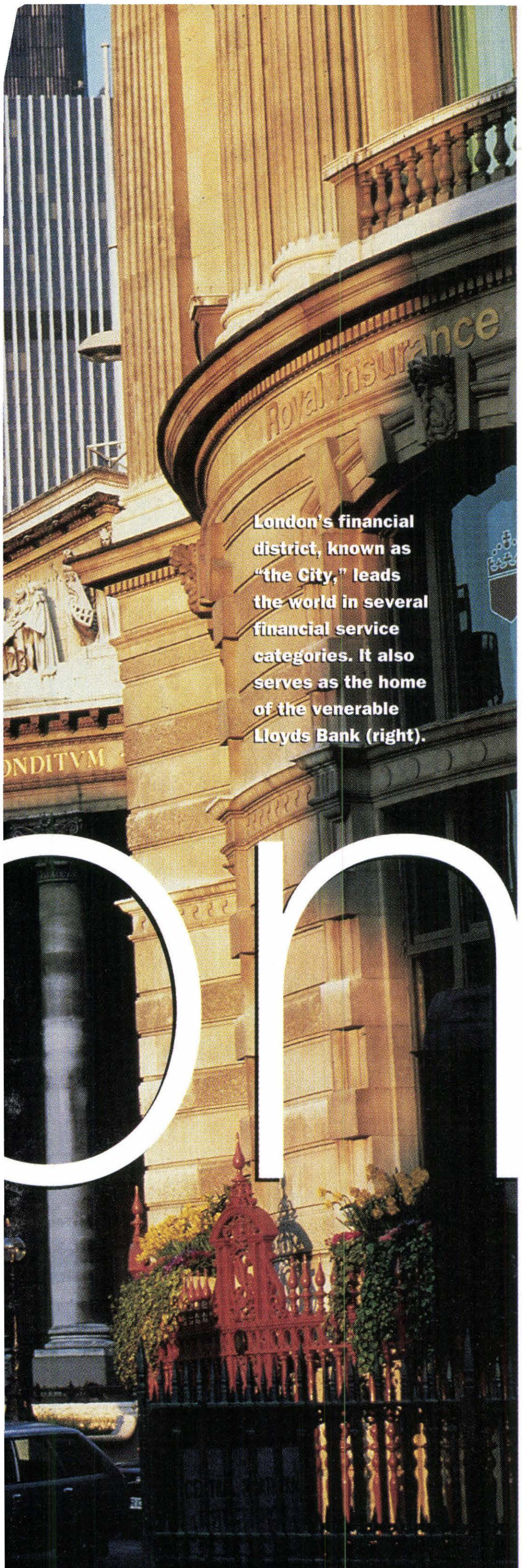
If it was a movie, it would be called *Euro Fear Stalks the City*. In real life, the arrival of Europe's single currency poses a potent threat to the dominance of London's financial district, the famous "Square Mile."

London's enthusiastic welcome for the start of trading in the euro on January 4 was tinged with a concern that it will pay a heavy price for the United Kingdom's decision not to join the first wave of eleven countries in economic and monetary union (EMU).

The presence of the European Central Bank (ECB) in Frankfurt provides a pointed daily reminder that London is an outsider in the world's biggest monetary event since the collapse of the Bretton Woods system of fixed exchange rates in the early 1970s.

During the tense run-up to the euro's launch, the City expressed confidence that it would retain its pole position, a view backed by most bankers, financiers, and traders abroad. There is no reason why London has to be inside the euro zone to trade in euros just as it trades in dollars and yen.

However, the doubts began to surface when the reality of the UK's exclusion from Euroland sank in. So much so that Chancellor of the Exchequer



London's financial district, known as "the City," leads the world in several financial service categories. It also serves as the home of the venerable Lloyds Bank (right).

Gordon Brown has made the impact of the euro on the City one of the five "economic" tests for the government before it decides whether to join monetary union.

There are telltale signs of panic on the trading floors. Lord Levene, the lord mayor of London, warns the City risks losing business to rival European financial centers if the government continues to postpone a decision on joining the euro. "In four to five years, London could start to lose out if the UK's entry into EMU is delayed," he declared.

London is ready for the euro, and the City still handles more euro-denominated business than all the euro zone countries combined, Lord Levene says. "London is still a major financial center, but it cannot hang on to that position if it does not take account of what is going on in the rest of the world."

The City was losing business to more nimble European rivals well before the euro hit the markets. For example, in January 1997, LIFFE, the London futures market, was trading 70 percent of the benchmark ten-year German government bond—*bund*—contracts, one of its most profitable operations. Today, DTB, the German futures exchange, has an 80 percent share.

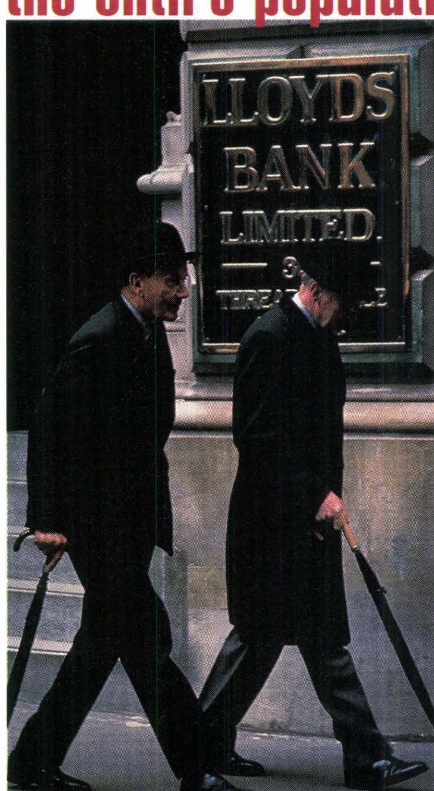
Meanwhile, the London Stock Exchange (LSE) was forced to do the unthinkable last year. Bowing to pressure from top investment bankers, it forged an alliance with the Deutsche Borse, the Frankfurt exchange, which has since been extended to smaller European exchanges. The euro was an essential factor, but globalization was the driving force for change, according to Gavin Casey, chief executive of the LSE.

The arrival of the euro was expected to shrink foreign exchange operations, a London specialty, as the national currencies disappear. However, the euro is sure to become a bigger international currency than those it is ousting. In its first month of trading, the euro was rivaling the dollar as a global reserve currency, accounting for half of all funds raised on the international capital markets, compared with 40 percent for the dollar. By contrast, the combined market share of the eleven euro zone currencies never exceeded 35 percent.

The big question, however, remains who will benefit from this new business. London is way ahead of its rivals, but they pose a bigger threat than ever with the arrival of the euro and the UK's absence providing a once-in-a-lifetime boost to their marketing efforts.

London, however, is a global financial giant among European pygmies. It is Europe's only global financial center, ranking alongside New York and Tokyo. It has more than 30 percent of the world's foreign exchange business, nearly twice that of its nearest rival, New York, according to latest figures from the Bank for International Settlements (BIS). It leads the world in international bank lending and has the world's second-biggest futures exchange. It handles two-thirds of international bond issues and three quarters of international bond trading. It also boasts numerous commodity markets from silver and tin to cocoa and sugar, the Baltic shipping exchange, and the famous Lloyds insurance market. Moreover, it has more US banks than New York and more German banks than Frankfurt. Furthermore, it is the world's biggest net exporter of financial services, raking in more than $8 billion in 1996, according to latest available figures.

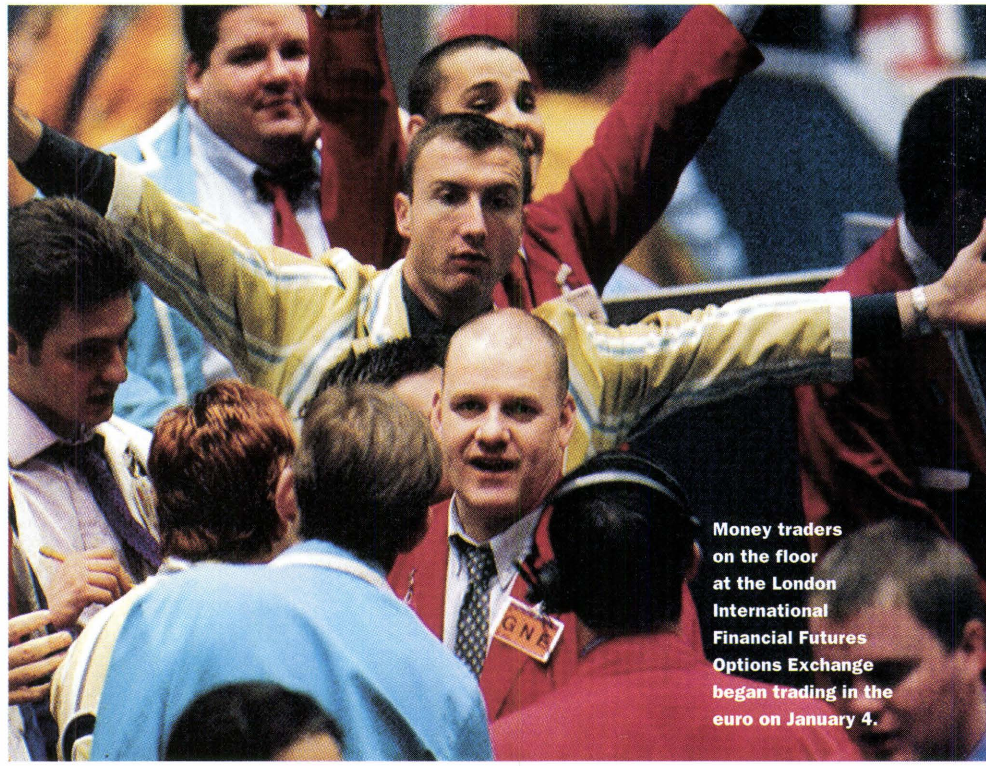
"The City" employs more people than the entire population of Frankfurt.



The City employs more people than

the entire population of Frankfurt, and its big paychecks helped make inner London Europe's wealthiest region last year.

London's rivals say it is sure to suffer from the UK's exclusion from the euro as business gravitates to the capital of Euroland, Frankfurt, and to other euro zone trading centers. "Time is not on London's side," Lord Levene warned. Europe's other financial centers are making up for a late start. Frankfurt is making a strong pitch for futures and derivatives, while Paris is becoming more cosmopolitan with some 35 percent of French stocks held by foreigners. Meanwhile, smaller exchanges and stock markets from Amsterdam and Brussels to Stockholm and Zurich are forging alliances. Europe also is more welcoming to small companies. London's AIM (Alternative Investment Market) index crashed 19.2 percent in 1998, as most investors concentrated on blue-chip stocks in the main market. However, the Euro NM index, an alliance of growth company markets, which is dominated by German high-tech companies, surged 127 percent with 103 listings raising some $5 billion.



Money traders on the floor at the London International Financial Futures Options Exchange began trading in the euro on January 4.

The City, however, is confident it can see off the challengers by using its wits to survive outside Euroland. LIFFE, for example, had virtually no trade in short-term interest rate futures based on Euribor, the euro zone interest rate benchmark, in the first week of trading in the new currency. Working around the clock to come up with a new scheme to allow its traders to switch to Euribor contracts, LIFFE's Euribor business was nearly four times that of Frankfurt and Paris combined within a week.

The City's confidence is boosted by two important factors. First, most foreign bankers, traders, lawyers, and other financial service workers prefer to work and live in London than in Frankfurt, its top rival. Second, the United Kingdom is expected to be a member of Euroland by 2002 when euro notes and coins enter circulation.

But until then fear will stalk the City. ⓔ

Bruce Barnard is a EUROPE *contributing editor and a Brussels correspondent for the* Journal of Commerce.

Vodafone-AirTouch

Europe's largest transatlantic takeover.

BY BRUCE BARNARD

It sounds fanciful. A virtually unknown British company beats two US giants in a battle for an American leader in one of the world's fastest growing businesses to pull off Europe's largest transatlantic takeover. But it's true. Vodafone Group PLC outbid Bell Atlantic and scared off MCI-WorldCom to snare AirTouch Communications, the San Francisco-based cellular phone services company, in a $62 billion deal that overshadowed the Daimler-Chrysler and BP-Amoco transactions of 1998.

The deal underlines the frantic activity in the global telecommunications market. Ten years ago nobody had heard of Air Touch or Vodafone, according to Sam Ginn, chairman of the US firm. It also underscores the fact that Europe is no longer playing second fiddle to the US in these new high-growth areas. While US auto and oil companies could be considered vulnerable to European predators, no one expected the US to be on the receiving end of bids in the high technology sectors. Bell Atlantic was only days away from acquiring AirTouch when Vodafone pounced with a bid worth some $17 billion more.

The Vodafone acquisition is in a league of its own. The largest ever cross-border deal, it has created the US's twentieth-largest firm, capitalized at more than $130 billion and bigger than Deutsche Telekom, Europe's largest telecommunications operator. Moreover, Vodafone's cricket-loving chief executive Chris Gent, who will run the newly merged group, says his aim is to grow Vodafone AirTouch into one of the world's top ten corporations.

The new company will have 23 million customers in twenty-three countries spanning five continents. It will be

Vodafone Chief Executive Chris Gent (right) and AirTouch Chairman Sam Ginn announced their companies' merger on January 18 in London.

the first time a mobile phone company will cover almost all of Europe, large chunks of the US, and the major Asian nations. By 2003 the subscriber base will swell to 40 million, according to a confident Mr. Gent.

The Vodafone coup confounds critics who claim sclerotic, hidebound, and risk-averse Europe will never produce high-tech worldbeaters and is doomed always to trail a more flexible and visionary risk-taking United States.

Vodafone has stolen a lead over its US and European rivals in a market with spectacularly lucrative prospects. Mr. Gent forcecasts that within a decade half the population of the industrialized world will have a mobile telephone, which will still leave an untapped market. It is reckoned that Scandinavia, where penetration is deepest, will have more mobile phones than people in ten years.

At present, Vodafone AirTouch is the only global operator with the other large players being mostly domestic—like Japan's NTT DoCoMo, the world's second-largest operator, and China Telecom, the world's number three.

Technological improvements and tumbling prices will permit fixed line phones to be replaced by mobile phones, putting companies like Vodafone AirTouch in a position to challenge the fixed line operators like AT&T, BT, and Deutsche Telekom.

Vodafone sprung from humble roots, starting life in 1982 as a division of Racal Communications, which won a competitive tender to build the UK's first cellular phone network. It won its independence from Racal in 1991 and continued to make steady, if less than spectacular, progress in the corporate market for mobile phones.

The mobile business didn't look like a moneymaker ten years ago. The phones were cumbersome, battery life was short, and calls were prohibitively expensive. In fact, AT&T sold off its mobile business believing it lacked any potential.

Vodafone's focus changed dramatically when Gent took the helm. He launched aggressive marketing campaigns to stimulate the unmined consumer market and started buying stakes in foreign mobile operators, totally convinced wireless telecommunications was a gold mine.

Gent also reinvented Vodaphone, which had become the market leader in the 1990s but had also become staid in the process, losing the marketing battle to more imaginative newcomers. He slashed prices, created a new logo, spent heavily on advertising, and launched "pre-paid" tariffs, which liberated customers from service contracts and monthly rental charges. Business grew twice as fast as the gung-ho Gent predicted, with Vodafone adding 993,000 new subscribers in the final quarter of 1998, taking its total worldwide customers to 9.1 million.

Vodafone is on a roll making pre-tax profits of $787 million on revenues of $2.58 billion in the first half of the current financial year. AirTouch is also powering ahead with net income surging 54 percent last year to $608 million on revenue up 44 percent at $5.2 billion. Meanwhile, the number of overseas subscribers jumped 83 percent to 5.7 million, overshadowing domestic growth of 'only' 18 percent.

Vodafone's success springs from the fact that Europe, and to a lesser extent Asia, are ahead of the United States in wireless telecommunications. The European industry grew on the back of a single digital standard, called GSM, and a largely deregulated market for mobile telecoms. The Nordic region boasted the most open market, which is why it has two of the world's top mobile phone manufacturers—Finland's Nokia, which is outselling Motorola, and Sweden's Ericsson. The European market for mobiles grew by 10 percent last year, twice the growth in the US, which suffers from having several competing digital systems.

Some industry analysts go so far as to suggest that mobile telecommunications could have a bigger impact on the way people live and work than the heavily hyped Internet. In time, it is foreseen that it will become an indispensable tool for cashless shopping, electronic banking, and the electronic newspaper.

There is so much at stake that the United States and the European Union are at loggerheads over a global digital standard for a third generation of mobile phones, although the transatlantic merger of Vodafone and AirTouch could help to resolve the dispute.

As the only truly global operator,Vodafone AirTouch is in pole position to win the coming marketing battle. But the competition is fighting back with the major players seeking alliances to narrow the gap with the frontrunner. AT&T says it wants to become a global force in the wireless business within five years either through overseas acquisitions or network agreements with companies such as British Telecom. Companies like the UK's Cable & Wireless, which has operations in thirty-three countries, and Luxembourg-based Millicom International, which is present in twenty nations, will seek partners to achieve global coverage.

Meanwhile, cellular phone operators are forging alliances with Internet software and technology companies to create wireless services that will make data accessible anywhere via palm computers and "smart" mobile phones.

It's a revolution and Europe is in on it.

The Vodafone coup confounds critics who claim sclerotic, hidebound, and risk-averse Europe will never produce high-tech worldbeaters and is doomed always to trail a more flexible and visionary risk-taking United States.

TRAVEL

EUROPE

UK Becomes Top Global Investor

The United Kingdom ousted the United States from the top of the global cross-border takeover rankings in 1998 with British Petroleum's $61 billion acquisition of Amoco accounting for almost half its total $127 billion spent.

It was the first time in eight years that the UK beat the US, which spent $124 billion on foreign firms, up 50 percent from 1997. The UK offered the most popular targets, underscoring the strength of the bilateral and investment relationship. The US accounted for 80 percent of cross-border deals by British firms, according to a survey by KPMG, the international accountancy firm.

The UK kept up the pace in 1999 with Vodafone's $62 billion acquisition of AirTouch of the US, confirming the continuing attractions of a US presence despite the launch of the euro.

The burst of takeover activity in 1998 and the first quarter of 1999 consolidated the UK's position as the biggest investor in the US ahead of Japan, which has slashed spending, and the Netherlands, which kept up the pace with insurer Aegon's $9.7 billion purchase of Transamerica Corp.

British investment is entering new territory with the steel and utility sectors attracting the attention of companies seeking global expansion. National Grid, one of the UK's two national electricity generators, spent some $4 billion in the past two months on utility companies in New England, and Scottish Power made a $11.8 billion bid for Oregon-based PacifiCorp. Meanwhile, British Steel is ready to spend as much as $800 million on an independent steel distributor in the US as part of a global expansion that may also involve moves into Germany and Poland.

British firms continued to move into niche markets. Recent deals include National Express's acquisition of its second US school bus operator, and Zotefoams, a maker of synthetic foams, investing in a new plant in Cincinnati to help expand its current 15 percent US market share.

—Bruce Barnard

Traveling Cheap

Low-cost European airlines are cutting fares and making travel easier.

BY DAVID LENNON

The EU's third liberalization package of December 1992 is not what the average airline passenger thinks of when purchasing a low-fare ticket in Europe, but perhaps he or she should.

The proliferation of airlines offering highly competitive fares since that date has revolutionized European air travel, especially from the United Kingdom. New airlines have been created, and today travelers can fly from most airports in the UK to almost anywhere in the world and for a price that is, frankly, unbelievable.

"You can fly from one end of Europe to the other for the cost of two hardback books," one commentator pointed out in an attempt to put the new airfares in perspective. "In the past, flying to the south of France was the preserve of the few," says EasyJet founder Stelios Haji-Ioannou, "now everyone can afford it."

Franco Mancassola, chairman of Debonair, says, "Our goal is to make air travel available to everyone. Deregulation stimulated the market, and today more people are traveling than ever."

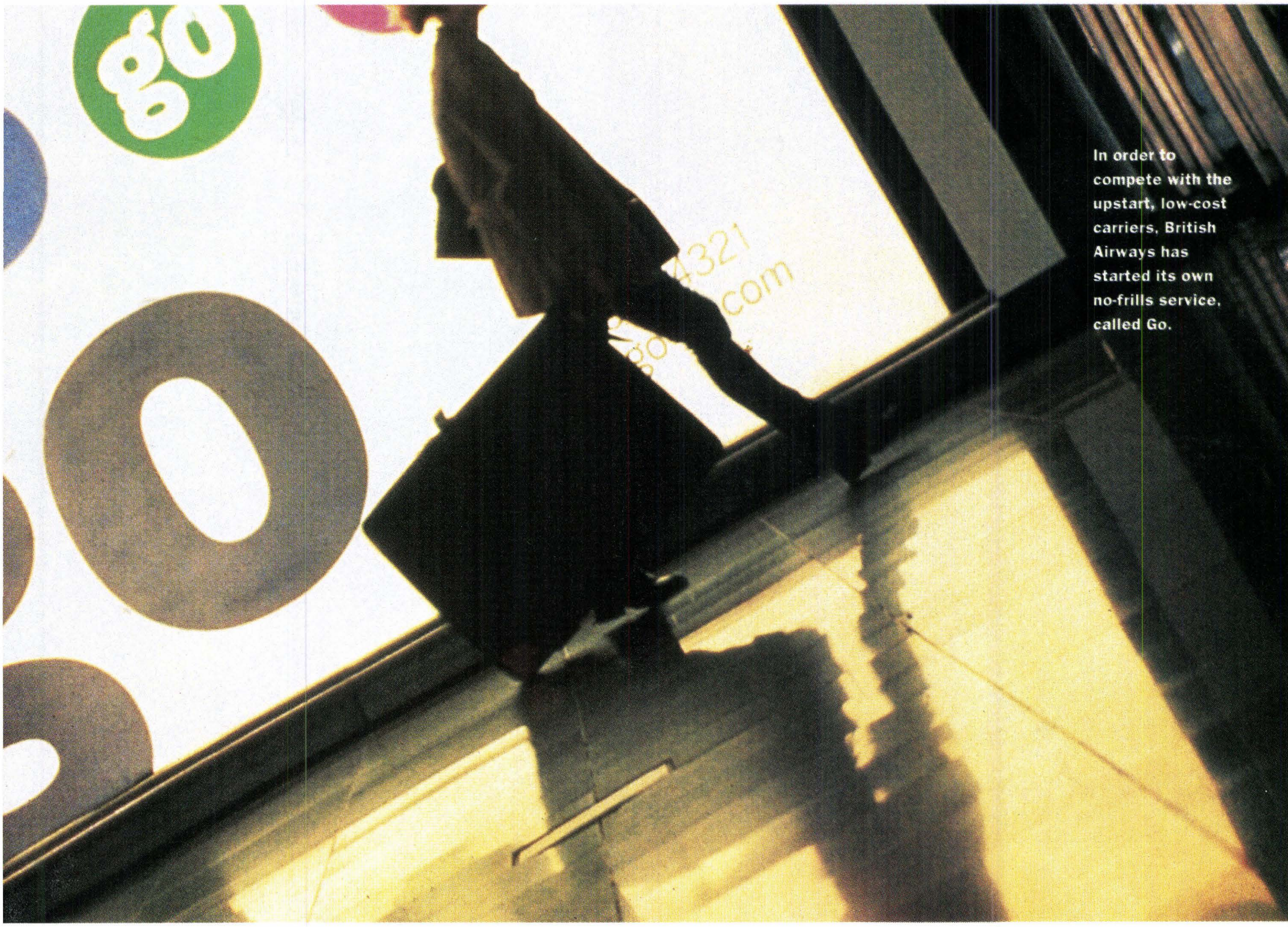
EasyJet, Debonair, and Ryanair are just three of the new players in the low-cost airline business. Competition became so fierce that national carrier British Airways had to set up a new airline to compete. It is called Go. "This altered the levelness of the playing field," complains Mancassola, and his view is echoed by the others.

Essentially the EU directive was similar to the US deregulation of the 1980s. It meant that any European carrier could fly to any destination and demand landing slots. In fact, British Airways took Air France to the European Court of Justice and won when the French carrier refused to give it additional slots in Paris.

The Civil Aviation Authority, which regulates British aviation, welcomes the dramatic changes. "Our view is that the competition improves the deal for the customers," explains Richard Wright of CAA.

The success of the new operators he ascribes to lower operational costs, high load factors, and no-frills service. He might also have added innovative

Stelios Haji-Ioannou's three-year-old EasyJet is already turning a profit.



In order to compete with the upstart, low-cost carriers, British Airways has started its own no-frills service, called Go.

marketing, such as one-way fares, direct marketing, and flying to and from secondary airports rather than the international hubs.

Why did they choose to set up in the UK rather than some other EU country? "Britain is at the forefront of the airline industry in Europe," explains Mancassola. "They pioneered charter flights in the fifties and sixties. They are great travelers, along with the Germans, and cost structures are more realistic."

However, even the new airlines do have to contend with similar passenger service charges at the airports, especially the departure tax, which was introduced here two years ago. In fact, Ryanair recently offered a London-Dublin-London ticket for £29 ($48), which their advertising specifically states "includes the ridiculous government tax of £20 ($33)."

EasyJet, which was set up three years ago by Haji-Ioannou, son of a Greek shipping tycoon, made pre-tax profits of $2.3 million last year, compared with a loss of $3.3 million in 1996–97. He is now planning to float the company on the London Stock Exchange and NASDAQ early next year.

EasyJet is a direct-booking-only airline—its telephone number is painted in huge numbers all along the fuselage of its planes—and the chairman is delighted to report that the Internet now accounts for 15 percent of sales.

Of course, there are some downsides to the lower fares. There may not be a backup aircraft available in case of any problems, and most tickets are not changeable or refundable.

The Civil Aviation Authority is delighted about the new competition because it lowers fares for passenger, but it is also concerned about the danger of fierce price competition between two airlines flying to the same destination resulting in them going out of business and then leaving the route to higher prices set by a sole operator.

"We need to be aware that after the wholesale deregulation in the US in the 1980s, today there are now fewer destinations being served by fewer carriers at higher prices," says Richard Wright.

"We could have the same result here if the EU regulators are not vigilant," says Debonair's Mancassola, who was vice-president international with Continental during the US deregulation. "They should stop those strategic alliances between the national carriers which are designed to crush competition."

The spread of the low-cost, no-frills carriers has been one of the most striking developments in airline competition in Europe in recent years. It remains to be seen whether they will be able to withstand increased cost pressures as they expand.

In the meantime, European travelers have to decide whether to buy a couple of books this weekend or to fly down to Rome. ⓔ

BUSINESS

Satellite photo showing Europe's night lights from space.

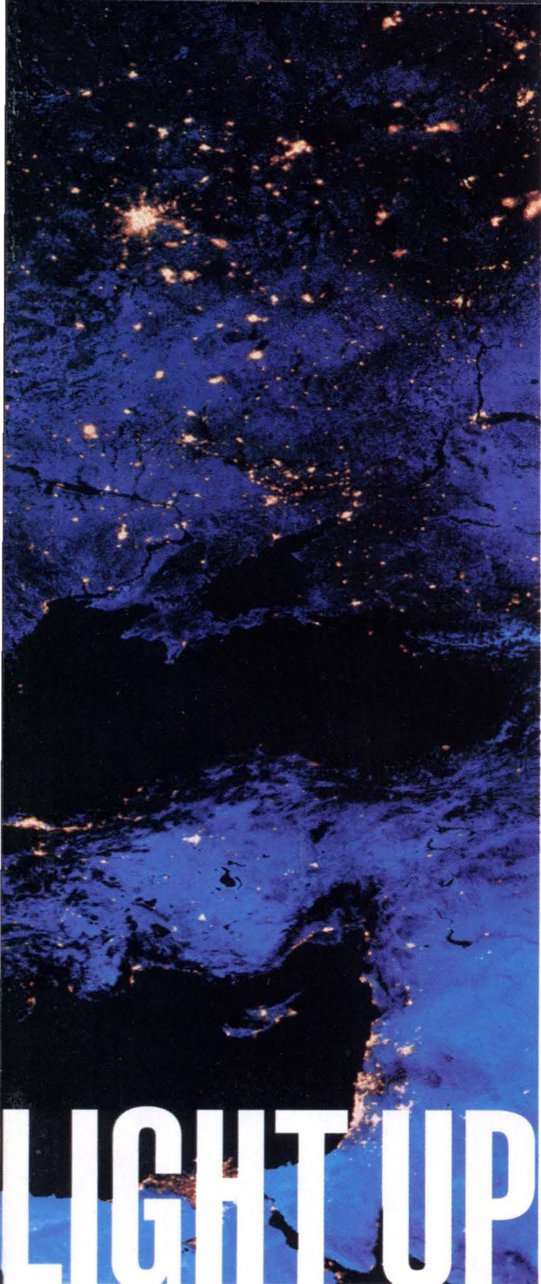
ELECTRICITY MARKETS

Power starts flowing through Europe's single market.

BY BRUCE BARNARD

Electricity is flowing through Europe's single market. Deregulation has finally swept through one of the last bastions of protectionism in the European Union—its $200 billion-a-year electricity market. In a landmark development, the industry was partially pried open on February 19, paving the way for cross-border competition and sharply lower energy prices for European companies.

The EU has opted for a step-by-step approach, reflecting the wide differences among its member states with



some like the United Kingdom, Sweden, and Finland operating open markets, while others like France were served by a single state-owned monopoly.

From now on, large industrial consumers using more than 40,000 megawatt hours a year, which account for around 23 percent of the market, can choose their supplier from anywhere in the European Union. The EU will gradually broaden the competition so that a minimum of 35 percent of the market will be open by 2003.

There are no technical obstacles to trading electricity across borders. A pan-European electricity grid has existed for nearly fifty years, but its use was restricted to swapping supplies to iron out fluctuations in national markets.

However, no one expects an overnight conversion to a free electricity market as the monopolies, abetted by their protective government owners, draw up their defenses against the newcomers. France, which fought hard to dilute liberalization, has made clear that Electricite de France (EdF), its former state monopoly and the world's biggest electricity company, will keep control of the French transmission grid.

Nevertheless, most analysts say liberalized markets like the UK and Scandinavia will "infect" relatively closed markets such as Italy and France to create a genuine single market, at least for large companies, within ten to fifteen years. At present, electricity prices vary widely, with industrial customers in Austria, Germany, and Italy paying up to 60 percent more than firms in France, which has a surplus of cheap nuclear generated supplies. High energy prices are often cited as one of the essential reasons for Europe's lagging competitiveness in global markets.

Liberalization will bring instant relief. British firms have reduced their electricity bills by as much as 30 percent since the power sector was deregulated in 1990, and Deutsche Bank reckons German companies can expect a 25 percent cut as they put electricity contracts for individual plants out for bid. Some had negotiated lower prices before the EU directive took effect and enjoy rates as low as those in the US and Canada. Moreover, French companies do not intend to be left behind despite the difficulties in their national market. Usinor, the steel maker, has spurned EdF and signed a contract with Air Liquide to supply electricity to its mill in the northern French port of Dunkirk. The UK continues to lead the way in the EU with ordinary domestic consumers being able to shop around for the cheapest supplies. It will be a long time before all EU households enjoy this freedom, but other countries are already planning such liberalizations. Spain, where electricity was a state-owned monopoly just a few years ago, plans to phase in UK-style deregulation by 2007.

Real competition will not flourish until continental Europe follows the UK's lead and breaks up the industry, separating the generators and the distribution companies.

In some parts of Europe, electricity is becoming a tradable commodity. A new electricity exchange will open in Amsterdam in May. Meanwhile, electricity is already traded in Nord Pool, the Nordic market, and in the United Kingdom.

Deregulation is also exposing Europe's electricity market to the mergers and acquisitions frenzy that has swept through most other sectors. US utilities were first off the mark, taking over eight of England's twelve regional utilities with the deal making climaxing last May when Texas Utilities Company paid $10.4 billion for Energy Group PLC, the UK's largest electrical distributor.

Europeans are now going on the M&A trail, with Imatran Voima (IVO) of Finland paying more than $2 billion for Stockholm Energi and EdF buying London Electricity, the British capital's supplier, from Entergy of the US for $3.2 billion.

DEREGULATION IS ALSO EXPOSING EUROPE'S ELECTRICITY MARKET TO THE MERGERS AND ACQUISITIONS FRENZY THAT HAS SWEPT THROUGH MOST OTHER SECTORS.

European utilities, facing stiffer competition at home, have also discovered the US and bought clutches of power plants across the North American continent. Among the most recent deals were Scottish Power's $11.8 billion bid for Oregon-based PacifiCorp and the UK's National Grid's $4 billion purchases of New England Electric System and Eastern Utilities. In another unexpected move, Vivendi, the French utility, teamed up with Marubeni, the Japanese trading group, to buy twenty-three power plants from the New Jersey-based utilities company GPU for $1.7 billion and a further twelve from Boston Edison for $657 million.

Electricity trailed telecoms, airlines, and even mail services in the EU liberalization drive, but it is fast making up for lost time.

EUROPE Update

APRIL 1999 VOLUME VII/NUMBER 4

WHAT THEY SAID
...ABOUT THE RESIGNATION OF THE EUROPEAN COMMISSION

"It is becoming difficult to find anyone who has even the slightest sense of responsibility."
—Excerpt from the report by the Committee of Independent Experts, which was appointed by the European Parliament to investigate allegations of fraud, mismanagement, and nepotism in the European Commission

"It is a disaster and it requires speed and ruthless determination to deal with."
—Sir Leon Brittan, vice-president of the European Commission

"No, it is not business as usual. It can't be. We resigned on Monday night."
—Neil Kinnock, European commissioner for transportation

"I note that on the basis of a tiny number of cases of fraud and malfunctioning, which did indeed merit criticism, the committee's report paints a picture of total absence of responsibility on the part of the institution and its officials. This picture is distorted. I consider the tone of the report's conclusions to be wholly unjustified."
—Jacques Santer, European Commission president

"Maybe I was a little careless."
—Edith Cresson, European commissioner for education and research, responding to the Committee of Independent Experts' report, which criticized her behavior as a commissioner

"It's necessary for the Commission to go. This is a devastatingly hard-hitting report about the failures of the European Commission."
—Pauline Green, leader of the European Socialists party in the European Parliament

"This is an opportunity for a new beginning and a new culture of political responsibilities and democratic accountability in the European Commission."
—Wilfried Martens, leader of the Christian Democrats in the European Parliament

"We have a very competent parliament, a council, and a presidency. Europe is not without leadership and that will become clear."
—Gerhard Schröder, German chancellor

"What we've got to do now is to use this event...to drive through root-and-branch reform in Europe."
—Tony Blair, British prime minister

"It is a serious situation for the EU, but I won't hide that I feel some relief."
—Göran Persson, Swedish prime minister

"There are a lot of allegations of irregularities that have not been addressed yet."
—Paul Van Buitenen, the Dutch auditor whose disclosures on fraud and nepotism led to the European Parliament's investigation

"Romano Prodi is a solid candidate who has demonstrated that he is competent and qualified to do this job."
—Abel Matutes, Spanish foreign minister

REPORTER'S NOTEBOOK

Elections in Finland

Finns went to the polls to vote for a new parliament on March 21. Although Prime Minister Paavo Lipponen's Social Democrats lost more than 5 percent, it retained fifty-one seats and maintained its position as the biggest party in the 200-seat Parliament. However, the main opposition Center Party, led by Esko Aho, won forty-eight seats and nearly one-fourth of all votes cast, a gain of some 4 percent over the last election.

Lipponen's government is comprised of an unorthodox four-party coalition that includes the Social Democrats and Socialists, the Conservatives, and two smaller parties, the Swedish Peoples Party (a party representing Swedish-speaking Finns), and the Green Party. Together the coalition won 140 seats, more than enough to remain in place for another four years.

However, Lipponen, who will remain as prime minister, called his party's performance "a defensive victory." Political scandals contributed to the party's troubles in the run-up to the election, but their biggest obstacle remained Finland's high unemployment. Four years ago, Lipponen had promised to halve the jobless rate. Many believe the party's traditional electorate would have responded favorably to a drop to 8 percent. But with nearly 11 percent of Finns out of work, voters held Lipponen and the Social Democrats responsible.

Although the Lipponen government has led Finland out of recession, the Conservative Party managed to capitalize on Finland's robust economy. It gained some seats but not as many as expected and not enough to unseat the Social Democrats' position as leader of the government.

Notably, the election saw the fewest Finns vote in nearly half a century. Only 65 percent of the electorate cast ballots in what was widely regarded as a lackluster campaign that included eighteen parties and some 2,000 candidates.

The results, however, likely elicited a sigh of relief from the EU bureaucracy in Brussels. Finland will assume the six-month EU presidency during the second half of this year. Since the current government will remain in power, the same, familiar pro-Europe officials are likely to usher in Finland's presidency.

—*Thomas Romantschuk*

EU NEWS

Berlin Summit Prepares for EU Enlargement

European Union leaders struck a landmark accord to reform the fifteen-nation bloc's finances to prepare for its expansion to the former communist countries on its eastern borders in the next century.

Last month's Berlin summit was dominated by the NATO bombing of Yugoslavia and the appointment of former Italian premier Romano Prodi as the new European Commission president. However, EU leaders also managed to hammer out a deal that broadly achieves the EU's aim of stabilizing its $105 billion annual budget in real terms until 2006.

The agreement on the so-called Agenda 2000 package was only "slightly above" the original aim of freezing spending, according to Gerhard Schröder, the German chancellor and summit host.

The compromise that emerged from twenty hours of horse trading, however, marked a defeat for countries like the United Kingdom and Sweden that had urged a radical reform of farm spending, which swallows more than 40 percent of the EU's budget. The summit agreed to limit spending on the Common Agricultural Policy (CAP) at an annual average of 40.5 billion euros ($43.5 billion) until the end of 2006. But it postponed plans to overhaul dairy prices from 2003 to 2005, cut the support for cereals by 15 percent (rather than the 20 percent proposed by the Commission), and threw out a plan to reduce direct aid payments to farmers over time.

While the agreement fell short of expectations, it ended a long period of uncertainty for five Central and East European countries that had been negotiating their entry into the EU in a vacuum, fearing that failure in Berlin would have further delayed their accession. However, Günter Verheugen, Germany's state secretary for foreign affairs, insisted after the summit that "the conditions for (EU) enlargement have been created."

The five Central and East European applicants—Poland, Hungary, the Czech Republic, Estonia, and Slovenia—began formal negotiations almost a year ago and had hoped originally to be EU members at the beginning of the new millennium. (Cyprus is also negotiating entry into the EU.) But the most realistic entry date for the front-runners, Estonia and Hungary, is around 2004, and further slippage is possible if the Berlin accord fails to keep EU farm spending in check.

Critics of the Berlin deal said it had failed to meet the twin targets of preparing the EU for enlargement and for talks to liberalize global farm trade that begin at the end of the year under the auspices of the World Trade Organization (WTO).

If the EU applies the same criteria for its "structural" funds (which are designed to promote economic development in its weaker regions) to countries like Poland as it does to say, Spain, spending will spiral out of control. Moreover, the CAP deal will have to be renegotiated in the WTO talks in the face of an onslaught by the US, Canada, and Australia against farm handouts.

—*Bruce Barnard*

EU Members' Views Differ on NATO Action

The long-threatened NATO air attacks against Serbia began as Europe's fifteen leaders gathered for their summit in Berlin and immediately exposed the differences between the EU's eleven NATO members and the four neutrals. Austria said that its neutral airspace could not be used by NATO warplanes. Finland and Ireland insisted that the EU's formal communiqué should contain no endorsement of the attacks, which had not been given an explicit mandate by the United Nations Security Council. Greece, a NATO member but friendly to Serbia and alarmed that an independent Kosovo could be the core of an Islamic greater Albanian nation that might destabilize the region, pointedly refused to make its aircraft or bases available for the NATO assault.

The main NATO allies, led by the United Kingdom, France, and Germany, remained steadfast, and aged veterans of World War II marveled at the way the UK's Royal Air Force and the German Luftwaffe were now flying bombing missions side by side as European allies. Italian Prime Minister Massimo D'Alema, whose coalition government depends on the votes of Communists who oppose the air strikes, said he hoped for an early political settlement.

The Kosovo crisis came embarrassingly early for the Europeans, who were hoping to make their new European defense identity into a reality by leading the planned NATO mission to enforce a Kosovo peace settlement. Serbia's refusal to sign the deal and the massive reinforcement of its forces in Kosovo in defiance of the cease-fire agreement reached last October forced NATO to carry out its threats of air strikes. The US led this aerial assault because the European allies had neither the cruise missiles nor the numbers of warplanes required to seize control of Serb airspace.

"The lesson is that Europe has to modernize its military capabilities," said British Prime Minister Tony Blair, as European leaders pondered how to stabilize and pacify the region after diplomacy had failed and military action had yet to prove its ability to force Serbia into compliance.

—Martin Walker

EU-US Beef Dispute

Last month the Clinton administration published a preliminary list of a number of European products that could be slapped with 100 percent duties this July if the EU does not lift its ban on hormone treated beef. The sanctions concern $900 million worth of European products, including cough drops, bottled water, chocolates, truffles, foie gras, mustard, and motorcycles. The EU, which stated that they regret this action, stands ready to continue discussions with the US with a view to reaching a mutually acceptable solution before the May 13 implementation deadline.

New German Finance Minister

Hans Eichel, Germany's finance minister-elect, will take up his new position on April 23. Until April 8, Eichel was premier of the German state of Hesse. Eichel, a tax expert, will replace Oskar Lafontaine, who resigned last month.

Commissioner to Seek Italian Presidency

Emma Bonino, the European commissioner for consumer affairs, humanitarian aid, and fisheries, has signaled her intention to run for Italy's presidency. Both houses of parliament elect the president, Italy's head of state.

NATO Adds Three Members

NATO ceremonies held at the Harry S. Truman Library in Independence, Missouri, officially welcomed Poland, Hungary, and the Czech Republic into the military alliance. NATO Secretary-General Javier Solana said, "The accession of the Czech Republic, Hungary, and Poland…is perhaps the clearest demonstration of the fact that Europe is growing closer together."

Slovakia Hopes to Join EU

Slovak Prime Minister Mikulas Dzurinda believes that by the end of the year his country would be ready to join the front-runners for European Union membership. "I'm optimistic, and I am sure that Slovakia will be invited," the Slovak prime minister stated in Frankfurt last month.

Website on Commission Mismanagement Gets One Million Hits

The Internet site hosting the report on mismanagement in the European Commission received more than one million hits on its first day, a European Parliament official reported. The report (**http://www.europarl.eu.int/experts**) was posted on a special page on the European Parliament's website.

European Balloonists Fly Around the World

Bertrand Piccard, a Swiss psychiatrist, and Brian Jones, a British pilot, became the first people ever to successfully fly around the world in a balloon. The historic 14,204-mile journey began in the Swiss Alps on March 1 and ended March 20 in Egypt.

BUSINESS BRIEFS

With the year only four months old, **Aegon**, the Dutch insurer, is already laying claim to be among Europe's top corporate performers in 1999. Fresh from the $9.7 billion purchase of San Francisco-based **Transamerica**, Aegon is casting around for fresh acquisitions within the US where it is now the third-largest life insurer. It is also eyeing Europe, but higher share prices and complex shareholder structures make it "extremely difficult" to find good opportunities, according to chief financial officer Henk van Wijk.

The company boosted net income by 24.5 percent to $1.4 billion in 1998 in what chairman Kees Storm called "another beautiful year," as **Providian**, a US insurer acquired in mid-1997 for $2.6 billion, made its first full contribution. For the current year, Aegon is forecasting earnings growth of 18 to 20 percent.

Aegon got a further accolade when it was judged to be the world's best-performing financial services company over the past five years, ranked by a new index of shareholder value. The company produced a 138 percent return for shareholders in 1998 alone with an investment of $10,000 in its shares five years ago worth around $125,000 in March, according to the index developed by **Oliver, Wyman and Company**, a financial services consultancy. In absolute dollar terms, Aegon generated $29.5 billion of shareholder value, second to **AIG**, the US insurer at $31 billion.

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AXA, the French financial services group, has also richly rewarded faithful shareholders during its dramatic twenty-year increase from a provincial insurance company to a European market leader and the world's third-largest money manager—thanks to its US acquisitions.

The company was ready to enter the super league in March as it was poised to become a significant shareholder in the world's biggest bank that would be created if **Banque Nationale de Paris's** hostile $37 billion bid to takeover over rival French banks**, Société Générale** and **Paribas** succeeds.

AXA has a small but significant 6 percent stake in BNP and 7 percent of the shares and 11 percent of the voting rights in Paribas, which put its chairman Claude Bebear in a position to play a key role in the negotiations between the three banks.

AXA picked up struggling **Equitable Life** of the US in 1991 for $1 billion, and now it is gearing up to make a $3 billion acquisition of its own. Its key asset is a 60 percent stake in **Equitable Companies** (the parent company of **Donaldson Lufkin & Jenrette Securities** and **Alliance Capital**, a money management firm) that has catapulted AXA into the elite league of money managers. It is still growing, most recently through a $5.6 billion acquisition of **Guardian Royal Exchange**, which made it the UK's third-largest property and casualty insurer. However, a successful BNP bid would put AXA into an ever-bigger league.

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Reliant Energy became the first US utility to pull off a large acquisition in the continental European electricity industry. Its $2.4 billion deal to be phased in over seven years for **UNA**, a Dutch generator, will likely trigger moves by its American rivals to exploit the recent market liberalization.

Until now, US utilities have concentrated on the long deregulated British market, snapping up more than 50 percent of the country's regional electricity distributors. However, the opening of the European power market last February has given a green light to move to the mainland. "Europe is the most important region outside the United States that offers the combination of deregulating power and gas markets and strong commercial, political, and legal infrastructure," according to Steve Letbetter, president of Houston-based Reliant.

Reliant beat out other large companies, including **Edison International** of California, **Texas Utilities** of Dallas, and the UK's **National Power** for Amsterdam-based UNA, one of four Dutch generating companies that provide 20 percent of the country's power.

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The jury is still out on whether French car maker **Renault's** decision to seek a 35 percent stake in **Nissan**, the troubled Japanese manufacturer, was a masterstroke or a high-risk $4 billion gamble. If successful, the deal would transform Renault from Europe's sixth-largest manufacturer into to a global player with a powerful presence in the US and Asia. Last year only 330,000 of Renault's record 2.13 million sales came from outside Europe.

A 35 percent stake in Nissan would be sufficient to give Renault significant management input in Japan's second-largest car maker but small enough to avoid consolidating its estimated $36 billion of debt.

Renault, which is 44 percent owned by the French government, has confounded its critics before, bouncing back from a near $1 billion loss in 1996 with a range of new cars and minivans to make a near record profit of $1.5 billion on sales of $40 billion in 1988.

But commentators question the logic of Renault pursuing a deal that had been spurned by **Daimler-Chrysler**, a much larger player, which was reportedly scared off by Nissan's debts and its very traditional Japanese-style management. "We remain highly skeptical of this proposed alliance and believe it could represent a major risk to Renault," the investment bank Goldman Sachs stated.

But Renault sees powerful reasons for the deal that would give it access to some of the world's most efficient auto plants and world-class technology and the North American and Asian markets where it has a very small presence. Nissan operates three of the world's most efficient plants measured by productivity per employee, according to the London-based Economist Intelligence Unit. Renault's top plant ranked thirty-ninth.

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Airbus says it must proceed with plans to build the A3XX super jumbo jet to ensure it maintains its 50 percent share of the global commercial airliner market. The four-nation European consortium split the $75 billion world orderbook in 1998 with archrival **Boeing**, but that was an exceptional year. Airbus is still on target for a 50 percent market share measured by orders and annual revenues, but "until we have the A3XX, we shall be unable to maintain that 50 percent market share," said Ian Massey, the Airbus financial controller.

Airbus is developing the A3XX, a 480-seat to 656-seat wide-body jet, to break the lucrative monopoly of the Boeing 747. Airbus recently said first deliveries of the A3XX would probably slip from 2004 to 2005, due to lower demand from cash-strapped Asian airliners. The company's four partners, **British Aerospace**, **Aerospatiale** of France, **DaimlerChrysler Aerospace**, and **CASA** of Spain, must also overhaul its structure to prepare for financing and production of the planned jet.

Airbus recently raised the estimated development cost from $9 billion to $10 billion largely because a 480-seat version has been put on the drawing board.

Airbus expects to deliver 295 planes in 1999, compared with Boeing's forecast of 620 aircraft, giving it a 32 percent share of deliveries. This figure will rise to 40 percent in 2000, based on Airbus's projection that it will deliver 317 jets compared with 480 forecast by Boeing.

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Deutsche Post consolidated a $3 billion-plus face lift that has transformed a dull postal monopoly into an aggressive pan-European package delivery firm by acquiring the major distribution elements of **Royal Nedlloyd**. In its third acquisition in as many months, Deutsche Post paid close to $590 million for the Dutch shipping group's trucking, parcels, and distribution assets.

The deal, following hard on the heels of Deutsche Post's $1.1 billion purchase of **Danzas**, a giant Swiss trucking and logistics firm, last December. That acquisition upped the ante in the battle between Europe's big postal authorities, to carve niches in the fast-growing, high-margin, cross-border express market ahead of the EU's deregulation of conventional mail activities in 2003.

Deutsche Post chairman Klaus Zumwinkel intends to make the company's distinctive logo of a black looped horn against a bright yellow background, an international brand. He wants the company to create a "yellow machine" in Europe just as UPS has created a "brown machine" in the United States. The group's other big buys included a 25 percent stake in global courier **DHL** for a rumored $700 million and a 50 percent stake in the UK's **Securicor Omega** package delivery group for which it paid $330 million.

TNT Post Group of the Netherlands, **La Poste** of France, and the UK's **Royal Mail** have also made large cross-border acquisitions in the recent months, and analysts say they are the only postal firms that can compete against the German giant.

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DaimlerChrysler displayed the world's first "zero emissions" fuel cell-powered car, which it hopes to have in the showrooms within five years. The German-US company has set aside $1.4 billion to bring the car—a variant of the Mercedes-Benz A-Class hatchback—into production in 2004. The "Necar 4" (new electric car) will be able to reach a maximum speed of ninety miles per hour and travel nearly 280 miles before refueling.

Other car manufacturers, including **GM**, **Ford**, and **Honda**, also hope to start selling fuel cell-powered cars by the 2004 target set by DaimlerChrysler.

Jürgen Schrempp, Daimler-Chrysler co-chairman, said the company had solved the most challenging technical problems. Until fairly recently the car's power plant could have occupied the entire inside space of a large van. The Necar's power plant, by contrast, will only be as big as a conventional gas tank although it will require more parts.

—*Bruce Barnard*

EUROPE Update

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EUROPEAN AFFAIRS

EU Leaders Set New Course After Commission Resigns

Europe's Opportunity

BY MARTIN WALKER

The European Union's fifteen leaders moved swiftly on the opening day of their Berlin summit to fill the power vacuum in Brussels and unanimously agreed upon former Italian premier Romano Prodi as their choice to lead the European Commission for the next five years with a strong reform mandate.

"Mr. Prodi is ideally suited," said German Chancellor Gerhard Schröder, current holder of the EU's rotating presidency. "He is rich in political and administrative experience and expert in economics, of indisputable human and personal integrity, and is solidly for reform."

Europe's political embarrassment at losing its entire leadership in Brussels, an unprecedented humiliation for a Commission, which had always seen itself as the guardian and architect of the European project, has given way to a sense of opportunity. The European Parliament, which brought down the Commission, sees a historic chance to change the balance of power between Europe's institutions in a way that permanently strengthens its role.

"This is good for European democracy," said Pauline Green, the British Labor member of the European Parliament (MEP), who leads the 214-strong Socialist group, the largest in the 626-seat parliament. "The MEPs are elected as the voice and watchdog of the people over the unelected commissioners, and we have at last asserted the clear principle that the Commission is henceforth fully accountable to us."

MEPs now move into their campaigns for the June elections across Europe, confident that the voters now understand that the European Parliament


At the helm of the EU during Germany's six-month presidency, Chancellor Gerhard Schröder chaired the closely watched Berlin summit.

is a far more important and potent body, with a high public profile after the months of crisis between MEPs and the Commission. They are hoping for a record turnout in June, which will give the new Parliament a powerful mandate to accompany the new powers Parliament assumes under the terms of the treaty of Amsterdam, which comes into force on May 1.

The Amsterdam Treaty gives Parliament the right to veto or approve the nomination of Mr. Prodi as the new Commission president and to hold US Congress-style hearings into all the new commissioners. Parliament will also get the power of co-decision over all new EU legislation, regulations, and policies, with the exception of foreign affairs and agriculture, still jealously guarded by the member states.

A new emergency EU summit is now being planned for Mr. Prodi and the national leaders to hammer out a blueprint for reform, which German Chancellor Schröder said would demand: "more openness, more transparency, more closeness to the European public, and better cooperation among the Union's institutions."

Europe's heads of government also see the chance of far-reaching change after the fall of the old Commission led by former Luxembourg premier Jacques Santer. A new emergency EU summit is now being planned for Mr. Prodi and the national leaders to hammer out a blueprint for reform, which German Chancellor Schröder said would demand: "more openness, more transparency, more closeness to the European public, and better cooperation among the Union's institutions."

"The most important thing for us is to get the reforms in place in Europe which guarantee a successful, more prosperous EU for the future," said British Prime Minister Tony Blair. He has proposed bringing in outside management consultants to redefine the work, pay, and conditions of the Commission's 17,000 staff. "The Commission needs to change in order to keep pace with the times."

The crisis in Brussels began last December, when the European Parliament refused to approve the Commission's stewardship of its 1996 budget, after a series of reports from MEPs and from the Court of Auditors, which suggested some fraud and more widespread mismanagement. The crisis escalated in January, when the Commission narrowly survived a vote of censure in Parliament by accepting an outside inquiry by the Committee of Independent Experts.

Their report, delivered March 15, was devastating, accusing former French prime minister Edith Cresson of having misused her post as education commissioner to find paid sinecures for friends. The report accused the twenty-person Commission of having "lost control of the bureaucracy" and presiding over an administrative culture in which "it is not easy to find anyone prepared to take responsibility." The entire Commission immediately resigned but remained in their posts as caretakers.

Confusion still reigns over the status of the outgoing Commission and how quickly Mr. Prodi can pick a new team of twenty commissioners. Pressed to confirm that disgraced French Commissioner Edith Cresson would not be allowed back, even on an interim basis, Chancellor Schröder said, "I am looking to the future, not the past."

Mr. Schröder added that the new twenty-strong Commission, with a five-and-a-half-year mandate, should be confirmed by the new European Parliament after the elections in June. However, the outgoing Parliament is also demanding the right to approve Mr. Prodi and the new team so a period of constitutional dispute, if not crisis, now looms. "Frankly we are still a bit unclear about exactly how this is going to work," Mr. Blair's spokesman commented.

Mr. Prodi is taking the job on condition that he is granted extraordinary powers to choose his new Commission, Italian Prime Minister Massimo D'Alema told his fellow leaders. The first Commission president from a southern European country since 1972, Mr. Prodi brings strong federalist convictions to the job. He has proposed a single European army, coordinated tax policies, and sweeping deregulation and privatization to create a genuinely single market.

A former economics professor, who studied at the London School of Economics, Mr. Prodi is a political centrist who is not guaranteed an easy ride before a European Parliament dominated by the Socialist group. After his reforming two years in office in Rome, he has bitter critics on the Left and among trade unions. His critics say that both the Italian economy and the euro are now paying the price for his various tax and budget ploys, including a special euro-tax and corporation taxes paid a year in advance, which allowed Mr. Prodi to knock the lira into sufficient shape to qualify for the single currency.

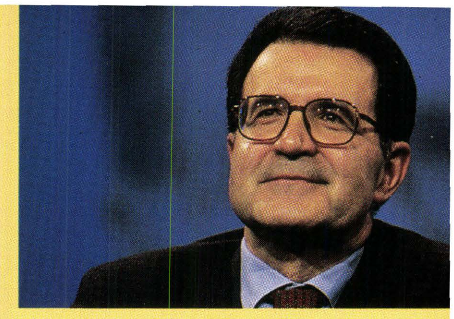
Silvio Berlusconi, the media magnate and former Italian premier who leads the Forza Italia party, has accused the Italian government of "buying the job" for Mr. Prodi. The former Communist (and now Social Democrat) Massimo D'Alema, who runs the left-of-center governing coalition, agreed at the Berlin summit to a change in the EU financing system, relying less on the VAT indirect tax system and more on a direct and inherently fairer levy based on the GDP of each member state.

This change, which was becoming inevitable sooner or later, will cost Italy some $1.2 billion a year and make it easier for other European leaders to balance the budget. It means that Germany's Chancellor Schröder will be able to fulfill his pledge to his voters that he would cut Germany's net contribution of some $12 billion a year to the EU budget. That certainly made it easier for the Berlin summit to agree quickly on Mr. Prodi—hence Mr. Berlusconi's jibe.

Mr. Prodi, who attended last September's 'Third Way' summit in New York with President Clinton and Tony Blair, is in close sympathy with the Blair-Clinton vision of a modernized and market-friendly social democracy, and with Chancellor Schröder's election rhetoric about the *Neue Mitte* (the new center). ⓔ

Martin Walker is a contributing editor to EUROPE *and the Brussels bureau chief of the* Guardian.

Romano Prodi



Popular Italian Takes on a New Mission

Romano Prodi, the new "Mr. Europe" as the nominee to be the next president of the European Commission, is an economics professor who was parachuted into politics as a technocrat when he was appointed industry minister in 1978. He spent the 1980s as a businessman, restructuring the vast state-owned Italian industrial holding company IRI. In the 1996 elections, he led a center-left coalition to victory and stayed in power for twenty-eight months of fast and furious reform, which against all the odds allowed the Italian economy to qualify for Europe's new single currency.

A genial fellow and keen amateur cyclist, who loves the mortadella sausage of his native Bologna, he has proven to be a formidable and popular election campaigner. A devout Catholic, who was married to his college sweetheart by Cardinal Ruini, head of the Italian conference of bishops, he was loosely associated with the Christian Democratic party. But after completing his doctorate on the perils of protectionism in trade, he took prestigious teaching posts at the London School of Economics, Harvard, and Stanford, using his fluent English to form an unusually wide-range of acquaintances in the Anglo-Saxon academic and business world.

"Although I am delighted to be an Italian, I like the Anglo-Saxons, their directness and their pragmatism and their firm approach to the rule of law," Mr. Prodi told the New York seminar on the 'Third Way' with President Bill Clinton and Tony Blair last September. That seminar is now starting to assume totemic significance in Europe, with Germany's new chancellor, Gerhard Schröder, also supporting the idea of a 'new center' in politics, which can bridge both the gap between Left and Right in Europe and between the US Democratic party and the European Social Democrats.

Mr. Prodi spoke in New York of a "global olive tree," a worldwide version of the center-left coalition he had forged in Italy under the name of a sturdy and fruitful tree with deep roots in history, whose shade could embrace a wide range of political views. It was his own version of the Francis Fukuyama thesis that the end of the cold war meant "the end of history" in that the great ideological disputes of the twentieth century were now outdated. The West had learned that untrammeled free markets needed state intervention to succor the old and the sick and the unemployed, just as the verdict of the cold war had shown that centralized state control of an economy would wreck it and crush any hope of a pluralist civil society.

In less than three years as prime minister, Mr. Prodi launched a series of sweeping reforms of the old Italian state. He privatized telecommunications and reformed the feather-bed system of pensions and state jobs. He attacked the endemic state budget deficits, cutting them by 4 percent of GDP. His reputation as a hard-headed reformer earned him the European job and gives him unprecedented bargaining power with the member states.

Prodi seems determined from the start to show the member states that he will be the boss in Brussels. He informed the Berlin summit, through Italian Prime Minister Massimo D'Alema, that he wanted the member states to offer him lists of their proposed candidates for the Commission and he would pick his own selection. Mr. Prodi also wants the right to select portfolios for the various member states in advance, so that a Frenchman might get trade, a Spaniard might get the farm job, and a Briton be assigned the competition office.

Mr. Prodi has not yet spoken about the kind of reorganization he wants to introduce in the Commission system. Nevertheless, Italian sources close to him say that he recognizes the current system of commissioners becoming powerful barons over their own fiefs is simply not working. He is likely to pick up a proposal floated in the Santer Commission last year for a group of three or four super-commissioners with the rank of vice-president and the authority over ordinary commissioners who report to them.

One will run the foreign affairs portfolio, overseeing an empire that would include all external relations and development aid, jobs that are currently divided among four commissioners. The agriculture job could widen to include rural development and even fisheries. Economic policy and the internal market and the competition portfolio also make a natural fit, to which smaller directorates like energy, telecommunications, and transport could report. This consolidation would leave the trade job either standing alone as a big job, entrusted to somebody of the kind of weight Sir Leon Brittan brought to the post, or under Mr. Prodi's own hand.

There are two big problems, however, that loom over the new president's head. The first is the complex constitutional procedures over his appointment and replacement of the Santer team. As Tony Blair's official spokesman explained, "We are still a bit unclear about exactly how this is going to work."

The second Prodi problem will come with the Commission staff. Part of his mandate from the Berlin summit is a sweeping reform of the Commission staffing system, with performance reviews and the ability to sack and move staff and change the hidebound pay and allowance system. The Commission trade unions last year mounted a daylong strike against much milder reform proposals.

The good news is that Mr. Prodi is a free trader who supports the World Trade Organization and has been critical in private of the way trade rows with the US like the banana dispute have been allowed to spiral out of control. If any single figure at the Commission can persuade both Europeans and Americans of the need for sensible compromise that averts the dangers of protection, it is likely to be him.

—Martin Walker

NATO From the Cold War to Kosovo

BY MARTIN WALKER

General Dwight D. Eisenhower visiting European forces participating in joint maneuvers in Hanover, Germany in 1951.

Still wracked by war and its economies still buried under the detritus of war, Europe at the dawn of 1947 was still an intensely dangerous place. There were 6 million troops in the Red Army, and almost half of them were in Eastern Europe. By contrast, the once equally sized Western armies were down to 390,000 American and 480,000 British troops. In Hungary, Romania, and Poland, the communist party fomented political crises that left them in charge and the token opposition parties neutered or worse.

The leaders of the Czech government, nominally led by Social Democrats, were summoned to Moscow in July of that year and ordered to withdraw their application to join the Marshall Plan. The Iron Curtain descending across Europe was no longer simply military; it had become political. The reality of Soviet military occupation was reinforced by the appearance of puppet 'peoples governments'.

"There is but one great power that emerged from World War II having conquered other territories, and that power is the USSR," declared Belgian Prime Minister Henri Spaak. He was to become a driving force in the slow accumulation of treaties and alliances that led to the creation of NATO.

The process began with France and Britain, which both signed the Dunkirk Treaty of March 1947, pledging "alliance and mutual assistance." Then Stalin's creation of the Cominform in September 1947 pledged to fight the Marshall Plan as "an instrument of American imperialism" spurred Spaak and other smaller European states to join. In March 1948, the three Benelux countries joined Britain and France in Spaak's great achievement, the Brussels Treaty of mutual defense.

Secretary of State George C. Marshall, representing the Democratic administration of President Truman, then invited the chairman of the Senate Foreign Relations Committee, the Republican (and veteran isolationist) Arthur Vandenberg, to discuss what role the US should play. As they spoke, Canada formally proposed a transatlantic treaty of mutual defense. Britain immediately agreed but insisted that it would only be meaningful if the US were to join it. Senator Vandenberg, persuaded that the frontier of American security now rested on the Rhine, introduced a Senate resolution that agreed in principle that the US would join "collective arrangements for effective self-help and mutual aid (including) the right of collective self-defense under article fifty-one of the United Nations Charter."

That resolution was barely agreed when the East Germans and Soviet troops sealed the roads leading to West Berlin and the Berlin blockade began on June 24. Twelve days later, Europe's ambassadors met at the State Department in Washington and began drafting what became NATO's founding document, formally signed as the Treaty of Washington on April 4, 1949. The five powers of the Treaty of Brussels, joined by the US and Canada, formally invited Italy, Denmark, Norway, Iceland, and Portugal to join them. Greece and Turkey joined in 1952, and the new federal republic of West Germany was invited to join, after considerable hesitation by France, in 1954.

Originally, NATO was simply a diplomatic alliance, which called for its members to support one another in case of attack. What made NATO unique was the way, under the Lisbon agreements of 1952, this treaty became a coherent system of unified command and control of the various national military forces. In effect, NATO became, under its first supreme commander, General Dwight D. Eisenhower, the general staff of all the national armed forces gathered in Western Europe. The Americans agreed to keep a permanent garrison of troops and warplanes in Europe under NATO command—some of whose grandchildren are serving today at the NATO military headquarters at Mons, Belgium.

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NATO has been the most durable and successful military alliance in history. It fulfilled its mission, to defend Western Europe against the threat of Soviet aggression, without firing a shot. With the crucial backing of the US nuclear arsenal, NATO deterred an attack and became part of a wider security system, which avoided a major war because both sides knew that a nuclear exchange would be too terrible to contemplate. NATO moreover became the essential mechanism by which the old wartime enemy of West Germany was successfully absorbed into the transatlantic family of democratic and increasingly prosperous nations.

An extraordinarily democratic body, in which decisions must be taken by consensus, NATO was the shield behind which the European Economic Community could form. It became the glue that bonded together the sprawling economic and cultural entity that NATO safeguarded to become known as the 'Free World'. We now call it the 'West', and neither its security nor its current prosperity could have developed without the military alliance.

Perhaps the best epitaph of the first forty years of the NATO alliance until the year that saw the fall of the Berlin Wall was that it survived. There were repeated shocks—France's withdrawal from the military command structure and the eviction of NATO headquarters from Paris in 1966; the studied refusal of the European NATO allies to support the ill-fated US military effort in Vietnam; and the military coup in Greece, which undermined NATO's democratic credentials. None of the shocks proved fatal to the flexible political structure of NATO in which the US might have been first among equals, but did not seek to impose its authority in the high-handed way the Soviet Union ran the Warsaw Pact. Lacking democratic legitimacy, the inflexible Warsaw Pact collapsed, where NATO survived and flourished by general consent.

UK paratroopers participated in joint exercises that brought together troops from fourteen NATO countries in Albania.

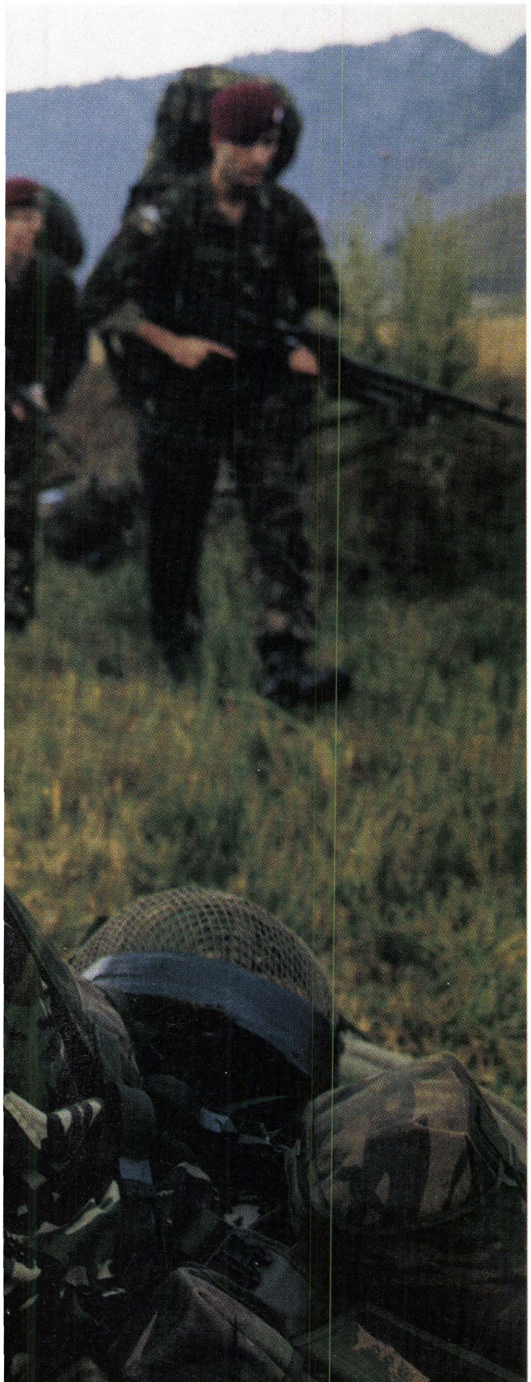
NATO Today

There is a one-word answer to the perennial question: Why should NATO survive, after the end of the cold war that spawned it? That answer is Bosnia. Cynics may say that had the Bosnian war not erupted, NATO might have been forced to invent it to justify its own survival. That misses the essential point that from 1991 onward, both the European Union and the United Nations had tried and failed to resolve the Balkan wars.

More than a hundred British, French, and other European soldiers died in the tragic failure to stabilize the region after the breakup of the old Yugoslav federation. It was only when the overwhelming military force and prestige of NATO was committed, after the 1995 Dayton peace talks, that peace came to the battered city of Sarajevo and the ravaged land of Bosnia.

No other force on earth could have achieved what NATO accomplished in Bosnia. It was not just the air armada of 430 warplanes and the 30,000 troops and the reserves of whatever ground force, from tanks to British SAS commandos, that might ultimately be needed.

The unique quality of NATO's Balkan exercise of force and threat in the service of diplomacy was that it came from



the eventual consensus of sixteen member nations, backed up by the moral force of several more that want to join it. During the Kosovo crisis, Romania, Bulgaria, and Albania announced that their airspace was open to NATO planes. Hungary's parliament also voted to offer airspace and bases, just as it provides the logistics base for NATO's peacekeeping mission in Bosnia.

At the fiftieth anniversary NATO summit in Washington, the formal enlargement of NATO will take place, bringing the Poles, Czechs, and Hungarians into the alliance as full members. This event will mark the real end of the cold war, the formal collapse of that old dividing line that separated Eastern from Western Europe after 1945.

To allow this to happen without reigniting the old hostility with Moscow, Russia has been brought into a nominal partnership with NATO through a Permanent Joint Council. This partnership gives Moscow "a voice, but not a veto" on NATO decisions. On the upside, it has established a habit of consultation and brought Russian troops alongside NATO forces in the peacekeeping operation in Bosnia. On the downside, it has not altogether eased Russian suspicions of NATO's enlargement, particularly since NATO stresses that the alliance is open to further new members in the future. Russia insists that a "red line" be drawn around former Soviet states, to bar countries like Ukraine or the Baltic States from joining NATO in future. This situation will cause trouble in the future.

The Kosovo crisis has highlighted one essential fact about NATO. It will not subordinate itself to the international community as represented by the United Nations. To give the UN Security Council a veto over NATO would be to give Russia a veto, and NATO's deliberate vagueness about its future missions means that the alliance will never swallow that.

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There are three reasons why NATO has survived, despite having fulfilled its long defensive mission. These also explain why NATO has started to use force and deploy troops (twice against Serbia) only since the Soviet collapse. The first is that NATO works as a unique amalgam of military potential and political unity in which hesitant members, like (in the Kosovo crisis) Italy and Germany can be pressured into going along on the argument that "NATO's credibility is at stake." Moreover, institutions that work are not lightly abandoned by statesmen who know how hard they are to rebuild.

The second is that NATO is the one international (and European) institution where the US takes the chair as of right. The supreme commander is always an American. It embodies the American commitment to European security, which is as much in US strategic interest as in Europe's. Furthermore, it welds together the two richest and most democratically stable groups of nations on earth. It is, they tell you misty-eyed late at night in the bar at NATO's headquarters at Evere in the northern Brussels suburbs, the umbilical cord that unites North America and Europe—their power, their interests, and their values.

The third is that because it works and because NATO's common values are assumed by its members to have universal validity, NATO is now the chosen vehicle for the enlargement of that transatlantic sphere of interest. Whether NATO's history impresses or appalls, its future promises to be far more ambitious.

NATO represents a kind of United Nations in arms, with the power and with the political will to fulfill that old idealistic dream of President Woodrow Wilson for "a moral force of the public opinion of the world." That, at least, is the theory and the case put forward by NATO's defenders. It is easily challenged, however, by three simple questions:

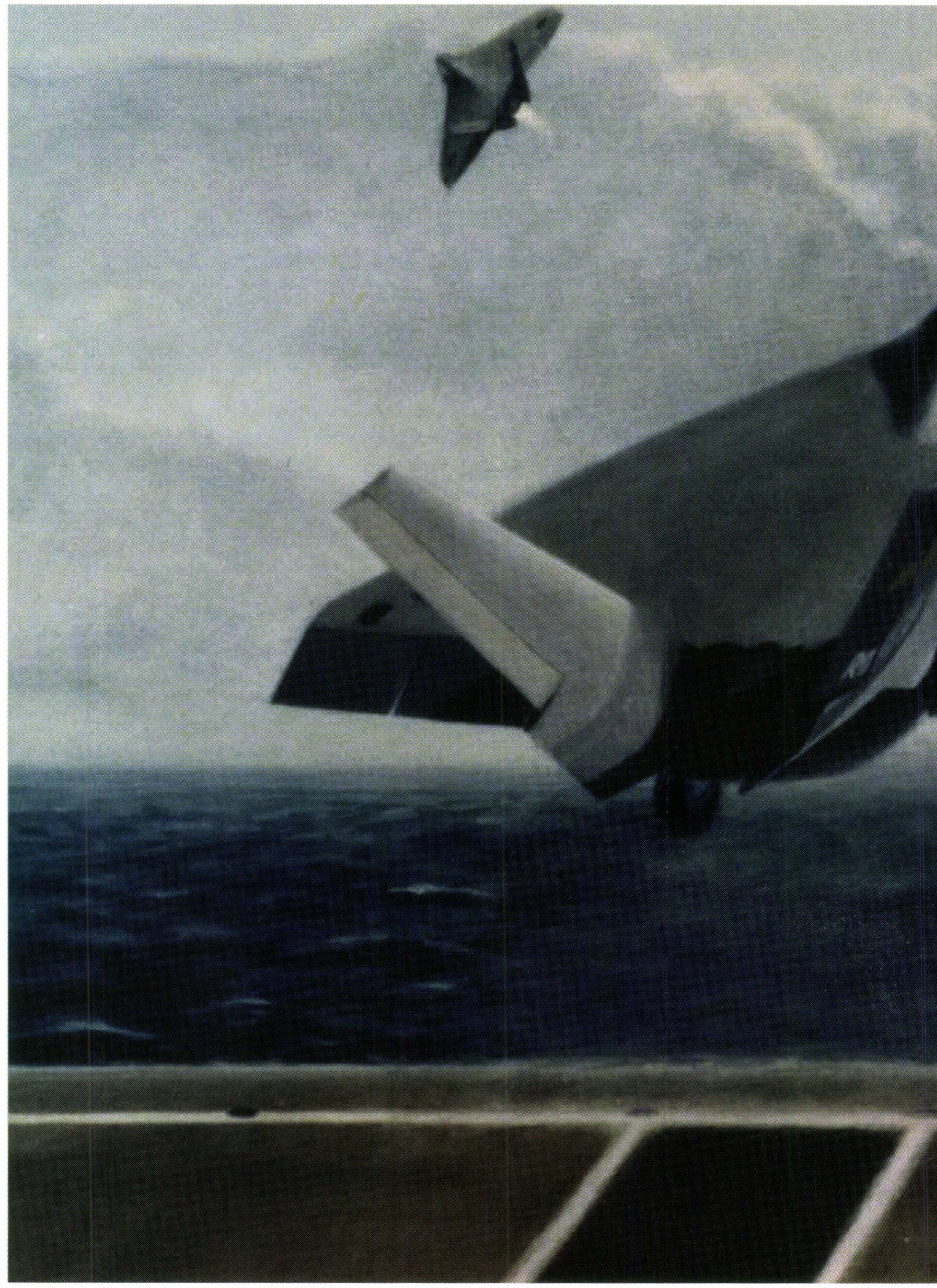
First, what took NATO so long to act over Kosovo when it had learned in Bosnia what Serb aggression meant?

Second, if moral force for world peace is the criterion, what is left of NATO's pretensions to represent the international community after Russia opposed military action from its seat on the UN security council?

Third, where does NATO stop, and why is war in the Balkans more compelling than the Islamic slaughter in Algeria or than the savage shelling of the Chechen capital of Grozny?

The short answer is that NATO is still feeling its way in the new world order. President Clinton—who will host the fiftieth anniversary summit in Washington where NATO's new 'strategic doctrine' will be formally agreed with the formal accession of the new members, Poland, Hungary, and the Czech Republic—put it this way in a recent interview:

"NATO is an organization in transition from being a military alliance directed against the Soviet Union to becoming a transatlantic security system which includes Russia." "Transition" is the crucial word.



NATO Tomorrow

NATO's new strategic doctrine is deliberately vague about its missions and area of operations in the future. The alliance will undoubtedly embark on future missions, even though NATO ministers speak in airy generalities about peacekeeping, antiterrorism, and spreading its zone of stability deeper into Eastern Europe.

NATO Secretary-General Javier Solana, a former physics professor and Spanish Socialist who used to demonstrate against Spain ever joining the alliance, gave the first foretaste of the new strategic doctrine to a recent NATO conference in Portugal. He proposed a new transatlantic bargain for a Euro-Atlantic community under which the EU and the US share responsibility through NATO for stabilizing a region stretching to Russia, the Iranian border, and North Africa.

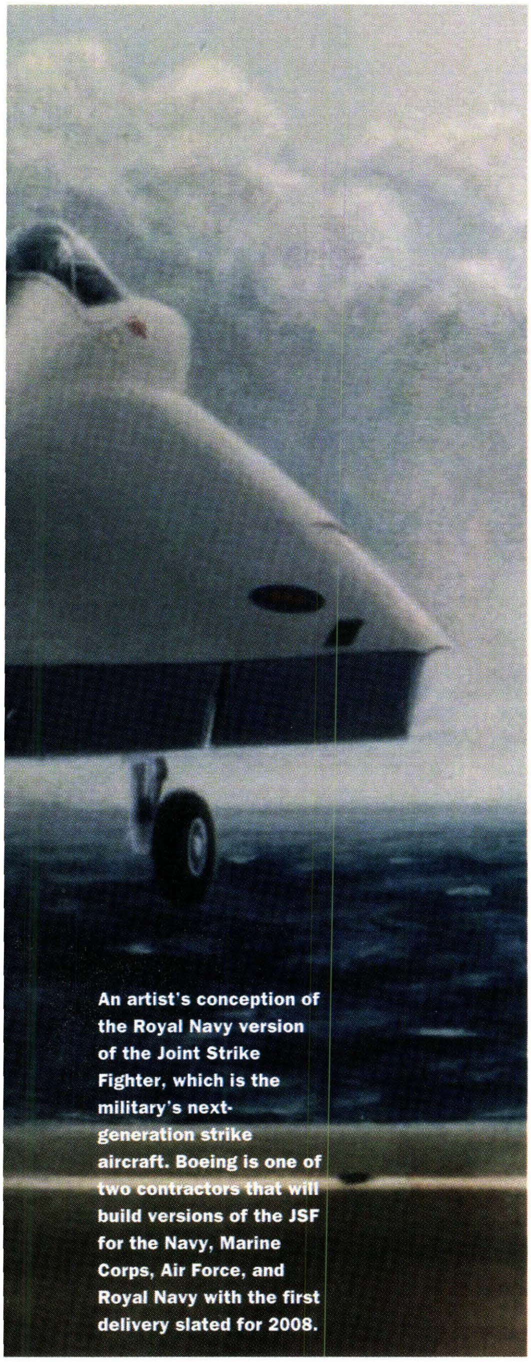
"Security remains a team effort, and there is no stronger team than North America and Europe," Mr. Solana stated in a speech titled "Preparing NATO for the Twenty-first Century." "Europe and North America must stick together. We cannot cope with globalization if our security approach, or indeed our economic approach, is marked by fragmentation."

Citing the Caucasus and the Balkans as areas of potential conflict where NATO "cannot remain aloof." Mr. Solana says, "Our work in building security and stability throughout the wider Euro-Atlantic region is not finished."

"Our security policies must become increasingly proactive...From preventive military deployments to economic assistance, there are many tools we have at our disposal. We are not condemned to be the victims of events that lie beyond our control—we can shape the future."

An essential issue of the new strategic doctrine will be how far NATO is prepared to extend its operations beyond its traditional geographic limits. NATO's enlargement into Eastern Europe—to include Hungary, Poland, and the Czech Republic—and its new Permanent Joint Council with Russia have dramatically enlarged NATO's sphere.

Completion of the new strategic doctrine will be the culmination of Mr. Solana's term at NATO, and one of his central goals is to put to rest the long argument over a European defense identity separate from NATO. What is now emerging—and is to be formalized



An artist's conception of the Royal Navy version of the Joint Strike Fighter, which is the military's next-generation strike aircraft. Boeing is one of two contractors that will build versions of the JSF for the Navy, Marine Corps, Air Force, and Royal Navy with the first delivery slated for 2008.

in the new doctrine—is a looser NATO structure in which European members can make use of NATO assets and command and communications systems to carry out their own operations, without the participation of US ground troops but under a NATO banner.

"In future, the US may not wish to take the lead in each and every contingency that may arise on the European continent. European allies have increasingly indicated a desire to play a security role commensurate with Europe's growing economic strength. Both developments point to a new transatlantic bargain," Mr. Solana explained.

"The arrangements we have developed with the Western European Union for European-led operations provide us with new political and military options. Politically, these new arrangements make sense because they reflect Europe's growing weight and responsibility in maintaining security on this continent. Militarily, these arrangements make sense because they ensure that a stronger European voice develops organically from within NATO and does not require wasteful duplication."

This is where the United Kingdom comes in. Aware last May that its presidency of the European Council was going rather flat, a high-flying Foreign Office diplomat, Robert Cooper, was told to prepare a confidential memorandum on maximizing the potential of the UK's future in Europe. One key recommendation was using British military assets to develop "a European capacity to act independently in the defense field."

This proposal dovetailed neatly with a phrase from Solana's seminal speech: "The European Union will become an ever stronger foundation of stability." The British plan, which was embraced by France at the Saint Malo summit last December, seeks to build an EU defense capacity that will be virtually indistinguishable from NATO. The Americans would thus be encouraged not to fear 'Fortress Europe', since they would be part of the garrison. In addition, the EU neutrals (Ireland, Austria, Sweden, and Finland) would learn that there are no free security rides.

One reason why this might work is that leading politicians in Austria, Sweden, and Finland (but not Ireland) are already campaigning openly for NATO membership. Moreover, the enlargement of the EU to Eastern Europe will bring in the new NATO members like the Czechs, Poles, and Hungarians. The overwhelming majority of the enlarged EU member states will be NATO members.

"Security remains a team effort, and there is no stronger team than North America and Europe," Mr. Solana stated in a speech titled "Preparing NATO for the Twenty-first Century." "Europe and North America must stick together. We cannot cope with globalization if our security approach, or indeed our economic approach, is marked by fragmentation."

The new NATO is not defending against any exterior threat, but it is protecting the existence of the institution by casting around for new roles that are extending its sphere of influence very far indeed. Today, it is Eastern Europe and the Balkans and extending its control over the Mediterranean to a new influence along the North African shore.

Tomorrow, from Solana's speech, it will include the oil and gas wealth of the Caucasus and the Caspian basin and a special relationship with Russia and the other former Soviet Republics, which will extend its influence deep into Central Asia. NATO conducts exercises almost routinely now in Russia, and it actively encourages Russian officials and aircraft to join the monitoring force in and over Kosovo.

NATO was always the defense club of the prosperous transatlantic democratic world. That world was also Christian—as the Muslims of Bosnia and Kosovo have come to understand, witnessing NATO-imposed settlements, which happened to exclude the emergence of any new Islamic state in Europe. If Russia falls into the embrace as NATO plans and expects, the alliance is on track to become (and do not the think the Chinese and the Islamic world have not noticed) not only a security system that reaches from Los Angeles to Vladivostok, but something more ambitious still—the rich white world in arms.

NATO, through its uniqueness, will continue to be one of the world's most successful military alliances. Don't be surprised to see a 100th anniversary celebration of NATO fifty years from now.

Martin Walker is a EUROPE *contributing editor and the Brussels bureau chief of the British newspaper the* Guardian.

TRAVEL

ISLE OF WIGHT

YAC AHOY

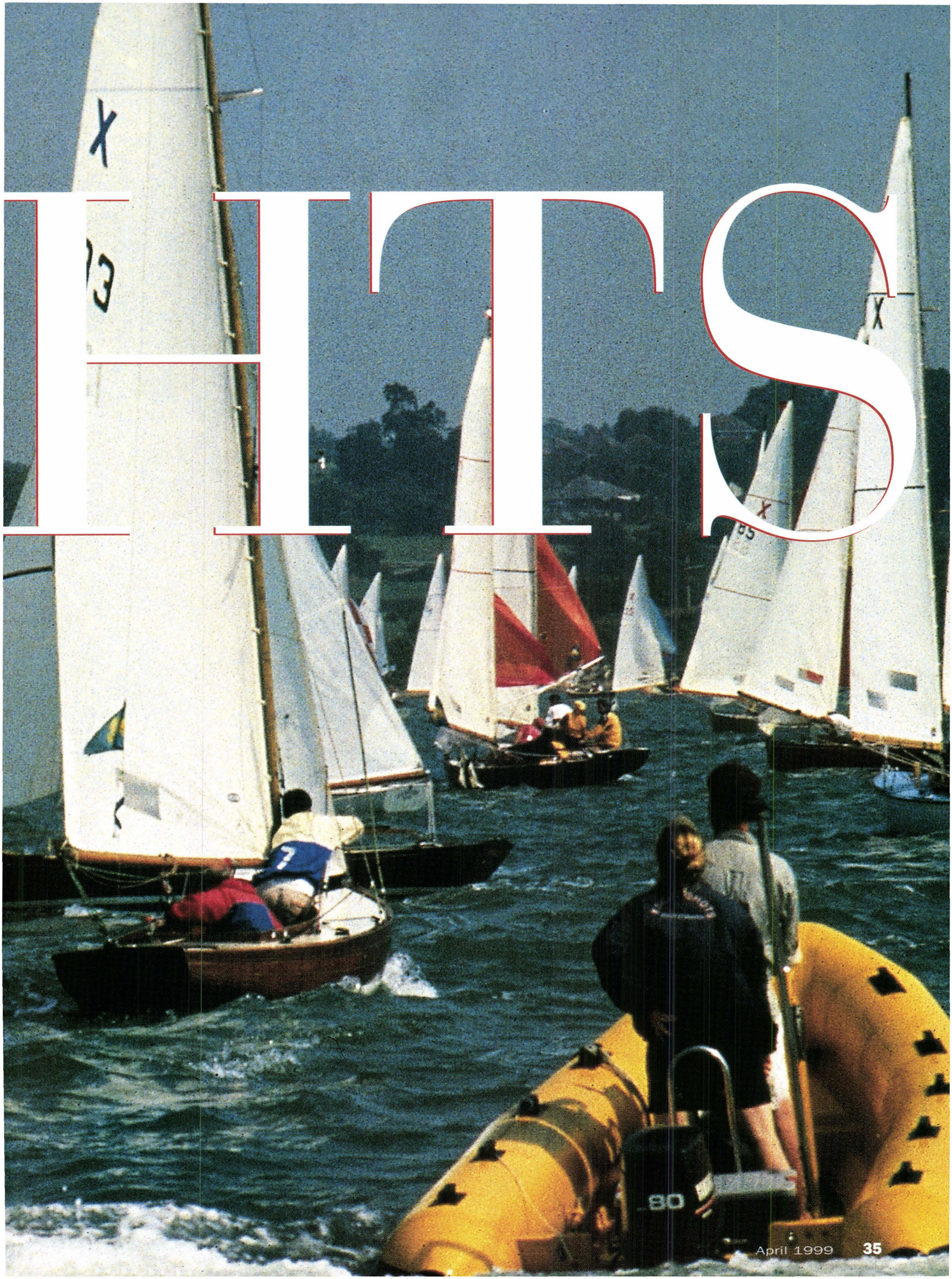
BY DAVID LENNON

The America's Cup yacht race was born here almost 150 years ago, watched by Queen Victoria, and every summer sailors come in vast numbers to sail its challenging waters in the world's biggest regatta. This is the Isle of Wight, a diamond shaped island off the south coast of England.

Although only two hours from London, the need to take a ferry or sail in on your own boat has meant that for most of the year this is a quiet place. But come August, the Isle of Wight explodes into a week of fiercely competitive yacht racing and nighttime partying. It is Cowes Week, the world's biggest and longest-running sailing regatta.

The little town of Cowes on the north coast heaves with thousands of sailors as boats and crews come from all over the United Kingdom and Ireland, as well as most EU coastal countries, plus the US and even Japan. Some 900 yachts, from fifteen-footers to eighty-foot millionaires' dream boats, and 10,000 sailors, from world-class stars to weekend warriors, pack the tiny

HTS



island, swamping the 19,000 local population.

What attracts them all is the tough challenge of sailing the local waters. The Solent, the stretch of water between the south coast of England and the Isle of Wight, has complex tidal flows, winds that can be hard to read, and numerous shoals and sandbanks. "Yacht racing here is an art form at the best of times," say the experts.

Hundreds of yachts of varying categories all racing through the narrow waters rigorously tests the skills of the sailor. Add to this the ferryboats, tankers, and container ships plowing through the same waters and you begin to get an idea of why Cowes is a challenge sailors love to meet.

"If you see a big ship coming up the eastern Solent, try to predict where it's going to turn, so you don't have to get out of its way," recommends British world-class yachtsman Adam Gosling. "The big ones can suck the air out behind them, so there's almost a vacuum. Something to avoid."

Excessive partying is something else he cautions about, but in reality, it's virtually impossible to avoid partying during Cowes Week. In fact, it is as much a social occasion as a sailing event. From the posh balls thrown by the yacht clubs, through the lavish entertainment on the big yachts, to the beer tents erected for the week, Cowes is serious party time.

It all began in earnest last century with the support of King George IV and later Queen Victoria, who loved to spend part of the summer at Osborne House, near Cowes. Sailing the Solent was already popular among the rich, but their donations of cups as race prizes really put the royal seal on Cowes.

It was in 1851 that the yacht *America* came over and challenged all comers for the 100-sovereign cup put up by the Royal Yacht Squadron. It won the race around the island, amid some controversy about tactics, and took the cup back home. Later, it was put up as the prize for the famous America's Cup series, which continues to this day.

The royal connection also continues to this day. Queen Elizabeth's husband Prince Philip has been a regular participant for the last forty years, often joined by the former King Constantine of Greece.

In order to survive in the modern age, it also needs commercial sponsors, and the lead sponsor is an insurance group, Skandia Life, whose name has adorned the event since 1995 and will continue at least until the year 2000. Traditionally staged at the beginning of August, this year Cowes Week runs from July 31 to August 7.

Cowes Week attracts a broad range of visitors, from members of "yachting society" to young revelers who come for the parties.

Today, the rigid social mores of the blazers and white caps of the royals and the old sailing crowd are ignored by the muscular, rowdy, shorts-wearing lads and lasses of new sailing. While 200 people might attend the elite Royal Yacht Club's opening night ball, up to 10,000 yachters party in the bars and beer tents.

"Some would put drinking and partying on a par with sailing," reports a local paper. "Cowes at night reminds you of a fashionable French ski resort," it continues. "Well-heeled young people enjoying physical exertion which gives you a tan and bleaches your hair, while requiring occasional risk-taking of the sort you can boast about later over a beer."

While the good folk of the island welcome the free-spending Cowes crowds and tolerate all sorts of wild shenanigans during the sailing season, they are also keen to promote their island home as a calm, tranquil place to visit, one of the last corners of southern England unspoiled by developers.

The local tourist office promotes it as "an island for all seasons." It extols the relaxing pace of life; the variety of landscapes, plants, and animals; and the benefits for walking, horse riding, or cycling around the island. The autumn, winter, and spring are great times to see the "real" Isle of Wight, say the brochures.

Perhaps this is true, but even for the non-sailor, the Isle of Wight is sailing and, above all, Cowes Week. Definitely not to be missed. Ⓔ

CAPITALS

AN OVERVIEW OF CURRENT AFFAIRS IN EUROPE'S CAPITALS

French drivers combat high gasoline prices by opting for diesel.

This month, we asked our Capitals correspondents to report on gasoline prices and other transportation costs in their respective countries.

Europe's Supreme Gasoline

High Taxes Support 'Green' Policies

Americans may gasp at the cost of gas across the Atlantic, but European drivers have accepted it as a fact of life since the birth of mass motoring. But the rationale behind the transatlantic price gap has changed over the past decade.

Once a simple way of raising government revenue, fuel taxes now play a pivotal role in Europe's twin campaigns of reducing pollution and easing congestion on its clogged motorways. Consequently, governments make no excuses for levying fuel taxes and motorists only have the occasional gripe.

Two important historical differences explain the gap between US and European stance on gas prices. First, Europeans traditionally drove smaller cars with lower fuel consumption over shorter distances so their bills tended to even out compared with the gas-guzzlers once favored by their American counterparts. Secondly, unlike the United States, Europe didn't produce its own oil until crude began to gush from the bottom of the North Sea in the mid-1970s.

Moreover, Europe took the brunt of the Arab oil embargo of 1973 and the subsequent quadrupling of prices by OPEC the following year. It was a hard-learned lesson that taught governments and consumers that the era of cheap oil was over. The decision to tax it accordingly became part of conventional thinking and continues to this day despite the subsequent weakness of the oil price. Oil is worth about the same now in real terms as it was in 1973, but government taxes are still rising. Oil may be worth only $14 a barrel but European consumers are paying the equivalent of nearly $180 per barrel at the gas station.

European governments defend high fuel taxes as part of a strategy to meet their objective of cutting carbon dioxide emissions and are enthusiastically supported by an increasingly "green" electorate in the Nordic countries, the Netherlands, and Germany and grudgingly accepted by less committed voters elsewhere in the European Union.

Car makers have responded by continuing to improve engine efficiency and thus lower fuel consumption. The result: Europeans break sales records year after year in the world's biggest market. General economic weakness, not the price of gas, is to blame for the occasional blip in sales in individual countries.

Moreover, higher gas prices so far have not reduced the number of journeys nor encouraged motorists to use buses or trains. Public transport is excellent by US standards, but Europeans will not abandon their cars despite steadily rising gas prices and increasing gridlock on the motorways. However higher taxes have made Europe less wasteful than the US where oil consumption per capita is twice that in Europe.

Gas prices have risen sharply again this year across Europe. Fuel taxes in the UK are among the highest in the world thanks to a so-called "fuel escalator," which increases duties by at least 5 percent above the rate of inflation each year. The government makes no apology as it pursues its target of cutting carbon dioxide emissions to 80 percent of 1990 levels during the next decade or 60 percent more than the cut required under the international protocol agreed in Kyoto in 1997.

The UK had the highest gas and diesel duties in the EU, according to figures from the European Commission published before they were raised by 6 percent in the March budget. Greece has the lowest duty, just under half of the British rate. One thing is sure: other governments will follow the UK's lead, albeit at a slower pace. Germany raised fuel taxes in March, which pushed it from eighth to sixth place in the European rankings.

Efforts toward an EU wide carbon tax broke down after the UK's previous Conservative administration opposed it largely for political reasons claiming Brussels had no right to interfere in domestic taxation. But in some EU countries like Sweden, carbon taxes are in effect, and they have appeared on the agenda in other EU capitals.

Europe's motorists are bracing for more "green" taxation. But most appear to accept it as a price worth paying for a more pleasant environment.

—Bruce Barnard

PARIS

DIESEL—DIRT CHEAP OR CHEAP DIRT?

Rudolf Diesel's motives were pure, but it turns out that his invention is not. In the 1880s, when the French-born Diesel (1858–1913) was working on the pressure-ignited heat engine that would bear his name, he was hoping to give small business—craftsmen and artisans—a power source that would help them compete against large industry, which was overpowering them with the expensive, fuel-wasting steam engine. He conceived the diesel engine as a readily adaptable, highly efficient device that could use locally available, low-cost fuels.

Patented in 1892, Diesel's prototype, a single ten-foot iron cylinder with a flywheel at its base, ran on its own power for the first time a year later. By 1898, at the age of forty, Diesel was a millionaire from franchise fees, and his engines were powering everything from pipelines and water plants to automobiles, trucks, ships, and factories.

The French have remained fiercely loyal to the German inventor who was born in Paris and created his namesake in a laboratory-workshop there. Nearly half of France's roughly 25 million private cars are diesel-driven.

This trend has less to do with national pride than simple arithmetic. Gasoline, even unleaded, is heavily taxed in France. The price at the pump for unleaded 95-octane gas—currently ranging from about $3.40–$4.50 a gallon, depending on where you buy it—consists of 80 percent excise duties and taxes. With daily sales of 41,000 tons of gasoline and 65,000 tons of diesel in France, those taxes pump $66 million dollars into the French government's tank every day.

Diesel, in contrast, costs at least 30 percent less at the pump in France and is 50 percent more efficient as well. Insurance also costs less for a diesel car, and the resale value is higher than of a gas-fueled one.

So much for the bright side. Peugeot, which is the leading diesel manufacturer in Europe, will tell you how clean diesel motors run. Because of complete combustion, no nasty carbon monoxide or ozone emissions pollute the air.

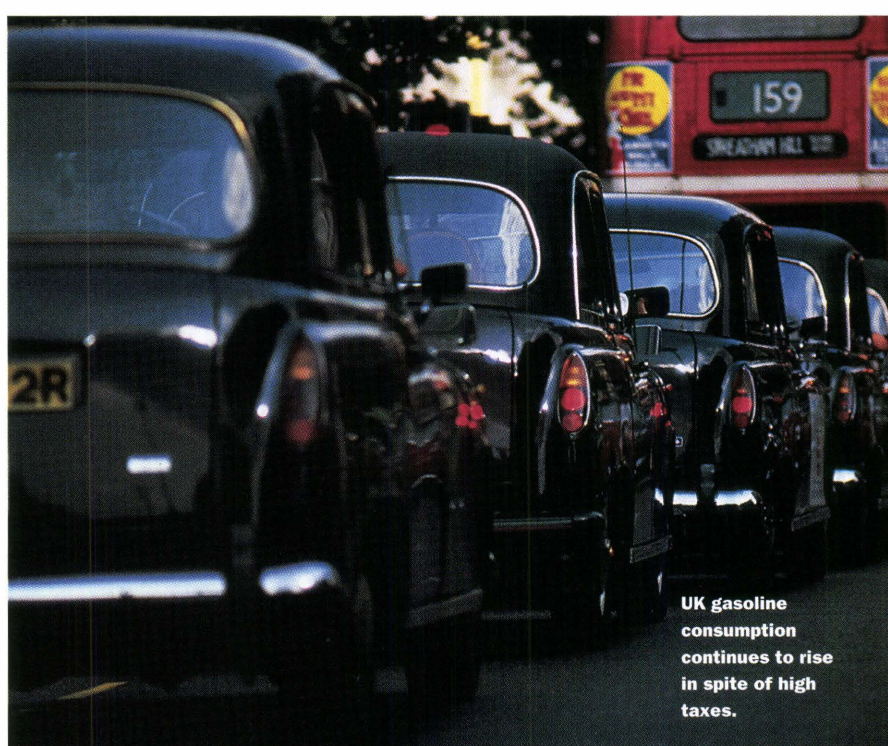
Anyone ever having followed behind a diesel-powered car will realize that not all offensive substances have been burned away. Diesel has a strong smell, no doubt about it; the motor is noisy, vibrating at low speeds, and is more expensive to buy and maintain because it is built of more durable and heavier materials. All of which is not as disturbing as reports circulating that diesel may emit more dangerous toxins than leaded gasoline. A 1997 German study estimated that between 60 and 70 percent of cancers caused by urban pollution are due to the extremely fine particles found in diesel exhaust. Numerous other reports, not quite so alarmist, have linked diesel exposure to an increase in health disorders ranging from respiratory illnesses to cardiopulmonary problems.

Dominique Voynet, France's Green environment minister, has tried to tackle the powerful automobile lobby over the diesel issue for the past two years, but her success has been minimal. The substantial tax increases on diesel that she advocates have not been passed yet, although in 1999 they were raised slightly while taxes on gasoline stayed stable for the first time.

In the meantime, the French continue to drive, four out of five of them preferring their own car to any type of public transportation. Eighty percent of households own a car, and one-third have at least two.

On a typical day in Paris, one million cars circulate within the city limits, another 1.1 million on the ring road surrounding the city. That means close to one million cars powered by Rudolf Diesel's "clean" machine.

—Ester Laushway



UK gasoline consumption continues to rise in spite of high taxes.

LONDON

TAX COLLECTORS DISGUISED AS GAS PUMPS

Last fall, I drove into a gas station in New Hampshire, filled the tank, and was astonished when it only cost me $9.20. A week later, I pulled into a petrol (gas) station in London and was enraged when it cost me $49 to fill the tank. As a rough guide, gasoline at the pump in the United Kingdom costs about $4 a gallon!

The big companies here all say the same thing. "It's not us, it's the government." The fact is that more than 80 percent of the gas station price is taxation. The local industry says that taxation on gasoline in the UK is the highest in Europe. "We are tax collectors," they say.

Not only that, but taxation has been increasing by 6 percent above inflation for a number of years. The Rio Earth Summit boosted this trend when it was decided to try to cut gas emission by discouraging the use of private cars through pricing. However, there has been no concomitant improvement in public transport to give this policy a chance of working. The reality is that London's transport system is creaking badly, and in rural areas, the transport system remains so inadequate that without a car one would be totally isolated.

Has it worked? Consumption of gasoline rose from 21 million tons in 1987 to 22 million tons in 1997. The number of private cars and vans on the road went up from 18 million in 1985 to 22.5 million in 1995, and is still rising despite a relatively stable population.

Since crude oil prices are low, drivers are increasingly irritated by the fact that the pump price stays high. The retailers are so enraged by the current situation that they launched a campaign in February together with the Automobile Association to explain to motorists that more than 80 percent of the price was tax that goes to the government.

"The retail fuel industry is legally obliged to show the full price of fuel and can't show tax separately, so we are showing the public the truth," says AA policy director John Dawson. More than 15 million drivers were targeted in the war to combat public ignorance about the UK's highest-ever fuel taxes, said the AA.

The number of retail gas stations in the UK has been in long-term decline. In 1980, there were 25,000, and last year that number had fallen to 14,000.

The biggest operator is Esso, with just less than 2,000 stations, followed by BP Amoco and Shell. They also have competition from many smaller operators and from the about 750 stations operated by the big supermarket chains who try to use low pump prices as a draw to attract customers to their stores.

—David Lennon

MADRID

SERVICE STATIONS ARE CHANGING

Despite excellent public transportation in most cities and commuter trains that link outlying suburbs to the city centers, many Spaniards still prefer to drive their own vehicles to work. Moreover, the two-hour break for the traditional siesta at lunchtime makes for dreadful traffic snarls four times a day.

But since the economic boom of the late 1980s, people in Spain have been on a car-buying binge. As more and more luxury models from makers such as Mercedes-Benz, BMW, and Volvo take to the Spanish highways, families are purchasing a second, more modest car for mom to take the kids to school and run them around afterwards to judo, piano, and swimming class.

This trend has continued despite the relatively high price of gasoline in Spain, although it has been dropping lately because of lower oil prices on world markets. At the end of last year, a liter of lead-free gasoline cost 107 pesetas ($0.75), down about four pesetas from the previous summer, or about $3 dollars a gallon.

That may sound like a high price for gasoline in the United States, but it compares well with Spain's EU partners. According to statistics published by the oil sector, only Greek and Luxembourg car owners pay less per liter. These same statistics show that the United Kingdom and the Netherlands have the most expensive gasoline with prices roughly another 30 percent higher.

Spain produces no oil of its own, and the big oil companies active in the country, including Repsol, Cepsa, and BP Amoco, purchase most of their petroleum from the Middle East and Latin America. These three firms constitute the principal retailers in Spain, with Repsol controlling about 55 percent of the market and Cepsa around 25 percent. BP shares the rest of the market with other, smaller retailers.

The retail business, however, is changing. Service stations that once offered just gas, oil, air, and water to drivers are now adding on minimarkets selling food, drink, and sundries, long a feature of the gasoline retail scene in the United States and elsewhere.

At the same time, BP and other companies are opening trucking centers across the country. Long-haul truckers can not only get their tank filled, but have a decent meal, grab a shower, take a siesta, pick up a music tape, and get that needed lube or brake job done before heading back onto highway.

—Benjamin Jones

BRUSSELS

FUEL CELL COMPANY TO BRING CHANGE

Gasoline emissions are as much a menace in Belgium as anywhere else, and it has to be admitted that Belgian governments have done very little about the problem. A ray of hope has come, however, from a small company in the Flemish town of Geel. For seventeen long years, the Elenco company conducted research into environmentally friendly fuel cells and was preparing to bring an alkaline-based cell on to the market when the company went broke. It was eventually taken over by the British-owned Zenco company and is now beginning to make an impact.

The first two Millennium taxis, which will soon ply the streets of New York, are nearing completion at Geel, and delivery vans fueled by hydrogen battery cells are being developed for the British Post Office and for a series of top British companies, including Marks & Spencer, Sainsbury, and John Lewis. The company is being floated on the London Stock Exchange, and its shares should soon be traded on the NASDAQ exchange.

Zenco has raised its sights and is preparing to challenge the market leaders in battery cell technology—the Canadian Ballard Systems, with Ford and Daimler-Chrysler as majority shareholders, and the Italian producer, De Nora, backed by Renault and Ford. It is planning production plants at Ramsgate (England), Leipzig (Germany), and as a joint venture, in the United States. It is now well on the way to becoming a major international production company, but its core activity—research and development of new products—will remain in Belgium, whose own atmosphere should, in time, be improved by the company's products.

—Dick Leonard

LUXEMBOURG

THE PLACE TO BUY GAS

Just about every border-hopping motorist in Europe knows that the place to buy gasoline is Luxembourg. Cross from France into this tiny country and gas prices suddenly drop by nearly a third—the equivalent of some 27 to 30 cents a liter. The difference is almost as great when one enters via Belgium. And although the gap between Luxembourg and German prices has narrowed in recent years, a motorist crossing the river Moselle into Luxembourg will still save a useful 20 to 25 percent at the gas pumps on the other side. A remarkable consequence of all this is that just six enormous service stations along Luxembourg's borders supply gas to a huge swathe of central Europe stretching outward from the Grand Duchy into France, Belgium, and Germany.

The Shell service station on the Luxembourg border with France is the company's largest in the world, and the same goes for the units operated by BP and Texaco on the frontier with Belgium. It is not uncommon for each of these giant outlets to sell 26 million gallons of gasoline a year compared to average sales of around 530,000 gallons for a station in Belgium, say.

Luc Delanghe, managing director of Shell Luxembourgoise, says that 80 percent of sales are in the form of transit volumes, that is gasoline bought by motorists coming in from outside Luxembourg. But there is more to it than just cheap gas, he explains. "The service stations also offer big price differentials for alcohol and tobacco so that people coming to fill up are making fantastic savings on these three items," he says. Business was up last year by 4 percent and 3 percent the year before that. "The only difficulty we have, and it's a major issue, is that we have to spend a great deal of money to ensure that the service stations conform to the environmental laws," he says. Luxembourg's environmental controls are among the toughest in Europe.

Gas prices in Luxembourg are supervised by the economics ministry, which sets maximum prices based on production and transportation costs and environmental requirements and takes into account the interests of both suppliers and consumers. Gas stations are free to sell below the set price.

However, the oil companies set profit margins relatively low so that there is little scope for competition through price-cutting. The major factor behind Luxembourg's cheap gas is, of course, the very low level of taxes imposed by the finance ministry compared to the taxes levied in neighboring countries.

This has been the case for many years, and in fact, the price difference has actually been narrowing recently. Alain Bellot, an official at the finance ministry, explains that Luxembourg's remarkably healthy national budget means the country has never really needed to raise gasoline taxes to increase revenues. "We've always had sufficient receipts from gasoline taxes, but the same is not true for our neighbors, and we're not responsible for the rises in other countries."

Tax rates for gasoline have nevertheless been increased in Luxembourg in recent years partly for political reasons. It goes without saying that France, Germany, and Belgium take a dim view of the loss of trade (which also involves alcohol and tobacco and for the same tax reasons) to the small competitor in their midst. More specifically, Luxembourg will come under pressure to raise gas prices if and when the European Union's energy directive comes into force. This directive will impose an energy tax wherever prices are below a prescribed minimum, as Luxembourg's are at present.

Bellot says Luxembourg is willing to participate in a minimum price regime but warns that a price differential will have to be preserved if the country is not to see its gas retail business wiped out. He says that while larger countries can absorb the loss of trade at the frontiers, Luxembourg could not because the entire country is "virtually 100 percent a border zone."

Looking still further ahead, the possibility of harmonization of indirect taxes throughout the European Union, which would end all of Luxembourg's advantages, has to be reckoned with. But if the threat is real, it is so far off that no one in the gasoline industry is perturbed, knowing that they will have at least ten, and probably more like twenty or more years, to prepare for the challenge.

—Alan Osborn

STOCKHOLM

'FILL IT UP' MEANS SHELLING OUT

Pull into a gas station in Sweden and say "fill it up" and those three words add up to an expensive proposition. Gasoline prices around the country are about 8 kronor per liter—roughly $4 a gallon. Environmental taxes and a 25 percent value added tax account for more than 75 percent of the total price at the pump.

Taxes are beyond the oil companies' control. However, there's also little price competition among gasoline chains. You might think that neighboring Norway, with its oil reserves, would give its Scandinavian neighbor a price break, but no such luck. Even when oil prices dropped below $10 a barrel late last year, Norway's Statoil maintained high prices at the pumps.

Obviously, the prohibitive cost of gasoline limits the number of cars on the road, right? Wrong. Registrations were up 9 percent in the fourth quarter of 1998 over the same period in 1997, according to Statistics Sweden. That's nine new registrations for every 1,000 people.

In part, Swedes drive so much because of the country's geography. Yes, you can take a train from north to south, or fly, but driving is often the most practical solution. In and around big cities, such as Stockholm, many people drive company cars. In other words, they're not paying for the gasoline.

Then, of course, there's the Swedish summer house culture. A motorist trying to get out of Stockholm on a Friday afternoon from April onward is guaranteed to get stuck in a crawling traffic jam. Eight kronor a liter or no, Swedes fire up their Volvos and head for the country every weekend.

Nor do fuel costs seem to stop hordes of European vacationers from maneuvering motor homes through Sweden every summer. Faced with increasing road traffic and greenhouse gas emissions, Swedish authorities have tried to encourage people to take public transportation and have subsidized environmentally friendly fuels.

Sweden was probably the first country in Europe to require use of lead-free gasoline. As in the States, its purchase was subsidized for a time. A special nonleaded fuel was also developed for older cars that couldn't use regular unleaded.

While you might expect that the number of older cars on the road would be steadily declining, that isn't the case. Older Volvos and Saabs run seemingly forever; models that are twenty years old or more are common. Perhaps in a perverse reaction against these indefatigable Swedish workhorses, the other old cars around are American gas guzzlers. The cult of the *raggar bilar*, as its known, embraces the flashy cars of the 1940s, '50s, and '60s. More than just show toys, the cars are regularly driven and sometimes even used to pull motor homes. Think of that miles-to-the-gallon ratio!

Even more surprising is the number of old station wagons on the road. These are the giant Country Squire-type wagons, the ones that could hold the kids, the dog, *and* the house. Even in the heyday of gas guzzlers, these babies set new lows in miles per gallon. But Volvo or woody, Saab or Squire, Swedes are increasingly climbing behind the wheel, unhindered by the high cost of gasoline.

—Ariane Sains

ROME

POOR PUBLIC TRANSIT KEEPS ITALIANS DRIVING

Every morning 20 million adults and a little less than 12 million students—out of a total Italian population of roughly 56 million people distributed over a territory roughly the size of Florida—leave their homes to go to work or to school. Only a few fortunate ones live close enough to walk. According to the latest official statistics, almost 70 percent of Italians who need transportation use an automobile.

In short, Italy is a nation composed of inveterate motorists. This is due in part to Italians' true love for four-wheeled vehicles but mainly because there are no valid alternatives. After all, Italy is the homeland of Fiat, which over the years has become the owner of not only Ferrari but of all the other prestigious Italian car makers, including Alfa Romeo and Lancia.

Rome's underdeveloped subway does little to encourage commuters to use public transport.

It isn't too unfair to suspect that the discreet pressure from Fiat, which is owned by the powerful Agnelli family, nudged the postwar governments to give preference to private automotive transportation, building a dense network of roads and highways, all to the detriment of public transport. The result is that only Milan has a real subway network, and it is rather small. Rome has only two subway lines, which do not provide access to most of the city. Moreover, Italy fares no better with busses and trams. According to surveys, passengers all over Italy find public transport dirty and inefficient. In fact, barely 5 percent of all workers and 12 percent of students use public transportation.

Therefore, it is no wonder that whenever the government needs quick money it usually dips into the pockets of motorists. Any excuse will do. The most recent increase in the price of gasoline, which occurred just a few weeks ago, was in the name of the environment. A "carbon tax" was attached to a new antipollution tax: the price of gas—even lead-free gas, which is theoretically less polluting—was increased an average 1 percent and now costs about $3.78 per gallon.

The result is that despite the general decrease in the price of oil worldwide, the Italian motorist remains heavily taxed. Three-fourths of the cost of a full tank of gas at a service station goes to the government. An Italian can only wonder how Americans would react to a $4 gallon of gas—perhaps it would be enough to set off another Boston Tea Party.

—Niccolò d' Aquino

VIENNA

AUSTRIANS GO FOR CHEAP DIESEL

In an attempt to combat some of the steepest gasoline prices in Europe, Hannes Farnleitner, Austria's economics minister, is pushing oil companies to reduce prices at the pump by about 5 cents per liter. If they don't cooperate, Farnleitner has threatened to use price regulations to cut costs for consumers.

Farnleitner's threats come in response to a recent study by the Austrian Institute of Economic Research, which shows prices per liter of super unleaded gasoline are about 5 cents more expensive than in neighboring Switzerland, which has higher wages and a higher cost of living.

In Vienna, super unleaded gasoline sells for about 10.70 schillings per liter (about $3.20 per gallon). Part of the problem is that the Austrian market is dominated by six major oil firms, and the limited competition has helped keep prices high in this country with a population of fewer than 8 million.

The east of the country, including the capital, has a bit more competition, with small oil firms holding a 20 percent market share, according to the economic institute's study. However, in western Austria, they've managed to gain only an 11 percent market share.

To battle high costs, people have started to switch to diesel automobiles, since diesel fuel costs about 8.30 schillings per liter ($2.50 per gallon)—a bargain by Austrian standards.

Despite the high gasoline prices and extensive public transportation networks, automobiles are sacrosanct in this mountainous country, with almost every family owning at least one car.

Many people, however, particularly in Vienna, use public transportation to commute to work or run errands each day. Tens of thousands of commuters use the five subway lines, an extensive regional rail system, and scores of trams and buses that link the farthest reaches of the capital city and stretch into the surrounding towns and villages.

Some people are deterred from driving by the continual congestion in the capital. Others are put off by the high parking prices, which averages about $3.25 per hour in a downtown garage. Even short-term, on-street parking doesn't come cheap, costing about $1 an hour in much of the city.

In addition, driving costs could become even higher. While the economics minister wants to see gasoline prices fall, the Greens are pushing for a tax reform that would boost taxes on most energy and fuel sources.

Unleaded gasoline prices would remain unchanged, but the tax on diesel fuel would increase by 37 cents per gallon. Between 1980 and 1996, carbon dioxide emissions from automobiles have climbed from 11.2 million tons to 15 million tons, and the new tax would be aimed at reversing this trend.

—Susan Ladika

HELSINKI

FINNS PREFER TO DRIVE

With a population as scarce as forty-three people per square mile and relatively long distances between cities, at least in European terms, one would imagine that petrol would be fairly cheap in Finland. A car is necessary in the more remote areas and makes life easier everywhere, in spite of the fact that public transport is well developed. But no! The price of petrol is far from even reasonable in this country. At least that's the consensus among consumers who pay nearly four times the price US drivers pay. These days, the happy American pays approximately one dollar for a gallon of gas. The less lucky Finn gets one puny liter—roughly one-fourth the amount—for that same dollar!

One can only wonder why? Although Finland itself has no oil deposits, it has a flourishing oil industry, which was originally built on a steady delivery of inexpensive Russian crude oil. It does not lack competition among retailers since most major oil companies have operations in Finland and compete with the local ones.

In fact, the high Finnish gasoline prices are due mainly to taxes. Altogether, some 80 percent of the price goes back to the government in the form of taxes. The situation is even worse when buying a car, when the taxman adds close to 150 percent to the price.

It is easy to realize that the car and gasoline are sources of income for the government, which offers many practical explanations—all assuredly true but used to the limit. For example, the government asserts that road building is exceptionally expensive in Finland. The temperature can vary from -40 degrees Fahrenheit on a very cold winter night to more than 100 degrees in the broiling summer sun. Such extreme conditions require especially durable and expensive roads. However, a close inspection of the government budget shows that the amount of money taken through car and gasoline taxes amounts to more than the money reserved for road construction and repair.

On average, the Finns drive the oldest cars in Europe. Considering the price they have to pay for them, they understandably keep them as long as possible. However, thanks to the EU, car prices will have come down to a more common European level. One more benefit the EU with its free movement of goods has brought the Finns.

In spite of a well-developed system of public transport—including frequent air routes, fast inter-city and commuter trains, coaches, busses, and streetcars in major cities, and a subway in Helsinki—the average Finn still prefers his car, regardless of the gas price. He always mutters about it, but the old saying seems to hold true: "If you can afford the car, you can afford the gasoline, too."

—Thomas Romantschuk

DUBLIN

CAR BUYING ON THE RISE

When I was a boy—and that wasn't yesterday—drive time was something the wealthier mortals spent on the golf course, and automobiles were the heady indulgence of the monied classes, the "professionals"—well-paid politicians, doctors, dentists, lawyers, and others pursuing similarly lucrative trades. Back then, most roads were winding and hazardous, and there were few stretches where high speeds could be reached with any certainty of safety. Driving was a pleasure…or an early chance of entering the newspaper obituaries.

Now, in the booming economic Ireland of the Celtic Tiger, things are different. Car ownership has mushroomed in recent years, with the young population flashing their newfound wealth as they splash out on the more expensive and exotic car models. Roads have improved beyond imagination, and regrettably, the Irish are now roughly within the EU average for road fatalities.

Not bad for a country that doesn't boast a single oil well and, surprisingly in the land of Henry Ford's forefathers, doesn't manufacture a single car. All gasoline is imported from other European countries or the Middle East, and motor vehicles are designed and manufactured elsewhere and imported fully assembled or (rapidly diminishing) in kit form for Irish assembly.

The growing Irish love affair with the automobile is surprising, given the hefty taxes that must be paid to indulge the habit. According to Keith Butler, statistical officer for the Society of the Irish Motor Industry (SIMI), taxation is "a huge burden" with value added tax (VAT) of 21 percent and vehicle registration tax (VRT) ranging from 22.5 percent for smaller cars and up to 30 percent for the larger models. In addition, there are hefty annual road tax charges to be paid to the local authority and some of the highest insurance premiums in Europe.

It doesn't stop there. Gasoline (or petrol, as we still quaintly call it) is also subject to large VAT—again at 21 percent—and excise duties. Take unleaded fuel. It costs anything from 53 pence a liter (or $2.80 per gallon) upward. About 68 percent of that cost is tax. Furthermore, in support of Europe's growing "green" image, leaded fuel attracts a tax of about 70 percent.

These taxes and excise duties, once imposed for improving roads and other facilities and still used in this area, are also sidetracked "for general government revenue purposes."

Other motor fuels are diesel, mainly used by trucks and some cars, and industrial gas (LPG). In the December budget, excise duty on LPG was reduced to encourage use of this less-polluting fuel.

Given the high taxation, it is surprising that more than a million of the Irish own their own cars. Admittedly, car ownership is still relatively small, but it is growing extremely fast. Last year, the Irish bought more than 140,000 new cars, a record figure.

Lack of investment in public transport may be partly responsible for the growing love affair with the car. Railways have been starved of capital investment and only now are large sums of money being set aside for improved main-line tracks and services.

However, services have also suffered from lack of investment, which probably accounts for the huge numbers of commuters using private transport. Even in Dublin, which has a fast, efficient, and soon-to-be-expanded electric rapid transit system (DART), the number of people using private cars to travel to work is very high, adding to the city's pollution. Moreover, it's unlikely to improve, at least in the short term: the people responsible for Dublin transportation say they expect that, this year, 73 percent of what are called "person trips in peak time" will be by car.

Nevertheless, Keith Butler, of SIMI, says that, while electric or hybrid cars are still awaited, greater fuel efficiency has seen smoke emissions "drastically reduced" throughout the country.

—Mike Burns

Germany has the world's second-biggest highway network, but traffic is an increasing problem.

BERLIN

GERMANS TRAVELING MORE THAN EVER

The German government is confronted with major challenges as the EU's single market and the opening up of Eastern Europe have increased Germany's importance as a trade and transport hub in the heart of Europe. The western states have a good transport network and the development of new systems in the eastern states is progressing rapidly. The infrastructure is crucial for the region's economic recovery. To this end, the German government will spend $244 billion to completely modernize the reunified country's rail, road, and waterway networks by 2012. Fifty-four percent of the investment is earmarked for rail and waterway systems, so this is the first time roads have received the smaller share.

For German citizens, however, private cars remain the most popular means of transport. The car is a symbol of freedom and mobility for Germans. Statistically speaking the entire population could be transported in the front seats of the more than 40 million German private cars. (By comparison, in 1988, there were 27 million passenger cars in West Germany.) The number of miles in Germany's highway network is second only to the United States.

The number of passenger cars will continue to rise, according to the German car industry association. In 1998, Germany's car makers made an energetic comeback, producing 14 percent more vehicles than in 1997 and exporting 61.3 percent of them. Bernd Gottschalk, the association's chairman, said 5.73 million passenger cars were produced in 1998, and the output should remain well more than 5 million in 1999.

Never before have Germans traveled as much as they do today. On the average, a German travels 8,000 miles annually. In 1997, the car accounted for 67 percent passenger miles, buses and railway systems 14 percent, air traffic also 14 percent, bicycles 2 percent, and walking 3 percent.

Although the car means a lot to the individual in terms of mobility and quality of life, it also has its negative aspects. Together with industry and private households, cars and especially trucks represent one of the main sources of air pollution.

At the Paris auto show in October 1998, Volkswagen presented a small compact model, the three-liter Lupo. With extremely low-fuel consumption and minimum exhaust emissions, it will reach the market later this year. All leading car manufacturers are busy developing "three-liter" cars, so the competition in this market segment is likely to be intense. VW's Lupo has been chosen by readers of *Auto Motor Und Sport* the best compact car of 1999 followed by Ford's Ka and Daimler-Chrysler's two-seater Smart.

Increases in gasoline and other energy taxes to reduce the use of cars and trucks are highly unpopular in Germany. When the left-wing Greens proposed tripling the price of gasoline to DM 4.8 per liter ($10.20 per gallon) at a conference in March 1998, their opinion poll ratings dropped almost 50 percent.

Nevertheless, in last fall's elections, the voters elected Gerhard Schröder's SPD, which joined with the Greens to form a coalition government. Although they backed off their original proposal, the Greens boast that they were instrumental in pushing through an "ecological reform" that will increase taxes in three steps on gasoline, heating oil, electricity, and natural gas by a total of $20 billion. The first step was implemented on April 1, when gasoline prices increased by 4 percent to $3.60 per gallon. Although the Greens favor the tax increase as a way to decrease traffic and pollution, the revenue they generate will fund cuts in statutory social security contributions carried equally by employers and employees.

However, the move may have backfired. In recent state elections in the state of Hesse, a Greens stronghold, the SPD-Green coalition lost control of the state government due to heavy losses by the Greens. Political analysts agree that the government desperately needs joint European action on energy taxation to provide political cover for its plans to push through unpopular increases in gasoline and other energy taxes.

—Wanda Menke-Glückert

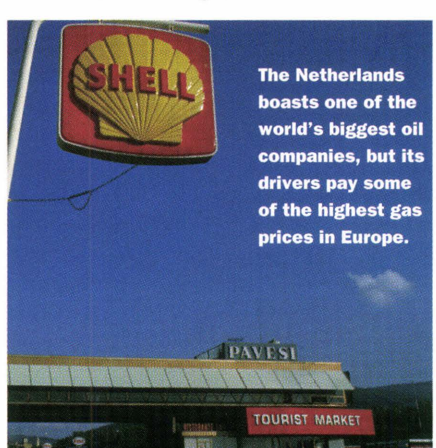
THE HAGUE

HIGH TAXES HAVEN'T SLOWED TRAFFIC

Why is gasoline in the Netherlands among the most expensive in Europe? It's taxes. A liter of gas costs about 2.20 guilders or $4.15 per gallon.

This situation, however, seems strange for a country that less than a quarter of a century ago was described as a 'semi-OPEC-nation' when huge natural gas fields were discovered in the northern province of Groningen and in the Dutch part of the North Sea shelf. The Dutch government was a 50 percent partner in the consortium (with Shell and Exxon) that exploited these gas fields. The prices of gas were linked to those of oil, and when the oil prices quadrupled in the 1970s, the government reaped a huge profit on the natural gas sales. The windfall was largely spent on social programs, and this policy of profligate spending became known as the 'Dutch disease'. The severity of this disease was made clear in the early 1980s when oil prices, and subsequently natural gas prices, collapsed. The Dutch treasury faced a sudden drop in income and a ballooning deficit.

Today, the government budget—and the Dutch economy as a whole—is much less dependent on natural gas than in the past.



The Netherlands boasts one of the world's biggest oil companies, but its drivers pay some of the highest gas prices in Europe.

Although the fluctuations of oil and gas prices on the world market hardly affect the Netherlands, gasoline prices remain a hotly debated political issue that stems from two related problems: increasing traffic congestion and air pollution. Therefore, the government has increased gasoline taxes to the point that they now constitute about 80 percent of the consumer price. Consequently, current low world oil prices are not reflected in Dutch filling stations.

After the government raised energy taxes again two years ago, Dutch gas prices were so much higher than those across the borders in Belgium (to the south) and Germany (to the east) that a massive flow of "gasoline tourism" developed. In a small country like the Netherlands, this threatened to ruin the gas stations in the border areas. After fierce protests and media campaigns, the government hastily came up with a compensation plan to supplement the incomes of the filling station owners in a broad zone along the entire border. Not surprisingly, the European Union subsequently vetoed these targeted subsidies as they ran counter to European competition policies. Last year, luckily for the Dutch government, both the new German government and the Belgian government decided to raise energy taxes, decreasing the price differences with the Netherlands.

In Dutch politics, there is no support for further tax increases. Attention is now moving toward the introduction of electronic toll payment systems on the highways in the Randstad, the crowded western part of the country. Like the energy taxes, it will raise government revenues. But whether it will contribute to less traffic congestion remains to be seen. The high energy taxes have certainly not deterred the Dutch from filling up their cars.

—Roel Janssen

COPENHAGEN

DANES PAY THE MOST FOR CARS

Although tourist brochures often show Danes biking—and they are ubiquitous in Danish city traffic—bicycles account for less than 5 percent of the 7,400 miles the average Dane travels every year. Cars fulfill three-fourths of Danish transport needs with public transport serving the remaining 20 percent.

These figures have been largely unchanged over the past ten years despite a political commitment to develop public transport as an environmentally friendly alternative. Commuting by train has increased slightly in major cities, especially Copenhagen, as congestion on roads increases, but an increasing number of workplaces have been relocated to suburbs, where access by car is a faster and more convenient mode of transport.

The average Dane spends 17 percent of disposable income on transport. This percentage has grown sharply as virtually all Danish families have two incomes and can afford to buy into what can be a very expensive mode of transportation.

A gallon of gasoline costs Danish consumers about $4.40; however, the Danish producer's price of about $1 is similar to the consumer price in most of the United States. The remaining $3.40 are various taxes, including 25 percent value added tax (VAT). For a long period, gasoline taxes were lower in Germany, creating a brisk border trade, and for a short time, they were lower than Germany's reversing that trade.

However, for the past two years Danish gasoline taxes have been broadly equal to those of its neighbors, and the Danish government has committed itself to match increases in German taxes. Nevertheless, Danish left-wing parties want prices at the pump to increase to $8 a gallon as soon as possible. That it is not in the cards, but there is no doubt that taxes are on an upward trend. Environmentalists and the ministers of finance will make sure of that.

The major difference between Denmark and its European neighbors is car prices. Two-thirds of the sticker price of a car in Denmark is pocketed by the state, making Denmark one of the world's most expensive places to buy a car. The obvious explanation is that Denmark does not produce cars, so Denmark has never had a local industry lobby with an employment argument to put a cap on car taxation.

In fact, the high taxation has enabled Denmark to buy its cars on the market cheaper than most other countries. Car producers compete fiercely on price in a market where any price change is thrice multiplied by taxes and where there is no entrenched local competition.

For some models, prices were 10-15 percent lower in Denmark without taxes, and a fair number were bought by EU consumers from outside Denmark, despite the vehement protests of producers and dealers in their home markets.

Germans had a special incentive to buy Mercedes cars in Denmark, as these traditionally have a longer waiting list on the home market. This window of opportunity is now closing. European car producers are hiking prices in Denmark in the wake of very strong consumer demand for cars virtually everywhere in Europe. However, it is unlikely that moderate increases in prices will have any real impact on Danish demand.

However, the combination of rising gasoline taxes, congested roads, and high-priced cars is likely to reinforce the trend toward buying smaller cars. Large US cars, especially sport utility vehicles, tend to look silly on Danish expressways, and long-range driving in Denmark is defined as anything more than sixty miles. Furthermore, parking a large car in a major city presents an almost impossible challenge.

Trains have captured market share in Danish long-range travel. The opening of the Great Belt tunnel between Zealand with Copenhagen and the island of Funen two years ago increased the number of business travelers over a distance of 100 to 200 miles. However, the loser was primarily the airlines, and last year the Great Belt Bridge was opened, restoring the comparative advantage of the car for many business travelers, despite high tolls on the bridge. Politicians will continue their battle against cars in Denmark, but most of them will do so from the back seat of their own chauffeur-driven cars.

—Leif Beck Fallesen

ATHENS

GOVERNMENT EASES CAR TAXES

The Greeks are taking to the road in ever-increasing numbers, thanks to a government decision to cut the special consumption tax on new cars. Unlikely as it sounds, the tax cut is part of Greece's effort to qualify for membership in the euro in 2001. Designed to help reduce the inflation rate, it has also triggered a dramatic increase in sales of new cars as showroom prices have dropped by around 12 percent.

Greeks prefer to drive to work, partly because public transport systems, while offering cheap tickets, fall far short of Western European standards. Lack of investment in the Athens urban transport company, for example, has resulted in poor services and declining passenger numbers on buses, trolleys, and the subway. Passenger numbers decreased 20 percent over the past decade and only about 30 percent of Athenians use public transport for getting to work.

After piling up more than $3 billion in debt, the company was restructured last year under a government program for modernizing state-controlled transport companies. The bus fleet is being renewed with more than 1,000 new vehicles due for delivery over the next three years. This, the government hopes, will increase demand for bus travel.

Meanwhile, a $4.4 billion subway extension is due to open next year, adding two new lines to the existing single-line system. The extension should relieve traffic congestion in the city center, but commuters will probably insist on driving to their nearest subway station, according to traffic projections.

The capital's car fleet has almost doubled to 2.2 million since the early 1990s. The odd-and-even driving ban, which keeps half the city's vehicles out of a two square-mile central zone on alternate days (according to the final digit of their license plates), remains in place. Back in the 1980s, the ban was blamed for increasing rather than reducing pollution, as commuters bought elderly secondhand cars to ensure they could drive downtown every day. However, pollution levels in the city center have shown a steady decline since the early 1990s, when tax breaks were introduced for new cars that used unleaded gasoline. Car owners who turned in an old car that belched exhaust fumes qualified for a big discount on a new vehicle. At the same time, businesses have moved out of the city center to suburbs, where a driving ban is unlikely to be enforced.

A sizeable percentage of commuters travel by taxi, taking advantage of the lowest taxi fares in the European Union. Local taxi drivers boast that the Athens taxi fleet is bigger than New York's. Nonetheless, demand for taxis is so strong that Athenians have to settle for sharing a cab with several other commuters traveling in the same direction.

Gasoline costs about 165 drachmas per liter or $2.11 per gallon of which $1.62 is a flat tax. Revenues from gasoline tax are used to finance the general government budget rather than being directed to related spending, such as highway construction or environmental protection. But car owners' associations complain that lack of competition in Greece's oil refining and petroleum products industry has kept gasoline prices high at a time when international oil prices are at low levels. Two oil refining companies—each with a retail subsidiary that controls a nationwide chain of gasoline stations—control 80 percent of the Greek market, while restrictions on the storage of petroleum products around the country have prevented independent distributors from joining the market.

—Kerin Hope

LISBON

PORTUGUESE BUYING MORE CARS

The Portuguese are crazy about cars. Vehicle ownership has soared in recent years, as cheap credit brought automobiles within reach of most families for the first time. There has always been a solid body of car fanatics in Portugal, but not everyone could act on their enthusiasm. Now, the century-old Automobile Club of Portugal (ACP) claims the largest membership of any organization. When the international Formula One motor racing authority announced in 1997 that there would be no more Grand Prix races held here until the racetrack at Estoril, near Lisbon, was rebuilt, it was seen as a national disaster. The downside of the car mania is that accidents are the most common cause of death among Portugal's under-forty-fives, with the overall rate the EU's highest.

However, as with mobile phones, which have spread faster than in any other EU country in recent years, automobiles offer consumers a chance to show off their newfound prosperity in a relatively useful way.

Spending per head on transportation and communications in this, the EU's second-poorest member state, is about 75 percent of the average, while overall consumer spending barely makes 50 percent of the EU average. Each Portuguese household allots 15 percent of spending to transportation, with one-third of that buying the automobiles and 45 percent funding their use and maintenance. In 1995, one in two households owned a vehicle, and the number of two-car families had doubled in four years.

Yet, with retail gasoline prices high, at about 165 escudos per liter of super unleaded ($3.40 per gallon), many drivers may be living beyond their means. Traffic problems in Lisbon tend to ease toward the end of the month, as many people who have stretched their finances to buy an automobile on credit are left with little money to buy gasoline before their next paycheck.

Gasoline prices are inflated by a hefty tax on petroleum products (ISP). It is currently about 75 percent of the pre-tax cost but varies as the government holds retail prices steady in the face of oil market fluctuations. Last year, the levy generated $2.5 billion, 11 percent of all tax revenues, against just 4.1 percent from the tax on vehicles themselves.

The ISP has the advantage for the government that it can be said to be good for the environment, by discouraging pollution. However, there is little sign of large-scale investment in clean or renewable sources of energy; initiatives tend to be private and often not-for-profit. One exception is Agueda-based manufacturer Famel, which recently unveiled an electric scooter it had developed mainly for export.

Revenue from the ISP is not earmarked for specific purposes. So with just 2 percent of state spending going on transportation and communications, it is difficult to trace a connection between what drivers pay and the services they receive. Governments have stepped up road building in the past ten years, after decades of neglect. However, much is funded by EU aid or via build-operate-transfer contracts with private companies.

Unfortunately for car owners, but unsurprisingly, the fact that more investment is funded privately has not meant lower taxes. When, in mid-December, they got an unexpected seasonal gift in the form of a cut in the ISP, it was only because the government had bumped up against the legal limit for the levy.

—Alison Roberts

ARTS & LEISURE

BOOKS

Making Peace

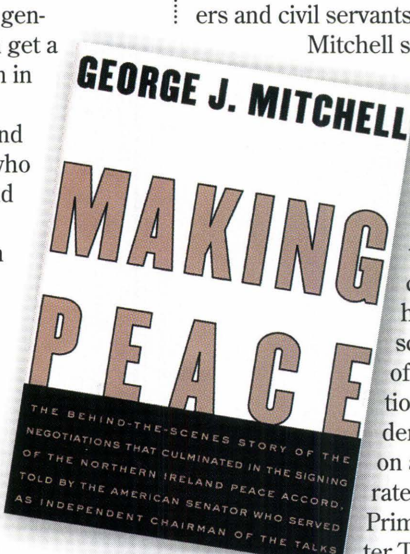
By George Mitchell; Knopf; 192 pages; $24

Little did he realize it when he took up an ostensibly short-term appointment running a trade mission, but former Senate Majority Leader George Mitchell had signed on for a three-and-a-half-year marathon that would produce the best chance yet for lasting peace in Northern Ireland. Mitchell's mission culminated in the accords signed last April 10, which turned out to be a Good Friday of special memory in a land torn so long in conflict between two strands of Christianity.

But what this taut and surprisingly well-written memoir reinforces is that peace remains a fragile commodity after three decades of civil war in the Six Counties. The issue that the peacemakers essentially put off last year—the decommissioning of arms by paramilitary groups and especially the Irish Republican Army—now threatens to delay indefinitely the implementation of the Good Friday accords.

On Saint Patrick's Day, which is celebrated more enthusiastically in the United States than in either the Republic or Ulster, Mitchell received the Medal of Freedom, the highest civilian honor awarded to Americans. The irony was double—the mediation of an American helped bring about a peace accord involving the British and Irish governments and political groups in Ulster. The question is how much more American mediation can achieve and how much is up to the parties to consolidate the peace.

Mitchell's memoir serves two sets of readers well. The specialist can absorb details not previously disclosed in the press. The general reader can get a basic education in the politics of Northern Ireland from a writer who on the one hand was immersed in them, but on the other still has a certain distance and detachment.

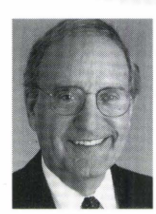


Certainly, from this successful negotiation one gains a better understanding of how and why previous peace efforts foundered on mutual suspicion and antipathy. Even the 1998 accord was a closely run thing, with perhaps exhaustion with violence that killed more than 3,000 people in thirty years a major factor in pushing the antagonists to agreement.

The issue that the peacemakers essentially put off last year—the decommissioning of arms by paramilitary groups and especially the Irish Republican Army—now threatens to delay indefinitely the implementation of the Good Friday accords.

In part, because he too is a politician, Mitchell renders his fellow politicians in a manner both credible and interesting. He is quite modest about his negotiating skills, some gained running the Senate, but they are visible as he moves among such figures as Gerry Adams and David Trimble as well as British and Irish leaders and civil servants.

Mitchell spreads praise amply, and the closest he comes to criticism is in his description of negotiations undertaken on a separate track by Prime Minister Tony Blair and Irish Taoiseach Bertie Ahern, which disrupted the timetable of the Stormont talks in their final days. However, the intervention of the leaders, once they arrived in Belfast, helped push the Ulster leaders to the accord. Mitchell is especially effective describing these leaders as humans—Blair's smooth adroitness giving confidence to Trimble at decisive moments and Ahern's personal drama, planning the funeral of his mother at one moment and readying his return to the negotiations the next.



The biggest surprise, perhaps to his interlocutors in Belfast but especially to those who followed his American career, is the emotional current behind the man most of us saw as a tightly controlled and disciplined political leader, especially who to American audiences was better known for his Lebanese rather than his Irish roots.

Yet another American captivated by the beauty and emotions of Ireland. But in this case, an American who was able to turn that emotion, not to demagogic or self-destructive gestures, but to ending, at least temporarily, the bloodshed that has so often marked the history of that troubled land.

—*Michael D. Mosettig*

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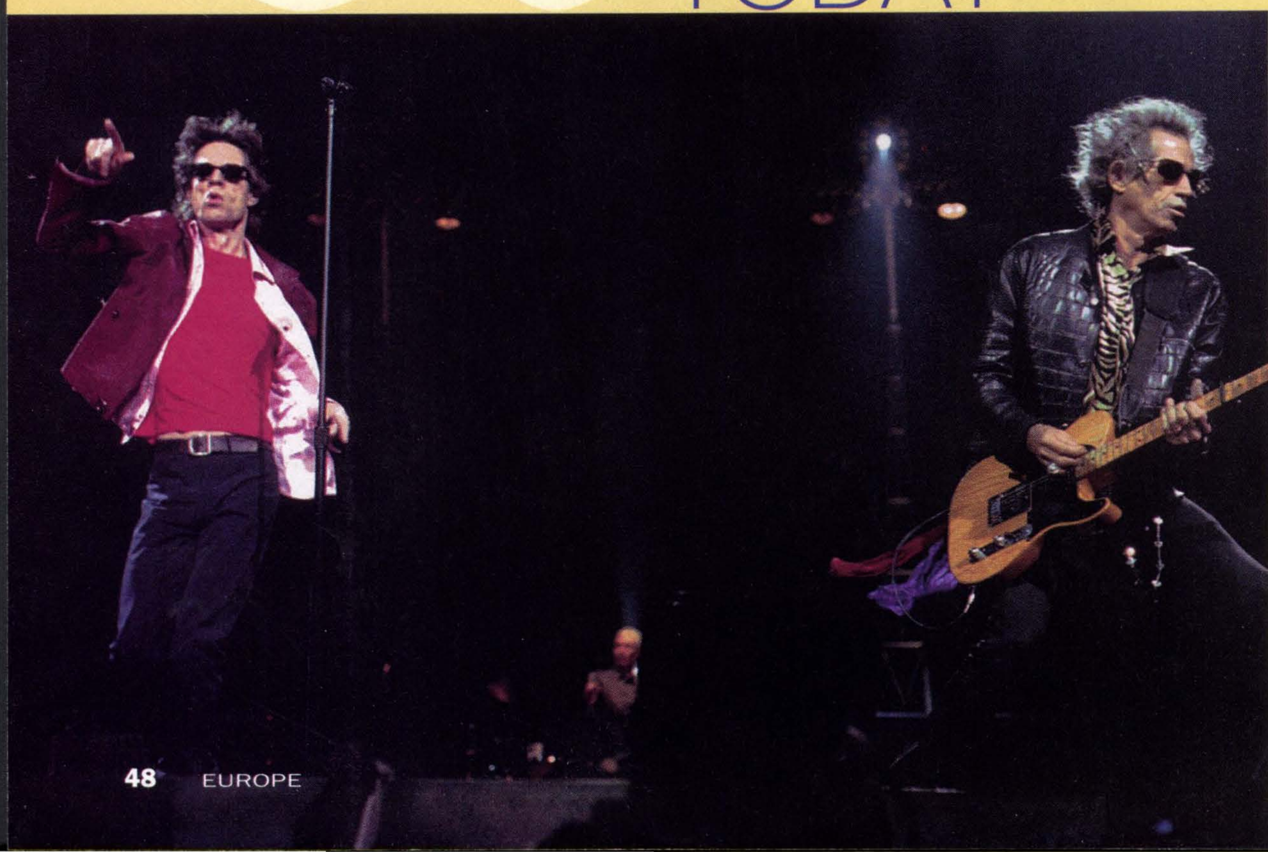
YESTERDAY & TODAY

The Invasion Continues: From the New York City stage of the Ed Sullivan Show, the Rolling Stones introduced their brand of rock-and-roll to US television viewers in 1966. In February, 1999—more than three decades later—Mick Jagger and company cranked up their amplifiers at the Palace of Auburn Hills in Michigan as part of their current No Security tour.



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MONTH COUNTRY PROFILE / BUSINESS FEATURE	TRAVEL FEATURE REGION PROFILE	ADVERTISING SPACE DEADLINE
APRIL		**MARCH 5**
UNITED KINGDOM London: Europe's Business / Financial Center Focus on Energy / Industry North Sea Oil	UK Airlines Manchester, UK	
MAY		**APRIL 2**
SWEDEN Largest EU Firms in US EU / US Trade Relations	Stockholm Malmo, Copenhagen	
JUNE SPECIAL EURO ISSUE		**APRIL 30**
THE NETHERLANDS Euro / Dollar / Yen Era How the Euro Will Affect Americans G7 Meeting in Cologne	Golfing in Europe Utrecht, Netherlands	
JULY / AUGUST		**MAY 28**
FINLAND / EU PRESIDENCY Europe's Common Foreign Policy Business in the Baltics Environmental Issues	Helsinki, St. Petersburg Helsinki, Russia, The Baltics	
SEPTEMBER		**JULY 2**
FRANCE French Firms Go Global Transportation the French Way	Provence Ile de France	
OCTOBER		**SEPTEMBER 3**
ITALY The Art World	Amalfi Coast Milan	
NOVEMBER		**OCTOBER 1**
GREECE Cyprus - Mideast Business Center	Holiday Cruises Top 10 Regions in Europe for American Investments	
DECEMBER / JANUARY SPECIAL MILLENNIUM ISSUE		**OCTOBER 29**
PORTUGAL / EU PRESIDENCY 100 Years of European Business Europe in the New Century	Algarve Region Greater Lisbon	

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