



Ladies and Gentlemen,

It is a pleasure to be here this evening at the London School of Economics and Political Science. This institution has educated many generations of Europe's leaders and policy entrepreneurs, and I can see the next generation sitting here in front of me.

I did my own doctorate at Oxford, but under the supervision of one of the LSE's leading lights over many years, William Wallace, now professor emeritus and still a working peer, Lord Wallace of Saltaire.

In the current debate on the future of Europe, it is worth recalling one of William's long-standing warnings against overly simplistic explanations of how European integration develops. He wrote: "It is far easier to agree on the interconnection between deliberate processes of political integration and informal processes of economic and social integration than to establish any clear line of causation between them."

It was William who taught me that European integration is an interactive process of economic and political forces – in other words, states and markets. These forces work on different timescales. Political development occurs over long periods of stability with sudden breaks of discontinuity, as we saw with the 40-year-long Cold War and its sudden end in 1989. Economic and technological change is more gradual and

continuous, following long cycles of innovation and consolidation which Joseph Schumpeter described as the 'creative forces of destruction', and short-term business cycles which stimulated the demand-management theories of John Maynard Keynes.

We see these dynamics at work in Europe today. The long, deliberate process of the political development of the EU has been disrupted by the referenda on the constitutional treaty in France and the Netherlands, prompting talk of crisis. But this sense of crisis also stems from slow economic growth and high unemployment, giving rise to social discontent and recently street violence in France's inner cities.

In reality, we need both an economic Europe and a political Europe. We need economic reforms to enhance competitiveness, and political reforms to make the Union more effective and democratic. The founders of the London School of Economics and Political Science were far-sighted in putting both disciplines together in this institution.

The same goes for deepening and widening of the European Union – or strengthening European political integration and extending the zone of peace, democracy and prosperity in our continent. Widening versus deepening is a false dichotomy. The EU has always pursued these two objectives in parallel. As the veteran Belgian diplomat Philippe de Schoutheete argues:

“The debate turns to a match between widening and deepening, or between those who support an intensive Europe and emphasise unity and those who support enlarging Europe and emphasise diversity. But this debate is not relevant, since Europe as a continent cannot give up enlargement without denying its vocation,

nor can it give up deepening without losing its dynamism. As we have always needed to reconcile unity and diversity, we should reconcile widening and deepening.”

The EU has always made its most significant developments at the same time as enlargement. The first enlargement in 1973 to the United Kingdom, Denmark and Ireland was preceded by two significant initiatives in 1970: the Davignon Report which kicked off European Political Cooperation (the precursor of the EU's Common Foreign and Security Policy) and by the Werner Report, which started the first, short-lived effort to create a monetary union. The two Southern enlargements of the 1980s to Greece, Portugal and Spain coincided with the adoption of the Single European Act in 1986, which helped to create the Single Market.

Then the Berlin Wall came down. The EU started the 21<sup>st</sup> century as a very different community from the one of the Cold War era. The history books of the future may well characterise the era that began in 1989 as the second great transformation of post-war Europe, following the first transformation after the Second World War, when European integration was established.

During Europe's second transformation, both deepening and widening have again moved ahead in parallel. Take widening: the EU has more than doubled its membership from 12 to 25 member states after the collapse of the Berlin Wall settled. Austria, Finland and Sweden joined in 1995, and in May 2004 came the Big Bang, when eight countries of Eastern and Central Europe joined the Union after successful democratic transformation, together with Cyprus and Malta. Bulgaria and Romania, part of the fifth round of enlargement, will join the Union in 2007 or 2008.

Take deepening: the Union has taken major steps in its political and economic integration while undertaking its biggest enlargement ever. We created the single market, monetary union and passport-free travel in the Schengen area, and reinforced the common foreign and security policy. A coordinated approach to internal security is vital to protect European citizens from the threat of terrorism. And with the euro, “every European has a little piece of Europe in his pocket”, as Romano Prodi put it. The EU’s ability to respond to its citizens’ concerns must increase, but enlargement does not stop it from doing so.

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The second transformation of Europe remains unfinished business, however. To complete it, we need to take a dynamic view of the world, not a static one – after this transformation, another challenge is sure to arrive. The EU’s great strength has been its ability to adapt to new circumstances. Although the integration project began in the very different context of post-war reconciliation, it has adapted Europe to meet the challenges of globalisation and the end of communism.

Adaptation is the key to the EU’s future success too. The EU is a living political animal, not a fossil. It must continue to evolve, and it can do this through practical steps to make the Union function better, starting under the current framework of Nice. I consider further institutional reforms necessary to make our decision-making more effective, efficient and fair, and to reinforce our common foreign and security policy.

I believe the best way out of our constitutional dilemma is to focus on concrete measures to improve the way the EU works, not a long theoretical debate. At heart, I remain a functionalist – and proud of it.

As a functionalist, I regard the performance of the European economy as the key to the success of the EU's performance, by rebuilding confidence at political level. Economic growth, employment and competitiveness bring security to citizens and increase the legitimacy of politicians. Political leaders have a greater margin for manoeuvre in dealing with policy challenges when their citizens have confidence that the economy can weather new storms and generate new jobs.

Enlargement is part of the solution to our economic problems. We have a sound economic story to tell about enlargement, for both new and old member-states. But we have failed to communicate this success story well. Both the Commission and national leaders have been better at doing enlargement than at explaining it!

The usual narrative on the economics of enlargement is a zero-sum game of low-cost production and delocalisation. But the alternative narrative is that of mutually beneficial industrial restructuring inside an enlarged and competitive Europe, based on cross-national production networks, which can be a genuine win-win situation for both old and new member states. Let's look at the empirical evidence for these two narratives.

Last year, the new member states grew at double the rate of the old EU-15, on average. Growth was even stronger in the countries in the accession process, at over 9% in Turkey and 8% in Romania. This dynamism in central, eastern and south-eastern Europe is welcome and will benefit all of us. New economic opportunities, both to produce goods

and to sell them in the markets of the enlargement countries, can create jobs in all of the member-states.

Trade between the old EU-15 countries and the Central and East European members has quadrupled since the first half of the 1990s. The number of jobs created in the old member states is much higher than the number of jobs lost owing to the movement of manufacturing plants to other parts of Europe.

The process of enlargement makes the legal framework for business similar right across Europe, raising common standards and evening out implementation of regulations to create a level playing-field. That process in turn opens investment possibilities for European companies to streamline their activities while re-organising their production and logistics to make them more efficient. In this way, their competitive position in world markets has improved.

The velvet revolutions of 1989 in Central and Eastern Europe opened up a market of 100 million people to the companies of Western Europe, providing great business opportunities; for example for French supermarket chains and car manufacturers, and for Dutch telecom firms and foodstuff producers, as well as for countless German *Mittelstand* companies.

The 'delocalisation' debate has also failed to include the positive impact of this kind of industrial restructuring – based on a 'diversity of production functions', as John Zysman points out – on the long-term competitiveness of the European economy. An example of job creation in Western Europe through industrial restructuring is the Renault Logan

car. The project has created more than 750 jobs in engineering, purchasing, and with suppliers in the old member-states of the Union through Renault's expansion of production in Romania.

It is not a question just of utilising cheap manual work. For example, Romania trains the largest number of IT engineers in the world after India. At the headquarters of the Microsoft in Washington, Romanians are the second largest group of foreigners after Indians. However, according to representatives of the company I met recently, during the last two years Romanians have been increasingly returning to their home country to take up new opportunities there.

This is a familiar story to anyone who has studied previous enlargements. As countries move towards EU membership, they become more attractive places for their best and brightest people to return to take a new job or start up a business.

We should also not forget the significance of Turkey in helping to balance the disproportionate demographics facing Europe in just a few decades. Part of my pension cheque will depend on the contributions of a young, well-trained Turkish engineer, working in the single market.

This conclusion leads me into a very hot debate in Europe right now – whether to liberalise further the possibilities for workers to move freely across the enlarged Union. The experience of this country shows clearly that there are major benefits to be gained from opening up labour markets. The many people from the new member-states working here have contributed some half a billion pounds to the British economy, and only a tiny percentage have sought social assistance.

These Poles, Lithuanians, Slovaks and others are mostly hard-working young people who are gaining experience abroad, while saving up for their future. Most intend to return home later on, taking back capital and new skills that will benefit their countries' economies. This temporary migration is more 'brain gain' than 'brain drain'. It is also better for both the exchequer and the rule of law if people work legally rather than remain unprotected and open to exploitation in the informal economy.

This experience is rather similar to what happened after Greece, Portugal and Spain joined the EU in the 1980s, when fears of a major disruption of labour markets proved to be unfounded. Ireland and Sweden have also welcomed workers from the new member-states, and their economies have benefited. I hope that the other member-states will consider lifting their restrictions in May, when the first two years of the transition period on the movement of workers will end.

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Ladies and Gentlemen,

I welcome the debate on EU enlargement. It is legitimate and useful to keep discussing the challenges posed by enlargement, and how to meet them. We should underline the consolidation of our enlargement agenda and certainly consider how to increase the absorption capacity of the EU. This debate has been going on for over four decades now, and it has been very comprehensive and inclusive. However, it should not be used to question our existing commitments under the consolidated enlargement agenda in South-Eastern Europe – that is, Bulgaria, Romania, the Western Balkans and Turkey. The EU has given all these countries the prospect of EU accession once they can meet the strict

conditions. I trust that European leaders will conduct a responsible debate that does not question these commitments and erode our credibility in demanding that they meet our standards. Otherwise we would weaken our ability to work for stability and democracy in the Western Balkans and thus harm Europe's own interests.

The enlargement process is helping to keep stable some of the most volatile parts of Europe – such as the Balkans – and delivering practical results in political and economic reforms in the aspirant countries. It is much better to export stability to the Western Balkans through the enlargement process than to import instability in the shape of refugees and criminal activities.

Enlargement policy should not be held hostage to a theological debate about the ideal shape of the perfect Union, or the final borders of Europe. We now have a consolidated enlargement agenda, so a theoretical discussion about whether Ukraine should eventually join the EU would benefit neither the Union nor the Ukrainians at this point in time.

Let's respect the principle of Article 49 of the EU's treaties, which states that any European country that respects and applies European values, especially democracy, human rights, the rule of law and fundamental freedoms, may apply for EU membership. That does not mean that every European country must apply, or that the EU has to accept every one. But it does mean that we should remain open to changes on our continent. To close the door forever, by drawing a line across the map to define Europe once and for all, would not be good for us or for any of our neighbours. Sometimes, the art of politics requires the art of ambiguity.

Enlargement has strong democratic legitimacy. Remember that nineteen of the 25 member-states were once enlargement countries, and every accession is agreed unanimously by all the member states and with the assent of the European Parliament. And a majority of EU citizens still support further enlargement.

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Ladies and Gentlemen,

In conclusion, my strategy for the future of enlargement is based on three Cs: consolidation of the enlargement agenda, rigorous application of conditionality, and better communication. This is the best way to ensure that enlargement is not made a scapegoat for the problems in Europe, but is seen as the success story it really is. The mission of enlargement is a vital part of the history of the EU. That mission is very much alive today.

Thank you for your attention, and I look forward to your questions.

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