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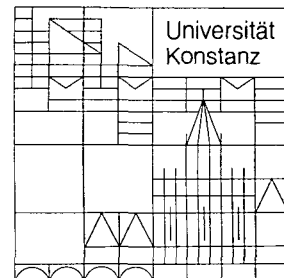
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**The Political Economy
of EC Protectionism
National Protectionism Based on Art. 115,
Treaty of Rome**

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THE POLITICAL ECONOMY OF EC PROTECTIONISM
NATIONAL PROTECTIONISM BASED ON ART. 115, TREATY OF ROME

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The Political Economy of EC Protectionism
National Protectionism Based on Art. 115, Treaty of Rome

Abstract

In this paper, I will explain the rôle of Art. 115 ToR (Treaty of Rome). Art. 115 serves mainly bureaucratic interests and domestic interests to obtain protection. The decision-making process suggests a mixed system of administered protection and influences from the political market. Protection results from a rather complex interdependence of bureaucracy, politicians and interest groups. Correspondingly, the level of protection depends on the economic situation as well as the institutional setting and its changes.

Looking at the structure of 115-protection, it is noticeable that textile and clothing manufacturers are the principal "clients". While Art. 115 accomodates specific protectionist interests of the textile/clothing sector it provides "low key" protection to other manufacturers. Finally, an empirical study will provide some support of the main hypothesis.

Art. 115, EEC Treaty

In order to ensure that the execution of measures of commercial policy taken in accordance with this Treaty by any Member State is not obstructed by deflection of trade, or where differences between such measures lead to economic difficulties in one or more of the Member States, the Commission shall recommend the methods for the requisite cooperation between Member States. Failing this, the Commission shall authorise Member States to take the necessary protective measures, the conditions and details of which it shall determine.

In case of urgency during the transitional period, Member States may themselves take the necessary measures and shall notify them to the other member States and to the Commission, which may decide that the States concerned shall amend or abolish such measures.

In the selection of such measures, priority shall be given to those which cause the least disturbance to the functioning of the common market and which take into account the need to expedite, as far as possible, the introduction of the common customs tariff.

The Political Economy of EC Protectionism

National Protectionism Based on Art. 115, Treaty of Rome

I. Introduction

In this introductory section, some institutional details on the wording, the history, and the procedural details of Art. 115 measures will be presented.

EC-trade is supposed to be governed by the CCP (Common Commercial Policy), based on Art. 113, ToR. But as long as the CCP is not fully implemented, countries can impose domestic quotas on or negotiate separate agreements for goods from non-member countries.¹ Art. 115 can apply to all goods imported from a non-member country for which there is no community wide treatment.

Art. 115 measures can be requested for three reasons. First, it can serve to "enforce" national quotas and voluntary export restraints (VERs) by preventing trade deflection. Italy, for instance, has limited the amount of Japanese cars through a very restrictive quota. Trade deflection through Germany is prevented with the help of Art. 115. Secondly, countries can take recourse to Art. 115 when quotas/VERs in one member country threaten to result

¹ Since 1/1/82, national quotas can only be imposed in "exceptional" circumstances. Separate agreements mostly consist of VERs that easily circumvent restrictions on domestic quotas. For an overview of the protectionist instruments of the Treaty see Hailbronner, Bierwagen (1989).

in economic difficulties from trade substitution. France, for instance, may ask for import barriers to prevent the use of the French market as a substitute for the Italian. Finally, there are EC quotas that have to be distributed over the member countries. Art. 115 can contribute to distribute and enforce these quotas.

Art. 115 applications are an excellent indicator for domestic protection towards non-member countries. Since Art. 115 can be used to enforce domestic quotas and VERs, such applications are an indirect indicator for national protection based on quotas or VERs. Secondly, countries can obtain trade barriers under the key word "trade substitution". Thirdly, EC-quotas can be distributed and enforced in a protectionist manner with the help of Art. 115. Single countries can strive to minimize their own quotas and thereby reduce imports. Joint internal action can result in a quota allocation across member countries that is detrimental to the interest of foreigners. Assume that the EC has a certain quota on winter coats. If it allocates the whole quota to Spain, the importer will find it difficult to ensure full utilization. The result is higher protection than the EC-wide quota suggests. Art. 115, therefore, captures the major national protectionist activities.²

² Some countries like Germany discourage recourse to Art. 115. National protectionist interests are forced to apply mainly for EC-wide measures.

The procedure looks as follows. Countries have to apply to the commission for non-application of community treatment against one non-member country. The commission (i.e. the responsible sub-directory) investigates the request and decides within five working-days. Sometimes, applications are withdrawn. Validity starts on average 3-6 months after the decision. In urgent circumstances till 1980, countries could engage in autonomous action and get retroactive permission. Measures apply usually for less than a year which requires periodic reapplications.³ Appeals are forwarded to the ECJ (European Court of Justice).

Despite of a well-defined procedure, a lot of discretion remains with respect to approval and measures. Approval of the application either results in surveillance of imports to the respective country or in more concrete measures i.e. import blocks or other quantitative restrictions. Approvals require the existence or threat of trade deflection and economic difficulties⁴.

Indicators used to prove economic difficulties for a country are in the case of "surveillance" measures: use of the good, market share of domestic producers, producers of the affected third country, and the market share of all non-member countries. Additionally, price collapses or

³ Other protectionist measures can apply for much longer periods (e.g. anti-dumping). However, the reapproval rate in 1988 was over 90%.

⁴ Trade deflection alone qualifies when Art. 115 measures serve to realize common trade policy.

price rises that were prevented, profits and losses, and employment are used as indicators of damage as a precondition for quantitative measures (Commission, 1980). These notions, however, are vague enough to facilitate protection-seeking at the domestic level (Hailbrunner, Bierwagen, 1989).

The application and interpretation changed significantly over time. Since 1968, measures had to be authorized by the commission. Since 1980, based on decision 80/47/EEG of the commission, protective measures have only been approved if (the threat of) trade deflection leads to economic difficulties. The ECJ required a strict interpretation but the formulation remained vague. Starting 10/87, decision 87/443/EEG requires a narrower interpretation and stricter application. Measures can only be granted for a limited period of time and when the situation is particularly serious (Hailbrunner and Bierwagen, 1989). It provides a detailed outline when which measures can be applied. The precondition of "economic difficulties" is supposed to be examined more thoroughly.

If the common market is to become reality in 1992, Art. 115 becomes obsolete because internal border controls are abolished.⁵

⁵ In the literature, doubts exist whether all border controls will be abolished (Hailbrunner and Bierwagen 1989, Oliver 1988). A special EC committee, however, seems to work on the question how to replace Art. 115 after 1992. Various scenarios are briefly discussed by Neme (1988).

Concluding this introductory discussion, Art. 115 is mainly used to enforce and obtain national protection above the level of EC-protection⁶. Supply and demand conditions in the process of putting to use Art. 115 are discussed in more detail in the next section.

II. The Level of Art. 115 Protection

In this section, the level of protection and its change over time will be subject to analysis. For lack of more explicit data, the applications and approvals will serve as a proxy. It will be argued that the Art. 115-sub-directory follows its bureaucratic interest. Various channels of control, however, force it to accomodate roughly the pressure from the heads of the commission and interest groups brokered by national governments.

The decision-making process suggests a model of bureaucracy for trade policy-making with rather strong control by politicians and interest groups.⁷ The commission (i.e. the sub-directory for Art. 115) deciding about 115 applications can be characterized as a bureaucracy. The respective EC bureaucrats enjoy considerable discretion with respect to the evaluation of applications and the

⁶ The EC, thereby sanctions national measures whose ratification would be controversial or "dirty work" for governments at home.

⁷ At a later stage I intend to include a more formal model of EC-trade-policy making.

implementation of measures (see section 1). As budget maximizers (Niskanen, 1968), they use this discretion to increase their budget. The output justifying their existence is decisions on trade protection. It is in their interest to reject few applications to increase demand for their output. A bias towards increasing levels of protection can be expected (Nelson, 1981).

Political control is less easy than for other trade policy measures (e.g. anti-dumping) because decisions are not subject to approval by the council. On the other hand political control of and influence on administered protection in the EC can be exerted through several channels. These allow only restricted pursual of bureaucratic expansionary interests.

First, the EC-commission is subordinate to member governments through the council. The council can request from the commission to change the procedure or, in other words, it can impose structural reforms on the commission to realign decision-making with the political optimum. It can appeal decisions by the commission at the ECJ. The number of commissioners and their salaries are fixed by the council.

National ministers (comprising the council) are interested in trade policy that represents their domestic interests in a "balanced" manner. Overboarding or too sparse protection gives them an incentive to request reforms.

The council's free-riding problem of control is relatively small. The council consists of various rounds of ministers and heads of government. The number is small. Consequently, Verreydt and Waelbroeck (1982) argue that there is not much difference between asking bureaucrats or lobbying the political process in the EC. Politicians can easily interfere with the bureaucratic process and complaints against bureaucratic behaviour are bad for the career. On the other hand decision-making is cumbersome, since far-reaching decisions require unanimous consent. The effectiveness of the council to control the commission is, therefore, probably more limited than Verreydt and Waelbroeck suggest.⁸ If the council initiates changes, they most likely accomodate national special interests.

The Court of Justice has to decide about the commission's decisions that are appealed. Benchmark-rulings on trade policy may also constrain the application of Art. 115. The court is interested in establishing authority through a well-functioning judiciary. On the other hand, its authority is severely restricted through limited independence and lack of powerful enforcement provisions. This may help to explain why the court's influence on Art. 115 measures is ambiguous. In recent years, the court has upheld the commission's decisions that allow national measures under the Multi Fiber Agreement and to enforce

⁸ This evaluation is implicitly supported by Peirce (1989) who reports that the council decisions are generally limited to minor issues with consent generated by log-rolling.

VERS (Hailbronner, Bierwagen, 1989). On the other hand, it is argued that the court contributed to toughen the procedure in 1980 through two restrictive rulings.⁹

The commission itself has a strong incentive to constrain the protectionist impact of the Art. 115 sub-directory. The heads of the commission have a strong interest to appease their national governments and interest groups because their reappointment or career at home is determined by their governments. They will correct excessive or unsatisfactory levels of 115 measures. Moderate deviations from political equilibria might be tolerated because council and court control are costly to initiate. Excessive expansion and contraction, however, will be prevented or corrected.

The heads of the commission will also restrict use of Art. 115 when "higher goals" (e.g. project 1992) emerge that serve their own bureaucratic, expansionist interests better. The goals of the commission's leading bureaucrats are the most important supply factor at the EC-level constraining Art. 115 decisions. Furthermore the heads of the commission have to broker between competing instruments. As far as instruments serve as substitutes, sub-directories have an incentive to expand their role at the expense of each other. Changes in the procedure may result from bureaucratic competition.

⁹ The Kaufhof (no. 29/75) and the Donckerwolcke rulings (no. 41/76) contained a narrow interpretation of quantitative restrictions and a rejection of national measures based on potential approval by the council.

On the demand side for trade policy, national governments exert pressure on EC trade policy making through the council of ministers and through the appointment of commissioners. In EC-trade policy matters, governments mainly broker special interests. Consumer/voters face high information costs due to the intransparent process. Voter participation is costly; voter influence on such detailed EC policy issues is, therefore, virtually inexistent. Interest groups constitute the predominant national factor for EC-trade policy making.

Interest groups not only voice their interests through national governments. The previous discussion of the commission and the council suggest a strong (direct and indirect) influence by both national and EC-wide interest groups on these institutions. Furthermore, domestic interests are well organized in various EC-committees; foreign producer lobbies can not work through such official institutions. It is widely known that there is a bias in favor of domestic protectionist interests in the political process. Protectionist interests largely determine EC-trade policy making.

Summarizing the previous discussion, bureaucratic tendencies to expand the role of Art. 115 can be expected. These may be dominated and corrected through various channels. While interest groups can put direct pressure on the commission's sub-directory they may also work through

national governments, the council, the court and the commission. Council, court and, most likely, the commission itself can initiate "realignments" of Art. 115 measures. Decision-making will be constrained mainly by the two principal interests: domestic pressure groups and the heads of the commission.

On the supply side, three "realignments" or institutional changes can be identified. After 1968, member countries had to submit an application subject to approval by the commission before national measures could be enacted. Before 1968, member states just informed the commission about their measures. In 1980, more emphasis was put on economic difficulties as a precondition for approval. Indicators of economic difficulties were introduced. In 10/1987, the procedure was further toughened by granting measures only for a limited time period. The situation had to be serious¹⁰ and the criterion of economic difficulties had to be applied strictly. The reforms reduced discretion to apply Art. 115, first of countries and later of the commission.

The reform in 1980 was induced by a dramatic increase in applications and approvals in 78/79 (see table 1). The danger of collapse loomed over the CCP (common commercial policy) due to excessive national measures. This was neither in the interest of the commission nor of national

¹⁰ "Nur wenn der Ernst der Lage es erfordert" (Hailbronner and Bierwagen, 1989).

governments and interest groups. The structural change was initiated by the commission (80/47/EEC) reflecting their interest in a continuation of the CCP. Pressure from council, interest groups/national governments and the court may have contributed to the realignment.¹¹ A strong decline in applications (lagged by one year) resulted, although not to pre-78 levels. It conforms to the argumentation that extreme increases in bureaucratic decisions lead to structural realignments.

The 87 reform (87/433/ECC) was induced by the Single European Act (1985) calling for a "true" common market in 1992. Again the commission initiated the change in procedure. The common market promises more profits for commissioners (higher budgets, seats in a potential European government) than the expansion of one sub-directory. The major interest groups also consent to project 1992.¹² The numbers for 1988 (table 1) do not indicate a strong decline in applications yet - maybe due to a lag in information etc. or because interest groups have not found a suitable substitute.

On the demand side for protection, 60-80% of the applications originate from the textile and clothing sector. The rest is manufacturing protection ranging from

¹¹ See the previous discussion on the court's role to control the commission.

¹² External barriers remain and may be increased to compensate potential losers (fortress Europe).

Brasilian sewing machines over Japanese cars to Chinese Espadrilles and bananas from the Dollar-zone.

The ratification of the Multi Fiber Agreement in 1974 and its successors MFA II (1978) and MFA III (1982) strongly affected the level of recourse taken to Art. 115. In MFA I, it was mainly agreed that imports do not rise by more than ca. 6% per year. MFA II resulted in a demand shock as it allowed "reasonable" departures from the 1978-6% rule. Applications almost trippled to take advantage of the new protectionist opportunities and to secure new quotas. MFA III made it harder for non-member countries to utilize previously underutilized quotas and resulted in a modest increase in applications. Manufacturing protection was significantly higher during the years 79-83, the latter three years because of the economic crisis.

This brief argumentation and interpretation of the available data illustrates that a public choice view on Art. 115 is justified. The data suggests that economic self-interest of bureaucrats, interest groups and politicians who react rationally to changing constraints (i.e. the 80 and 87 reforms, MFA II and III) can explain a large share of domestic protectionist trends within the EC. Section IV of this paper provides preliminary empirical test of the hypotheses. The next section will discuss the structure of Art. 115 applications.

III. The Structure of Art. 115 Protection

or: Who wants Art. 115, why?

• So far, the choice of particular protectionist instruments has not received thorough analysis from political economists. It is frequently argued that interest groups prefer quotas to tariffs because the first provide protection at more predictive levels. Apart from this demand-side argument, Cassing and Hillman (1985) argue that supply of tariffs vs. quotas depends on the trade off between political support and revenues.

In this section, I will discuss further determinants of the choice of protectionist instruments. Politicians and interest groups will opt for the instrument(s) that maximize(s) their profits. Organization costs, product homogeneity and various other factors affect the choice of policy instruments. Furthermore, recourses to Art. 115 have to be seen in the light of the legal/institutional framework of the EC. The choice of Art. 115 may, therefore, not be optimal for the involved parties but the best one within the political feasibility space. Art. 115 measures are preferred by the textile industry because of the latter's very specific protectionist interests beyond the MFA. They are supplied to some sectors because of their "low key" character.

Looking at the structure of Art. 115 applications (table 1), it is noteworthy that 55-81% come from the t/c

(textile/clothing) sector. To explain this phenomenon, the trade-off between national and EC-wide measures has to be analyzed and to be applied to the t/c sector. First, various factors on the demand side are discussed.

National measures will be preferred when organization costs at the EC level are very high. Another argument in favor of protection at the national level is product heterogeneity requiring very specific protection. Industries selling mainly at the national level do not want EC-wide measures. Common protectionist measures are preferred when the producers operate EC-wide. Economies of scale in lobbying also further the interest in common trade policy making.

Looking at the statistics, the t/c sector is highly atomized. Table 3 displays that the number of companies in the textile industry is several times as high as (e.g.) in the vehicle/motor industry. In Germany, there were about 4000 companies in t/c but only 59 in vehicles in 1986. In other countries the situation is similar. Strong competitive pressure is indicated by the vehement industry contraction over the period from 1970 to 1986 when the industry declined from almost 10000 to 4000 companies. The industry structure results in high organization costs and free riding problems. On the other hand, three factors facilitate organisation and increase political leverage of the t/c sector. The industry is regionally concentrated and an important source of employment. Regional concentration and the competitive threat of sudden import penetration facilitate organization (Verreydt, Waelbroeck, 1982). The

textile industry is well represented nationally and also organized immediately after the founding of the EC in 1958 - despite its high organization costs.

In spite of strong import competition, the t/c industry exports a significant share of its production.¹³ Many producers operate internationally. EC-wide measures will be preferred by many producers considering the degree of organization and internationality. On the other hand, producers in particular countries or subsectors who sell predominantly in the domestic market prefer national measures.

A strong argument for national measures in the textile sector is product heterogeneity. Table 2 illustrates the high degree of product differentiation in the t/c sector. While there are 750 product groups in the t/c sector, vehicles are only subdivided into 19 groups by the German statistical office. Therefore, protection is only effective if overall measures are broken down into various product categories. Every product group needs its own explicit quotas i.e. shirts, pants etc.. Otherwise, protection will not be balanced over the whole range of products but import penetration may increase particularly in some subsectors. The consequence is that the negotiation process for protection is very time-consuming, expensive and cumbersome. Protection at the national rather than the EC-level is preferred because interest groups can lobby at a lower level in the political hierarchy where less

¹³ Statistisches Bundesamt, 1988: Produzierendes Gewerbe, Fachserie 3.1.

information is lost. Protection at the domestic level can be influenced in a more detailed and specific manner than at the EC level. Negotiation costs are lower because less measures have to be agreed on. While this argument definitely applies to producers for domestic markets, it does not apply to all producers selling EC-wide. The latter prefer EC-wide measures. Nevertheless, they also promote specific domestic protection if more encompassing barriers are too costly to obtain.

Finally, national measures may also reinforce EC-wide protection. As discussed in section 1, EC-wide quotas may be distributed in a manner that increases the protectionist impact of the quota. Art. 115 for textiles can serve this purpose.¹⁴

The previous discussion suggests the following hypothesis: the t/c industry will strive for protection at both levels. EC-wide measures will keep a "lid" on the overall level of imports serving international producers and taking advantage from economies of scale. Specific national measures (backed by Art. 115) will accommodate specific protectionist demand and provide additional protection. Art. 115 helps to secure the domestic part of an effective protectionist bundle for the t/c industry.¹⁵

¹⁴ EC-quota utilization is a good indicator for the additional protectionist impact of Art. 115 beyond the MFA.

¹⁵ Some countries do not apply for Art. 115 measures. The German government, for instance, opposes recourse to Art. 115 and refers interest groups to the anti-dumping procedure. Vaubel argues it diffuses accusations of being protectionist this way. A thorough analysis of preselection at the national level goes beyond the scope of this paper.

On the supply side for protection, politicians have to take the legal/institutional framework as given. Only in the long run, they can try to change supply conditions. The choice is not simply between tariffs and quotas or some other combination of trade barriers as some economists implicitly suggest. The EC-trade policy making is mainly constrained by the GATT and its own law. They only allow for certain kinds of protection though grey area protection is thriving.

Politicians have a strong incentive to accomodate protectionist interests in the textile and clothing industry. As briefly discussed in the previous section, the t/c sector is regionally concentrated and a major employer. Table 4 indicates that the share of the t/c industry is over 5% in most countries and e.g. 17% in Italy (1980). It is probably an even more important employer since it is mostly labor intensive. Consequently, several representatives in each legislature are likely to see after the interests of this constituency.

On the supply side, national measures are preferred if EC-wide protection results in strong international or consumer/voter resistance etc. EC-wide measures for instance invite stronger protests or retaliation from other countries and provide a stronger incentive for consumer lobbying. If the costs from "high key" measures outweigh the benefits from encompassing measures, politicians and

bureaucrats prefer "low key" and intransparent measures under Art. 115. This argument does not apply for textiles - an EC-wide instrument exists anyways in the form of the MFA. The use of Art. 115 measures is, therefore, mainly demand determined - to accomodate the very specific protectionist demands of the t/c sector.

Summarizing the discussion of the t/c sector's trade policy interests, the existing policy mix effectively considers the particular political and industry situation under the given legal/institutional constraints. The MFA determines overall protection while detailed measures to protect certain industries in certain countries are implemented with the help of country quotas, VERs and Art. 115. The role of Art. 115 is in particular to enforce quotas and VERs as well as to provide means against trade substitution and efficient quota utilization.

Protection for other manufacturing industries ranges from umbrellas to shoes, from televisions to cars. 19-45%¹⁶ of Art. 115 applications serve to protect manufacturers. The first main argument for industries to take recourse to Art. 115 is similar to the demand side argument in the case of textiles. France's espadrille industry for instance produces mainly for the national market. Art. 115 suits well for the very particular interests of this industry. It

¹⁶ These include very few cases of agricultural protection under Art. 115.

does not necessitate EC-wide lobbying with its high organization costs.

On the other hand, car or TV producers can easily lobby at the EC level and obtain encompassing protection. The argument against it is supply side related. EC wide trade barriers are too "high key". They would obtain too much attention from foreign producers and governments. Even consumers/voters might reject such far reaching, obvious and costly protection. A VER for cars to Italy spreading to other countries with the help of Art. 115 might achieve the same effect with less resistance from various interests. The detour through domestic protection reduces for instance the transparency and the danger of retaliation.

In this section, the structure of Art. 115 protection was discussed. It was shown that public choice theory can also contribute to explaining why particular industries apply for Art. 115 (in conjunction with quotas, VERs, the MFA) and not for other instruments.

IV. An Empirical Analysis of Art. 115 Protection

The following econometric study intends to show the determinants of demand and supply of Art. 115 protection empirically. Since the equations have only got eight to ten degrees of freedom, the results have to be interpreted sceptically. An analysis of a longer time series was

prevented by the limited availability of data.¹⁷ The results illustrate the main hypothesis of this paper: Art. 115 protection is determined mainly by bureaucratic interests and special interest pressure.

Applications/approvals serve as a proxy for Art. 115 protection. The exact extent of protection is hardly quantifiable because data is not available. In a first step, the number of total applications is used as dependent variable in a reduced form equation (equations 1-3). The approval rate serves as dependent variable in an estimation of supply (equation 4). Finally, a simultaneous estimate of supply and demand is undertaken. Approvals is the dependent variable to be estimated (equation 5).

Several economic macro variables are used to estimate the level of applications. Unemployment and two business-cycle variables are tested as indicators of the influence of interest groups. Unemployment should be positively correlated with 115-applications and approvals. An increase in unemployment puts increasing pressure on politicians to "do something" i.e. to protect domestic industries and jobs. Unemployment data, however, indicates increasing rates and levels almost over the whole period so that difficulties with this variable were expected.

17 I could only obtain annual data for the thirteen year period from 1976-1988. For data before 1976, the commission referred to the EC Gazette which is published daily.

The first business cycle variable was computed from GDP growth in the EC and indicates deviations from average GDP growth during the period. These are expected to be inversely related to the number of applications. The variable captures changing special-interest pressure for protection over the business cycle. If GDP-growth is above average, it is less profitable to invest in redistribution. On the other hand, low growth will make protectionist rent-seeking more profitable compared to productive investments.

The Production Index Manufacturing is used for the same purpose. It should show equivalent results as "deviations from average GDP growth". The expected sign of the coefficient is negative because interest in protection will decrease with improving industry performance.

Institutional changes were discussed in detail in the previous sections. They are tested with the help of dummy variables. On the demand side, the two Multi Fiber Agreements (II and III) are expected to increase demand for protection. Two separate and one common variable are tried out to take into account MFA related changes. The major change occurred with the second MFA while MFA III only changed a few aspects. It is expected that applications react quickly and positively to the MFAs.

Two dummies reflect the supply shifts as a consequence of the 80 and 87 reforms. Both are expected to have negative signs since they render supply of protection more difficult. The second reform in 1987 may not be significant because there is only one observation afterwards.

Both variables are lagged by one period. First, there is an information problem with respect to the new procedure: many applicants may not know about it. Secondly, there is a lag between the decision to try to get Art. 115 measures and the actual application with the EC. Thirdly, many applicants will test whether the commission is really committed to toughen the procedure. Therefore, applications react to inward shifts of supply with a lag.

A lagged variable of the approval rate is included to further incorporate supply shifts on the demand side. It should have a positive sign.

Equation (4) estimates the effect of supply factors on the approval rate. The lagged dependent variable is supposed to capture the tendency of bureaucracies to expand. The Art.115-sub directory increases the approval rate incrementally to expand but also to avoid attention from controlling institutions. The expected sign of the lagged approval rate is positive.

The reform in 1980 is expected to reduce the approval rate because it toughened the procedure. In the following years, the rate is increasing incrementally again from a lower level. A dummy that is 1 in 1980 and 0 in all other years reflects the impact of the 1980 reform and should be negative.

As argued in section 2, bureaucracies are not interested in sudden shifts in the level of protection. The response to a demand shock like the MFA should be a reduced approval rate. The dummy for the impact of the MFA

II/III in 1978 is expected to have a negative sign, analogous to the reform-80 dummy.

Supply and demand will be estimated simultaneously in equation (5). Approvals are determined by lagged approvals, the impact of the reform 1980, and applications. Applications are estimated with equation (2) excluding the reform-1987 variable. Analogous to the argument for the lagged approval rate (bureaucracy), lagged approvals are expected to have a positive sign. The impact of the reform-80 on approvals should be negative but immediate.

The following equations were tested:

- (1) $APPL = \alpha C + \beta_1 REF80-1 + \beta_2 MFA + \beta_3 PIM$
- (2) $APPL = \alpha C + \beta_1 REF80-1 + \beta_2 REF2-1 + \beta_3 MFA + \beta_4 DGDP$
- (3) $APPL = \alpha C + \beta_1 REF80-1 + \beta_2 MFA + \beta_3 DGDP + \beta_4 PAP-1$
- (4) $PAP = \alpha C + \beta_1 PAP-1 + \beta_2 REFIMP + \beta_3 MFAIMP$
- (5) $APPR = \alpha C + \beta_1 APPR-1 + \beta_2 REFIMP + \beta_3 APPL$

$$\text{with } APPL = \alpha C + \beta_1 MFA + \beta_2 REF80-1 + \beta_3 DGDP$$

where APPL = No of applications,

APPR = No of approvals,

PAP = Approval rate,

C = Constant term,

REF80-1 = Reform 1980 lagged,

REFIMP = Reform 1980 impact on supply,

REF2-1 = Reform 10/87 lagged,

MFA = MFA II and III,

MFAIMP = supply impact of the MFA

DGDP = Deviation from the GDP's growth trend,

PIM = Production Index Manufacturing.

Results:

The regression results illustrate the relevance of interest groups, bureaucracies and institutional changes in the process of trade policy making. Interpreting the results for equation (1-3), the legal/institutional variables (reform 1980, MFA) have the right sign and are highly significant. The MFA variable yielded about the same results when split into two variables for each MFA (not indicated).

The dummy for the reform of 1987 has the right sign in equation (2). However, the variable is not significant. As argued before, it could be attributed to the fact that there is only one observation after the implementation. It may be too early to judge the relevance of the 87 reform to reduce 115 protection. The variable was inapplicable in equation (1) because the data for 1988 was incomplete. In (3) it did not yield better results and was omitted.

The null hypothesis for the influence of past approval rates on applications could not be rejected. It is insignificant and it has the wrong sign.

The study suggests an influence of industry pressure on applications, indicated by the business cycle variables. As expected, unemployment (both levels and changes) caused "difficulties": it was always insignificant with changing signs. Deviations from the growth trend, however, yielded better results. Growth above average resulted in a decline

in the amount of applications significant at the 5% level. The production index for the manufacturing industry was also significant. These results further support the interest group approach to protection.

Equation (4) supports the hypotheses about the behaviour of bureaucracies. The lagged dependent variable was significant with the right sign to explain the approval rate in equation (4). The coefficients of both institutional dummies (MFAIMP and REFIMP) have the right negative sign; the MFA-variable, however, is not significant. The results suggest that the sub-directory follows an expansionist path but reacted to the structural realignment of the heads of the commission immediately.

Equation (5) provides modest support in favor of supply variables to explain approvals. Both the lagged dependent variable and the reform 1980 are significant at the 10% level. The estimated levels of applications are highly significant.

In all equations, the F-values are significant at least at the 5% level, the Durbin-Watson statistics are acceptable (where applicable) and the R^2 are in the range of 0.91 to 0.94 for all equations except (4). Despite of the limited value of the regression results, they support the public choice approach to the analysis of EC-trade-policy making.

V. Conclusion

In this paper, national protection within the EC was analyzed. It was argued that Art. 115 is an excellent indicator for domestic protection because it enforces domestic quotas and voluntary export restraints. I also provides some supplementary protection. Art. 115 protection is not granted for some social or economic motive but to provide protectionist rents to special interests and bureaucrats under the existing (though changing) legal/institutional constraints.

Art. 115 is paraticularly useful for the textile/clothing industry to obtain protection in conjunction with the MFA, quotas and VERs because of the atomistic industry character and product heterogeneity. This reason applies also to some manufacturing protection as well. On the other hand, various industries/countries take recourse to Art. 115 to prevent high key protection for sensitive products at the EC level (e.g. Japanese cars for Italy). Empirical tests support the hypothesis that Art. 115 protection is determined by public choice related factors.

Similar to GATT, the EC has included several escape provisions for protectionist interests into their founding document, the Treaty of Rome. These exceptions from external as well as internal free trade were necessary to

accomodate particularly strong interest groups.¹⁸ The latter could have blocked the unificaton process through their national governments otherwise. Meanwhile, EC industries have increasingly gone international. Interest in domestic protection has decreased while interest in a "true" common market rose. Momentum towards reduced internal barriers increased further when major institutional obstacles were removed with the Single European Act. In this context, the project "1992" looks promising even from a public choice perspective. Remaining protectionist pressure may drift toward anti-dumping policy and EC-wide VERs - Art. 115 might "have to go".¹⁹

18 See Baldwin (1988) for a discussion of the role of escape clauses etc. in the GATT-document.

19 Fears of a "Fortress Europe" are rational in this context.

Table 1:

Year	no of applications			approved		rejected	
	total	textiles	other	total	%	total	%
1976	110	72	38	74	67	36	33
1977	121	75	46	79	65	42	35
1978	317	258	59	197	62	120	38
1979	347	269	78	260	75	87	25
1980	356	273	83	222	62	134	38
1981	255	184	71	166	65	89	35
1982	241	156	85	174	72	67	28
1983	253	176	77	188	74	65	26
1984	215	155	60	165	77	50	23
1985	211	143	68	176	83	35	17
1986	184	131	53	141	77	43	23
1987	182	122	60	157	86	25	14
1988	153	84	69	128	84	25	16

Table 2

Product Homogeneity in Various Sectors
Indicator: Number of Product Groups per Sector in the
Producer Statistics of the German Federal
Office
for Statistics

Iron / Steel	55
Vehicles	19
Textiles	500
Clothing	250

Source: Fachstatistiken des Statistischen Bundesamtes,
Serie 4
Reihe 3.1 Produktion improduzierenden Gewerbe
des In- und Auslandes. Stuttgart, Mainz: W. Kohlhammer,
1986.

Table 3

Number of Companies in Various Sectors

	Period	Steel Sector	Vehicles + Motors	Textiles	Clothing
Country					
Germany	1986*	168	59	1685	2370
	1970**	264	51	3782	5894
Denmark	1970***	9	61	431	502
France	1969	353	163	8255	19135
Ireland	1969	-	-	237	324
Italy	1969	666a	-	4662	2709
Luxem.	1969	3	-	\ 40b/	
Netherl.	1971	52	-	528	942
UK	1968	788	-	6183	7131

a : includes founding

b : textiles and clothing together, period: 1965;

*Source: Statistisches Bundesamt: Produzierendes Gewerbe; Fachserie 4, Reihe 4.1.2 Betriebe, Beschäftigte und Umsatz im Bergbau und im verarbeitenden Gewerbe nach Beschäftigten-größenklassen. Stuttgart, Mainz: W. Kohlhammer, 1986.

**Source: Statistisches Bundesamt Wiesbaden: Industrie und Handwerk, Reihe 1: Betriebe und Unternehmen der Industrie, 1. Betriebe, Beschäftigung und Umsatz, Brennstoff- und Energieversorgung. W. Kohlhammer, 1970.

***Source (for Denmark and the following countries): Statistisches Bundesamt Wiesbaden: Industrie und Handwerk, Reihe 8: Industrie des Auslandes, Die Industrie in den europäischen Ländern; Sonderbeitrag. Stuttgart, Mainz: W. Kohlhammer, 1973.

Table 4

Textiles : Share of total industry *		
	share	
extiles	original weight	share of total
extiles	base period	industry of the
Country		country
Belgium	1980	8.2
Denmark	1980	5.9
France	1970	4.7
Germany	1980	2.4
Greece	1970	18.8
Ireland	1980	7.3
Italy	1980	17.0
Luxem.	1980	1.9
Netherl.	1980	3.0
Portugal	1970	11.2
Spain	1972	14.9
UK	1980	5.2

Source: OECD: Indicators of Industrial Activity, 1987-4, Paris, 1987.

* Weight in the production index per country

Table 6. Art. 115 Protection in the EC from 1976-1988

OLS: Dependent Variable is NO OF APPLICATIONS (1-3)

% OF APPROVALS (4)

TSLS: Dependent Variable is NO OF APPROVALS (5)

Variables	Results - Estim. Coefficients (t-Statistics)				
	(1)	(2)	(3)	(4)	(5)
Constant	659 (3.6)	134 (8.58)	225 (3.5)	0.31 ^d (2.00)	1.09 (0.07)
Reform 80 (lagged)	-112.8 (-8.22)	-131 (-9.1)	-126 (-8.56)		
Reform 10/87 (lagged)		- 38 (-1.6)			
MFA II }MFA MFAIII	225 (12.37)	210 (11.04)	227 (11.2)		
GDP growth (dev fr. trend)		-15.6 (-2.85)	-17.8 (-2.95)		
Prod. Index Manufacturing	-5.8 (-2.99)				
(3-4): %, (5):NO Approvals (lag)			-160 ^a (-1.76)	0.62 (2.92)	0.2 ^d (2.04)
Ref80 Impact (eff. in 80 only)				-0.15 (-2.65)	-42 ^d (-2.19)
MFA Impact (eff. in 78 only)				-0.09 (-1.57)	
Appl (estim. value in TSLS) ^b					0.6 (8.1)
No of Observ.	12	13	12	12	13
Durbin-Watson	2.27	1.73	1.79	2.52 ^c	1.98 ^c
Adjusted R ²	0.94	0.93	0.94	0.597	0.92
F value	57.8	44.8	48	6.43	44

a Wrong sign and insignificant.

b Appl is estimated with equation (2) without Reform 87.

Instruments in TSLS: C REF1 MFA REF80(-1) DGDP APPR(-1)

c Durbin Watson distorted due to lagged dep. var..

d Rejection of the null hypothesis at the 90% level

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