Parliamentary Assembly
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COUNCIL OF EUROPE
CONSEIL DE L'EUROPE

Doc. 801
11 April 1958

European Free Trade Area

Report[1]
Committee on Economic Affairs and Development
Rapporteur: Mr John HAY, United Kingdom

1. 1958 - 10th Session - First part

A. Draft Recommendation

The Assembly,

1. Recalling that by paragraph 2 of its Recommendation 152 of 29th October 1957 it expressed its conviction that the creation of a Free Trade Area including the European Economic Community was essential to the development of a unified European economy;

2. Noting that the Treaty establishing the European Economic Community came into force on 1st January 1958;

3. Noting the progress made in the negotiations in the Intergovernmental Committee of the 0. E. E. C. for a Free Trade Area, and that provisional solutions to a number of important problems appear to have been reached already;

4. Noting that a solution to the problem of trade in agricultural and fishery products is being sought on the basis of a draft Agreement directed to the expansion of such trade and the co-ordination of policies, to be linked to a Free Trade Area Convention as suggested by the Assembly in paragraph 9 of its Recommendation 152;

5. Expressing its appreciation of the fact that the views of the Assembly as set out in its Recommendation 152 have been forwarded by the Committee of Ministers to the Council of the 0. E. E. C, and have been taken account of by the Intergovernmental Committee;

6. Noting that alternative proposals, to solve the overall problem of associating States which are not members of thè European Economic Community with the Common Market, have recently been made by the Government of France, and are at present under discussion in the E. E. C; and also that suggestions have been made by the Government of Italy designed to minimise the problems of deflection of trade;

7. Considering that, despite the absence of detailed information concerning these proposals, enough is known to permit the Assembly to offer general observations upon the problems which have prompted those proposals and suggestions;

8. Believing:

a. that no serious disequilibrium as between rights devolving upon and obligations to be undertaken by Member States is inherent in the conception of a Free Trade Area to such, an extent as to render participation economically dangerous or hazardous for any Member;

b. that problems of harmonisation of social charges and other factors affecting costs and prices of goods to be traded in a Free Trade Area do not appear so difficult as to be an insurmountable obstacle to the foundation and successful working of such an Area;

c. that an examination of the related problems of origin rules and the diversion of trade indicates that these difficulties will not present themselves in any acute form from the outset and that it should be possible gradually to work out solutions to meet them as they emerge, without requiring detailed a priori remedies to compensate all or any of the Members or to guarantee them against losses;

d. that special measures would be required for the economically less developed countries.

9. Recommends to the Committee of Ministers that it should urge the Council of 0. E. E. C.

a. to seek solutions to the problems outstanding in the negotiations for a Free Trade Area, taking account of the legitimate preoccupations of countries or groups of countries, in a spirit of compromise rather than allowing conflicting interests to result in rigid and doctrinaire negotiating positions;

b. to keep firmly in mind the ultimate objective of associating the Common Market of the Six with the other member countries of 0. E. E. C. by means of a multilateral agreement, based on the fundamental principles of reciprocity and non-discrimination laid down in the OEEC Convention of 1948;

c. to make every effort to achieve the greatest possible measure of synchronisation in the development of the Free Trade Area and the Common Market compatible with the vital economic interests of each of the member countries, of the overseas countries and territories associated with the Common Market and those constitutionally linked with other member countries of the 0. E. E. C;

d. to provide the necessary safeguards to ensure that the European economic system to be set up will not, either in the short term or in the long term, inflict damage on the trade of countries which are traditionally suppliers of European markets or which traditionally provide markets for European goods.

B. Explanatory Memorandum

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1.1. Introduction

1. The last debate of the Consultative Assembly on the European Free Trade Area in October 1957 coincided with a number of important decisions on this matter by the Council of 0. E. E. C. With these decisions the 0. E. E. C. passed from the exploratory phase to the decisive phase of negotiations at ministerial level. These negotiations are still going on, and, while it is known that provisional agreement has been reached on many of the complex problems involved, it is also common knowledge that profound divergences remain on other points.

2. At the time of writing, the time-table of the negotiations—and, in the view of some, their very outcome—appears to be in danger. On the one hand, there is the statement by the Chairman of the Intergovernmental Committee, Mr. Maud-ling, that he hoped that the necessary political groundwork at ministerial level would be completed at the mid-March meeting of the Committee and that by early April the drafting committees could begin their work[2]. On the other, there is the announcement that the French Government is consulting its partners in the Common Market upon alternative proposals for the creation of what is termed in the press a " European Union of Economic Co-operation ". The French proposals appear to represent a radically different approach to the problem of associating the other OEEC countries with the Common Market.

3. The following explanatory memorandum is divided into four parts.

4. In the first part, the course of the negotiations is described and the points set out on which substantial agreement appears to have been reached.

5. In the second, an attempt is made to set out the major points still at issue as objectively as possible and to comment on them.

6. The third part examines the counterproposals recently put forward by the French Government and certain proposals for the harmonisation of external tariffs made in the Intergovernmental Committee by the Italian Government.

7. The fourth part breaks new ground with a matter which appears not yet to have been considered by the Intergovernmental Committee —the possible repercussions of the planned Free Trade Area on world trade. This question appears to be one on which the prior views of the Assembly might well be valuable to the negotiators when they come to deal with it and would enable it once more to perform its advisory function.

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2. See The Times, 19th February 1958.

1.1.1. The OEEC Negotiations

8. The Resolution of the Council of 0. E. E. C.[3] on the European Free Trade Area and problems linked therewith, unanimously adopted on 17th October 1957, contained four major decisions:

8.1. a declaration of the Council's " determination to secure the establishment of a European Free Trade Area " which would comprise all OEEC countries, associating the European Economic Community with the other OEEC countries on a multilateral basis, and which would " take effect parallel with the Treaty of Rome ";

8.2. a similar declaration of intent to reach agreement at the same time on methods of cooperation in agricultural matters with a view to ensuring an expansion of trade in this sector;

8.3. a further declaration of intent to take full account of the interests of the economically less-developed member countries; and, finally,

8.4. a decision to set up an Intergovernmental Committee at ministerial level to carry on the negotiations, of which Mr. Reginald Maudling (United Kingdom) was appointed Chairman.

9. Three points emerge, which deserve stressing.

9.1. First, the determination expressed in Resolution 221 had the support of all the OEEC countries, including the six signatories of the Rome Treaty.

9.2. Second, the negotiations on the Free Trade Area, on agricultural problems and the problems connected with the economically less developed countries, though they were to proceed separately, were envisaged as part and parcel of the same negotiation.

9.3. Third, the Free Trade Area was to take effect parallel with the Treaty of Rome, i.e. on 1st January 1959.

10. The negotiations have since proceeded on the basis of an Annotated Agenda, prepared/ by the Chairman in the light of the earlier negotiations, adopted by the Intergovernmental Committee, and listing the range of questions divided into five groups[4] on which agreement must be reached. The Committee has since held eight, usually two-day, meetings up to early April.

11. As indicated earlier, broad agreement has been reached on a substantial number of points, though many technical matters have been referred to expert groups for further study, and agreement in principle on any particular point does not constitute a final commitment on the part of any Government, since no over-all view of the many problems involved is possible until the whole Agenda has been dealt with.

12. With regard to problems of freeing trade, it may be said, briefly, that almost all the countries taking part in the work of the Intergovernmental Committee are agreed to adopt roughly the same time-table and the same rules as the Rome Treaty for the reduction of tariffs and the elimination of quantitative import restrictions. In this connection it was also agreed from the start that the problem of the definition of the origin of goods admitted to Free Trade Area treatment should be approached in a liberal spirit, while at the same time account would be taken of the necessity for avoiding deflections of trade and economic activity which might otherwise result from disparities in the external tariffs of member countries. As will be seen, the French and Italian proposals would substantially modify the situation on both these points.

13. Agreement in principle has also been reached on the necessity for providing rules of competition in the Free Trade Area Convention. These would relate, inter alia, to Government aids, quantitative export restrictions—which should be rapidly abolished—and restrictive business practices in private enterprise. It has also been agreed that the Convention should contain provisions regulating the activities of public undertakings on the lines of the corresponding rules of the Rome Treaty, and that rules on dumping would also be required.

14. Further, it has been agreed that institutional arrangements, probably involving majority decisions in certain clearly-defined cases, will be needed to ensure close co-operation in matters of general economic and financial policy, and that the existing arrangements within the 0. E. E. C. shall serve as as a starting-point for the study of this matter. (Nevertheless the whole question of institutions has, by agreement, been deferred until a later stage in the negotiations). It has also been agreed, in principle, to abolish all obstacles to current

3. Resolutio n 221, 17th October 1957 (Doc. AS/Ec <9) 20).

4. (1) Problems of freeing trade ; (2) Agriculture and Fisheries ; (3) Economic and Financial Questions; (4) Problems of Particular Sectors (e. g. Coal and Steel) ; (5) Constitutional Questions.

invisible transactions during the transitional period, and to examine what provision must be made with regard to capital movements in order to obtain the full advantages expected from the liberalisation of goods and services.

15. Finally, the Committee agreed in principle that the economically less developed countries should be exempted for a certain time from some commitments and that special measures would be required to help them. In this connection, it was decided to study the question of development finance for these countries.

16. While this enumeration of the points on which broad agreement has been reached is not exhaustive, it is believed to give a fair picture of the positive results of the negotiations. It is important to note the close similarity between the principles agreed on for the Free Trade Area and those embodied in the Rome Treaty, and it may be added that on several points it appears that the Intergovernmental Committee has already reached the drafting stage.

17. On a number of other problems, however, little progress has been achieved in the course of the negotiations, and deep-rooted divergences remain.

18. The three most controversial questions appear to be the content of the agricultural agreement, the problem of harmonisation, and the question of deflection of trade. Difficulties also appear to subsist on a number of important, but perhaps secondary, problems, such as the freeing of capital movements, freedom of movement of workers, the right of establishment, and with regard to the problem of non-discrimination in transport.

19. Although the outstanding problems have all been discussed separately and on their own merits, according to the agreed procedure, there has been a tendency in public discussion of these matters in France to link them—and particularly the first three—with certain other objections to the Free Trade Area formula of a more abstract nature: an absence of balance or equilibrium of obligations and rights within the Free Trade Area as compared with the Common Market, and an incompatibility between the Free Trade Area and the European Economic Community. The exact content of the counter-proposals which these misgivings on the Free Trade Area formula have led the French Government to put forward has not been published at the time of writing, but apparently reliable summaries have appeared in the press. Since they constitute the only Government-sponsored alternative to the Free Trade Area, this Report will next examine the objections to the Free Trade Area formula which have given rise to the French counter-proposals, and then the contents of the proposals themselves. It will, however, be borne in mind that they are, as stated above, being discussed by the Six, and what may emerge from those discussions may be yet another alternative plan which would then be the proposals of the Six.

1.1.2. The Main Issues

1.1.2.1. Agriculture

20. The problem of agriculture and fisheries and of intra-European trade in products in this sector in the Free Trade Area was discussed at considerable length in the Report[5] presented by the Economic Committee to the Assembly in October last, and need not therefore be gone into again here. It will be recalled that the Report took a moderately optimistic view of the possibilities of reaching compromises on this issue and that the Recommendation adopted by the Assembly at the close of the October debate contained a series of suggestions on how the problems could most pr ofitably be approached[6].

21. In particular, the Report argued that the problem was not a clear-cut issue of " free trade " versus " protection ", and hence could not be discussed in summary terms of " including " or " excluding " agriculture. On the whole, it would appear that this truth has now been generally recognised, and that the problem of agriculture is now almost generally viewed as a matter of ensuring sufficient reciprocity in the Free Trade Area to countries more or less heavily dependent on agricultural exports without violently disrupting national agricultural policies. Almost all these involve a considerable degree of protectionism, and none of the countries concerned are prepared rapidly to modify them to any great extent.

22. Yet agriculture remains one of the most important points at issue in the Free Trade Area negotiations. How have the issues evolved in the course of the negotiations, and where do the lines of division appear at the present time?

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5. Doc; 698, Report of the Economic Committee on the Free Trade Area, 18th September 1957.
6. Recommendation 152, para. 9 (in) (a) — (g).

23. The acceptance by the United Kingdom of the paragraph relating to agriculture in the Resolution of 0. E. E. C. referred to earlier constituted at least some modification of its original position on agriculture. It certainly indicated a willingness to reach an agreement on agricultural questions to ensure an expansion of trade in this sector. On the other hand, this decision did not commit the British Government to eliminate or reduce its remaining tariffs on agricultural products for the benefit of its Free Trade Area partners in any way that might interfere with Commonwealth preferences.

24. It has been known for some time that the British Government placed its hopes for solving the agricultural problem on building up the Ministerial Committee for Agriculture and Food attached to the 0. E. E. C. This Organisation, created in 1954, had already in 1956 and 1957 adopted two potentially far-reaching Resolutions; on the confrontation of general agricultural policies, and the co-ordination of price and other support policies[7]. Its members had simultaneously agreed on certain basic objectives: to increase productivity and bring about freer intra-European trade in foodstuffs while securing adequate standards of living for the farming and fishing communities and a reasonable degree of market stability.

25. Starting from here, the British Government in January last[8]tabled for discussion a draft Agricultural Agreement which would aim at these objectives and in addition provide certain rules for trade along the following lines:

25.1. an undertaking to " freeze" existing quantitative restrictions and to draw up a joint plan to secure the gradual elimination of such restrictions on imports whether in private or State-controlled trade;

25.2. special measures to develop trade on a non-discriminatory basis, concentrating on the conclusion of commodity arrangements, and leaving the issue of tariff reduction for further study; and

25.3. the prohibition of export subsidies on foodstuffs where they result in export prices being lower than domestic prices, or would otherwise result in giving a country a larger share in export markets than that country has enjoyed in an earlier base period.

26. While all decisions would remain the prerogative of the OEEC Council voting by the unanimity rule, the British proposal envisages the creation of a Board, an Advisory Committee to undertake an Annual Review of Production, Prices and Trade, and a Complaints panel, all making recommendations by majority voting. The Board would undertake the task of " confrontation " and co-ordination of policies, and would examine the possibilities of freeing, and expanding trade on a " product by product " basis.

27. That these proposals represent an evolution of the original British position can hardly be denied. Nevertheless, they are known to be considered inadequate by a number of the United Kingdom's partners in the OEEC negotiations. The question therefore arises whether the criticisms directed against the British proposals is justified. In examining this question, the problem as viewed by the European Economic Community will be discussed separately, and the question of reciprocity, which affects certain of the six countries as well as other OEEC countries, thereafter.

28. As regards the first question it would appear that criticism of the British proposition on the ground that it does not envisage (as does the Rome Treaty) the elaboration of a " common agricultural policy " is still voiced on the part of the Six and particularly by France, although perhaps more categorically among representatives of farming interests than at governmental level. Superficially this criticism seems quite justified; a common agricultural policy implemented by an organisation with the powers of the E. E. C. is something different from a co-ordination of policies by mutual agreement even with provision for complaints procedures. A close scrutiny of the Treaty, on the one hand, and the British proposals, on the other, however, reveals that the difference is more apparent than real.

29. The simple truth is that the common agricultural policy is not set out in any detail by the Treaty and that it will be for the Community's institutions to elaborate it on the basis of certain procedures. Judging by the Treaty, it is moreover clear beyond serious doubt that the common policy cannot be fully developed until near the end of the 12-15 year transitional period. It is true that a conference is to be convened in 1958 to compare national policies and draw up a statement of resources and needs, and that proposals are to be laid before the Council of the E. E. C. before the end of 1959. At the same time it should be observed that during the whole of the first and second stages of the transitional period, i.e. during the first eight to eleven years, the Council will decide in this matter by means of an unanimous vote.

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7. SeeDoc. 698, paras 74-77.
8. See The Times of 17th January 1958.

30. It will also be recalled from earlier discussions of the agricultural section of the Treaty that Art. 39, 2 (a) explicitly stipulates that clue account shall be taken of " the particular character of agricultural activities arising from the social structure of agriculture and from structural and national disparities between the various agricultural regions ". This, in combination with the very elastic Treaty rules concerning the maintenance of minimum prices and the development of long-term contracts, tends to strengthen the impression that the agricultural policies of the Six are unlikely to undergo any radical •changes within the next few years.

31. The contention that the British proposals would not permit a sufficient co-ordination of agricultural policies in the Free Trade Area (by comparison with the Common Market) would thus appear to be based more on an erroneous interpretation of the real significance of the Treaty's agricultural provisions than on any serious divergence of views on the possible extent and rate of integration in the agricultural sector.

32. If anything, what the Community countries, and particularly France, may well fear in the British proposals is that some of the non-Six would attempt to use the Free Trade Area machinery to press for a relaxation of the discriminatory internal regulations of prices and production envisaged in the Common Market. The most objectionable feature of the British proposals might, on this interpretation, be the suggested rules relating to export subsidies, which are in •clear conflict with Art. 45 (3) of the Treaty. This Article permits the Council to grant, by an unanimous vote, payments necessary to compensate for the higher price charged by another Community country for raw materials obtainable outside the Community and needed for the production of goods destined for export outside the Community in competition with producers in third countries.

33. This, of course, in no way invalidates the demands of the Six on the United Kingdom to provide a greater measure of overall reciprocity in the distribution of burdens and advantages resulting for each country from the Free Trade Area formula; in these demands they are supported by several other OEEC countries, particularly Denmark.

34. It is difficult to say to what extent the British proposals, as summarised above, would be able to meet the claims of other Free Trade Area countries for some widening of their markets for agricultural products in the United Kingdom, since, according to those proposals, this would be a matter for subsequent negotiation.

35. While it must be accepted that the United Kingdom Government is not prepared to give up Commonwealth preference, some new outlets might still be found on the United Kingdom market for agricultural exports from the other Free Trade Area countries[9].

36. To sum up, it is clear that much remains to be done to reach a satisfactory agreement in terms of real commercial interests, but, equally, that there is no fundamental clash of policies that could not be overcome with good will.

1.1.2.2. Deflection of trade

37. The problem of the deflection of trade is inherent in the Free Trade Area concept and stems from the fact that while trade within a Free Trade Area, once established, is free, each of the participating countries retains separate tariffs against imports from outside. This is not the case in a Customs Union, such as is part of the European Economic Community, which has a uniform external tariff. As a constituent part of a Free Trade Area, however, the Community would be in exactly the same position as any other member country of the Area. Depending on whether its common tariff were higher or lower than the tariffs of another participating country in regard to any particular product, it could generate a deflection of trade operating against the interests of such a country, or be the victim of such a deflection. This applies fully only to a Free Trade Area once it is finally established, i.e. once trade between its members has become completely free. Although deflections may arise already in the transitional period, the effects of tariff disparities will normally not be important until tariff reductions inside the Area have become quite substantial; they would hence tend to be felt only towards the latter stages of the transition period.

38. Broadly speaking, the danger is twofold: (i) that basic materials, semi-manufactures and components from outside may enter a country in the Area with a high tariff through another country in the Area with a lower tariff, thus defeating the purpose of the former country's tariff protection; and (ii) that the temptation might arise for enterprises to set up assembly plants in the low tariff country in order to process goods there and thus qualify for area treatment under existing origin rules. - The latter form of deflection is perhaps potentially the more important, because it would not only circumvent protection in the high tariff country but might also entail a drain on its investment resources and affect the volume of employment.

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9. SeeDoc. 698, paras. 58-65.

39. While the existence of the problem cannot be denied, and is considered very serious by certain countries, it would not appear to be insoluble. For one thing, its extent should not be exaggerated, since for a number of products the danger does not arise at all: duty-free products, products on which tariff disparities are small, bulky products for which freight and handling costs usually exceed any tariff disparity, products for which processing capacity may not exist in the low-tariff country, etc. Secondly, it is technically feasible to avoid deflection of trade by devising and applying " origin rules ". This was already recognised by Working Party 17 of the 0. E. E. C. in January 1957 1[10]and it has not, to the knowledge of your Rapporteur, been challenged by any country in the course of the Intergovernmental Committee's negotiations.

40. These negotiations have been proceeding on the understanding that effective checks must be found by means of agreed origin rules to avoid deflection, and considerable work has been done on examining the effectiveness of the various methods of definition of origin in relation to particular groups of commodities. But while a good deal of disagreement still persists as to the merits of the one or the other method in relation to different commodities or commodity groups, it does not appear to be these differences on technicalities that are at the root of this controversy but considerations of a rather more serious character.

41. First, there is what may be termed a quarrel over method, where two schools of thought confront each other. The one, represented by the United Kingdom and a number of other countries, holds that the danger of deflection will arise only gradually—in fact cannot be discerned in detail in advance—and that it is therefore sufficient to provide for principles and procedures to cope with the problems as they emerge. These principles would include a code of good conduct, and a general authorisation for countries adversely affected to take action to protect their interests. The other school claims that the dangers of deflection can to some extent be foreseen and that arrangements must in any case be made in advance, since vested interests would otherwise be created before action could be taken and industrial planning would be rendered more difficult. This issue, again, while certainly difficult, would not appear to be incapable of solution by compromise.

42. The real issue at stake goes deeper and is concerned with the scope of the Free Trade Area, which is conditioned by the degree of liberality of the origin rules. It is apparent that the same countries that insist on strict arrangements agreed in advance and narrow rules of definition (principally France and Italy) are also those that press most energetically for the right to impose compensating charges on products containing a substantial proportion of the materials to be protected when imported from countries with lower tariff levels, and, as a last resort, the exclusion of certain products from the Free Trade Area arrangement.

43. In reality, the problem of deflection of trade thus to a large extent coincides with the problem of protection against competition in the Free Trade Area, and it is clearly essential to recognise this if the real conflicts of interest are to be approached in a realistic manner and solutions found.

44. To sum up, the problem of deflection of trade is neither a theoretical nor a practical obstacle to the establishment of a Free Trade Area. Furthermore, it should be observed that the mechanism for tariff reduction provided in the Rome Treaty, which has been accepted in principle also for a Free Trade Area Convention, is in fact quite flexible and permits the maintenance of a considerable degree of selective protectionism— up to 60 % of the " basic duty "— until the beginning of the third stage, i.e. for another 8-11 years.

45. Assuming that a general agreement by compromise can be reached on the technicalities of definition of origin and on the procedures for implementing rules of good conduct for the largest possible number of products, it would stillfappear to be necessary to envisage one or other, or a combination, of the following alternative solutions in special cases where national interests would otherwise be severely affected. These alternatives are: to harmonise tariffs, to allow compensating charges, or temporarily to exclude certain products from the Free Trade Area arrangement.

46. The possibility of resorting to the latter two solutions is, however, limited by the condition laid down in the General Agreement on Tariffs and Trade that a Free Trade Area must extend to substantially all trade. Considering the fact that a certain volume of agricultural products would presumably not receive full Area treatment, this would in practice mean keeping any further restrictions within such limits that G. A. T. T. could reasonably be expected to waive the above-mentioned requirement. How much room for manoeuvre these two devices could provide it is not possible to say. It may safely be assumed that they would have to be reserved for the protection of particularly sensitive or important industries. By contrast, the harmonisation of external tariffs, in principle at least, offers wider scope for negotiation on a basis of compromise.

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10. See Chapter I, " Definition of Origin ", in the Report on the possibility of creating a Free Trade Area in Europe, O. E. E. C, Paris, Jan. 1957.

47. The chances of success of this pragmatic approach would be increased if, in their negotiations on the common tariffs to be applied to the many important raw materials and semi-manufactures enumerated in List " G" of the Rome Treaty, the Six would give due attention—in consultation with the other OEEC countries— to avoiding creating further disparities, and the latter countries also made an attempt to review some of their tariffs with the same end in view.

1.1.2.3. Harmonisation

48. The harmonisation issue revolves around the question whether or not national differences in labour costs, and especially in social charges, constitute an obstacle to free trade in the sense that if they are not equalised or harmonised they will distort conditions of competition. If this were so, two economically and socially undesirable consequences would ensue: production and trade would be diverted artificially, i.e. for economically non-justifiable reasons, and the countries with the higher labour costs and/or social charges would be the sufferers.

49. Before examining the positions on this issue in the Free Trade Area negotiations, it may be instructive to see how it was resolved in the negotiations on the Rome Treaty where it also played a major role.

50. Here again two schools of thinking confronted each other, one asserting that the operation of the Common Market required far-reaching harmonisation of social legislation within the six countries, the other maintaining that it was sufficient to eliminate the effects of so-called specific distortions which handicap particular branches of industry and that, moreover, the Common Market would itself have harmonising effects.

51. The first line of thinking was argued energetically by France, which claimed that French employers pay their workers higher social security benefits, give longer holidays and make larger overtime payments, and, finally, that France was the only country to apply the principle of equal pay for men and women. French industry was therefore (so the argument ran) under a competitive handicap for which the proper remedy was to harmonise social legislation and social benefits in the other countries up to the French level.

52. A searching analysis of this problem came to the general conclusion that international comparisons could not be restricted to the partial wage costs made up of various social charges but must be based on total labour costs. Assuming that exchange rates are realistic, overall differences in the levels of such labour costs generally reflect corresponding differences in productivity. Such differences do not economically justify any harmonisation.

53. The outcome of this discussion is reflected in the Rome Treaty. While France's more sweeping demands for a harmonisation of social and fiscal policies were rejected, certain concessions were made by its partners on specific points. The Treaty is thus essentially based on the confident belief that equalisation in an upward direction of living and working conditions as well as of social welfare standards will follow as a result of the economic expansion engendered by the Common Market. To be sure, there are also certain general provisions calling for close collaboration in the social field and procedures for the elimination of disparities which distort competitive conditions, but these provisions are cautiously formulated (Art. 100-102).

54. As for concrete harmonisation measures, the Treaty lays down only one categorical commitment: the principle of " equal remuneration for equal work as between men and women workers " must be implemented within the first four years after the entry into force of the Treaty (Art. 119). Another harmonisation undertaking is couched in less mandatory form: that Member States " shall endeavour to maintain the existing equivalence of paid holiday schemes " (Art. 120). Finally, as regards the harmonisation of overtime payment, a Protocol[11]to the Treaty, expresses the belief that the establishment of the Common Market will result, by the end of the first stage, in achieving parity of the rules governing overtime rates, and further authorises France, if this situation should not come about, to take safeguard measures under certain conditions determined by the European Commission. It should be added that the decision to create a European Social Fund probably facilitated the reconcilialition of the opposing views, inasmuch as this institution was considered by France to make up for the lack of further harmonisation by providing assistance for the retraining and resettlement of workers.

55. It was inevitable that the same conflict of views should crop up in the Free Trade Area negotiations in an even more acute form. Obviously, both the real disparities and the attitudes to them are multiplied when the circle of negotiators is widened to include all 17 OEEC countries, and, as could have been anticipated, the issue principally centres on the French-demands. Worried about any additional sharpening of competitive

11. Protocol relating to Certain Provisions of Concern to France.

conditions in the Free Trade Area, France again insists on harmonisation provisions, and safeguards at least equivalent to those contained in the Treaty. To some extent the French claims are supported by the other Common Market countries.

56. On the other side, the United Kingdom, the Scandinavian countries and Switzerland from the outset expressed their preference for restricting harmonisation to a minimum and relying on intergovernmental co-operation to cope with problems of this nature if and when they arose. Besides refuting the theory and even questioning the practical need for general harmonisation provisions, the " non-Six " also pointed out that they did not have the powers to regulate working conditions such as paid holidays and overtime pay by act of law, these and similar matters being settled directly between employers' and workers' organisations. The views of these countries have since evolved somewhat, but while, as stated by Mr. Maudling, there is now general agreement that there must be some harmonisation, divergences persist as to its form and content. The concessions made by the non-Six with a view to meeting the French claims have been considered inadequate by France, not only with respect to their content but also as regards the procedural measures envisaged, principally the complaints procedures.

57. Here again, it is important to face the basic issue frankly if it is to be approached realistically and resolved, and the issue at stake is undoubtedly once more French fears of competition and reluctance to dismantle its protection unless substantial safeguards are provided for its industry and agriculture. It would unquestionably be more profitable if the harmonisation issue were discussed and resolved on its merits, as the non-Six appear to be prepared to do, and if the residual and more important problem of providing adequate safeguards for France were discussed as a separate matter.

1.1.2.4. Disequilibrium and incompatibility

58. Recurring themes in the criticism levelled against the Free Trade Area are that it suffers from a lack of balance, or that it is incompatible with the Common Market. Before examining what is meant by these two ideas and how justified they are, it may be useful to try to establish what they do not mean.

59. To take first the idea of an internal disequilibrium pertaining to the Free Trade Area concept, there appears to be no evidence of this in the sense of an inherent flaw that makes it unworkable. In so far as a comparison with a Customs Union is implied, all that can be said is that the Free Trade Area concept presents one major technical difficulty, which the Customs Union does not—that of necessitating measures to avoid deflection of trade. But, as shown above, this is a difficulty that can be met. Further, while the Free Trade Area concept is admittedly unfamiliar, for experience of functioning regime of this type is very limited, it is none the less a concept firmly established in economic theory, and, what is more, in the rules of G. A. T. T., where it is defined—with the Customs Union—as one of the two permissible types of closer international integration. As for harmonisation in the context of the Free Trade Area, this question is in no sense different, in principle, from that which arises in a Customs Union. What practical differences there may be are determined by the disparities existing between the particular set of countries planning to form, a Free Trade Area or a Customs Union. Per se the Free Trade Area concept is just as viable as the Customs Union concept, and the two concepts are not incompatible, in the sense that they cannot be combined as it is proposed to do.

60. Leaving the realm of ideal concepts, what are the concrete objections on grounds of disequilibrium or incompatibility against the Free Trade Area formula as discussed in the Intergovernmental Committee? This question cannot simply be settled by logic or reference to objective standards. In the last resort it remains a matter of consensus of opinion among the interested parties. Reviewing the discussion in the preceding three sections from this angle, one may summarise the conclusions reached as follows:

61. The United Kingdom's insistence on maintaining its remaining tariffs on agricultural imports from its partners in the Free Trade Area does create a difficult but not insoluble problem of overall reciprocity in the burdens and advantages resulting from the Free Trade Area regime. However, it was noted that the effects of the British limitation are far more apparent than real inasmuch as (possibly with the exception of Denmark) none of the countries concerned were prepared to dismantle rapidly their other and far more important regulations on agricultural production and trade.

62. As regards deflection of trade, it was seen that this problem was considered to be soluble and that the real issue hinged on defining the scope of the Free Trade Area in a manner acceptable to France and Italy. In doing so, however, certain GATT conditions had to be fulfilled. Apart from this aspect, no fundamental disequilibrium in the Free Trade Area can be detected—nor any incompatibility with the Common Market—on the grounds of the definition of origin problem. Much the same, it was seen, applies to the harmonisation question where the real issue, again, is a matter of conflicting economic interests.

63. One is, however, bound also to examine other interpretations of the two key-words " disequilibrium " and " incompatibility ". Here one is at once lost in conjecture, since these words are seldom defined, and when defined, they are seen to be highly subjective.

64. Sometimes the term " disequilibrium " may be understood to imply a criticism of the Free Trade Area on the grounds that it is exclusively a trade arrangement with none of the built-in safeguards and stabilisers, such as the rules on competition, on co-ordination of economic policies, on harmonisation, etc., provided in the Rome Treaty. Yet the summary review of the Free Trade Area negotiations given in the first chapter of this Report and the more detailed discussion of the three principal points at issue clearly indicate that this charge is inaccurate. Not only have the Free Trade Area negotiations proceeded on lines very similar to the Brussels negotiations, but the Rome Treaty itself has in large parts been accepted as a model for the Free Trade Area Convention. In fact, the Annotated Agenda on which the OEEC negotiations are based reads like a virtually complete catalogue of the chapter headings of the Treaty. On the same grounds, the charge that the two systems are incompatible because the Free Trade Area is only concerned with trade is equally wrong.

65. At other times, the term " incompatibility " appears to refer to the unwillingness of many countries to take decisions in advance, in the form of explicit provisions in a Free Trade Area Convention on a number of problems. This, it is said, compares unfavourably with the Treaty of Rome and would make the two instruments incompatible. To this it may be replied, first, that insofar as certain countries hold this position it is a fact that must be accepted with the same equanimity as these countries accepted the decision of the Six to set up their common institutions by a different formula. Secondly, it should be observed that the Rome Treaty itself, despite its length, also remains a traite-cadre, a " framework " Treaty, laying down principles and establishing procedures, but leaving much to be filled in by subsequent action.

66. Another version of the incompatibility argument seems to hinge on the assumption that the Free Trade Area institutions would be subject to unanimity decisions, whereas the Treaty institutions are said to have supranational powers. This institutional difference, while it exists, should not be exaggerated. For one thing, majority, decisions of the Council of the E. E. C. are carefully regulated, being limited to certain questions and as a rule reserved for the later stages of the transitional period. Also, as indicated earlier, there appears to be a growing willingness to find firmer ground for future co-operation in the Free Trade Area scheme among the OEEC countries. The difference might, therefore, in the end turn out to be far less substantial than is at present believed by many people.

67. Further, when speaking of the " incompatibility " of the two systems, it is often said that participation by the Community countries in a Free Trade Area would slow down or dilute the Common Market. As for the slowing-down argument, this would appear to be inaccurate since the Free Trade Area would be largely geared to the Common Market; as for diluting, it is difficult to see what is meant, since the Common Market would be governed by its Treaty in all matters of common concern to the Six, and by the Convention only in its relations with the other Free Trade Area countries. In fact, in matters of trade, for instance, where the Six have undertaken to conduct a common commercial policy, as in many other matters, it is hardly deniable that the Six will, on the contrary, have a very strong bargaining position outside as well as inside the Free Trade Area. The fears, if any, might more understandably be found in the other camp.

68. That the Free Trade Area is designed to wreck the Common Market, or that it would inevitably have the effect of doing so, as is sometimes said in public discussions, is, of course, worse than nonsense. The Treaty has entered into force and there is no incompatibility between it and the Free Trade Area formula. The only sense in which it could conceivably affect the operation of the Common Market is if one or more of the member countries of the Community were so adversely affected by the liberalisation of trade and factors of production in the Free Trade Area, as distinct from the Common Market, that they could not fulfil their obligations under the Treaty or required more help from their Common Market partners than these could provide. Any such danger must naturally be met, and there would appear to be every advantage in doing so squarely and within the framework of the 0. E. E. C, which has a long tradition of co-operation to fall back on in dealing with the financial or trade problems of its member countries.

1.1.3. The French Counter-proposals

69. At the time of writing, the French Government is reported to be discussing its proposals for the creation of a " European Union for Economic Co-operation " with its five partners in the European Economic Community, apparently with the intention of obtaining their support for a joint counter—proposal to be presented to the OEEC Intergovernmental Committee. The details of the plan are not available, but certain suggestions, which may. perhaps be taken as a rough indication of its main points, have appeared in the press[12]. The following description and analysis of the French proposals are therefore very tentative, all the

more so as it is known that all France's partners in the E. E. C. do not share all its objections to the Free Trade Area. The final version of this counter—proposal may therefore differ in important respects from the original version.

70. Before examining these proposals, it may be useful to try to sketch the economic background to the French misgivings about the Free Trade Area as outlined in the previous chapter.

71. Besides the drain on France's resources caused by the war in Indochina and the present conflict in Algeria, which has undoubtedly affected the rate of productive investment and aggravated the balance of payments deficit, the economic problems which it is believed that France would have to face in a Free Trade Area are attributed to other and more fundamental causes. Very roughly, French fears of intensified competition stem from two considerations. The first is that the dismantling of long-standing and highly effective protectionist policies and practices would expose the French economy to more severe dislocations (and necessitate more radical adjustments) than in other Free Trade Area countries. The second, not unrelated to the first, is that France derives the bulk of its raw materials from the French Union and their price structure has been geared to that of Metropolitan France. As regards the first, anxieties are aggravated by the existence of obsolete marketing and distribution systems; and, as regards the second, it is feared that the United Kingdom, particularly, would have a considerable competitive advantage in a Free Trade Area owing, inter alia, to Commonwealth Preferences.

72. Obviously, very much the same problems confronted France during the negotiations for the Rome Treaty. She feels, however, that the strains which will be placed on the French economy in the Common Market are balanced by safeguards and commitments by France's partners and that these are securely anchored in the " Community " character of the Treaty organisation. It is therefore often claimed that France could only take on further commitments at the present time in a similar " Community " framework, if at all.

73. The chief innovation in the French proposals appears to be that the idea of a multilateral Convention for a Free Trade Area is to be replaced by a series of Protocols, to be negotiated separately for different industrial sectors. While it does not emerge clearly from the information available, it would seem to follow from the terms of the Rome Treaty that these separate agreements would be entered into by the six countries as a bloc. It is not clear whether the Protocols would regulate not only the trade of the Six with the Eleven but also the trade of the Eleven with one another.

74. To give a measure of coherence a " general framework " is contemplated. This would involve prior agreement on basic aims and, particularly, recognition of the principle that conditions of fair competition should be worked out simultaneously with the widening of competition. Escape clauses and the institution of a closer co-ordination of economic policies are also foreseen. For the smooth running of the whole scheme, it is suggested that the existing agencies of 0. E. E. C. be strengthened rather than create a new organisation. The unanimity rule, it seems, would be maintained in full.

75. With regard to tariff reductions the French proposals suggest a twelve to fifteen-year transitional period as in the Rome Treaty, but with three qualifications: that the passage from the first to the second step would require a unanimous decision, that the first round of tariff reductions under the Protocols would not take place until the second round of tariff reductions in the Common Market began, and that the final elimination of tariffs would not take place until three years after the E. E. C. had accomplished this. It is also reported[13]that the French proposals contain a suggestion that compensation for increased competition in the territories of Members of the Union should be obtained by preferential concessions from British Commonwealth countries.

76. Granted that it is hazardous to analyse a complex matter like the French proposals on the basis of incomplete information, the first question to ask is—what do they mean?

77. One thing appears to be clear. The centre-piece of the proposals is the idea of a sector-by-sector approach to the task of associating the other OEEC countries with the integration effort of the Six. The purpose of this arrangement is clearly to permit a differentiation in respect of the rate of tariff reductions, rules on definition of origin, harmonisation, etc., adapted to the relative competitive strength of different branches of industry. In other words, tariff reductions and eventual free trade' will await the capacity of each individual industry in each country affected fully to meet foreign competition. Those industries which can easily compete will be free to do so at once, while those which cannot will remain protected until they can. The system is thus

12. See, inter alia, Le Monde of 28th February and 9th- 10th March 1958.
13. See The Economist of March 1st 1958.

at once selective and calculated to reach only the lowest common denominator of agreement. While it undoubtedly presents advantages for countries that are hesitant to give up longstanding protectionist traditions, such a plan raises formidable difficulties.

78. The first of these is concerned with the compatibility of the proposed system with the rules of G. A. T. T. As mentioned earlier, the General Agreement only admits two types of agreement—a Customs Union or a Free Trade Area—for the purpose of establishing a closer international integration. Now, there can be no doubt but that the proposed system amounts in fact to a -preferential arrangement, for the mutual tariff and other trade concessions to be negotiated would not be extended to all other GATT Members in accordance with Article II of G. A. T. T.—the " most-favoured-nation-clause ". Since, however, the proposal is clearly not ntended to result in the formation of a Customs Union, it would necessarily have to be presented as a Free Trade Area. Despite its new name, the proposal in principle remains an attempt to establish a Free Trade Area (in the GATT sense) and must so remain.

79. The question whether as such the proposed alternative would or would not be found compatible with G. A. T. T. is, of course, difficult to establish with certainty at the present time, the answer depending upon the political imponderables invol ved and its final shape. If one is to judge by the mere outline of the proposal, it is impossible not to entertain the gravest doubts on this score. The principal effect of the proposal being to restrict the scope of the free trade regime, it is more than questionable whether it wouldme et the condition of covering " substantially all trade ". It is true that the proposal envisages a time-table of reasonable length and would thus appear to comply with another GATT condition. But it may be questioned again whether a series of protocols would carry the conviction that the contemplated free trade regime would be carried out fully, which is a sine qua non of the GATT rules.

80. The second innovation in the French proposals is connected with the implied suggestion to delay the operation of the protocols until about the end of the first stage of the transitional period established for the Common Market, or, alternatively, to proceed with tariff reductions at a slower pace than in the Common Market.

81. This clearly conflicts with the view, shared by all OEEC countries only six months ago when Resolution 221 was adopted, that it is of the greatest importance that the elimination of trade obstacles in the Free Trade Area should be geared to the schedule of the Common Market in order to avoid a reappearance of discrimination.

82. There were good reasons for taking this view—and they are equally valid for any other free trade regime associated with a customs union. Not only would it lead to endless administrative difficulties to maintain two sets of tariffs, within the system, one in respect of the Six and a second in respect of other Free Trade countries, but the simultaneous existence of two sets of tariffs within the Area would in effect imply discrimination between the two groups of countries. A faster dismantling of trade barriers among the Six would give exporters in these countries a competitive advantage in the Common Market by comparison with exporters in the other Free Trade Area countries. It is easily realised that this could have very serious consequences if one remembers that many of these countries do a large share of their trade with the Six; thus, for Austria, this share is no less than one half of its total commodity trade. A systematic discrimination of this kind is, of course, in fundamental opposition to the principles underlying the work of 0. E. E. C. and the E. P. U. in the field of intra-European trade and payments. Considering that the whole sterling Area, for which the United Kingdom acts as banker, has been covered by the EPU Agreement, the consequences of such a development, if it came to pass, could be very serious for all parties concerned.

83. Having pointed to those weaknesses, one is also bound to ask whether the French proposals provide a better scheme than the Free Trade Area from the point of view of the objective which all have in mind—to ensure as rapid and as smooth as possible a move towards closer economic co-operation. As regards the pace of progress that may be expected in this direction, the answer must inevitably be negative, and, as regards the smoothness of operation, it is generally admitted in economic theory that " the larger the number of commodities or groups of commodities or industrial sectors in respect of which liberalisation of trade is undertaken simultaneously, the smaller the problems of transition "[14].

84. The suggestion that Union countries should be provided with new export outlets in the British Commonwealth, presumably on the same terms as the United Kingdom, while it may appear attractive at first sight, seems rather unrealistic on closer scrutiny. The reason is that it overlooks a number of hard facts.

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14. Social Aspects of European Economic Co-operation, I. L. 0 . , Geneva, July 1956, para. 271 (ii).

85. The Commonwealth countries are entirely independent in trade matters. It is hardly conceivable that the Commonwealth countries, highly protectionist as respects their own industrial development, would be willing to give preferential treatment to all European countries, for they are only with difficulty persuaded to continue their preferential treatment of British goods, which is in fact being slowly whittled down. Even assuming that the European countries would all be willing to give preferential treatment to Commonwealth goods in return—and this is hardly likely—the arrangement, which would obviously neither be a customs union nor a free trade area, would run head on into the " no-new-preference " rule of G. A. T. T., with exceedingly small chances of an approval by that body.

86. To sum up the preceding very summary analysis[15]of the French proposals, they would not appear in their present form to present a workable or preferable alternative to the Free Trade Area scheme. Apart from the difficulties over the GATT rules, they might well prove contrary to the real basic interests of France and of the other Common Market countries. For all these have a stake in ensuring that their joint venture shall be able to operate in a climate of mutual European understanding and assistance, for which reciprocity and non-discrimination in trade matters is vitally necessary. It is further difficult to see how that gradual and ever closer co-ordination of the general economic policies of OEEC countries on which so many countries have placed emphasis, and which may turn out to be the most important aspect of a general agreement, particularly in a period of stagnating or declining economic activity, could be better achieved on the lines of the French counter proposals.

87. In mid-March it was reported in the Press that the Italian Minister of Foreign Trade, M. Carli, had tabled a proposal designed to bridge the main differences in the Intergovernmental Committee. A group of experts was set up by the Committee to study the proposal.

88. Although the exact contents of the so-called Carli proposal have not been made public, it seems that its principal objective is to achieve a certain harmonisation of external tariffs. To this end it is proposed that agreement should be reached on a tariff " spread " within which individual countries could set their tariffs at will without foregoing the advantage of Area treatment for the goods in question. Products the tariffs on which fall outside the agreed " spread " would be subject to compensating taxes in the importing country equal to the difference between its higher external tariff and the lower external tariff applied by the exporting country. It is claimed that besides constituting an incentive to harmonise external tariffs, the proposal would make origin rules and certificates of origin superfluous. It will be observed that the Carli proposal is based on ideas resembling those suggested in (former) paras. 45-47 of this Explanatory Memorandum, although they appear to constitute a more comprehensive and systematic approach to the problems at issue. Unfortunately, it is almost impossible to judge whether the claims mentioned above are valid or not without further details of the proposal[16].

1.1.4. Relations with outside countries[17]

89. Considering that the United States and Canada have already given a blessing to the Free Trade Area project, the main interest in examining the possible effects of the Free Trade Area on Western Europe's relations with the outside world centres on the non-industrial, mainly primary producing areas[18]. The importance of the Free Trade Area project to these countries is illustrated by the fact that the Western European countries together accounted for no less than 45 %, on an average, of the total value of the exports of such averas in the years 1953/1955.

90. The problem is twofold. First: will the establishment of the Free Trade Area by itself help to sustain or accelerate the high rate of economic growth which Western Europe has experienced in the past decade and which has also acted as a powerful stimulus to the economy of overseas countries? Second: how will the preferences involved in the scheme affect trade with the non-industrial countries?

91. As for the first question, it is clear that the very purpose of the Free Trade Area is to stimulate economic growth and raise living standards. Moreover, it is generally recognised that there exists a close correlation between the volume of industrial production and the volume of imports, and it is a fact that in the case of Western Europe, the ratio of total imports to value of production is very high. In the years 1953/55, it stood at

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15. If this is warranted by the publication of any further authoritative information on the French Counter-proposals, your Rapporteur will endeavour ro make à further communication to the Assembly.
16. If this is warranted by the publication of any further authoritative information on the Italian proposal, your Rapporteur will endeavour to make a further communication to the Assembly.
17. See also the Appendix to this chapter (" Commodity Notes ") page 34, which gives details of the position of particular commodities of importance in trade with outside countries.
18. Future relations with the Soviet Union and Eastern Europe, which present special problems, are not considered here.

about 30 % as compared with 6.5 % in the United States. It must be added, however, that there is no assurance that the closer integration of Western Europe will make it possible to ward off the possible effects of a slump originating elsewhere, e.g. in the United States, which would inevitably also have repercussions on European trade with the primary producing countries.

92. In regard to the second question, it is also possible to be relatively reassuring in respect of global trade. A recent study by G. A. T. T.[19]shows that the OEEC trade liberalisation programme, which has been openly discriminating vis-a-vis outside countries, has not resulted in a systematic tendency for imports of any given commodity from European sources to rise faster than imports of any given commodity from outside areas. This is, however, considered to be attributable to the high level of general economic activity that prevailed in Europe in these years. Discriminatory or preferential arrangements are more likely to result in trade diversion when total trade values are falling. In general. G. A. T. T. estimates indicate that the relative importance of the Western European market in world trade is likely to increase considerably by comparison with North America in the next fifteen to twenty years.

93. When one considers different commodity groups separately, however, the situation varies considerably from one commodity group to another. Prospects for fuels and metals are considered to be distinctly favourable; for timber, hides and natural fertilizers, favourable; for textile fibres and natural rubber, distinctly less favourable.

94. As regards foodstuffs, the inevitable uncertainties surrounding future market prospects appear to be even greater than for other commodity groups. Recent experience would appear to indicate that those foodstuffs which cannot (or cannot easily) be grown in the main industrialised areas should be distinguished from those that can, the value of world trade in the former having increased much faster. This difference is ascribed by the F. A. 0. to " national policies of self-sufficiency aimed directly at correcting an imbalance of foreign payments, and to price support policies designed primarily to stabilise farm incomes, but which may in addition have tended to stimulate domestic agricultural production "[20].

95. Whereas for tropical beverages (cocoa and coffee) and fruit the outlook is thus promising, in respect of other foodstuffs future market developments are quite uncertain, depending entirely upon the rate of growth of production and consumption in the industrial countries.

96. In fact, it cannot be denied that the level of agricultural production in Western Europe in the years to come will have a decisive influence on imports of foodstuffs other than tropical beverages, fruit and vegetables. In 1953/55, Western Europe's net imports of such foodstuffs averaged 2.9 thousand million dollars.

97. It is well known that the primary producing countries are already alarmed at the fact that the proportion of trade moving between industrial and non-industrial areas has been on the decline since before the war, although a large part of this decline is accounted for by eight semi-industrial countries. The concern of the primary producing countries is, of course, sharpened by the present signs of a deterioration in their terms of trade. They have also voiced strong misgivings concerning certain features of the European Economic Community Treaty which would in all probability also apply to a Free Trade Area scheme involving similar features. Their anxieties apply in particular to the agricultural regimes in Western Europe and, in the case of the Common Market Treaty, to the association agreement with the Overseas Territories.

98. In this connection particular attention will have to be given to relations with Finland, Spain, Yugoslavia and Israel. All four countries are, in respect of trade and in many other ways, closely linked with Western Europe, and the establishment of a Free Trade Area that did not make special provision for preventing discrimination against their trade with the OEEC countries would without any doubt gravely affect them. It is, obviously, for these countries themselves to decide whether they would wish to seek some form of special association with a Free Trade Area. But while the initiative must come from them, your Rapporteur believes that the West European countries should make it clear that such an initiative would be examined in a favourable light and with due regard for the special problems with which their economies would be faced. Whereas Yugoslavia and Spain already participate in certain activities of 0. E. E. C, Finland and Israel have no official relations with this Organisation at the present time, although Israel is linked to most OEEC countries by a network of bilateral agreements in the field of trade and payments, shipping and aviation.

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19. G. A. T. T., The Possible Impact of the European Economic Community, in particular the Common Market, upon World Trade, Geneva, December 1957.
20. The State of Food and Agriculture, 1956, Chapter I I I.

99. The traditionally close relations between Finland and the other countries of Western Europe are well known—one half of its foreign trade being with that area—and its strong interest in the Free Trade Area scheme would appear to be a foregone conclusion. Israel's interest in it may at first sight seem less evident. A brief survey of its present trade relations reveals, however, that Western Europe is Israel's principal supplier and principal customer. In 1956, total Israeli commodity imports amounted to 364 mill, dollars and exports to 107 mill, dollars. Out of total imports, 46 % came from the EPU area and no less than 66 % of total exports went to that area, the most important customer being the United Kingdom (about 25 %). The mainstay of Israel's export trade is citrus fruit and citrus products (appr. 40 % of total exports in 1956), commodities which are competitive with the exports of some OEEC countries and of other Mediterranean countries, including French North Africa and Spain. On the import side, approximately 40 % of total imports consist of industrial raw materials, 28 % of investment goods and 13 % manufactured consumer goods. Although Israel's exports have increased in volume and value in recent years, the country remains in heavy deficit on trade account. The interdependence of the economy of Israel with that of Western Europe explains why Israel is following the progress of Western European economic integration with close attention.

100. To sum up, it may on the whole be said that there are good reasons to be optimistic concerning the future development of trade of the Free Trade Area with the primary producing countries, provided that the rate of economic growth in Western Europe is maintained. Even on this assumption, however, special attention will undoubtedly have to be given to the trade problems which may arise in the agricultural sector. Every effort will thus have to be made to ensure that the establishment of the Free Trade Area does not prejudice the legitimate export interests of particular outside countries for particular products, since such countries are often heavily dependent on the export of one or two primary products.

Appendix APPENDIX TO CHAPTER IV

Relations with Outside Countries

Coffee

1. Since pre-war days coffee production in the Associated Territories has almost quadrupled, and in the British Overseas Territories it has approximately doubled, bringing total production of all OEEC Overseas Territories up to about one-sixth of world production. It is considered that the African territories may considerably increase their production in the future.

2. Production in the rest of the world — the largest producers being Brazil, Colombia and Central America, has remained relatively stable since pre-war.

3. In the years 1953-1956, coffee imports of the OEEC countries combined averaged about 600,000 tons — a little more than one-half of U.S. imports in the same years. About one-third of these imports came from Associated and other Overseas Territories and two-thirds from the rest of the world, especially from South and Central America.

4. Export prospects to the Free Trade Area are largely determined by taste preferences for the one or the other of the two main varieties, Robusta and Arabica.

5. The former variety, Robusta, dominates in Africa, representing 90 % of the exports of the Associated Territories and 60 % and 90 % respectively, of the exports of the British and Portuguese Overseas Territories. Unless there is a marked change of consumers' habits in "Western Europe, it may be expected that the African territories will not significantly increase their share of European imports.

6. It is interesting to note that from 1952 to 1956 the share of the Associated Territories in the expanding market of the six countries declined slightly. As production in the Territoriees simultaneously increased more than their exports to the Six, the surplus production was increasingly exported to the United States ; similar trends are observed in the British and Portuguese territories.

7. Present per capita consumption in Western Europe varies greatly from one country to another, and is still low in such countries as Italy (1.6 kg) and Germany (2.6 kg.) by comparison with the United States (7 kg.), and forecasts of future consumption levels are rather uncertain. Although the response of coffee consumption to price changes is relatively weak, it should be noted that the retail price of coffee in many Western European countries includes a very large tax element.

Cocoa

8. The share of different countries and regions in world production of cocoa has changed somewhat since pre-war. Whereas Ghana's production has declined from 38.5 to 29.2 % from 1934-1938 to 1953-1956, the present Associated and Overseas Territories have increased their share from 28.5 to 31.5 % and the rest of the world, mainly Brazil and Central America theirs from 32.7 to 38.3 % (1953-1955). World production in the same postwar years averaged 836,000 tons compared with 733,000 tons in the pre-war period.

9. The fastest production increase took place in the Associated Territories and this is reflected in a considerable increase in their share of world exports of cocoa beans which rose from 12.4 % to 19.3 %. Production in and exports from the British Overseas Territories remained fairly stable, and the production increase in the rest of the world was not proportionately reflected in export trade. Simultaneously, production declined in Ghana and its exports fell from 39.1 to 31.6 % of world exports of cocoa beans.

10. Whereas the Associated and other Overseas Territories thus supply about 30 % of world exports, the OEEC countries combined imports of cocoa beans averaged about 53 % of world imports in the years 1953-1956, a slight increase over their pre-war share (51.2 %). The greater part of imports from other sources comes from Ghana, two-thirds of the exports of which go to OEEC countries ; as for Brazil, the OEEC countries account for no more than 30 % of its exports, the bulk of which, about 57 %, go to the United States.

11. Future prospects of cocoa producers in general are more likely to be determined by the possibilities of increasing production than by insufficient demand in Western Europe or in other industrialised countries. Although the trend of consumption has been affected by rising prices, relatively important consumption increases have nevertheless been observed in the Common Market area, particularly in Germany, Italy and the Netherlands.

Bananas

12. The shares of the Associated Territories, the French Overseas Departments and the British Overseas Territories in total world exports of banahas were 8.6, 4.7 and 7.4 % respectively in 1954 i. e., just above 20 %. In the case of the two former groups of territories, this represented a doubling compared with pre-war (1934-1938), whereas the figure for British Overseas Territories reflected a decline by about one-half. Considerable changes in the relative importance of banana exports since pre-war have also occurred among the several Central and South American countries that together account for almost three-quarters of world exports.

13. In 1954 the OEEC countries combined took 32.5 % of world imports as against 28.5 % in pre-war. "While tlie imports of France, Italy and the United Kingdom largely originated in their respective Overseas Departments and Territories, most other OEEC countries took the bulk of their imports or their entire imports from other sources.

14. There are prospects for an expanded production in most areas. Moreover banana production could expand rather rapidly, the lapse of time between planting and harvesting the first crop being from one year to one year and a half.

15. Although banana imports to "Western Europe have risen rather rapidly in recent years, consumption per caput is still low, as compared with the United States. Trade patterns are all to a considerable extent determined by taste preferences. The most popular of the two principal varieties, the Gros-Michel banana, is only grown in two of the Associated Territories, the Belgian Congo and the French Cameroons. In France and Italy imports mainly consist of the other variety, the fig banana. Future trade patterns could be affected by increased production in some of the Associated and Overseas Territories of a third variety, the Plantain banana, which combines the size and better appearance of the Gros-Michel with the stronger flavour of the fig banana.

Citrus fruit

16. Production in the main supplying countries has expanded rapidly during the last ten years, except in Spain, and world exports have increased by about 60 % since 1948-1950.

17. Consumption in "Western Europe has risen rapidly in the same period, except in the United Kingdom ; between 1948-1950 and 1954-1955 imports doubled in the Common Market countries and also rose fairly rapidly in the Scandinavian countries and in Switzerland and Austria.

18. The largest supplier of citrus fruit among the OEEC countries is Italy. Its average exports In the years 1953-1956 amounted to about 373,000 metric tons, of which an average of about 158,000 tons went to other Common Market countries and 25,000 tons to the United Kingdom.

19. Among the Associated Territories, Algeria Morocco and Tunisia are the largest producers and exporters. In the years 1953-1955 (1954-1956 for Algeria) exports from these three sources averaged about 400,000 tons, the bulk of which goes to France and covers about 55 % of this country's requirements.

20. Dutch and British territories export relatively small quantities.

21. A very large proportion of the citrus fruit imports of the combined OEEG countries is supplied by Spain, -which covers about 60 % of imports of the Common Market countries taken together. Other suppliers outside the Free Trade Area are Israel, the Union of South Africa, the United States and Cyprus.

Oil and Oilseeds

22. As illustrated by the following two tables, Western Europe and its overseas territories hold a dominant position in world trade both in the import and the export side for three of the main categories of oils and oilseeds, the exception being copra and coconut oil where the OEEC countries import far more than their Territories produce.

SHARE OF WESTERN EUROPE IN WORLD IMPORTS (%) 1953

	Groundnuts and Groundnut oil	Copra and Coconut oil	Palm oil	Palm kernels and palm kernel oil
Common Market	47	31	45	37
United Kingdom	34	8	41	49
Other OEEC countries	6	11	2	5
OEEC countries combined	88	51	88	91
Rest of world	12	49	12	9
World total	100	100	100	100

SHARE OF OVERSEAS TERRITORIES IN WORLD EXPORTS (%) 1953

	Groundnuts and Groundnut oil	Copra and Coconut oil	Palm oil	Palm kernels and palm kernel oil
French Terr.	37	3	4	16
Belgian Congo	2		24	15
Assoc. Terr.	39	4	28	29
U. K. Terr.	34	13	46	59
Portug. Terr.	4	3	2	3
All O. T.'s	77	20	76	91
Rest of world	23	80[21]	24[22]	9[23]
World total	100	100	100	100

According to the F. A. O., consumption of oils and fats for food uses in Western Europe is now as great per head of population as pre-war, and demand is increasing only slowly. The production of groundnuts and copra is not expected to increase significantly, for palm oil and palm increase kernels medium term prospects are that they will by about 5 % annually and exports by 3.5 %.

23. Owing to the fact that oil and fat products can relatively easily be substituted the one for the other, market forecasts are all practically impossible.

Tobacco

24. World production of and trade in raw manufactured tobacco is dominated by the United States which accounted for an average of 31.4 % of the former and 36.5 % of the latter in the years 1953-1956.

25. Production of tobacco in Western Europe covers less than half of its requirements. In 1956 the OEEC countries combined produced 346,000 tons, or 10.5 % of world production, and imported 365,000 tons representing no less than 59 % of world imports. Within the Common Market, Italy is the only exporter of any significance, Greece and Turkey being the two most important European tobacco exporters, their combined exports averaging about 18 % of world exports.

26. Whereas the Associated Territories taken together account for about 10 % of world production and less than 1 % of world exports, the Federation of Rhodesia and Nyasaland is the largest tobacco exporter after the United States, accounting for 11.3 % of world exports in 1956, half of which went to the United Kingdom.

27. As regards the development of demand for tobacco in Western Europe as a whole, the F. A. O. holds the view that the outlook is good in the long run although new production techniques and the preference for filter-tip cigarettes have reduced manufacturers' requirements of raw leaf per unit.

21. Philippines 43 %, Other producers 38 %.
22. Indonesia.
23. Indonesia 5 %, Liberia 2 %.

28. It may also be noted that the possibilities for an expansion of production in Greece and Turkey in lower grade tobaccos are considered to be relatively good.

Sugar

29. About 60 — 65 % of world sugar "supply has in recent years consisted of cane sugar and the remaining 30 — 35 % of sugar produced from beet, grown mainly in Europe and the United States.

30. OEEG countries in 1956 accounted for 15 % of world production. 10.8 % of world exports and over 30 % of world imports. Out of the total sugar imports (raw, refined, molasses, etc.) of OEEC countries in 1956, 4,580,500 tons, less than 10 %, originated within the area.

31. Whereas the Associated Territories are generally not suited for sugar production[24]British Territories, the British West Indies and Mauritius in the first place, account for about 12 % of world exports, the bulk of which went to the United Kingdom, which country also takes most of the not inconsiderable exports of Australia and the Union of South Africa. It is interesting to note, in passing, that other OEEC countries than the United Kingdom do not figure among the customers of the British West Indies, Mauritius, Australia and the Union of South Africa.

32. The other most important suppliers of the OEEC countries are Cuba, the world's main sugar producer, which sold 15 % on average of its total exports to Western Europe in 1954-1956, the Dominican Republic and Brazil, for which the corresponding figures for the years 1953-1955 were 72 % and 44 % respectively.

33. According to F. A. O., production of sugar in exporting countries has recently been stimulated by the rising price levels. A United States Department of Commerce survey also indicates that mill production is going to expand in most areas, including Africa, where sugar production, while still inadequate to meet the area's needs, is rising rapidly.

34. On the basis of its long-term forecasts on the rate of economic activity and population trends in Western Europe, and assuming an income elasticity for sugar of 0.5, the GATT estimate is that sugar consumption in this area will increase by about 46 % up to 1973-1975.

35. Sugar production in the OEEC countries has increased by comparison with pre-war by about 57 % but world production simultaneously increased somewhat more, or about 63 % (averages 1934-1938 and 1953-1956).

24. The French Overseas Departments, however, export an average of some 360,000 tons, three-quarters of which go to France (1954-1956).