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Intereconomics

Balanced or Unbalanced Growth in the EEC

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According to Article 2 of the Treaty establishing the European Economic Community it is the task of the Community to achieve a continuous and balanced growth of real per capita incomes within the integration area and at the same time secure full employment, stability of prices and an equilibrium in the balance of payments. There are two ways of reaching this aim:

1. the establishment of a Common Market;
2. the gradual adjustment of the economic policies of Member States.

The Common Market as a customs union, which satisfies the additional requirements of free movement of capital and services, freedom of establishment of nationals of a Member State and unrestricted mobility of labour, is regarded as promoting growth. Its realisation, it is hoped, will bring increased competition within the integration area and thus, compared with the original situation will allow competition to fulfil its functions in a better fashion.

The static theory of integration, under the dominating influence of J. E. Meade, had still seen the advantages of a Common Market mainly in improving the effectiveness of the so-called static functions of competition. Today the prevailing view is that the process of integration can have a decisive impact on growth mainly by strengthening the dynamic functions of competition: through increasingly enforcing the application of technical progress in respect of products and production methods as well as the flexible adjustment of output capacities to the constant changes of non-economic factors.

There is hardly a measure of economic policy which does not directly or indirectly influence the growth of a national economy. But there are three particular spheres of governmental economic policy which are of special importance for the speediest and smoothest possible growth of real per-capita income:

☐ the policy of promoting competition: its effectiveness largely determines whether a growing potential intensity of competition arising most probably from lowering trade barriers between integration partners will also lead to an increase in the actual intensity of competition[1]; whether therefore the impulses released by the process of integration are not—so to speak—"inactivated" by new restrictions on competition;

☐ the policy of growth, by which is understood the total of all those measures which are directed primarily towards a long-range expansion of the whole economy's supply. Here government investments in the social sector are of outstanding importance, e.g. in transport, health services, education and research;

☐ the structural policy meaning the totality of measures designed to influence the division of the productive capacity of the whole economy in sectors and zones.

Economic Union Still in Its Infancy

The establishment of the customs union as the nucleus of the Common Market has been regulated in great detail in the EEC-Treaty. But as regards the gradual adjustment of the economic policies of Member States, the Treaty as a rule contains mere outline programmes the detailed elaboration of which is left to co-operation among the Treaty partners and to the efforts of the EEC authorities. These comparatively non-committal arrangements for the co-ordination of the economic policies of Member States were doubtless due to their reluctance to accept additional losses of sovereignty in favour of a supra-national authority such as the EEC-Commission.

At this juncture, nobody will surely maintain that Member States have meanwhile become ready for such a change. The result is: while the EEC has largely materialised as a Customs Union, its extension to an Economic Union is still in its infancy. Even the second phase of the transitional period has ended without the EEC Commission being able to make any appreciable progress in carrying out its "action programme" of October 1962, which envisaged "the co-ordination in one common system of national government activities that are economically relevant".

Meanwhile the Commission's ideas about the adjustment of national economic policies have become more modest. But the EEC would still be a long way from becoming an Economic Union if, contrary to expectations, the governments of Member States could be persuaded to accept and adhere to the economic policy directives contained in the EEC Commission's "Draft-programme for the Community's medium-term economic policy (1966 to 1970)". The Commission submitted this draft programme to the Community's Ministerial Council in April, 1966.

On July 1, 1968, the functional integration within the EEC will be finally accomplished by the removal of the remaining internal customs duties and the final adjustment of national customs duties to the common external tariff. But this achievement will have

[1] About concepts of potential and actual competitive intensity see: E. Kantzenbach, "Die Funktionsfähigkeit des Wettbewerbs", Göttingen 1966, pages 40 et sequ. 102 et sequ.

to be secured without being buttressed by institutional integration. In some special fields, as e.g. taxation policy, measures towards further synchronisation may be taken. Yet a comprehensive adjustment of national economic policies as advocated by the EEC Commission must be regarded as impracticable in the foreseeable future.

In other words: in all three areas of economic policy which have a particularly strong impact on economic growth considerable disparities will persist in the coming years as to type, extent and intensity of intervention by the various Member States.

This applies in particular to structural policy to which the EEC Treaty, except in its general regulations on State aid (Articles 92 to 94), refers only indirectly. The draft programme for a medium-term economic policy also treats this matter with great reserve and leaves considerable freedom of action to the national governments.

The same applies to policy of growth. Here the comprehensive and purposive promotion of growth in France, by its "planification", must be compared with the unsystematic and badly co-ordinated activities of those responsible for West German economic policy. This comparison very clearly shows the great discrepancies between the various Member States as regards the policy instruments they have available and the use they make of them. In all probability these disparities will persist in the foreseeable future.

As to the policy of promoting competition, Article 85 of the EEC Treaty, para 1, gives the Commission rather far reaching powers. But it does not necessarily follow that the national cartel policies of the various Member States will become superfluous in the future and that the existing differences between them will thus be of no significance.

This would only be true if the EEC Cartel Authority were actually to prohibit all restrictions on competition which "are liable to affect trade between Member States" and were to succeed in enforcing this prohibition throughout the whole Common Market.

It is hardly realistic, however, to assume that the national governments will be prepared to give the EEC Commission the necessary comprehensive powers. In view of the Member States' different attitudes towards mergers and agreements between enterprises the EEC Commission is more likely to be forced to follow a cautious middle-of-the-road policy. The present disparities between the cartel policies in the various EEC countries will remain of considerable importance if the so-called "two-bound theory", advocated by the President of the Federal German Cartel Authority, should prevail. According to this theory countries with comparatively strict anti-trust rules can also prohibit agreements to which the EEC Commission has declared the prohibition as per Article 85, para 1, to be "not applicable" (in conformity with para 3 of the same Article). And the differences will be the more significant the more frequently the EEC Commission avails itself of this exemption clause in Article 85.

Competition in Growth

What impact on economic growth within the EEC can now be expected from the fact that considerable disparities are very likely to persist in the policies of competition, structure and growth in the Member States? Our answer is:

☐ The process of economic growth will presumably not follow a balanced pattern but will be marked by imbalances.

☐ It cannot be said with certainty, however, whether the rates of unbalanced growth will be greater or smaller than those of a balanced growth would be.

☐ Article 2 of the EEC Treaty aims at a "balanced" economic expansion within the integration area. What is to be understood by this? Certainly not a "participation of all economic sectors in this expansion", as is stated in one of the commentaries to the Treaty?[2] For structural change, which is involved in every economic growth and is caused by the uneven increase in demand and the unequal impact of technical progress, will always favour some sectors to an above average degree, while reducing sales and profits in others. A structural policy which puts emphasis also on social

[2] E. Wohlfahrt, H. J. Everling, B. Glaesner and B. Sprung: "Die Europäische Wirtschaftsgemeinschaft, Commentary to the Treaty"; Berlin-Frankfurt 1960, page 5.

policy can only delay a fall in incomes and the drift from sectors which are affected by the structural change, but it cannot prevent it in the long run.

It, therefore, appears to make more sense to interpret the meaning of "balanced economic expansion" as giving all Member States in the long run almost identical benefits from the growth impulses which the Common Market has created. A permanent and marked lagging of economic growth in one Member State behind the growth of the others must therefore be avoided. A balanced growth—and this means a uniform long-term trend of growth rates (without implying a complete identity of the rates)—offers the best guarantee for making the least possible use of the protective clauses of the EEC Treaty. [3]

How far can this aim be reconciled with the fact that the various Member States will, also in the foreseeable future, largely follow autonomous policies of competition, structure and growth?

There is the well-founded view that if important action-parameters in the field of economic growth continue to remain under the control of Common Market Members, this will lead to a "competition of growth between the States" (K. Stegemann), and this is a competition for markets and production factors which the EEC countries pursue by economic policy measures. The term "competition of growth" means that EEC Members will presumably compete by measures which promote economic growth and that they hasten growth in this way. [4]

A high growth rate of the gross national product is today, next to maintaining a comparatively stable level of prices, the most vital aim of economic policy in all EEC Member States. In the long run no government within the EEC can afford being criticised for having failed in this respect without seriously endangering its position. This is all the more so since in the case of an EEC country continuously lagging behind its partners in the competition of growth the result will be a drift of valuable elements of production from the competitively weak country to the competitively stronger EEC states. On the one hand, this may lead to widening the existing margins between the rates of growth. It may, on the other hand, lead to a determined demand for an intensified promotion of growth, because otherwise the failure of the economic policy of the weak competitor would become too obvious.

Since the measures taken by the various governments towards economic growth are not being centrally planned for the whole integration area and, most probably, may not even be sufficiently co-ordinated, the economic growth within the EEC will be unbalanced in two respects:

☐ In the first place disparities can hardly be avoided. In relation to the whole Market of the six integrated national economies surplus capacities may arise in certain fields and bottlenecks in others.

☐ Secondly, it is hardly probable that all Member States will conduct their policy of promoting growth with equal energy and success. Some countries have extensive resources for promoting economic growth. In other countries long-term planning of structure- and growth policies is still in its infancy. Some countries are conducting a comparatively strict anti-trust policy. Others widely tolerate the formation of trusts. Nor will all governments be equally successful in resisting the demands of certain sectors of the economy to take measures to preserve their structures and to conduct instead, a structure-policy which promotes speedy adjustment of output structure to the changes of non-economic factors.

Consequently the rise in real per capita income in the various countries will be probably greater than the differences in growth which result from the diversity of their resources and other "natural" elements of growth.

Mechanism of Adjustment

If the view is accepted that a continuance of considerable disparities between the Common Market policies of competition, structure and growth of the various governments favours an unbalanced growth in the above way, another question arises: could such an unbalanced growth release forces which have the effect of reducing or even removing in the long run the imbalances that have arisen? Such a "mechanism of adjustment" could become effective in three ways:

☐ In the first place, an adequately working market mechanism will ensure that temporary bottlenecks and surplus capacities resulting from insufficient ex ante-coordination will be removed or at least reduced. In the case of adequate mobility of production factors within the Common Market, chances for above average profits which exist in trades experiencing a strong excess of demand will attract additional output and this will in the long run lead to increasing supply. Conversely, supposing the national economic policy does not prevent contraction, there will be a drift away of trades with surplus capacities until here again an adjustment of supply and demand has been reached.

☐ Secondly, it can be assumed that governments which are less fortunate in their policies of economic growth will try to copy the policies of the more successful countries. They would, for instance, copy certain planning techniques. Stegemann has pointed out that the competition of growth between countries would thus be similar to the creative competition between enterprises—as described by Schumpeter. "Some governments (the "pioneers") try to secure a developing lead for the growth industries of their countries; other (the "imitators") promote the same industries in order not to lag behind, or even

3) See Art. 46; Art. 91, para 1; Art. 95; Art. 107, para 2; Art. 108 and 109, Art. 115 and Art. 226 of Treaty establishing the European Economic Community.

4 See K. Stegemann: Wettbewerb und Harmonisierung im Gemeinsamen Markt, Cologne 1966, Page 89 et sequ.

try to outstrip the others by stimulating still better methods and products; or they switch over to new fields of production which, at least temporarily, can offer them new advantages in international trade." [5]

☐ Thirdly, it is, of course, conceivable that productivity losses which with unbalanced growth are caused by wastage and can hardly be avoided, are generally regarded as so undesirable that even governments which still regard co-ordination as unduly restricting their scope will ultimately accept greater adjustment of their policies of competition, structure and growth.

The first two of the above-mentioned ways can effect only a belated correction to imbalances which have already become apparent and thus replace an insufficient ex ante-coordination by ex post-adjustment. The adjustment of policies of competition, structure and growth could, at least theoretically, prevent imbalances from the start, and this possibly within a programme of medium-term economic policy which is binding on all member countries. The problem we have discussed would then no longer exist, since its conditions would have disappeared.

Balanced and Unbalanced Growth

The conclusion that balanced growth is superior to unbalanced growth, since it makes a higher growth rate possible, can hardly be proved. The contrary is equally conceivable since advantages and disadvantages of both forms of growth can be shown. Most arguments in this matter are primarily relevant to developing countries. But some of the arguments can also be applied to the growth of highly developed national economies.

This applies to the view—taken by Streeten [6] and Hirschman [7]—that an unbalanced growth provides a stronger incentive to technical progress and net investment than the "unexciting" balanced growth which tempts people to maintain their traditional economic behaviour and to renounce new and creative initiative.

In other words: in the case of a balanced growth, productivity losses which result from parallel efforts may perhaps be avoided. The effect would be that the problem of the best possible allocation of given means of production (taking into account given production techniques) can at a certain time be solved to a larger extent than unbalanced growth would allow.

Also a uniform cyclical trend in the EEC countries, such as propagated by the advocates of the widest possible harmonisation of national economic policies, is not necessarily preferable to a development which is marked by alternating phases between different countries. For a reduced growth in important partner countries enables a country with a pronounced expansion of demand to limit the inflationary impact by rising imports from these countries and falling exports (measured by their growth rates) to them. In reversed order, the economy of the country whose growth rate has become temporarily weak will be strengthened by a mounting import demand of the country with a high growth rate. We are inclined to agree with Stegemann who in this context takes the view that such phase displacements could stimulate competition in oligopolitical markets: for "in case of a uniform economic trend in the common market closer links of solidarity would "ceteris paribus" develop between the enterprises; it would be simpler to stabilise the various market shares. In case of a generally full use of output capacity enterprises need not fear any effective competition of others; in case of generally poor employment the fear of causing ruinous competition or of being opposed as outsiders would largely make them refrain from aggressive competitive action". [8]

This result obtained under cyclical aspects may also be transferred to a consideration of growth problems. Thus an unbalanced growth could offer the advantage of making it more difficult to secure the oligopol peace by agreements which restrict competition. This widens the scope of competition. If static gains from allocation were not completely used up dynamic gains from growth could become possible and in certain circumstances these could more than compensate for the others.

It has to be emphasised, however, that these arguments are purely hypothetical. The fierce dispute between the followers of "balanced growth" and the supporters of "unbalanced growth" as the growth strategy of the developing countries shows that these suppositions must be regarded as still largely unproven.

Anyhow, the conclusion can be drawn that such temporary disparities in the structure of production as can probably not be avoided within the EEC owing to the competition of growth between the Member States need not necessarily impede growth; a constantly balanced growth, on the other hand, need not necessarily lead to the highest possible rate of growth.

[5] op. cit., page 105.

[6] P. Streeten, Economic Integration — Aspects and Problems, 1st Edition, Leyden 1961, page 96 et sequ.

[7] A. O. Hirschman: The Strategy of Economic Development, 9th Edition, New Haven — London 1965.

[8] K. Stegemann: Wettbewerb und Harmonisierung im Gemeinsamen Markt; Cologne 1966, page 132.