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Orig. I

EUROPE AND THE OTHERS: ECONOMIC PROBLEMS

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and non-member countries"

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1. This is a very wide subject, comprising so many matters of such varied nature that the short duration of this meeting and the limited space of an introductory report would be hardly sufficient even to list them. I propose therefore, if you will allow me, to examine only one problem - one which seems to me to be of particular interest today after six years of the Common Market and in view of discussions which are being held everywhere both in the Community and outside on the subject of "the EEC's international relations". It is the fundamental question: what have been the effects on the world economy of the creation and activity of the Community?

I shall not attempt to go into such an important question in all its aspects and implications, but shall confine myself to some of the salient points.

2. The policy which individual states have traditionally tried to follow in their international economic relations is the outcome of two attitudes which on occasion come into conflict. The first tends to give priority, in the choice of economic policy, to the satisfaction of the direct and immediate interests of economic operators, groups and sectors in the nation. The other is derived from concepts according to which decisions on national economic policy tend to be governed by criteria that take into account not only the particular and immediate interests of individuals and groups at national level, but also of the general welfare considered from a broader angle. It would not be going too far to define the latter attitude as taking its inspiration from the obligations of the "international moral code".

The theory of the international division of labour tells us that, in the long run, total freedom of movement of goods, services, capital and persons is the only means of satisfying both national and international interests.

In the short run and on the practical plane, of course, things are much more complicated.

An attitude which conforms strictly to the principle of freedom of trade and, consequently, of improved long-term economic benefits, often involves decisions which at first sight are not in harmony with the needs of national policy.

Moreover, the calculation of the net effects of an economic policy decision which creates or abolishes, increases or diminishes, some activity or other, is so complex that it is often difficult, and sometimes impossible, to make a forecast which is at all objective.

In practice the importance attached to these two spheres of interest varies according to time and from one country to another.

The years between the two World Wars saw an almost general predominance of the first of the two attitudes, while during the second post-war period considerable progress has been made in understanding the interdependence between what is national and what is international.

The result is that the major principles of the "international moral code" in the economic sphere (freedom of trade, non-discrimination, full employment, balanced expansion of the industrialized countries, and respect of the rules of trade and of the code of behaviour between debtor and creditor countries) have been embodied in a number of important international agreements over the last twenty years. Though it may be exaggerated to claim that the present-day world possesses, in the sphere of international relations, a body of laws which are consistently precise and effective, nevertheless these basic principles and the rules derived from them constitute points of reference, to which all states in general, and the industrial countries in particular, are obliged to turn more and more often to judge their own actions.

Individual countries, however, continue to be influenced by their origins or by their economic history. One large industrial country, the home of free trade, has maintained, since the economic troubles of the thirties, the most protective of customs tariffs in respect of manufactures; while another country, the biggest

of them all, has preserved in its system of protection the characteristics of a developing country anxious to press forward its own industrialization.

In almost all industrialized countries, policies on immigration and movement of labour continue to be influenced by a great fear of underemployment - by what has been called "nationalized socialism".

Countless other examples could be quoted: economically misguided agricultural policies, exports of capital tied to exports of national goods, extremely restrictive attitudes towards low-cost countries, which are almost always developing countries, exemptions, sometimes extensive, from GATT rules, obtained by some country or another merely for political reasons.

3. The formation of the European Economic Community naturally gave food for thought to those who are concerned with the fundamental aspects of international economic relations and keep a careful watch on the swings of the world economic pendulum between the two attitudes already referred to.

The undertaking contained in the Treaty of Rome to transform six separate markets into one single market, was an event of major importance on the international stage. The intervening six years have shown, even to the many who had been ignorant of the Treaties of Rome or had greeted their signing with scepticism, how important this event was for international economic relations.

On the quantitative plane everyone now admits that the Common Market is becoming a unified economic area of the first importance in international relations. Its significance can be measured today by the following figures: about 175 million inhabitants with a gross product amounting to some \$220 000 million and rapidly expanding. The size of this market, of course, is still well below that of the United States (189 million inhabitants, \$550 000 million). In terms of international trade, however, the six countries have already reached a turnover which is appreciably

the international weal in the wide sense. It would be more correct, in my opinion, to judge the matter in realistic terms: the advance towards economic integration of the member countries of the Community, according to the letter and the spirit of the Treaty of Rome, will on balance have more favourable consequences for non-member countries than would its non-existence.

5. By definition the EEC is "preferential" in nature and thus will inevitably tend to "distort" traditional trade flows. The extent of such effects will depend, in the long run, mainly on the effective degree of protection granted to producers inside the area against those outside it.

But these "distorting" effects will be offset by "compensatory" effects; the form they take will depend on the impact of integration movements on the rate of overall economic development. Such "compensatory" effects will have varying origins and will be manifest in different ways, such as an increase in the volume of imports, absolutely, or in relation to the gross national product.

Our methods of economic calculation do not make it possible to measure the relative extent of these two kinds of effect and certainly not to make forecasts about them. But on examining in the light of developments since 1958 and of changes since the appearance of the Common Market, the factors determining the relation between the direct and immediate interests of local economic operators; groups and sectors and external interests, we perceive how important such "compensatory" effects are.

6. Some observers have claimed to see, in the faster expansion of trade within the EEC than between the Community and non-member countries, a sign that the "distorting" effects have already stolen ahead of the "compensatory" effects. This conclusion is probably mistaken and is certainly over-hasty.

The tendency to regionalize trade made its appearance before the Common Market and can be observed in other associations of neighbouring countries. The tendency has doubtless gained momentum during the five years in question, but this is largely due

to the establishment of new commercial relations, mainly as a consequence of reciprocal ventures by firms in the Community. Such new relations are to be attributed not so much to tariff discrimination applied during this period as to the prospects, rendered possible by the Treaty of Rome, of lasting liberalization of trade between Member States and to the "anticipation" by firms of special situations which will follow on the entry into force of the Treaty. These relations seem to correspond substantially to the creation of new trade flows as a result of the Common Market rather than to any "distortion" at the expense of imports from non-member countries; this largely explains the disparity between the growth rates of the two import flows.

7. If we consider the EEC from the point of view of external trade, we find that between 1958 and 1962 the ratio between its imports and its gross product has remained stable at about 10%. The gross product of the EEC has expanded more than that of any other economic unit (except Japan): the increase was some 38%⁽¹⁾. In the same period imports from non-member countries also went up by 38%⁽²⁾. Essentially this parallel trend may be taken to mean that owing to the pressure of demand in the Community its demand for imports from non-member countries has been stimulated to a relative degree which has not varied between 1958 and 1962.

As for trade between the EEC and the United States the stimulus has been even stronger, since EEC imports from the United States increased by 46% during the same period.

(8) It is also interesting to note that during the same period in the United States and the United Kingdom the gross national product expanded more (24.8% in the USA and 21.8% in the UK) than imports (21.5% in the USA and 19.8% in the UK).

From the following table it will be seen that, by value and at current prices, EEC imports from non-member countries have increased more sharply between 1958 and 1962 than total imports by the United States and the United Kingdom.

(1) From \$160 400 million in 1958 to \$221 700 million in 1963.

(2) From \$16 100 million to \$22 600 million.

	<u>EEC imports from non-member countries</u>	<u>US imports (from all coun- tries)</u>	<u>UK imports (from all countries)</u>
	\$ '000 million		
1958	16.1	14.6	10.4
1962	<u>22.3</u>	<u>17.8</u>	<u>12.6</u>
Increase:	<u>+ 6.2</u>	<u>+ 3.2</u>	<u>+ 2.2</u>

9. These facts, of course, do nothing more than offer a basis for the supposition that the discriminatory effect of the EEC has been offset by its compensatory effect.

In such an elusive subject, it is practically impossible to furnish mathematically accurate proof that the net specific effect of the Common Market on world trade (i.e. the "compensatory" effects, mainly in the shape of incentives to development, less the effects of "distortion" resulting from discrimination), considered apart from all the other simultaneous influences on trade flows and the Member States' economy, has been beneficial. It would be a question of making a comparison between facts, which can be ascertained from development statistics (described above), and a hypothetical situation (in which the specific "Common Market" element would be excluded).

Now even the boldest economic analysis will not enable us to evaluate precisely what role the formation of the Common Market has played in world economic development. The same may be said of its discriminatory effect on trade.

Two conclusions, however, may be drawn from an analysis of the period 1958 to 1962 - though it must be stressed that any discrimination results not only from effective tariff changes but also from those that are "anticipated":

- (a) While the preferential effect is more considerable (on account of such "anticipation") than would appear from measurable quantitative factors (reduction of obstacles to

Consequently the economic growth of the EEC must inevitably make itself felt in non-member countries which produce raw materials. In this respect there is a fundamental difference between the Common Market and other "common markets" which have been set up in continental-scale economies down the centuries: for example, the United States. During its development that country has given an unimportant - and dwindling - place to international trade in relation to its own gross national product, precisely because the raw materials needed for its growing industries could be found until recently almost entirely or very largely within its own territory.

Europe, on the other hand, is obliged by economic geography constantly to share the fruits of its own expansion with external countries.

12. Although, for the reasons indicated above, a final judgment must be reserved on the impact of a common agricultural policy on the rest of the world, it can already be pointed out how under this heading protectionist tendencies will be kept within certain limits.

They will be the outcome principally of the diversity of the member countries' fundamental interests in this sphere and of the need for compromise in order to reconcile the different points of view. The negotiations during the December "marathon" aptly demonstrated this need.

Secondly, as regards giving effect to the compromises arrived at, an important factor will be the scarcity and high cost of labour in all Common Market countries. This means that there has to be a continual flow of manpower from less remunerative jobs, especially in agriculture, towards manufacturing industry.

The great change of attitude on the part of industrialists in certain Common Market countries which are traditionally more protectionist than others (for example France) is a convincing proof of such tendencies. In an interview with "Le Monde" on 3 December last M. Villiers, President of the Comité National du Patronat Français, said:

"The EEC must beware of autarkic tendencies in the agricultural sphere ... Food prices and the burden of public expenditure needed for price support and the resorption of surpluses appreciably affect industrial costs ... French industry has just entered upon a period of liberalized trade such as it had not known for nearly a century past; its dependence on external relations is becoming more and more vital as expansion proceeds ... The concern of our industrialists to protect themselves against foreign competition has given way to a determination to conquer export markets. This change of outlook ... is a powerful factor making for progress."

But in agriculture, transgressions of the international division of labour do not result only from "autarkic" tendencies; they may be aggravated by the policy of subsidizing local production, not only to replace imports of products from regions more suitable for their cultivation, but even to allow dumping outside the Community. In various quarters there has recently been a tendency to indulge in extrapolation regarding the Common Market and to make out that implementation of the common agricultural policy combines two kinds of transgression of the international division of labour:

- (a) There is said to be a tendency for self-sufficiency, which previously was limited to the national level, to be elevated to the Community plane;
- (b) Secondly, the changed market conditions (possibility of selling on the Community market) are alleged to make new transgressions (dumping) of the international division of labour easier than before.

This view does not lack historical justification. Many examples could be given; some of the most outstanding, to go by their financial backing, are to be found in the United States and concern cotton and various cereals.

What is the likelihood of seeing such cases recur in the Common

Market? Some elements of the common agricultural policy show that there is none at all. But, once again, we must bear in mind the basic structural differences between the European and American economies. One has a larger ratio of exports to the gross national product than the other. In the European economy the industrial sector is much more important and does practically all the exporting; it tends to be much less protectionist than the agricultural sector.

Across the Atlantic, on the contrary, there is less divergence between the two sectors either on the economic plane or on that of political influence. The industrial sector continues to be marked by traditional protectionist tendencies, while the agricultural sector (South and Middle-West), which is free-trading by tradition but has never in the course of American history since the civil war imposed its will on the industrial east and north, now has sufficiently powerful means at its disposal to obtain from the American nation as a whole a generous aid policy which is translated into dumping.

Such differences in structure indicate that there will in future be far more rigid limits imposed on any economically misguided agricultural policy in the Common Market than there are at present or have been in the past in the United States.

13. Until recently it was generally agreed that the common external tariff for manufactures would, on the whole, have less protectionist effects than the former national tariffs.

The common external tariff represents the unweighted arithmetical average of the national tariffs. For obvious reasons (protection of national production) the rates for manufactures were generally much higher than for other classes of product. This difference has persisted in the common external tariff.

The common tariff, however, has brought with it an innovation of considerable importance in the structure of European tariff protection; it has tended greatly to reduce the differences of level between individual duties.

Consequently the common external tariff presents considerably smaller divergences than those existing in the tariffs of the principal industrial countries. Since the degree of protection afforded by a tariff depends more on differences between the individual rates of duty than on the average level of the tariff, the creation of the common tariff is a progressive step in that it offers wider openings for external trade.

14. A report which recently aroused considerable interest - the Brookings Report - reopens the controversy over the protectionist effects of the common external tariff. This issue is of great importance because it will affect the prospects of the Kennedy round negotiations. The subject needs going into more deeply than is possible in this brief report.

The Brookings Report claims that the effective degree of protection afforded to manufactures by the common external tariff is greater than that of the old national tariffs. The argument runs briefly as follows.

The degree of protection afforded to Community producers by the common external tariff cannot be measured simply by a comparison between this tariff and the average of the existing national tariffs. By the very fact of the institution of a single market, the competitive position of the Community as regards a given product will become that of its cheapest producers, while the others are doomed to disappear. The degree of protection offered by the Community tariff may therefore be compared to the previous degree of protection only in respect of the more efficient producers.

According to whether protection of such producers is strengthened or weakened, the common external tariff is to be considered as more protectionist or less so than the sum of the old national tariffs. This view presupposes the identification of the more efficient producers. The Brookings Report takes the main exporting country (the "dominant supplier") to be hypothetically the most efficient producer⁽¹⁾.

(1) Identification of the most efficient producer with the principal exporter - even though it may be valid in principle - is nevertheless open to numerous objections, if only because efficiency is measured at the level of the firm, where production is generally interdependent, and not at product level.

A comparison must therefore be made between the dominant supplier's national tariff and the common external tariff for the various products; such a comparison carried out for 61 classes of product suggests that the Community tariff is generally higher than the old national tariff taken as the reference figure in this hypothesis. The Report concludes that there is a general deterioration in the competitive position of non-member countries, and of the United States in particular, on Community markets and that the latter enjoy an increased degree of protection. This result is then extended to industrial products as a whole and it is proposed to estimate the effects of such increased protection.

Such an original analysis of the problem provides food for thought.

The Report states that the dominant supplier is generally found to be Germany and presumes that this will tend to remain the case. Such reasoning casts a certain doubt on the validity of the method used.

If the statement were true, producers in Germany would seem to enjoy a considerable advantage in the great majority of industrial sectors, but this would lead over the years, thanks to almost complete freedom of movement for the factors of production, to a concentration of industrial production in Germany. This in turn would involve divergences in the relative development of prices and costs within the Community and, most important, a rise in German costs which would undermine the advantageous position of producers in that country. The costs of German producers, therefore, could not be invariably lower than those of their competitors in the Community, except in consequence of influences of a general nature: unequal rates of inflation or structural differences in some component of cost prices and, in particular, in the indirect impact of food prices on the wage level and variations therein.

But one of the fundamental elements of the Rome Treaty is the progressive narrowing of just such differences, which are considered incompatible with the Common Market. In these circumstances a line of reasoning based on the assumption that

German costs will almost invariably be lower than those in other EEC countries, even supposing it were justified at the moment (which is far from proved), would not hold for the future.

And so, even if it were possible to select today's most efficient producer of a given product, there is no reason for supposing that the same producer will continue to be most efficient in the future. It is a premise of this kind that constitutes one of the bases for the calculation made by the authors of the Report.

15. The foregoing sections, which dealt principally with the effects of the common external tariff and the common agricultural policy, were intended to indicate the limits within which the "discriminating" or "distorting" effects of the Common Market tend to be confined.

Since the Common Market is by definition a preferential grouping, there will inevitably be a relative intensification of trade between its members and they will in the first place pass on to each other the advantages accruing from exchanges of every kind and to a greater extent than in the past.

From the narrow viewpoint of imports from outside the Community, it may be expected that in the long run the ratio of such imports to the gross product of the Community will tend to diminish. The main question remains whether, despite this relative reduction, the impulse given to European development by the specific "Common Market" factor will tend to promote a greater diffusion of European expansion towards countries outside the Community than if the Common Market had not existed, mainly by reason of the increased volume of "extra-Community" imports in absolute terms.

These observations from experience strongly suggest that over the years the net effects of the Common Market have been beneficial to non-member countries.

Furthermore it has been shown why, both in the past and for the future, it was impossible to furnish irrefutable proof of the existence of such effects when considered from the same limited viewpoint that is being taken here.

If we take a broader view, widening our field from the effects of customs union to those of economic union, we can make other conjectures.

Effects of the first kind are, in a certain sense, almost mechanical. They are the consequence of improved use of resources made available by the cessation of activities rendered unprofitable by new competitive conditions. More rational employment of resources in the setting of a large market brings with it an increase in Community income which is apt to stimulate an increase in imports from non-member countries. These adjustment effects can be called "static", in the sense that they are connected with the readjustment of the conditions of production and demand to a new situation. This development takes place once and for all, though it may well be spaced over a very long period.

The second kind of effect can be visualized independently of the adjustment effects just dealt with.

It derives mainly from the new conditions in the union in which economic policies are being prepared: improved co-ordination of national conjunctural policies and their eventual merging in a single anti-cyclical policy; progress in working out common policies in certain spheres (competition, regional development, energy, etc.) and, on the whole, an improved attitude on the part of Community countries as regards ensuring regular, sustained expansion. Compensatory effects of this type are truly specific results of EEC development; they are of a dynamic nature since their appearance will not be confined to the build-up period of the Common Market but will persist indefinitely.

Though effects of this kind elude any accurate method of measurement, they are none the less real and important. By agreeing to merge their economies, the six countries have endowed the Community area with a new dimension which adds up to much more than the sum of the individual countries as they were.