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From the Private Secretary

7 March 1990

INSEAD

Thank you for your letter of 2 March, enclosing a note on the INSEAD competitiveness study. The Prime Minister was grateful for this material.

(PAUL GRAY)

Duncan Sparkes, Esq.,
HM Treasury.

A handwritten signature, likely of Paul Gray, located in the bottom right corner of the page.



Treasury Chambers, Parliament Street, SW1P 3AG
01-270 3000

2 March 1990

Paul Gray Esq
Private Secretary to the
Prime Minister
10 Downing Street
LONDON
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me

Prime Minister²

*You may like to see this Treasury
commentary on the study to which
Trevor Holdsworth referred when he came
to see me in January.*

Dear Paul,

at 11.15

*Rach
1/3*

In your letter of 24 January, recording the Prime Minister's meeting with Sir Trevor Holdsworth, you suggested that we might look into a competitiveness study by the French business school INSEAD, which had been mentioned by Sir Trevor. This apparently showed the UK in a second position in Europe behind Spain. I apologise for the delay in replying - it has taken some time to track down the source of Sir Trevor's information.

... I attach a short note on the INSEAD study.

Yours,

Duncan

DUNCAN SPARKES
Assistant Private Secretary

EEC Integration towards 1992

Damien J Neven, INSEAD and CEPR

The competitiveness study mentioned by Sir Trevor Holdsworth to the Prime Minister during their meeting on 23 January 1990 was conducted by Dr Damien Neven, as part of his work on the implications of 1992, and is not yet published. (He has promised to send us a copy on publication, probably in a few weeks.) We have, however, spoken to Dr Neven on the telephone, and we have seen a related paper of his on gains and losses to be expected from the Single Market programme.

2. The competitiveness paper, when published, is unlikely to have as strong or as general a conclusion as that referred to by Sir Trevor - that the UK is in a second position in Europe behind Spain. However, on the telephone, Dr Neven said that he found the UK to be in a "pretty good position in a number of industries", and the UK's position has "improved tremendously in the 1980s". In particular, he found that the UK performed well in industries intensive in human capital. According to the paper we do have, these are chemicals, pharmaceuticals, transport equipment, and electrical and mechanical machinery.

3. Dr Neven has performed a standard analysis of competitiveness, assuming technology is the same in the different countries and comparing labour costs and value added per worker in different industries at a fairly disaggregate level. He has used data from Eurostat (the EC source) and the US Bureau of Labour Statistics.

4. The paper on gains and losses from the Single Market examines the possible exploitation of comparative advantage and economies of scale. The conclusions are favourable to the UK. The main beneficiaries of 1992 will be the Southern European countries, which will benefit both from a better exploitation of their comparative advantage and from a better use of scale economies to a much greater extent than the countries of Northern Europe. Northern Europe has little to expect from the Single Market, with the exception of the UK, which can expect some gains, because it is less integrated and has an unexploited comparative advantage in industries intensive in human capital.

5. Dr Neven finds a high share of R&D personnel in total employment in the UK, and a high share of graduates among R&D personnel. This suggests to him that human capital is used intensively. His calculations show that labour costs in the UK are 25 per cent below the Northern European average, indicating that the price of human capital is low (i.e. lower wages of graduates/scientists etc.), and therefore that there is scope in the Single Market for specialization in industries intensive in human capital (listed above - para. 3), where the net trade position of the UK is currently negative.

6. Dr Neven also observes that wages in the UK tend to be lower, in comparison with the continent, in industries where non-tariff barriers are high, and thus "UK industries which have been prevented from exporting to the continent because of NTBs should be in a favourable position to increase their exports when these barriers are removed". Beverages, foodstuff, metals, electrical and mechanical machinery and motor vehicles are cited as industries with the highest NTBs.

7. We will have to await publication, but we have the impression that the competitiveness paper will not provide a particularly useful source of briefing points.

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