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Regional Integration in Europe

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Regional Integration in Europe

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1. Introduction

The European Community (EC) has evolved considerably since the Treaty of Rome was first implemented in 1958. To use the Euro-jargon, there has been much 'deepening' and 'widening'. From a mere customs union with six members, it has been transformed into a fully fledged single market with twelve members sharing common micro- and macro-economic policies. And by the end of the century, the Community should become an Economic and Monetary Union with fifteen or more members.

The foundation of European economic integration is internal trade liberalisation. The process of trade liberalisation within the EC has undergone three major phases. The first, starting in 1958, was the elimination of customs duties and quantitative restrictions. It was completed in 1968 with the introduction of a common external tariff. The second, between 1973 and 1986, witnessed successive enlargements from six to twelve members (see Table 1), but also reduced fervour for the elimination of internal trade barriers. The last, ending in 1992, is the completion of the internal market for goods, services, capital, and labour.

The purpose of this paper is to analyse the effects of European integration on trade and welfare. Analysis focuses entirely on merchandise trade. The remainder of the paper is divided into three parts. Section 2 examines the effects of EC integration on the extent and type of trade inside the Community. Section 3 studies the impact of EC integration on welfare and distribution both within and outside the Community. Section 4 concludes.

2. Effects of European economic integration on trade

The purpose of this section is to measure the effects of EC integration on trade flows. Two separate issues are considered. The first is the extent of regionalisation associated with European integration. The second issue concerns the relative importance of intra- versus inter-industry trade.

A. Extent of regionalisation

The extent of regionalisation is commonly measured with the share of intra-area trade in total trade, where trade refers to exports and/or imports. An increase in the intra-area share is taken as verification of the effect of regionalisation on trade flows. However, as Lloyd (1992) notes, this can only be considered as weak evidence since changes in the intra-area share capture many other effects besides integration.

The regional structure of total EC-12 merchandise trade for the period 1958-1991 is reported in Table 2.¹ For the moment examination will focus entirely on the first column,

¹ EC-12 refers to the present 12 EC members. Using EC-12 for the entire period avoids the problems of changing membership.

which shows the share of intra-EC trade in total EC trade. As far as exports are concerned, the figures confirm the three phases of integration presented in the Introduction. The share of intra-EC exports increased steadily following the Treaty of Rome, jumping from less than 40 percent in 1958 to nearly 55 percent in 1970. It remained roughly constant until 1985 and increased again thereafter, reaching over 60 percent in 1990.² The latter trend suggests a significant impact of the 1992 project.

The picture is similar on the import side, but here the composition of trade has added a strong price component to the evolution in the share of intra-EC trade. Whereas the EC exports mainly manufactures whose price fluctuates relatively little, she imports large quantities of raw materials which have undergone large price fluctuations during the period under investigation. The share of intra-EC imports for all merchandise commodities rose from 35 percent in 1958 to nearly 55 percent in 1973. It plunged below 50 percent in 1974-1976, after the first oil-shock, and again in 1980-1981, after the second oil-shock. There was a significant rise after 1985.³

A more instructive picture of the share of intra-EC imports can be obtained by focusing on processed products. This was done by Jacquemin and Sapir (1988a) who examined EC-10 imports for the period 1963-1983.⁴ They found that the share of intra-EC imports for all processed goods behaved differently before and after 1973.⁵ During the first period, there was a steady increase in the share from 51 to 61 percent. There was stagnation thereafter, with an eventual decline to around 58 percent. The figures at the bottom of Table 3 indicate that this trend has not been reversed to date.⁶ This would seem to contradict the 1992 effect detected above.⁷

Jacquemin and Sapir (1988a) also examined the evolution in the share of intra-EC imports for individual member states and individual industries or sectors (i.e. groups of industries). In the former, they observed an interesting convergence phenomenon between old and new members after the first enlargement in 1973. This resulted from a decrease in the share of intra-EC imports for the old members and an increase for the new.⁸

2 A year-by-year examination of the data confirms that 1985 corresponds to a structural break in the series. In 1981, 1982, 1983 and 1984 the intra-EC export share was 53.2, 54.4, 55.0 and 54.6 %, respectively. It was 57.4, 58.9, 59.8 and 60.2 %, respectively, for 1986, 1987, 1988 and 1989.

3 The intra-EC import share was 51.7 % in 1984 and 57.9 % in 1986.

4 EC-10 excludes Portugal and Spain.

5 Processed goods as defined here comprise the products of all the industries belonging to sectors 2, 3 and 4 of the NACE classification.

6 There is a slight difference in the composition of the EC between the Jacquemin-Sapir (1988a) study and Table 3. The latter pertains to EC-9 which, in addition to Portugal and Spain, also excludes Greece.

7 Using a somewhat different definition of processed products and looking at EC-12 trade flows, Lloyd (1992) also finds that the share of intra-EC imports has not significantly risen after 1985.

They also found important differences across sectors and industries. It turned out that the evolution observed at the aggregate level after 1973 was the result of three different trends: a declining share in engineering products (sector 3), stagnation in ore processing and chemicals (sector 2), and a rising share in other manufactures and processed agriculture (sector 4). The figures in Table 3 show that these trends have persisted until 1991.

Wide differences of behaviour across sectors and industries confirm that import shares are affected by factors other than EC integration. These include changes in external trade policy and competitiveness vis-à-vis non-EC members. Thus, the continuous decline in the share of intra-EC imports for footwear and clothing reflects primarily the changing comparative advantage of the EC in labour-intensive products. On the other hand, the steady rise in the intra-EC share for processed agricultural products is a reflection of the protectionist Common Agricultural Policy (CAP).

The only way to disentangle the effect of regional integration from other effects on intra-area trade shares is to regress these shares on a set of relevant variables. Such an exercise was conducted by Jacquemin and Sapir (1988b) who examined the 1973 and 1983 shares of intra-EC imports in four countries (France, Germany, Italy, and the United Kingdom) and across about one-hundred NACE 3-digit industries. Three findings from their regression analysis are particularly relevant in the context of the present paper. First, the accession of the United Kingdom to the EC has significantly increased the share of her imports from other member states between 1973 and 1983.⁹ This supports the hypothesis that EC integration has had a substantial impact on trade flows. Second, the presence of non-border barriers among EC members contributed significantly to lowering the share of intra-EC imports for products (such as telecommunications equipment) where scale economies matter. This finding was cited as evidence in support of the 1992 project for the completion of the European internal market.¹⁰ Finally, between 1973 and 1983, the CAP played an important role in boosting the share of intra-EC imports in processed agricultural goods, thereby confirming its increasingly protectionist effect.

In summary, it appears that the share of intra-EC trade has significantly increased since 1958. Although the evidence suggests a strong effect of EC integration, it also calls for two caveats. The first relates to the wide differences, across sectors, in the evolution of EC trade shares over time. These differences are accounted for by many factors, including external trade policy and competitiveness. The second concerns the numerous extensions of EC membership, which have played an important part in maintaining the momentum of integration at the level of EC-12.

⁸ A similar phenomenon occurred after the accession of Greece, Portugal and Spain. See also Lloyd (1992) who shows clearly the diverging trends in the share of intra-area imports for EC-6 and EC-12 after 1973.

⁹ The United Kingdom joined the EC in 1973.

¹⁰ See Commission of the European Communities (1988).

B. Intra-industry versus inter-industry specialisation

One of the most distinctive features of intra-EC trade liberalisation has been the growth of intra-industry trade. This feature was first noted by Balassa (1966). He showed that the early (1958-1963) expansion of intra-EC trade in manufacturing took the form of intra-industry rather than (as had often been assumed) inter-industry specialisation. This was confirmed over a longer period by Balassa (1975), whose results are reported in the left-hand panel of Table 4.¹¹ It shows a rapid increase in intra-industry specialisation in all member states following the Community's establishment. It also reveals that Italy stood somewhat apart from her partners.

Balassa's finding provoked great interest on the part of both conceptual and policy-oriented economists. It gave empirical support to the work by Linder (1961) and Drèze (1961), who had emphasized the importance of product differentiation in international trade among countries at similar levels of development.^{12,13} It also reassured policy-makers about the consequences of trade liberalisation among industrial countries. Indeed, Balassa's results indicate that such liberalisation is likely to entail only modest adjustment costs since it leads to specialisation within industries rather than movements of resources from import-competing to export industries.

A link between regional integration and intra-industry trade has been observed for other arrangements besides the European Community. It was therefore natural to examine whether there are reasons why economic integration may spur intra-industry trade to a greater extent than extra-industry trade. This task was performed by Greenaway (1989) who identified three channels which might establish a causal relationship between economic integration and intra-industry trade: overlapping demands, scale economies, and factor movements. Given the strong presence of all three channels in the Community, Greenaway (1989) concluded that there exists a deterministic link between EC integration and intra-industry trade. This conclusion was also reached by Balassa and Bauwens (1988) who have analysed the determinants of intra-industry specialisation in bilateral trade among European countries.

The importance of intra-industry specialisation in intra-EC trade has persisted over time, as confirmed by the figures in the right-hand panel of Table 4. These figures indicate that the extent of intra-industry trade has risen in nearly all EC countries between 1970 and 1987. At the end of the period, three layers of countries emerged in terms of the degree of intra-industry trade. At the bottom: Greece and Portugal; in the middle: Denmark, Italy, Ireland, and Spain; and at the top: Netherlands, Germany, Belgium-Luxembourg, the

¹¹ Similar results were obtained by Grubel and Lloyd (1975). These authors found that more than 70 % of the increase in intra-EC trade between 1959 and 1967 was in the form of intra-industry trade.

¹² Thus, the difference in the behaviour of Italy was ascribed to a lower level of industrial development.

¹³ It was also instrumental in the theoretical models of Krugman (1979), Lancaster (1980) and Helpman (1981).

United Kingdom, and France. In accordance with the previous discussion, the three layers correspond to three levels of industrial development.

The successive enlargements have resulted in a Community which now incorporates twelve members with a much greater variance in the level of industrial development than was the case among the original six. The result seems to have been, after 1980, a slowing down in the extent of intra-industry trade for the more industrialised members, which contrasts with the rapid increase in some of the less-developed members. Hence, the convergence phenomenon between old and new member states observed previously for the share of intra-EC trade in total EC trade appears to extend to the share of intra-industry trade in total intra-EC trade.

3. Effects of European economic integration on welfare and distribution

As Waelbroeck (1976) correctly warned, not too much interest should attach to the effects of economic integration on trade. The latter is an 'irrelevant variable', interesting simply because of its impact on the primary objectives of economic policy, welfare and income distribution.

This section examines the welfare and distributional consequences of the trade effects measured above. It is divided into two parts. The first explores the effects of EC integration on the welfare of the member states. The second analyses the effects on the distribution of income both internationally (between the EC and third countries) and inside the EC.

A. Effects on welfare and growth

The literature on economic integration traditionally distinguishes between static and dynamic effects. The former represent changes in the allocative efficiency of member states, taking their productive capacity as given. By contrast, dynamic effects measure the impact of integration on the productive capacity of member states.

Static effects

Economic integration is, by definition, a second-best proposition since it involves a shift from one protection-ridden situation (with equal protection against all countries) to another (with protection against non-partners and no protection against partners). Its welfare consequences are, therefore, an empirical matter which depends upon the particular configurations of individual schemes.

Traditional (Vinerian) customs union theory distinguishes between two welfare effects: trade creation and trade diversion.¹⁴ In any member state, integration reduces the price of

¹⁴ Viner (1950).

supplies from other union members relative to those from domestic producers, thereby creating trade at the expense of domestic production. At the same time, integration drives a wedge between the price of supplies from member and non-member countries, hence diverting trade from the latter to the former. Trade creation increases welfare, while in general diversion has a welfare cost. The net welfare effects of integration depend on the relative size of trade creation and trade diversion.

Although the second-best nature of economic integration prevents any abstract judgement about its welfare consequences, a presumption can be derived from considerations on the expected relative size of trade creation versus trade diversion. The following factors are generally considered in the economic literature as influencing positively the welfare effects of trade integration:¹⁵ a large number of members; a high proportion of intra-area trade before integration; low transportation costs among members; low common external protection.

What has been the record of EC integration in terms of trade creation and trade diversion? After a thorough review of the empirical evidence regarding the initial phase of EC integration, Balassa (1975) concluded that "*trade creation has been substantial in absolute terms and has exceeded trade diversion several times.*" (p.116). The conclusion only applied to manufactured goods; elsewhere the Common Agricultural Policy (CAP) produced severe trade diversion and welfare costs.

Balassa's view has continued to prevail throughout the 1970s and 1980s. This can be seen using Truman's methodology, which is based upon a decomposition of expenditure on apparent consumption into three shares: domestic production (net of exports), intra-EC imports, and extra-EC imports.¹⁶ For the period 1975-1982, Jacquemin and Sapir (1988a) found that cases of trade creation far outweighed instances of trade diversion in four member states. Table 5 extends the analysis for the period 1980-1991. The left-hand panel of Table 5 relates to all processed products.¹⁷ It shows that for EC-9 the share of consumption from domestic suppliers has steadily declined. At the same time, the shares supplied by EC partners and non-EC producers have both risen, a situation often referred to as 'double (internal and external) trade creation'. A drastically different picture is painted in the right-hand panel of Table 5, which focuses on processed agricultural goods.¹⁸ Here, some (internal) trade creation coexisted with (external) trade diversion from 1980 to 1985. Thereafter, only trade diversion was apparent.

What emerges from the above record regarding the impact of EC integration on welfare is the key role played by the common external trade regime. Where it has been liberal (generally in manufacturing), EC integration has been welfare-enhancing. On the

15 See Balassa (1987) and Hazlewood (1987).

16 Truman (1975).

17 Sectors 2,3 and 4 of the NACE classification.

18 Industry 41-42 of the NACE classification.

contrary, where the trade regime has been highly protectionist (most notably in temperate agriculture), integration has generated welfare costs.

Community participation in successive GATT rounds has been crucial in shaping her external trade regime in manufacturing. Her active role in multilateral trade negotiations was dictated partly by her own liberal charter and partly by the insistence of her trade partners, most notably the United States.

European integration was the main driving force behind the Dillon and Kennedy rounds of multilateral trade negotiations which produced substantial tariff reductions. Table 6 shows the average tariff rates in the EC member states in 1958 (before entry), in 1968 (after entry and after the Dillon Round), and after the Kennedy Round. The figures indicate that, together with integration, the two GATT rounds not only substantially decreased the EC-wide average tariff (from 13 to 6.6%), but also restored the average German tariff to its low initial level.

The above evidence suggests that the process of EC integration was a catalyst in the reduction of Europe's external protection. This view seems to be shared by most authors.¹⁹ For instance, Hufbauer (1990) states that *"France and Italy, in particular, would have strongly resisted making any trade concessions in the 1960s, and Germany would not have made trade concessions in isolation from its continental partners."* (p.5). Regarding France, Messerlin (1992) notes that the *"first impact of the Treaty of Rome was to impose...[a] macroeconomic environment [which] allowed the progressive opening of the French economy...As a result, the protection granted to the French manufacturing sector vis-à-vis both the Community and the rest of the world...decreased during the 1960s."* (p.159).

The simultaneous lowering by the EC of her internal and external protection in manufacturing did not end with the Kennedy Round in the late 1960s. The first enlargement of the EC, in 1973, was followed by multilateral tariff cuts on manufactured goods during the Tokyo Round, which was completed in 1978. And the third enlargement, in 1986, was immediately followed by the launching of the still-unfinished Uruguay Round.

The situation in agriculture has run counter to that in manufacturing, with trade diversion far exceeding trade creation. The root of the problem lies with the *de facto* exclusion of most of temperate agriculture from the GATT. The trade-diverting effect of the Common Agricultural Policy has progressively increased with each successive EC enlargement. In the early 1980s, the staggering costs of trade diversion provoked a rising opposition both within and outside the Community. The outcome was the inclusion of agriculture in the Uruguay Round with the view to extending GATT discipline to this area. Failure by the EC and her trade partners to reach agreement in agriculture has, so far, prevented a

¹⁹ For a dissenting view, see Winters (1992).

successful conclusion of the Round. The EC reforms of the CAP (the so-called MacSharry plan) approved in mid-1992 should, however, open the door toward such agreement.

As yet, only two welfare effects have been considered, namely trade creation and trade diversion. In the presence of scale economies, however, Corden (1972) has shown that two additional welfare effects can be expected: cost reduction and trade suppression. The first arises if integration increases the scale of existing domestic production. In this case, specialisation results in lower average costs of domestic supplies. Cost reduction is, therefore, welfare-improving for the domestic economy and for the union as a whole. Trade suppression occurs when imports from outside the union are replaced by newly established domestic supplies which, despite the fall in average costs due to integration, would not survive without protection. The latter effect is akin to trade diversion: it is detrimental to the union's welfare because a costlier source replaces a cheaper one. Like trade diversion, its magnitude depends crucially upon the external trade regime. The more protectionist the regime, the greater the extent of trade suppression.

Attempts to measure the cost reduction and trade suppression effects of EC integration have been few. The most significant *ex post* contribution is by Owen (1983), who found that cost reduction has been substantial for the original six EC-members. In its *ex ante* study on the impact of 1992, the Commission of the European Communities (1988) also found that the completion of the internal market would produce a large welfare-enhancing cost reduction effect.

Dynamic effects

It has long been postulated that economic integration produces substantial growth effects through better exploitation of scale economies and greater competition resulting in higher productivity. These effects received much attention in early writings on EC integration by Scitovsky (1956), Allais (1960), and Balassa (1961). But measurement difficulties have generally precluded *ex post* attempts to evaluate their importance. This is unfortunate since there seems to be a consensus that dynamic effects are far larger than static ones.²⁰ An interesting exception is the work by de Melo, Panagariya and Rodrik (1992) who present cross-country regressions of per capita income growth on several explanatory variables, including membership in regional trade integration schemes. Their results suggest that EC membership has had no impact (either positive or negative) on per capita income growth.²¹

20 It has been estimated that the welfare gain associated with trade creation in manufactured goods amounts, for the EC, to 0.15 % of GNP. See Balassa (1975).

21 One of the explanatory variables used in the regressions is the share of investment in GDP, which is likely to be positively correlated with EC membership. The ordinary-least-square procedure employed by the authors is, therefore, biased against finding a positive effect of EC membership on growth.

Dynamic effects lie at the heart of the 1992 project. Efforts to measure their size have been attempted in the *ex ante* studies by the Commission of the European Communities (1988) and Baldwin (1989). The Commission's report focused on one-time effects on productivity and output and estimated 1992 will raise EC output by between 2.5 and 6.5 percent. By contrast, Baldwin measured the truly growth effect to be had from the completion of the internal market. Using a calibrated endogenous growth model, he found that 1992 might permanently add between one-quarter and nine-tenths of one percentage point to the EC growth rate.

Economic integration is, obviously, not the only channel available to raise the level of competition and produce growth effects in the European Community. An alternative (or, at least a complement) to internal trade liberalisation may be external trade liberalisation. A recent study by Jacquemin and Sapir (1991a) sheds some light on this issue. These authors have examined the relative trade discipline effects of intra- and extra-EC imports (actual as well as potential) on an index of competition, price-cost margins. Regarding actual imports, the study finds that only extra-EC trade flows exert a significant competitive effect. On the other hand, it confirms the pro-competitive effect expected from the removal of intra-EC trade barriers. These results suggest that the combination of internal and external trade liberalisation may be a superior strategy to internal liberalisation alone as far as growth is concerned. Hence, although some external liberalisation follows automatically from the 1992 programme, such strategy should be actively pursued.

B. Effects on income distribution

European integration affects the distribution of income, not only between the EC and third countries, but also inside and between member states.

International distribution of income

The effect of EC integration on non-member countries is directly related to the static and dynamic effects examined previously.

Since the European Community is obviously a 'large' economic entity, her existence affects international trade prices. As a result, trade diversion and trade suppression involve not only a welfare loss to member states, but also a gain resulting from an improvement in the EC's terms of trade. The latter is due to the shift in EC demand away from products originating in third countries which causes a fall in their relative price. Obviously, this terms-of-trade effect is a zero-sum game: a gain for the EC necessarily implies a loss for third countries.

It has often been suggested that improvements in the terms of trade provide a strong incentive for the establishment of regional trade arrangements. In the case of the EC, the only empirical study available is by Petith (1977), who used an *ex ante* methodology to determine the terms of trade gains resulting from integration in manufactured products. He found that the gains from terms of trade improvements far exceed the existing

estimates of trade creation.²² Hence the conclusion that: "*the improvement of the terms of trade, as well as being the principal economic effect, was also one of the major goals of the integration of trade in manufactures by Western Europe.*" (p.272).

Although the paper by Petith is frequently cited in the economic literature, it contains a major flaw which seems to have gone unnoticed. Its central result rests on "*the rather strong assumption that the common external tariff of the union is exactly half-way between [the] initial tariffs [of its members].*" (p.264).²³ In other words, the height of the EC-wide average tariff is assumed to have been the same before and after the establishment of the Community. This completely ignores the substantial cuts in the common external tariff which resulted from the Dillon and Kennedy rounds.

In fact, the previous discussion on the figures in Table 6 suggests that, with respect to manufacturing, the EC meets the Vanek-Kemp-Wan test.²⁴ She has sufficiently lowered her common external tariff to ensure that the rest of the world is, in general, at least as well off as it would have been, *ceteris paribus*, in the absence of integration. Regarding agriculture, however, there is broad agreement that the CAP has been welfare-deteriorating for agricultural exporting nations as a result of its depressing effect on certain commodities.

Turning to dynamic effects, there is a general consensus that non-member countries have gained collectively from the income effects associated with EC integration, via the increased demand for their exports. The effects differ among countries, depending upon the income elasticity of their exports to the EC.

On the whole, therefore, considering both static and dynamic effects, it appears that EC integration has generally benefitted third countries. The major exception concerns nations which specialise in temperate agricultural products covered by the CAP. *Ex ante* studies suggest that 1992 will have a similar positive effect, especially if the Uruguay Round succeeds in extending GATT rules to new areas (such as services) covered by the internal market project.²⁵

Distribution of income inside the EC

Successive enlargements have considerably modified the distributional aspects of EC integration. Before the first enlargement, the Community was a fairly homogeneous group of countries in terms of factor endowments. Integration resulted, therefore, in an increase

²² Petith's estimates of the gains from terms of trade improvements range from 0.3 to 0.9 % of GNP, which is considerably more than the 0.15 % referred to in footnote 21.

²³ For simplicity, Petith assumes that the EC comprises only two members, one with low initial tariffs (Germany) and the other with high initial tariffs (France). Hence the term 'half-way'.

²⁴ Vanek (1965) and Kemp and Wan (1976).

²⁵ See Sapir (1990) and Hufbauer (1990). There are some fears, however, about the impact of 1992 on developing countries. See Koekoek et al. (1990).

of intra-EC trade predominantly in the form of intra-industry flows. This meant relatively modest income redistributive effects within member states, as their industrial structure was little affected by intra-industry specialisation.

The situation has radically changed with the accession of new members to the Community. The EC is now divided into a North (with a per capita GDP above the EC-12 average) and a South (with a per capita GDP below the EC-12 average), the latter comprising of Greece, Ireland, Portugal, and Spain.²⁶ This has tended to give relatively greater importance to inter-industry specialisation associated with exploitation of comparative advantage.²⁷ In turn, such specialisation may be causing more adjustment problems than past integration.

In addition, the new Community configuration raises the crucial issue of the linkage between economic integration and inter-country income disparities. Two opposite views prevail. Those who believe in the neoclassical paradigm, adopt an optimistic attitude. This is the case of Neven (1990), who examined the distribution of the benefits from 1992 among member states. He found relatively small gains for the North, but important ones for the South. On the other hand, those who attach more importance in the role of non-convexities in shaping economic outcomes, are less optimistic about the automaticity of convergence inside the EC. For instance, the theoretical analysis by Bertola (1992) suggests that a tendency towards production concentration in the North can be expected in post-1992 Europe if economic growth is driven solely by private investment decisions.

Mindful of the convergence issue, the Community has undertaken large income transfers from the North to the South. Today, such transfers account for about one-quarter of the EC budget and represent a substantial proportion of the South's investment in physical infrastructure.

4. Conclusion

At the end of the day, the evidence strongly suggests that the process of EC integration has been beneficial to both the Community itself and her trading partners. This favorable outcome is, to a large extent, due to the fact that integration has led to substantial multilateral trade liberalisation, beyond what could have materialised without the EC. As Lawrence (1991) noted: *"The postwar experience of the EC is heartening. Increasing European integration after the Treaty of Rome was quite compatible with the lowering of Europe's external barriers."* (p.26). The obvious exception is temperate agriculture, where increasingly high levels of external protection have produced great costs.

²⁶ Based on purchasing-power comparisons. See European Economy, No.50, Table 9.

²⁷ Neven (1990).

Some might, however, wonder whether the EC is likely to maintain her active support in favour of the multilateral trade system. Those who worry point to two developments. The first concerns the network of regional agreements built around the EC and described in Table 1. Half the share of extra-EC trade is accounted for by trade with regional partners: EFTA, eastern Europe and southern neighbours (Mediterranean and ACP countries). If one adds this to the share of intra-EC trade, one can observe that roughly 80 percent of EC trade is intra-regional (see Table 2). The second concern relates to the parallel movement towards regionalism in America and Asia.

The emergence of a tripolar world raises vital questions. In the coming years, regionalism can either contribute to or be detrimental to the multilateral trading system. As Jacquemin and Sapir (1991b) remarked, the outcome will depend upon which of the 'natural integration' or 'strategic integration' scenarios will prevail. The former refers to a situation where natural trading (i.e. regional) partners form a trading arrangement with an open external trade policy, which benefits the world at large. On the contrary, the latter implies an arrangement aimed at making gains at the expense of other nations. If the three blocs decide to play a noncooperative game, natural integration would be used as leverage for strategic conduct, with detrimental consequences for all.

The construction of the European Community is a noble, but difficult task. Has it been successful? The answer is, undoubtedly, yes. The EC has contributed to create a zone of peace in a continent which had been torn apart by two world wars and where nationalism is always latent. It has also brought prosperity to its citizens. However, as with any such endeavour, there is always a risk that the architects may lose sight of the global picture and fall prey to 'eurocentrism'. So far, the Community has avoided this danger by generally pursuing a liberal external trade policy. As it moves towards deeper and wider integration, the EC should strive to reinforce its commitment toward the multilateral trade system in order to ensure cooperative solutions.

Table 2

The Regional Structure of EC-12 Trade, 1958 - 1990 (As percent of total EC-12 trade)												
Partners												
Year	Western Europe				Eastern & Southern Neighbours				Rest of the World			
	EC-12	EFTA	TOTAL	Eastern Europe	Neighbouring Countries	ACP	TOTAL	Developing Countries	Industrial Countries	TOTAL	TOTAL	
1958	37.2	12.2	49.4	2.7	7.8	6.6	17.1	15.3	18.2	33.5	100.0	
1965	49.6	13.0	62.6	2.9	4.8	4.4	12.1	9.4	15.9	25.3	100.0	
1970	53.4	11.7	65.1	3.4	4.8	3.6	11.8	7.1	16.0	23.1	100.0	
1975	52.4	10.6	63.0	4.9	6.7	3.6	15.2	9.6	12.2	21.8	100.0	
1980	56.1	11.2	67.3	3.5	5.9	3.5	12.9	9.2	10.6	19.8	100.0	
1985	55.2	10.0	65.2	2.8	5.2	2.3	10.3	8.7	15.8	24.5	100.0	
1990	61.2	10.4	71.6	2.3	4.2	1.6	8.1	7.3	13.0	20.3	100.0	
1958	35.2	9.3	44.5	2.9	4.5	6.8	14.2	19.2	22.1	41.3	100.0	
1965	44.9	9.0	53.9	3.4	4.7	5.2	13.3	12.7	20.1	32.8	100.0	
1970	50.3	8.7	59.0	3.2	4.7	4.4	12.3	10.3	18.4	28.7	100.0	
1975	49.5	7.9	57.4	3.5	3.8	3.8	11.1	16.3	15.2	31.5	100.0	
1980	49.3	8.6	57.9	3.7	4.2	3.8	11.7	15.6	14.8	30.4	100.0	
1985	53.4	9.4	62.8	3.9	5.1	3.5	12.5	9.8	14.9	24.7	100.0	
1990	59.0	9.6	68.6	2.7	3.8	1.8	8.3	8.2	14.9	23.1	100.0	

Source: Eurostat

Table 3

	Commodity Group	1980	1985	1987	1989	1991
22	metal processing	52.2	54.0	55.5	54.7	54.2
24	mineral processing	76.2	73.5	74.1	72.1	69.3
25-26	chemicals	70.0	67.9	69.0	67.2	66.8
2		62.3	63.2	64.9	62.9	62.8
31	metal articles	69.6	68.7	69.2	67.2	66.7
32	mechanical engineer	65.7	61.1	62.8	61.8	60.9
33	office machines	49.4	50.0	51.3	50.3	49.5
34	electrical products	54.6	49.6	51.5	49.6	49.2
35	motor vehicules	77.6	71.3	72.5	70.6	68.5
36	other transport equ	32.9	39.9	43.9	48.8	47.3
37	precision instrumen	47.2	43.7	47.0	45.4	46.3
3		60.9	57.1	59.5	57.7	56.7
41-42	food, drink and tob	62.3	65.1	68.8	69.7	71.5
43	textiles	57.6	58.8	55.2	52.5	49.6
44	leather products	43.7	46.2	42.6	38.7	36.8
45	footwear and clothi	48.9	47.0	43.2	40.3	37.7
46	wood and products	35.2	39.3	40.8	41.4	44.6
47	paper and products	42.7	44.8	46.0	44.6	47.8
48	rubber and plastic	75.9	73.8	74.1	71.7	70.7
49	other manufactures	22.7	27.1	31.2	37.6	38.5
4		49.4	52.6	53.1	52.4	53.1
Total		57.3	57.2	58.6	57.3	56.9
EC-9.						

Table 4

Share of Intra-Industry Trade in Intra-EC Trade (As percent of total intra-EC trade)						
Country	1958(*) (1)	1963(*) (2)	1970(*) (3)	1970(**) (4)	1980(**) (5)	1987(**) (6)
Belgium-Luxembourg	0.54	0.60	0.66	0.69	0.70	0.77
Denmark	-	-	-	0.41	0.52	0.57
France	0.61	0.68	0.73	0.76	0.83	0.83
Germany	0.47	0.57	0.67	0.73	0.78	0.76
Greece	-	-	-	0.22	0.24	0.31
Ireland	-	-	-	0.36	0.61	0.62
Italy	0.42	0.48	0.59	0.63	0.55	0.57
Netherlands	0.50	0.57	0.64	0.67	0.73	0.76
Portugal	-	-	-	0.23	0.32	0.37
Spain	-	-	-	0.35	0.57	0.64
United Kingdom	-	-	-	0.74	0.81	0.77

(*) computed with EC-6 trade data, (**) computed with EC-12 trade data.

Sources: Balassa (1975) for columns (1) (2) and (3), and Buigues et al. (1990) for columns (4) (5) and (6).

Table 5

Shares of EC-9 apparent consumption accounted for by three sources (in percent)											
Year	All processed products					Food, drink and tobacco					
	Domestic Production	Intra-EC Imports	Extra-EC Imports	TOTAL		Domestic production	Intra-EC Imports	Extra-EC Imports	TOTAL		
1980	66.7	19.1	14.2	100.0		82.1	11.1	6.7	100.0		
1981	65.3	19.6	15.1	100.0		81.4	11.6	7.0	100.0		
1982	64.3	20.5	15.2	100.0		81.1	12.0	6.9	100.0		
1983	63.8	20.7	15.5	100.0		81.4	11.7	6.9	100.0		
1984	61.6	21.5	16.9	100.0		80.6	12.1	7.3	100.0		
1985	60.6	22.6	16.9	100.0		79.9	13.1	7.0	100.0		
1986	61.2	22.6	16.2	100.0		81.1	12.9	6.1	100.0		
1987	60.5	23.2	16.4	100.0		81.0	13.1	5.9	100.0		
1988	58.8	23.5	17.7	100.0		80.0	13.8	6.2	100.0		
1989	57.1	24.6	18.3	100.0		79.9	14.0	6.1	100.0		
1990	57.4	24.5	18.1	100.0		80.5	13.7	5.8	100.0		
1991	56.1	25.0	18.9	100.0		80.1	14.2	5.7	100.0		

Source: Own computations based on Eurostat data.

Table 6

Average Tariff Rates in the European Community Before and After Integration (In percent)			
Country	1958	External Tariff in 1968	External Tariff after the Kennedy Round
Benelux	9.7	10.4	6.6
France	17.0	10.4	6.6
Germany	6.4	10.4	6.6
Italy	18.7	10.4	6.6
Simple average	13.0	10.4	6.6
Change from previous level	-	-20%	-40%

Source: Resnick and Truman, (1975), Table 2.4.

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