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Trends in the European Union and Russia: Implications for the United States

Nile Gardiner, Ph.D.

The introduction of the euro in 1999 and the expansion of the European Union (EU) from 15 to 25 member states in 2004 were heralded by many European leaders as the birth of a new, unified Europe, a powerful phoenix rising from the ashes of the biggest war in the history of mankind. In many ways, the EU has been an extraordinary experiment, the creation of the world's biggest single market, with the free movement of goods, services and peoples across an extremely diverse continent. The relative stability of the single currency, and the smooth entry of former communist countries in Eastern and Central Europe into a Western European-dominated club are undoubtedly impressive achievements, and it is with an air of confidence that the EU is looking to further expansion in 2007, when Romania and Bulgaria will make it a group of 27.

However, the superficial success of the European Union masks major underlying economic problems, as well as deep political divisions and rising concern over threats to national sovereignty. The rejection of the European Constitution in France and Holland in 2005 was a huge wake-up call to European elites who believed in what is called "the finality of European integration." The French and Dutch referenda were symbolic of growing unease among European publics with the increasingly undemocratic nature of the European project.

This paper examines both economic and political trends in the European Union and its giant, unpredictable neighbor to the East, Russia, assessing their long-

Talking Points

- The superficial success of the European Union masks major underlying economic problems, as well as deep political divisions and rising concern over threats to national sovereignty.
- The increasing centralization of political and economic power in Europe is detrimental not only to America, but also to the European continent itself.
- The continent faces a stark choice between a Europe based around the principles of free markets, free trade, limited government, national sovereignty, and decentralized power, and a federal Europe that worships at the trough of socialism and supra-nationalism.
- The United States works most effectively when it cooperates directly with national governments, employing a "coalition of the willing" strategy. Europe is not, and never has been, a united political entity, and U.S. policy must support a Europe of nation-states.

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term implications and impact upon U.S. interests. It explores how the increasing centralization of political and economic power in Europe is detrimental not only to America, but also to the European continent itself. It also looks at the rise of anti-Americanism in Europe, and the threat it poses to the Anglo-American special relationship.

Economic Trends in the European Union

The Economic State of the EU. Europe's finance ministers are starting to feel increasingly bullish. Following several years of economic stagnation, the 12-member eurozone has begun to stage an apparent revival, growing at a faster rate than the United States for the first time since 2001. Despite an 80 percent rise in oil prices, eurozone growth is forecast to rise to 2.5 percent for the final quarter of 2006.

However, the renewed sense of optimism in Brussels may not last into 2007. There remain deep-seated underlying problems with the eurozone's largest economies. Over-regulation, draconian tax regimes, ageing populations, inflexible labor laws, relatively low levels of public consumption, and limited working hours all contribute to a Europe that is significantly underperforming in the global marketplace. The euro may have contributed to financial stability, but has not stimulated economic growth or created jobs.¹

Despite the spin being put out by Brussels, Europe's long-term economic prognosis is bleak. A 2005 study by Eurochambres, the Association of European Chambers of Commerce and Industry,² concluded that "the economic performance of the EU is about 20 years behind that of the U.S.... [T]he current EU levels in GDP [gross domestic product], R&D [research and development] investment, productivity and employment were already reached by the U.S. in the late 70s/early 80s." The study found that it would take the EU until 2023 to reach American levels of employment, if growth exceeded that

of the U.S. by 0.5 percent per annum. It would take the EU a staggering 50 years to reach U.S. productivity rates; 67 years to attain U.S. levels of income per capita; and 118 years to achieve parity with U.S. levels of research and development, if Europe consistently achieved a half-point growth advantage over America.

Another study, by Swedish think tank Timbro,³ came to similar conclusions regarding the comparative advantage of the U.S. economy over that of its European competitors. The Timbro analysis, conducted in 2004, found that "per capita GDP is lower in most of the countries of Europe than in most of the states of the USA." Italy, France, and Germany had lower per capita GDP than "all but five states of the USA." Sweden, often held up in Europe as an example of economic prosperity combined with social liberalism, "would rank as one of the very poorest states in the Union."

According to Timbro, the gap in GDP between the United States and the average EU country is an astonishing 39 percent. The per capita GDP gap between the U.S. and Europe's richest country stands at 17 percent. Many U.S. states have GDP levels that greatly outperform those of Europe's biggest economies. The state of Connecticut, for example, has "almost twice the material prosperity of old European great powers like France and the U.K." The Timbro report concludes that "the USA has greatly overtaken Europe to become the unrivalled leader of the world's economy. Most Americans have a standard of living which the majority of Europeans will never come anywhere near."

There is growing frustration across Europe with socialist policies that inhibit economic creativity. In September 2006, Swedish voters unceremoniously dumped their Social Democrat government in a massive rejection of the much touted "Swedish model." As author Daniel Mitchell points out, "Sweden has the biggest burden of government in the

1. For background, see "Euro Blues," *The Economist*, April 29, 2006, at www.economist.com/people/displaystory.cfm?story_id=E1_GRVDNSR (February 14, 2007).
2. Eurochambres, "U.S. Economy Ahead of EU By at Least 20 Years," March 11, 2005, at www.economist.com/people/displaystory.cfm?story_id=E1_GRVDNSR (February 14, 2007).
3. Frederik Bergstrom and Robert Gidehag, "EU Versus USA," Timbro, June 2004, at www.timbro.com/euvsusa/pdf/EU_vs_USA_English.pdf (February 14, 2007).

developed world,” with government spending at 54 percent of GDP, and taxes consuming 55 percent of GDP—the highest among industrialized nations. Although Sweden boasts an official unemployment rate of just 6 percent, the real figure is between 15–20 percent.⁴

Europe also remains wedded to protectionist policies that raise food prices, harm producers in developing countries, and weaken European competitiveness in global markets. The EU’s Common Agricultural Policy (CAP) remains the greatest barrier to free trade in the world. The CAP is a vast system of farm subsidies that benefits many of Europe’s richest farmers at the expense of producers in the Third World. It has been described by the British Ambassador to Poland as “the most stupid, immoral state-subsidized policy in human history, give or take communism.”⁵ The CAP accounts for a staggering 40 percent of the EU’s 100 billion euro budget, and European taxpayers are forced to pay over 80 billion euros in subsidies and higher food costs.⁶ The biggest beneficiary has been France, whose farmers receive up to one-quarter of EU agricultural subsidies, amounting to over 150 billion euros between 1994 and 2003.⁷

A recently released Organisation for Economic Co-operation and Development (OECD) report stated that a 50 percent cut in global trade tariffs and subsidies would add \$44 billion to the world economy.⁸ The World Bank has estimated that a successful conclusion to the Doha talks (where the CAP is

the main obstacle) could give a \$300 billion boost to the world economy over the next ten years.⁹

Italy: The Sick Man of Europe. Italy’s economy in many ways encapsulates the broader long-term economic problems facing the European Union. The Economist Intelligence Unit’s (EIU’s) latest report on Italy’s economic growth performance describes it as “the worst among the EU member states in the last 10–15 years. After expanding by just 0.1 percent in 2003 and by 0.9 percent in 2004, GDP rose by a mere 0.1 percent in 2005.”¹⁰ The EIU forecasts that Italy’s gross domestic product will grow at most by just 1.5 percent in 2006–2007. Italy’s budget deficit is expected to rise to 4 to 4.5 percent of GDP in 2006–2007, significantly above the 3 percent ceiling set by the EU Stability and Growth Pact.¹¹ To compound matters further, Rome’s public debt stands at 106 percent of annual GDP, forcing the Italian government to spend 4.6 percent of GDP (\$79 billion) per year just to service it. In the face of mounting competition from Asia, Italy’s share of world trade has fallen from 4.6 percent in 1995 to just 2.7 percent in 2005.¹²

The long-term prognosis for Italy is exceedingly gloomy, with poor demographics adding to problems of heavy debt and weak competitiveness in global markets. Italy’s population is among the oldest in Europe, with a birthrate of just 1.3 children per woman.¹³ Italy has the lowest employment rate among its working-age population in the entire European Union, at just 58 percent. Since the intro-

4. Daniel J. Mitchell, “Hoping to Restore Growth, Voters Rebel Against Sweden’s High Tax Welfare State,” Heritage Foundation *WebMemo* No. 1219, September 21, 2006, at www.heritage.org/Research/Taxes/upload/wm_1219.pdf.
5. Quoted by Ferdinand Mount, “Blair Should Keep Our Rebate and Give Cash to the EU Needy,” *The Daily Telegraph* (London), December 16, 2005.
6. Charles Bremner and Anthony Browne, “French Farmers, the British Rebate and a European Moment of Truth,” *The Times* (London), June 14, 2005, p. 8.
7. *Ibid.*
8. “OECD Says Tariff Cuts Worth \$44 Billion,” BBC News Online, June 9, 2006, at <http://news.bbc.co.uk/2/hi/business/5064364.stm> (February 14, 2007).
9. See Dominic Rushe, “Bush Goes on Trade Rescue Mission,” Times Online, June 18, 2006; and Damien McElroy, “Trade Deal Promises Billions for World Economy,” *Sunday Telegraph* (London), August 1, 2004.
10. Economist Intelligence Unit, *Italy: Country Forecast, 2006-07*, *The Economist*, at www.eiu.com (February 15, 2007).
11. *Ibid.*
12. Tony Barber, “Roman Evasion: How a Diminished Europe is Enduring an Electoral Dialogue of the Deaf,” *Financial Times*, April 4, 2006, p. 15.

duction of the euro in 1999, unit labor costs have climbed by 10 percent.¹⁴

It is doubtful that the new Italian government, headed by socialist Romano Prodi—held political hostage by the Communists and powerful trade union interests—will have the political will, vision, or ability to implement the market reforms necessary to reverse Italy's long-term economic decline. Prodi's pledge to reverse laws introduced by former Prime Minister Silvio Berlusconi's government to increase competitiveness in the labor market will only further weaken the Italian economy, and send completely the wrong signal.

The defeat of the enigmatic Berlusconi, Italy's longest-serving Prime Minister since Mussolini, brings to an end a five-year period of relative political stability marred by economic decline in a country that has suffered through nearly 60 governments since the Second World War. His successor, once described by the somber *Frankfurter Allgemeine Zeitung* as "the chief bore" at EU summits,¹⁵ and who has been appropriately described by cynics as a glorified "undertaker," is now tasked with bringing to life an Italian economy that is clearly on its deathbed. Like the hapless Sisyphus pushing a boulder up a hill, Prodi's multi-colored and possibly short-lived coalition will almost certainly find it an impossible challenge. What Italy needs is an economic revolution with true liberal market reform, rather than more empty rhetoric and state intervention. Unfortunately a Prodi administration is likely to veer heavily toward the latter.

How Britain Prospers Outside the Eurozone. Italy is a prime example of a eurozone member whose economy has declined since the introduction of the euro. Great Britain is a perfect example of a nation that has thrived and prospered without the European single currency, despite the gloomy predictions of Brussels bureaucrats who had warned of British isolation and decline. According to the OECD, the U.K. is the world's top destination for foreign direct investment (FDI), overtaking the United States in 2006. FDI flows into Britain rose from \$56.3 billion in 2004 to \$164.5 billion in 2006.¹⁶ Investment is pouring into the U.K. from the Far East: London alone has attracted 15 percent of all Chinese investment into Europe since 2002.¹⁷

As Europe's biggest financial center, the City of London has boomed since the introduction of the euro, despite Britain's refusal to give up the pound. London accounts for half of European investment banking activity, 20 percent of global cross-border bank-lending, and 31 percent of global foreign exchange turnover. Nearly 50 percent of Europe's private equity assets are managed from London, as well as over 75 percent of Europe's hedge fund assets.¹⁸ Many of the world's largest international non-U.K. banking operations are now run primarily from London, including German flagship Deutsche Bank and French giant BNP Paribas. Since March 2005, 152 international companies have joined the London Stock Exchange (LSE) compared to 54 that have joined the New York Stock Exchange and NASDAQ combined.¹⁹ The LSE now accounts for 70 percent of all European IPOs (initial public offerings).²⁰

13. Bronwen Maddox, "Rome Fiddles as the Economy Burns," *The Times* (London), April 5, 2006, at www.timesonline.co.uk/tol/news/world/europe/article702061.ece (February 14, 2007).

14. "A Sad Italian Story – Italy's Election," *The Economist*, April 8, 2006, at www.economist.com/world/displaystory.cfm?story_id=E1_GSGRPRV (February 14, 2007).

15. Quoted by David Haworth in Toby Helm and Bruce Johnston, "Prodi Goes on the Offensive Over 'Stupid Press Lies,'" *The Daily Telegraph* (London), November 1, 2001, at www.telegraph.co.uk/news/main.jhtml?xml=/news/2001/11/01/wprod01.xml (February 15, 2007).

16. Gary Duncan, "U.K. Becomes Top Choice for Foreign Direct Investment," *The Times*, June 29, 2006, at <http://business.timesonline.co.uk/tol/business/economics/article1095140.ece> (February 14, 2007).

17. Scheherazade Daneshkhu, "London is Leading Location for Chinese Investment in Europe," *Financial Times*, September 15, 2005, p. 3.

18. Martin Dickson, "Capital Gain: How London is Thriving as it Takes on the Global Competition," *Financial Times*, March 27, 2006, p. 11.

19. Clare Furse, "Sox is Not to Blame – London is Just Better as a Market," *Financial Times*, September 18, 2006, p. 19.

Economic growth in Britain has consistently outpaced that of the eurozone countries for the past ten years. Her economy has grown by 28 percent since 1997 (a compound rate of 2.8 percent).²¹ The U.K. is now ranked as the freest large-size economy in the world by the Heritage Foundation's *Index of Economic Freedom*, ahead of the United States.²² According to OECD figures, Britain has achieved a higher GDP per capita than Germany, France, or Italy (it was 46 percent lower than West Germany's and 41 percent lower than France's in 1977). Oxford Economic Forecasting predicts that by the year 2030, Britain will overtake Germany as Europe's largest economy.²³ Within the G-8, Britain is now second only to the United States in terms of national income per capita.²⁴ Employment in the U.K. has risen by 15 percent (3.5 million people) since 1993, and unemployment has fallen from 10.5 percent to 5 percent in the same period.²⁵ Britain's working population expanded by 450,000 (1.6 percent) between 2005 and 2006.²⁶

There are, however, storm clouds gathering on the horizon for the British economy, largely due to an increase in government regulation, spending, stealth taxation, and general red tape. While Chancellor of the Exchequer Gordon Brown has been careful not to undo the major reforms of the Thatcher Revolution of the 1980s, and largely built upon them, he has been steadily increasing the level of government intervention in the economy, which will have dam-

aging long-term implications for the U.K. and which may well come to haunt him if he becomes Prime Minister. British government spending as a proportion of GDP has risen by 8 points since 2000, a jump from 37.5 percent to 45.6 percent, just below that of Germany's 46.1 percent, and the eurozone's average of 47.3 percent.²⁷ In addition, Britain continues to suffer from poor productivity levels. Output per hour is 15 percent higher in the United States, and 19 percent higher in France.²⁸

Political Trends in the European Union

Long-term economic trends in the European Union do not bode well for the United States. Sluggish growth and increasing protectionism pose long-term threats to U.S. interaction with the global economy. Europe remains America's most important trading partner with U.S.–EU trade worth almost \$1 trillion per year,²⁹ and the U.S. has a huge stake in the economic performance of the EU.

If the economic prognosis for Europe looks gloomy, the political outlook for Europe is even darker. There are many concerns from the perspective of Washington. The top three threats to U.S. interests are the increasing centralization of political power in Europe and its implications for U.S.–European relations; the stunning rise of anti-Americanism across Europe, even in America's closest allies, such as Great Britain; and the growing threat to U.S. and international security from Islamic extremism in European countries.

20. Stephen Fidler, "How the Square Mile Defeated the Prophets of Doom," *Financial Times*, December 10, 2005, p. 11.

21. Martin Wolf, "The Stable Isle: How Labour Has Steered an Economy Going Global," *Financial Times*, September 18, 2006, p. 17.

22. Marc A. Miles, Kim R. Holmes, and Mary Anastasia O'Grady, 2006 *Index of Economic Freedom* (Washington, D.C.: Heritage Foundation and Dow Jones & Co., Inc.), p. 13.

23. "Make My Day," *The Economist*, May 2004, at www.economist.com/world/europe/displaystory.cfm?story_id=E1_NGQSPPR (February 14, 2007).

24. Martin Wolf, "The Stable Isle."

25. "Lustre Lost," *The Economist*, May 23, 2006, at www.economist.com/research/backgrounders/displaystory.cfm?story_id=5669877 (February 14, 2007).

26. Christopher Smallwood, "Reserve Army Can Defuse Demographic Timebomb," *Sunday Times* (London), August 27, 2006, Business Section, p. 4.

27. Martin Wolf, "The Stable Isle."

28. "Why British Productivity Still Lags," *The Economist*, January 21, 2006, at www.economist.com/research/backgrounders/displaystory.cfm?story_id=5421856 (February 14, 2007).

29. William H. Cooper, "EU–U.S. Economic Ties: Framework, Scope, and Magnitude," Congressional Research Service, January 17, 2006, at <http://fpc.state.gov/documents/organization/62662.pdf> (February 14, 2007).

The fundamental dynamics of the transatlantic relationship have been transformed in the post-9/11 era, and will require a shift in U.S. strategic thinking. The United States should reassess its traditional support for ever-closer integration in Europe, and adopt a more “Eurosceptic” approach. Washington must also recognize the huge long-term threat to U.S.-led alliances posed by the exponential growth of anti-Americanism, particularly among younger Europeans who do not share the older generation’s memories of America’s defense of Europe in the Cold War and World War II. If the growth in opposition to U.S. foreign policy continues in Europe, America may be left with no significant transatlantic allies two to three decades from now.

The explosion of Islamic militancy in Europe must also be addressed as a top priority for the U.S. It is no coincidence that the 9/11 attacks, as well as the foiled plot to blow up U.S. airliners over the Atlantic Ocean in August 2006, were meticulously planned on European soil. In the case of the attempted airline attacks, as well as the July 2005 London bombings, the suicide bombers were British citizens, many of whom were born in the U.K.

Britain, for years a safe haven for Islamic militants across the world, has become a hornet’s nest of Islamic terrorists. The United States must apply concerted pressure on the U.K. and other major European countries with large Muslim populations to crack down on Islamic extremists, who through the visa waiver program have easy access to the United States. It will take extensive U.S.–European cooperation to ultimately defeat the scourge of terrorism in an increasingly globalized world.

The Rise of a Federal Europe. The rejection of the European Constitution by voters in France and Holland in 2005 was the best news Europe has had in years. The French and Dutch referenda derailed a stampeding juggernaut, steered by bureaucrats in Brussels, heading toward the destination of “ever closer union.” The Constitution, a blueprint for the creation of a federal Europe, posed the greatest

threat to national sovereignty in Europe since World War II. Its defeat was a momentous event—a popular rejection of the imposition of power from above without a democratic mandate.

That is the good news. The bad news is that the Brussels establishment, as well as many of Europe’s national leaders, wish to resurrect the Constitution, and seek to push many of its goals through the back door. Despite huge divisions within the EU25, the European Union Common Foreign and Security Policy continues to gain strength, as does the creation of a European Union standing army.

German Chancellor Angela Merkel has called for the resurrection of the Constitution. No less than 15 countries have ratified the Constitution, thirteen of them without a referendum.³⁰ Belgian Prime Minister Guy Verhofstadt has just published a book entitled “The United States of Europe.” A pro-federalist axis has been formed between Paris, Berlin, Madrid, and Rome, all led by strong supporters of further political integration in Europe.

Defending a Europe of Nation-States. The U.S.–EU divide over the war on terrorism, sharply illustrated by divisions over rendition and the detention facility at Guantanamo Bay, is likely to grow wider in the months and years to come. There exist irreconcilable differences between Washington and Brussels both with regard to how to confront the threat of global terrorism and with regard to the nature of the conflict the West is engaged in. Many leading EU bureaucrats simply do not grasp the magnitude of the al-Qaeda threat. As a senior European Union official recently remarked, “[W]e do not have a war on terror,”³¹ an extraordinary statement considering the fact there have been three major terrorist attacks on European soil in the past three years, in London, Madrid, and Istanbul.

However, tensions between the United States and the European Union and Council of Europe should not weaken the ability of Washington to cooperate effectively with individual European nation-states, many of which have strongly supported U.S. efforts

30. The exceptions are Luxembourg and Spain, whose populations have both voted on the Constitution.

31. Quoted in Daniel Dombey, Hugh Williamson, and Jimmy Burns, “International Security,” *Financial Times*, December 14, 2005, p. 17. The official is not named in the article.

in the war on terrorism. Rendition has proved a highly effective tool in the war against al-Qaeda and has pulled hundreds of extremely dangerous terrorist suspects off the streets. In all probability, many lives, both American and European, have been saved by this practice.

The United States must continue to pursue aggressively those who threaten the security of the free world and should continue to work closely with allies in the fight against Islamic terrorist groups. Most importantly, the U.S. must resist the temptation to blunt its most effective weapons in the face of criticism from the EU, the U.N., and other supra-national institutions.

The increasing political centralization of Europe poses a fundamental threat to U.S. interests. Washington must back the principle of national sovereignty in Europe, and President Bush should welcome last year's defeat of the European Constitution in key EU member states such as France and Holland as an important democratic rejection by European voters of the further centralization of power on that continent.

The United States works most effectively when it cooperates directly with national governments, employing a "coalition of the willing" strategy. Europe is not, and never has been, a united political entity, and U.S. policy must support a Europe of nation-states. Washington's political capital in Europe must be spent not in Brussels or Strasbourg, but in the national capitals, where America's strongest allies are to be found.

The Growth of Anti-Americanism: A Threat to the Special Relationship. The Anglo-American special relationship today faces one of its greatest challenges since World War II—rising public opposition in the U.K. to Britain's close ties to the United States. The recent YouGov/*Spectator* poll of British attitudes toward U.S.–U.K. leadership of the war on terrorism should be major cause for concern for policymakers in both Washington and London.³²

While just 12 percent of respondents believed that Britain should soften its foreign policy in response to the terrorist threat (a specific demand made by British Muslim leaders), 79 percent disagreed with the view that Britain and America were "winning the war against terror[ism]." Only 14 percent of those surveyed supported the view that Britain should "pursue a foreign policy agenda closer to that of the United States"; and 45 percent believed that "Britain should position her foreign policy closer to that of the European Union."

The poll represents a sea change in attitudes among a British public that is traditionally pro-Atlanticist and skeptical of European integration. In part, the survey is a reaction against an unpopular Prime Minister, Tony Blair, who is closely aligned with Washington and whose standing internationally greatly eclipses his domestic image. Blair's approval rating remains at less than 30 percent. It is also, however, representative of a broader rejection of U.S. leadership on the world stage, and a rising anti-Americanism on both the left and right of the political spectrum.

Several other recent polls conducted in the U.K. have produced negative findings in relation to British perceptions of U.S. foreign policy, and Downing Street's support for it. A July ICM poll for *The Guardian* found that 63 percent of Britons thought the U.K. was "too close to the USA."³³ In a June YouGov/*Daily Telegraph* poll, 77 percent of those polled disagreed with the view that the United States was "a beacon of hope for the world," and 58 percent supported the description of America as "an imperial power."³⁴ Sixty-seven percent expressed "little or very little confidence" in "the ability of the United States to deal wisely with present world problems." Sixty-five percent of respondents supported the view that U.S. policies made the world "a somewhat or much worse place to live in."

Worryingly, anti-American views are now as widespread or even more prevalent in the U.K. than they are in some continental European countries

32. YouGov/*Spectator* Survey, August 14–15, 2006.

33. ICM/*Guardian* Poll, July 21–23, 2006.

34. YouGov/*Daily Telegraph* Survey, June 26–28, 2006; Anthony King, "Britain Falls Out of Love with America," *The Daily Telegraph*, July 3, 2006, at www.telegraph.co.uk/news/main.jhtml?xml=/news/2006/07/03/nyank103.xml (February 14, 2007).

with a far deeper tradition of public skepticism toward the U.S. In the latest *Financial Times*/Harris poll of opinion in five of the EU's largest member states, a staggering 36 percent of Britons surveyed described the United States as "the greatest threat to global security." (Just 19 percent of British respondents cited Iran as the world's greatest threat). In contrast, 28 percent of Frenchmen, 21 percent of Italians, and 24 percent of Germans shared this view. Only in Spain was the negative perception of U.S. foreign policy greater than in Britain.³⁵

If this trend continues, with the British public moving further away from the United States and sliding closer to the European Union on major international issues, the long-term future of the special relationship will be placed in jeopardy. In many ways, Britain is at a turning point in its history, faced with a choice between further political, legal, military, and economic integration with the EU, or a deepening of its alliance with the United States and other English-speaking allies such as Australia. As Tony Blair discovered with the Iraq war, the two competing visions are largely incompatible.

From the U.S. point of view, it would be a geostrategic disaster if Britain leaned toward Brussels rather than Washington. The most prominent casualty of a fully developed EU Common Foreign and Security Policy would be the Anglo-U.S. special relationship, forcibly consigned to the scrap heap of history. America's closest ally would be unable to operate an independent foreign policy and stand alongside the United States where and when it chose to do so. The consequences for America would be hugely damaging.

For Britain, there is much to lose from a weakening of the Anglo-American alliance—the further loss of national sovereignty, the diminishment of British global power and influence, the loosening of defense and

intelligence ties, and a weakening of the close-knit financial, trade, and investment relationship.

For both U.S. and U.K. policymakers and politicians, the defense of the Anglo-American special relationship should be a top priority. On the U.S. side, public diplomacy in the U.K. should be greatly stepped up by the Bush Administration. Little has been done so far to effectively project and communicate America's foreign policy message to British and European audiences. In London, the Blair government must do more to explain how the alliance with America enhances Britain's national security rather than undermines it, and why the special relationship is a two-way street that brings Britain huge benefits. At the same time the British government should not seek to undermine the alliance with America by supporting further political or defense integration in Europe.

Britain and the Rise of Islamic Extremism. The 2005 London bombings and the thwarted 2006 airline attacks prompted growing awareness within Europe regarding the threat posed by homegrown Islamic militants working in conjunction with foreign al-Qaeda terrorists. The British intelligence service MI6 believes that there are 400 to 600 al-Qaeda terrorist suspects in the U.K., some of whom have been trained in camps in Afghanistan and Pakistan.³⁶ Although the London bombings were carried out by British-born terrorists, the bombers were almost certainly part of a larger international network. The latest evidence suggests the attacks were probably a sophisticated al-Qaeda operation, masterminded by experienced international operatives with local extremists acting as foot soldiers.

The scale and complexity of the problem involving young Islamic extremists in Britain was highlighted in a major British Foreign Office/Home Office study, "Young Muslims and Extremism."³⁷

35. John Thornhill, Daniel Dombey, Edward Alden, "Harris Poll of Adults in Five European Countries," *Financial Times*, August 21, 2006, at www.ft.com/cms/s/9590f894-ff2f-11da-84f3-0000779e2340.html (February 15, 2007).

36. David Leppard, "At Least 400 Al-Qaeda Terrorist Suspects Are at Large in Britain," *Sunday Times* (London), April 9, 2006, p. 1, at <http://business.timesonline.co.uk/tol/business/law/public/article703516.ece> (February 15, 2007).

37. British Foreign Office and Home Office, "Young Muslims and Extremism," May 2004, at www.globalsecurity.org/security/library/report/2004/muslimext-uk.htm (February 14, 2007). See also Robert Winnett and David Leppard, "Leaked No.10 Dossier Reveals al-Qaeda's British Recruits," *The Sunday Times*, July 10, 2005, at www.timesonline.co.uk/tol/news/uk/article542474.ece (February 14, 2007).

Terrorist organizations such as al-Qaeda have found a fertile hunting ground in the U.K., where half of Muslims are under the age of 25, and where there is widespread opposition to the U.S.-British-led war on terrorism.

The report revealed that extremist groups are secretly recruiting well-educated, affluent Muslims from British universities, in addition to impoverished, underachieving Muslims through mosques and prisons. The British government study concludes that “intelligence indicates that the number of British Muslims actively engaged in terrorist activity, whether at home or abroad, or supporting such activity is extremely small and estimated at less than 1%.” This translates, however, into potentially 16,000 British Muslims out of a total population of 1.6 million. An estimated 10,000 U.K. Muslims attended an extremist conference in 2003.

The study cites a series of polls of British Muslim opinion on foreign policy issues, which raise considerable cause for concern regarding the loyalties of some U.K. Muslims in the global war on terrorism. While the vast majority of British Muslims condemned the 9/11 attacks, 15 percent supported them in a November 2001 BBC poll. In the same poll, 80 percent believed that military action against Afghanistan was unjustified, and 24 percent approved of “British Muslims going to fight America and its allies in Afghanistan.”³⁸

Another BBC poll, in December 2002, showed that 44 percent of British Muslims thought that further attacks by al-Qaeda were “justified on grounds that Muslims are being killed by America and its allies using American weapons.” Fifty-six percent of respondents stated that the USA and its allies were unjustified in blaming Osama bin Laden’s al-Qaeda group for the attacks in America on September 11. Seventy percent of respondents disagreed with the view that “the war on terror is not a war against Islam,” and 26 percent of those polled did not “feel very or fairly loyal/patriotic towards Britain.”³⁹

The poll figures make disturbing reading. While waging war against al-Qaeda internationally, the United Kingdom must at the same time redouble its efforts to defeat Islamic extremism on home soil. The U.K. has for far too long provided a safe haven for Islamic militants from across the Middle East and North Africa. Tougher anti-terrorist legislation and stronger immigration and asylum laws are required to help prevent further terrorist attacks on British cities.

The London bombers were driven above all by an evil doctrine of hatred and loathing, based on an extreme misinterpretation of Islam, which has as its ultimate goal the destruction of liberal democracy across the world, whether it be in the West or the Middle East, and the establishment of a Muslim caliphate.⁴⁰ It is an ideology that cannot be appeased or negotiated with, but which must be defeated. The terrorist bombings in London, and the attacks of 9/11 in Washington and New York, were not the consequences of U.S. or British foreign policy, but part of an epic confrontation between the forces of barbarism and the forces of civilization.

The British government must pursue a policy of zero tolerance toward Islamic extremism, which is a deadly threat to the fabric of British society. Foreign Islamic clerics who preach violence and hatred should be deported from Britain, and terrorist suspects must be extradited to friendly countries that request it, especially the United States.

Britain also clearly needs a new generation of Muslim leaders, untainted by association with or sympathy for Islamic extremism, and who are proud of their British identity. They must be willing to condemn terrorism unequivocally in all its forms, and help root out extremists from Muslim communities. Their role in helping defeat Islamic terrorism will be invaluable.

Economic and Political Trends in Russia

Fifteen years since the inglorious fall of the Soviet Empire, Russia remains a huge foreign policy chal-

38. BBC Radio 4/ICM Poll, November 2001, at www.icmresearch.co.uk/reviews/2001/today-muslims-poll-nov-2001.htm (February 15, 2007).

39. BBC Radio 4/ICM Poll, December 2002, at www.icmresearch.co.uk/reviews/2002/bbc-today-muslims-dec-02.htm (February 15, 2007).

40. This is a point made powerfully by the British Prime Minister in a July 16, 2005 speech.

lenge for the United States. President Vladimir Putin, hugely popular with the Russian people, has successfully restored both economic and political stability to a country that had been on its knees at the end of the last millennium. As a mark of its growing confidence following soaring oil prices, the Russian government repaid \$22.5 billion to the Paris Club of creditor nations in August 2006, 14 years ahead of schedule, eliminating one-third of its total \$70 billion foreign debt.⁴¹ A resurgent and newly confident Russia hosted the G-8 summit in St. Petersburg in July 2006.

With 27 percent of the world's gas reserves, and 6 percent of global oil reserves, Russia is now the world's second-largest oil exporter, and state-owned Gazprom is the world's second-biggest energy firm by market value.⁴² Russia supplies one-third of Europe's gas needs, and has accumulated foreign currency reserves of \$277 billion (the third largest in the world). Russia currently has a balance of payments surplus of \$100 billion, or 12 percent of GDP.⁴³ Russia's Stabilization Fund, established as a safeguard against a financial meltdown, is now worth nearly \$80 billion.⁴⁴ Foreign investment is pouring into the country, attracted by a well-educated, skilled, and relatively cheap workforce, helping fuel an annual growth rate of over 6 percent. FDI in the first half of 2006 amounted to \$14 billion, nearly equal to the total for the whole of 2005.⁴⁵

Russia's revival, however, disguises some major long-term economic problems. The economy is heavily dependent upon oil and natural gas revenues, and will be hit hard by any significant drop in oil prices. Demographic trends also militate against an optimistic long-term economic prognosis for the Russian economy. Russia's population has fallen by six million since the collapse of the Soviet Union and now stands at 143 million. With its population dropping by 700,000 a year, *The Economist* predicts there will be fewer than 100 million Russians by the middle of the 21st century.⁴⁶

Leading demographics scholar Nicholas Eberstadt has observed that "Russia's current depopulation bears all the trappings of a "demographic shock," reflecting abrupt and violent changes in the nation's vital rates in the immediate wake of a momentous, system-shattering, historic event. This shock is probably not just a temporary disturbance: There are good reasons to believe that Russia's population trend defines a new norm for the country."⁴⁷ Eberstadt notes that Russia has a staggeringly high death rate of 170 deaths for every live 100 births, in contrast to the European average of 103 deaths for every 100 births.⁴⁸ Russia's male life expectancy has fallen by five years since the 1960s, and now stands at just 59, comparable to that of many Third World countries.⁴⁹ According to the World Health Organization, Russia ranks 127th in the world in terms of global health care standards.⁵⁰

41. Gabriel Rozenberg, "Putin Hails the New Economy as Russia Wipes \$22 Billion Off Its Debts," *The Times*, August 22, 2006, at <http://business.timesonline.co.uk/article/0,,16849-2322844,00.html> (February 14, 2007).

42. Mark Franchetti and Sarah Baxter, "Putin Slaps Down 'Russia is Back' Warning to West," *Sunday Times* (London), July 9, 2006; and "Moscow Rises Again," *The Guardian*, May 13, 2006, at www.timesonline.co.uk/tol/news/world/article685043.ece (February 14, 2007).

43. Roger Bootle, "Be Bullish About Russia's Future," *The Sunday Telegraph* (London), July 9, 2006, City Section, p. 4.

44. Tony Halpin, "Eight Years Ago It Was Meltdown. Now Pride Has Been Restored," *The Times* (London), August 22, 2006, at www.timesonline.co.uk/article/0,,5-2322845,00.html (February 14, 2007); and Adrian Blomfield, "Western Leaders Have a Duty to Challenge Russia at the G-8," *The Daily Telegraph* (London), July 12, 2006, at www.telegraph.co.uk/opinion/main.jhtml?xml=/opinion/2006/07/12/do1204.xml (February 14, 2007).

45. Economist Intelligence Unit, *Russia, Country Forecast*, *The Economist*, July 2006, p. 43.

46. "A Sickness of the Soul: Russian Health and Demography," *The Economist*, September 7, 2006, at www.economist.com/world/europe/displaystory.cfm?story_id=E1_SRJTNVJ (February 14, 2007).

47. Nicholas Eberstadt, "The Emptying of Russia," *The Washington Post*, February 13, 2004, at www.washingtonpost.com/ac2/wp-dyn/A38176-2004Feb12?language=printer (February 14, 2007).

48. *Ibid.*

49. "A Sickness of the Soul," *The Economist*.

Political considerations also weaken Russia's long-term market appeal. Investor confidence will be ultimately harmed by the increasing heavy-handedness of the Kremlin. Russia has not quite returned to the dark days of Soviet-style totalitarianism, but it is increasingly an authoritarian regime that acts ruthlessly to protect its interests—what the *Financial Times* calls “a managed democracy.”⁵¹ Unlike during the Cold War, Russians have freedom to travel abroad and benefit from the fruits of global capitalism. Few Russians are willing, though, to openly confront the iron fist of President Putin's leadership.

Putin has weakened the powers of parliament, stifled the media, neutered the power of regional governments, and reduced the independence of the judiciary. Businessmen who pose a challenge to Russia's political elite have had to face the consequences. Mikhail Khodorkovsky, once the head of Russia's foremost oil company, Yukos, now resides in a Siberian prison camp.⁵² Non-governmental organizations, especially foreign groups, have faced a huge crackdown. Freedom House ranks Russia 168th out of 192 countries in terms of political rights, while Transparency International places Russia 126th out of 159 nations in its ranking. In terms of judicial independence, the World Economic Forum puts Russia in 84th position out of 102 countries, and ranks it 88th out of 108 for property rights.⁵³

As Vice President Dick Cheney noted in his powerful remarks to the 2006 Vilnius Conference:

In Russia today, opponents of reform are seeking to reverse the gains of the last decade. In many areas of civil society—from religion and the news media, to advocacy groups and political parties—the govern-

ment has unfairly and improperly restricted the rights of her people. Other actions by the Russian government have been counterproductive, and could begin to affect relations with other countries. No legitimate interest is served when oil and gas become tools of intimidation or blackmail, either by supply manipulation or attempts to monopolize transportation. And no one can justify actions that undermine the territorial integrity of a neighbor, or interfere with democratic movements. Russia has a choice to make. And there is no question that a return to democratic reform in Russia will generate further success for its people and greater respect among fellow nations.⁵⁴

While flexing muscle at home, Putin is also projecting power abroad. Even with nuclear weapons, Russia's days as a global superpower are long gone. Russia still, however, ranks as one of the four most powerful countries in the world in terms of global power projection after the United States (the others are Britain, France, and China). And she is increasingly aligning herself with America's biggest enemies, including Mahmoud Ahmadinejad of Iran and Venezuela's Hugo Chavez. This is part of a broader strategy to strengthen Russian strategic influence on the world stage. Moscow is helping to build Iran's \$1 billion nuclear reactor at Bushehr, and in December 2005 agreed to a \$1 billion arms sale to Tehran, including \$700 million worth of surface-to-air missiles. Russia sold the Iranian regime \$2.7 billion worth of arms between 1994 and 2004.⁵⁵ Russia recently signed a \$3 billion deal with Venezuela to supply 24 Su-30 advanced fighter jets, as well as 53 helicopters—despite strong objections from Washington.⁵⁶

50. Jonathan Steele, “Russia Deserves More Than Stability From Putin's Last Year,” *The Guardian*, September 14, 2006, at www.guardian.co.uk/comment/story/0,,1871871,00.html (February 14, 2007).

51. “Taking the Measure of Putin's New Russia,” *Financial Times*, July 10, 2006, at www.ft.com/cms/s/829a83c2-0fb0-11db-ad3d-0000779e2340.html (February 14, 2007).

52. “Democracy, Russian Style,” *The Washington Post*, July 18, 2006, at www.washingtonpost.com/wp-dyn/content/article/2006/07/17/AR2006071701297.html (February 14, 2007); and “Richer, Bolder—and Sliding Back,” *The Economist*, July 15, 2006, at www.economist.com/research/articlesBySubject/displayStory.cfm?subjectid=348903&story_id=7161380 (February 14, 2007).

53. Andrei Illarionov, “Why G-8 Could Jeopardize the Fate of Democracy in Russia,” *The Daily Telegraph* (London), May 24, 2006, p. 17.

54. Dick Cheney, “Vice President's Remarks at the 2006 Vilnius Conference,” May 4, 2006, at www.whitehouse.gov/news/releases/2006/05/20060504-1.html (February 15, 2007).

Washington is right to be concerned by developments in Russia. While it is an increasingly important market for Western goods and investment, Russia remains a strategic competitor and is evolving into an energy superpower with pretensions of grandeur on the world stage. Moscow's growing military support for Tehran and Caracas does not bode well for the future. In addition, strongman President Putin's departure in 2008 may give way to an even more authoritarian regime in the Kremlin, further reinforcing the need for the United States and other Western allies to maintain the pressure for reform and human rights in Moscow.

Conclusion

Europe is a continent in great transition, uncertain of the course it must take in the 21st century. There is a battle taking place for the heart and soul of the future of the European Union. Europe can move in one of two directions—toward the creation of an artificial superstate, a political rival to the United States, or it may return to a Europe of nation-states, where national governments retain control of foreign and domestic policy. At the moment, Europe is somewhere in between.

Unfortunately, despite the rejection of the Constitution, the pendulum is swinging toward closer integration. Increasingly, the EU is acting as a common entity on the international stage, whether it be at the United Nations, in negotiations with Iran, or in intervention in the Israeli-Hezbollah conflict. This does not mean that Europe is united—far from it—but there is undoubtedly a growing willingness to develop consensus positions on big international issues.

Nothing is ever certain in history. The drive toward ever-closer union can still be halted. A great deal will depend upon how Britain moves with regard to Europe if the largely Eurosceptic Conservative Party takes the reins of power in 2009 or 2010, the year of the next British election. Britain, Poland, the Baltic states, and the Scandinavian

countries may form a counter-weight of power within the EU to the dominance of Germany and France. Possible Turkish entry to the EU a decade from now would fundamentally alter the nature of the organization, and would greatly complicate the creation of a united political entity in Europe. Further, economic problems in the eurozone could prompt defections from the single currency. Italy would undoubtedly be the first to jump ship if the euro hit an iceberg.

Economic integration is essentially a politically driven project, and any crack in the edifice of the single currency would have huge implications for political integration. It is no coincidence that the most successful economies in Europe today—Britain, Switzerland, Norway for example—remain outside the eurozone.

In other words, there is still all to play for in Europe. The continent faces a stark choice between a Europe based around the principles of free markets, free trade, limited government, national sovereignty, and decentralized power, and a federal Europe that worships at the trough of socialism and supra-nationalism. It is to be hoped that Europe will choose the former, a formula that worked for centuries as a recipe for success for Europe's great powers.

It is not only the future of Europe that is at risk, but also the future of the Anglo-American special relationship, NATO, and the broader transatlantic alliance. The United States has a stake in the future direction of Europe and must develop a coherent strategy toward Europe that reflects fundamental U.S. interests.

—Nile Gardiner is Director of the Margaret Thatcher Center for Freedom at The Heritage Foundation. This lecture was delivered at the Durell Colloquium on "The Role of Markets and Governments in Pursuing the Common Good" at Hillsdale College's Center for the Study of Monetary Systems and Free Enterprise, in Hillsdale, Michigan, on October 28, 2006.

55. James Phillips and Peter Brookes, "Iran's Friends Fend Off Action at the U.N. Security Council: Here's Why," Heritage Foundation *WebMemo* No. 1071, May 11, 2006, at www.heritage.org/Research/MiddleEast/wm1071.cfm.

56. "Deal Approved to Send Russian Jets and Helicopters to Venezuela," *The New York Times*, July 28, 2006, at <http://travel2.nytimes.com/2006/07/28/world/americas/28Venezuela.html?fta=y> (February 14, 2007).