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for membership

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## Background

On 28 March 1977, on behalf of the Government of the Portuguese Republic, the Prime Minister, Mr Mario Soares, submitted to the President of the Council of the European Communities Portugal's application to accede to the European Coal and Steel Community (ECSC), the European Economic Community (EEC) and the European Atomic Energy Community (Euratom).

The Council at its session on 5 April 1977 agreed to initiate the procedure provided for in Articles 98 of the ECSC Treaty, 237 of the EEC Treaty and 205 of the Euratom Treaty, adding that the Commission in drawing up its opinion 'will remain in close contact with the Member States on the one hand and Portugal on the other'.

Contact with the Portuguese authorities has been conducted through the 'Commission on European Integration', set up by the Portuguese Government to promote and coordinate the proceedings preparatory to accession. By this means the Commission's staff have been provided with extensive documentation on the situation of Portugal. The Member States for their part have been kept abreast of the Commission's proceedings in the preparation of its opinion.

The Commission in addition forwarded to the Council on 20 April 1978<sup>1</sup> a communication setting out general considerations of problems of enlargement, in which considerable attention is devoted to Portugal, and the specific aspects of its situation among the three applicants and the kind of arrangements these necessitate are dealt with in particular.

That communication, and the texts which supplement it, form the basis for this Opinion, which in effect represents the application of the general considerations in the specific case of Portugal.

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<sup>1</sup> Bull. EC 4-1978, points 1.1.1 to 1.1.7; Supplements 1/78, 2/78 and 3/78.

## Part One

### General remarks

1. The Treaties of Rome and Paris signify the clear intention that other European States sharing the democratic ideal of the European Community's Member States should be able to accede to the Community. It was in this context that Mr Soares placed his country's application to do so, stating that it came within this perspective of solidarity among peoples and was the guarantee of Portugal's turn to democracy, which had begun on 25 April 1974 and had led within months to the restoration of public liberties, the recognition of political parties, the ending of arbitrary repression and the effecting of decolonization. On 25 April 1975 a Constituent Assembly was elected which framed the Constitution of 2 April 1976, the preamble to which proclaimed 'the decision of the Portuguese people to establish the principles of democracy'.

2. Democracy in Portugal is now an established political fact. It has already ridden out testing times, due to the aftermath of the revolution and the problem of reabsorbing the refugees from Angola and Mozambique, and has speedily gained indisputable international authority.

3. The Community cannot leave Portugal out of the process of European integration. The resulting disappointment would be politically very grave and the source of serious difficulties. The accession of Portugal, which set its face firmly towards Europe almost as soon as its democracy was restored, can only strengthen the European ideal. The Commission accordingly feels that an unequivocal Yes should be given promptly to the Portuguese request to open accession negotiations as soon as possible. It should moreover be noted that Portugal's accession, given in particular its policy of openness to the outside world and its traditional ties with Latin America, Africa and the Far East, will enhance the role of the Community in the

world. Political considerations must not, however, be allowed to obscure the economic difficulties discussed in the following pages, in which the Commission sets out the arrangements which will need to be instituted on both sides in order to make a success of Portuguese accession.

4. For the Community, the economic impact will be very limited, in view of the relative weight of the Portuguese economy. Portugal represents only 3% of the present Community of Nine in population, and 1% in gross product (GDP).<sup>1</sup> The problems liable to arise would stem primarily from the fact of appreciable disparities in development, which would accentuate the Community's heterogeneity. This being so, decision-making in the Community institutions could be rendered more difficult.

5. For Portugal, the prospect of accession makes it all the more necessary to remedy certain shortcomings in its economy. In the 1960s the radical reforms of its economic and social structures that could have prepared it for integration into a modern economic entity like the Community were not effected, although this was a time of stability and sustained growth in the Portuguese economy. Thus investment remained extremely low throughout those years, and the main result of the economic policy followed was the accumulation of foreign-exchange reserves.

This has produced a society and economy with major structural weaknesses in all sectors of activity. Twenty-eight per cent of Portugal's working population is still employed in agriculture, which, however, accounts for only 14% of GDP. This is due *inter alia* to the fact that although Portugal's agricultural potential is limited, major deficiencies are currently preventing the full exploitation of this productive potential. As a result the country has for some years been heavily in deficit agriculturally. Its industrial structure is dominated by traditional sectors at present depressed all over the world (e.g. textiles,

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<sup>1</sup> 1976 figures, at current prices, in USD.

footwear, food processing); in addition plant is very dispersed and uncompetitive. Services, despite the country's great tourist potential, represent only a comparatively small proportion of GDP. There is much disparity in development between the regions, with industrial activity heavily concentrated along the seaboard from Braga to Setúbal.

6. On top of these structural weaknesses have come since 1973 troubles due on the one hand to the world recession following the oil crisis and on the other to the aftermath of the revolution in 1974. Decolonization was rapid, which involved the abrupt repatriation of half-a-million Portuguese nationals, the demobilization of a large number of young men who had been fighting in the colonial wars, and the loss to Portugal of an important market. The leap in wages in the period immediately after the revolution, coupled with the soaring world prices of raw materials and above all of energy products, caused galloping inflation at home. Furthermore, an unstable social climate bore especially hard on agriculture, particularly in the centre and south of the country, leading to a steady fall in production which forced Portugal substantially to increase its agricultural imports, which now account for something like 50% of its trade gap.

The climate of uncertainty induced by nationalizations which affected much of industry and the services sector in 1974 and 1975 adversely influenced investment and caused a sharp drop in productivity.

Economic activity in the last few years has been stimulated much more by private and public consumption than by capital formation and exports.

7. The combination of structural weaknesses and cyclical difficulties affecting the Portuguese economy, accompanied by a simultaneous deterioration in the terms of trade, was bound to produce a growing, and in the long term intolerable, deficit on current account. The current-account balance swung from being USD 350 million in credit in 1973 to being USD 800 million in deficit

in 1974, and by 1977 the deficit had reached USD 1 500 million.<sup>1</sup> This has meant massive erosion of the reserves.

8. Accession, by completing the process begun under the 1972 Agreements<sup>2</sup> of opening the Portuguese market to competition from Community industry, would be liable to aggravate Portugal's economic difficulties: it could force enterprises not yet fully developed to go out of business altogether and it could further accentuate regional disparities.

In agriculture the repercussions of accession would be less clear-cut. As concerns market policy, extension of the Community system of price support might benefit some Portuguese production lines: this would be so in the case of products not at present enjoying price support in Portugal and of those for which support prices are lower than Community prices. On the other hand the opening of the market to products from Member States and third countries having preferential agreements with the Community would mean keener competition which could hit the less competitive production lines very hard indeed. This, and the adoption of the Community system of agricultural levies, would adversely affect Portugal's current-account balance, owing to the rise in the level and costs of imports. The Community structural policy corresponds to Portugal's essential requirements and would therefore have beneficial effects. In its present form, however, it would probably prove inadequate to cope with the scale of the problems to be tackled.

9. In view of the problems described, it is indeed urgent for the Portuguese Government to effect radical economic and social reforms to bring about the necessary restructuring of the country. The first aim is undoubtedly to scale down the balance-of-payments deficit. Accordingly, the agreement with the IMF for the second tranche of a loan to assist the balance of payments, on which the release of the funds of the 'Por-

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<sup>1</sup> Approx. 10% of GDP.

<sup>2</sup> Point 49.

tugal Consortium' set up in 1977 by a number of OECD countries depends, calls for stabilization measures.

A 1978-79 stabilization plan just adopted is aimed primarily at reducing the 1978 balance-of-payments deficit to less than USD 1 000 million, to limit inflation to 20%<sup>1</sup> and to avoid too heavy a fall in employment, while maintaining some economic growth.<sup>2</sup> These measures represent a great sacrifice for the people, especially as last year's action to limit wage increases to 15% meant a real cut of nearly 10% in the wage-earners' purchasing power. Such a sacrifice can be accepted only if the reconstruction of the economy in 1978 enables the basis to be laid for a policy of structural reform, from which sustained economic recovery can be looked for from 1979 onwards.

10. To this end the Portuguese Government is to lay before Parliament in October the 'Main economic guidelines for the 1979-84 plan', which is to carry on from the short-term stabilization measures. The Government has already said that the focus will be first and foremost on industrial and agricultural restructuring and on the development of services and infrastructures with a view in particular to reducing regional disparities. The policy will seek also to keep imports within bounds and to boost exports, and in addition will include supporting measures in the social field, notably with regard to education and vocational training. The policy will be based on some containment of consumption and very rigorous development of public and private investment. To this end it will be necessary to mobilize disposable savings in the country and establish the conditions of confidence that will encourage foreign investment.

11. The above guidelines will be a practical proposition only if Portugal receives from the Community certain indications as to the accession process. The economic options of restructuring and renewed expansion are both dictated by and conditional on integration into Europe—dictated by it because the de-

velopment gap is a major obstacle to integration which means that Portugal must achieve faster growth than the Community's, and conditional on it because the restructuring must dovetail into the economic coherence of an enlarged Community.

12. Hence, the Community's reply to Portugal must be given soon. The Community must state its willingness to support the restructuring drive the Portuguese authorities will be undertaking on the basis of the above guidelines.

13. As the process goes forward, the Commission will propose to the Council the support measures the Community should adopt. It would, however, recall the broad outlines of the arrangements set out in its communication on enlargement dated 20 April 1978, which should underpin the Portuguese accession negotiations.<sup>3</sup>

14. As it then pointed out, sustained growth faster in Portugal than in the Community will facilitate the process of Portugal's adjustment. But that growth will only be possible if it is based on a high level of investment, drawing on internal and/or external savings, in a climate of stability and confidence. To this end care must be taken to see that that climate is not marred by external monetary disturbances.

15. As Portugal's balance-of-payments position will probably be somewhat precarious for several years to come, Community support during this time would be particularly valuable.

The Community ought therefore to take all possible steps to see that such support is forthcoming. As in the past, action should be taken in the first instance through the appropriate international bodies, notably the IMF.

<sup>1</sup> Inflation in 1977 was running at 27%.

<sup>2</sup> The aims sought would be pursued *inter alia* by a more restrictive and selective credit policy and by a budget policy designed to stabilize public and, through taxation, private consumption.

<sup>3</sup> See 'Background' on p. 5.



Since Portugal's future lies in Europe, it would also be desirable to consider action at European level. The Community should examine the possibilities of actively participating in such action.

It would thus be desirable to support the Portuguese Government's efforts to raise funds in the international capital markets, and to consider the possibilities for recycling certain loans falling due. Consequently, it is all the more necessary to make rapid and substantial progress towards economic and monetary union: this would facilitate the action described above and give the Community new legal and financial instruments for helping the Portuguese economy directly, or by way of guarantees.

16. Alongside these moves to assist the balance of payments, the Community's cooperation projects for furthering Portugal's economic and social development should be proceeded with. In this context, consideration might be given to speeding up utilization of aid under the Financial Protocol signed in 1976. At the same time the Community should prepare from the outset of negotiations to support Portuguese development, particularly in the industrial and agricultural sectors. Appropriate development programmes drawn up by the Portuguese authorities in collaboration with the Community, with Community cofinancing, could provide a suitable framework for intervention.

17. Also, the Community should declare its willingness to engage in consultations with Portugal on the measures planned in the present Community to restructure industries in difficulty and agriculture. This would involve Portugal's abiding by jointly agreed rules of discipline, notably in the industrial sector, and Community contributions to the financing of measures in Portugal, where these entailed sacrifices like those made in the Community with the aid of the Community Funds for like purposes.

18. Such concerted action, forestalling conflicts of interest, would enable the Commu-

nity to exempt Portugal from import restrictions in respect of products vital to its industrial restructuring and the restoration of its balance of payments where marketed under normal conditions of competition. Furthermore, the Community should show flexibility over certain provisions in the 1972 free trade agreement so as to enable projects of importance to the development of the Portuguese economy to go ahead.

19. In conclusion to these general remarks, the Commission would observe that Portugal in opting for Europe has shown its desire to enter a Community which is politically and economically strong. Hence accession must not act as a brake on the process of Community integration; at the same time it cannot be at the cost of difficulties and sacrifices too heavy for Portugal to bear. It is essential therefore to institute some precautions with regard to the process of integration, and, similarly, to ensure greater coherence of the economy within the borders of a Community including Portugal. In Portugal's case the selection of the transitional measures will be of particular importance: they will have to be organized as to pace and procedure in the light of the adjustment problems which can be properly pinpointed only in the sector-by-sector negotiations.

## Part Two

### Specific considerations

In its Communication on enlargement dated 20 April 1978,<sup>1</sup> the Commission examined the specific situation in the various economic sectors in Portugal, and the problems relating to individual sectors and to the country's macro-economic situation. Part Two of this document is therefore confined to various additional remarks on the adoption by Portugal of Community policies and rules.

#### Customs union

20. Portugal's integration will be facilitated by the EEC and ECSC Agreements concluded in 1972,<sup>2</sup> which provide for the progressive dismantling of tariffs on industrial products, to be completed by 1985. All quantitative restrictions on imports of these products were abolished on 1 January 1973. Since 1 July 1976 ECSC products and virtually all EEC industrial products originating in Portugal have been able to enter the Community free of customs duties. The Common Customs Tariff (CCT) rates for certain fresh and processed agricultural products have been partly reduced. Since 1 July 1977 the Community has enjoyed exemption from customs duties on approximately 40% of its industrial exports to Portugal. Exemption for approximately 37% is scheduled for 1 January 1980 and the remaining 23% are to become exempt on 1 January 1985. No provision has been made for any concession to the Community on agricultural products. Major problems are unlikely to arise in connection with Portugal's adoption of the CCT as the Portuguese customs tariff is not significantly higher than the CCT.

Portugal has already largely abolished customs duties of a fiscal nature applied to industrial products. These duties will be completely abolished by 1 January 1980 at the latest. Customs duties of a fiscal nature on products not covered by the 1972 Agree-

ment, which are almost exclusively agricultural, will have to be abolished or replaced by an internal charge, which should not involve any difficulties.

21. The import surcharge, which is intended mainly to bring the balance of payments into equilibrium, is applied to imported products irrespective of origin. There are two rates, and since October 1976 these have been increased from 20% and 30% to 30% and 60% respectively. An estimated 28% or so of 1976 imports are subject to the first of these rates and approximately 2% to the second. The Portuguese Government has expressed its intention to replace the import surcharge by internal measures of a fiscal nature. Such measures adopted before accession will have to be brought into line with Community provisions. The Portuguese Government has, moreover, already taken steps to that end by abolishing the import deposit system on 1 January 1978.

22. It will be necessary to examine whether the arrangements applied in Portugal to the importation and marketing of industrial alcohol, hydrocarbons and certain agricultural products subject to market organization in the Community are compatible with Community provisions.

#### Agriculture

23. Agriculture accounts for 12% of Portugal's GDP and employs 28% of the working population. The development of agriculture, which is necessary for Portugal's economy in any event, becomes even more of a necessity given the prospect of accession. It is, in particular, essential for Portugal to reduce, or at least prevent any increase in, the proportion of the trade deficit accounted for by agricultural imports, since the rate of self-supply for several products, including basic foodstuffs, is very low, despite the proportion of the labour force employed in agriculture. In 1975, agricultural products represented 22.9% of

<sup>1</sup> See 'Background' on p. 5.

<sup>2</sup> Point 49.

total imports in value terms, and only 16.6% of total exports. The trend recorded over the last few years shows, furthermore, that this imbalance is tending to increase.

24. The difficulties affecting Portuguese agriculture and preventing its potential from being used to the full are social and structural. In order to improve productivity and production techniques, it is necessary to make changes in the land tenure structure; in particular, this involves an increase in the size of farms and less fragmentation, especially in the north of the country, injections of capital and improved vocational training for farmers. These measures should progressively bring about an increase in and better returns from agricultural production. However, they will entail a reduction in the farming population and will therefore be at least partly conditional upon the alternative job opportunities. Since the prospects of alternative employment seem slight for the next few years, the process will take quite some time to carry out, even if considerable financial resources are made available. In view of this, the structural operations should be backed up by measures to encourage production of products that are of prime necessity.

25. The adoption of the common agricultural policy could have certain beneficial effects for Portuguese producers, owing to the system of Community guarantees providing price support in the event of a crisis. The benefits would, however, be significant only in the case of products for which there is at present no guarantee in Portugal (fresh fruit and vegetables) or for which the level of guaranteed prices is at present lower in Portugal than in the Community (durum wheat, olive oil and wine). On the other hand, the liberalization of trade with the Member States of the Community and the changes in the arrangements for imports from other countries will increase competition. A vigorous structural policy would greatly ease the adoption of the Community policy on prices and markets, particularly in the medium term.

26. As regards the Community, Portugal's accession should, generally speaking, cause only small changes in the supply rate for the main products, since Portuguese production and consumption of agricultural products are relatively low compared with Community production and consumption.

### **Fisheries**

27. Fishing accounts for 1.2% of GDP and employs 0.9% of the working population. Fishery products play a relatively important part in trade, however. Fresh and chilled fish constitute about 10% of agricultural imports and preserved fish about 15% of agricultural exports.

Portugal, which has hitherto not fully exploited its own fishery resources, has been hit very hard by recent international development as regards fishing zones. Over the last five years one-third of its catches came from waters from which it is now largely excluded. Accession will involve a reallocation of fishing quotas among Member States in the Community fishing zones. It will also involve the denunciation by Portugal of bilateral fisheries agreements and in some cases the revision of the fisheries agreements concluded by the Community. Furthermore, Portugal will have to withdraw from the international fisheries conventions to which it is a party as the Community is a signatory to all conventions which are of importance to Community fisheries.

### **Industry**

28. Portugal's industry accounts for 47% of GDP and employs 33.5% of the working population. Portuguese industry will have to be strengthened fairly rapidly, in order not only to improve Portugal's ability to withstand Community and international competition, but also to sustain the attempt to improve living standards, and create jobs to bring down the high level of unemployment and cope with the consequences of modernizing agriculture.

