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Reply to the Tenth Annual Report of the Organisation for European Economic cooperation

Report[1]
Committee on Economic Affairs and Development
Rapporteur: Lord Frederik MULLEY, United Kingdom, Socialist Group

1. 1959 - 11th Session - First part

A. Draft Recommendation

1. The Assembly :

2. Thanks the 0. E. E. C. for the transmission of its Tenth Annual Economic Review;

3. Notes with satisfaction that in most European countries :

3.1. inflation has been checked;

3.2. the foreign payments position has substantially improved; and

3.3. convertibility on current non-resident account has been introduced as a step towards a better international division of labour;

4. Notes with concern that after eighteen months of virtual standstill in the level of economic activity :

4.1. there are only small signs of a revival of economic expansion; and

4.2. the trends of investment, stocks and exports, together with the amount of unused productive capacity, are discouraging in that they reflect an the absence of positive forces for expansion and indicate the stagnation of effective demand;

5. Recognises that the need to avoid the recurrence of inflation has justified some caution and that the introduction of convertibility and of greater freedom of trade will make European economies generally more vulnerable to economic fluctuations and, in particular, expose their external balances to greater pressures;

6. Believes, nevertheless :

– that the suggestions set out in the Tenth Review for policies for sustainable, sound economic growth under-estimate the urgency of the need for resumed growth and that a bolder approach is required;

– that existing resources, both industrial capacity and foreign balances and reserves, could sustain increases in overall demand;

7. Expresses the conviction that the situation calls for more effective co-ordination of national business cycle policies as part of a concerted programme for expansion designed to :

7.1. encourage a steady rate of growth in demand by means at the disposal of Governments, including, wherever appropriate, fiscal induce-cements, public investment, arid measures aiming at an increase of private investment;

7.2. stimulate trade and particularly intra-European trade, by reducing remaining barriers to trade, especially quantitative restrictions, with particular emphasis on agricultural products;

7.3. establish a long-term programme for the economic development of the less developed countries and regions, both inside and outside the OEEC area, including increased Government expenditures, the encouragement of private capital investment, and expanding markets for the products of those countries;

7.4. improve the speed of collection and the standardised presentation of economic data (covering stocks, order-books, and investment) for analysis and short-term forecasting;

8. Stresses that such a concerted programme for expansion would be an earnest of the desire to promote the cause of European integration and that its achievement depends in large measure upon the bigger countries of 0. E. E. C, and upon the recognition of the particular responsibilities of the countries in a stronger economic position;

9. Recommends Member Governments and the Council of 0. E. E. C. :

a. to take immediate steps to develop a concerted programme for expansion on the lines suggested above;

b. to overhaul the machinery of 0. E. E. C. in order to make possible an effective co-ordination of business cycle policies as the foundation for carrying out the programme ;

c. to agree to make frequent and regular reports to the Consultative Assembly on the working of the policy co-ordinating machinery and on action taken by Member Governments to implement a programme for expansion ; and

d. to report to the Assembly before its next part-Session on the action taken on this Recommendation.

B. Explanatory Memorandum

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1. INTRODUCTION

1. The 0. E. E. C.'s Tenth Report, Policies for Sound Economic Growth, was only published in March, and the time remaining until the April session was too short to undertake a detailed study of all the issues discussed in the Report. Nevertheless, the Economic Committee has felt that its central themes should be brought to the attention of the Assembly at the first opportunity. For, apart from their intrinsic importance, these themes are particularly relevant to the way in which economic co-operation is organised at present. This problem is of particular importance at the present juncture, when the deadlock in the negotiations on a European Economic Association has created the risk of a split in Europe.

2. The Tenth Report is centred on the current standstill in economic activities and the short-range prospects for resuming and sustaining a satisfactory rate of growth. Although the diagnosis of the current situation and the forecast for the immediate future is in no sense alarming, there are clearly weak spots in the European economy which require to be watched. Moreover, the recent move towards convertibility and the setting up of the European Economic Community present new and important problems. In particular, the Report bears out the need for more effective co-ordination of national economic policies if expansion is to be resumed and maintained. While this admittedly reflects a growing recognition at Government level of the importance of this need, there can be no doubt that this recognition by the Governments has not yet been translated into an adequate programme of action. But it is not sufficient merely to press Governments to act. Government policies must have public support. One of the main purposes of the Assembly's debate must therefore be to bring home to public opinion in all countries the close interdependence of the European economies and the consequent need to take account of the interests of other countries in framing national policies for renewed economic growth.

2. The Current Economie Situation

2.1. The Background

3. From 1953 to about mid-1957 the West European economy went through a period of expansion, which in its last two years developed into a boom. From about mid-1957 there were signs of slackening economic activity—and since the last quarter of 1957 industrial production in the OEEC countries combined has stagnated, unemployment has reappeared and intra-European trade has declined. Simultaneously, however, inflation has abated and the foreign balances of member countries have been greatly improved.

4. The 0. E. E. C's analysis shows that the current standstill in economic activity is largely a consequence of developments associated with the preceding boom. The excesses of that boom led to inflation and balance-of-payments crises, and the restraining measures which were taken to correct external and internal imbalances, in achieving their aim, also exerted a marked dampening effect on production, employment and trade.

2.1.1. The boom

5. The economic expansion which started in 1953 arose entirely from demands in the civilian (private) sector of the economy, and predominantly from the pent-up demand for consumers' durable goods and investment. Sales of consumer goods increased by a yearly average of 13 per cent in the years 1953—1955. This demand was in most countries stimulated by Government action in the form of tax-reductions, relaxations of earlier restraints and easier credit conditions. New housing was also one of the chief elements in the expansion, the volume of spending in this sector increasing by 19 % in 1953 and 13 % in 1954.

6. Demand for investment goods was encouraged by Governments at the same time, and an investment boom of record proportions developed which reached its peak in 1955, when fixed investment (excluding house-building) in member countries rose by 13 per cent.

7. From the middle of 1955 stocks were sharply increased, which added to the other expansionary forces and resulted in great pressure on labour markets and a sharp increase in imports, particularly of certain basic materials and fuels. From then onwards the boom manifested clearly inflationary characteristics.

8. In spite of continuous increases in capacity, in domestic output and in imports, demand exceeded available resources and pushed up prices. The average price-level in member countries combined rose by 3 per cent in 1955, 5 per cent in 1956 and 3.5 per cent in 1957, and these figures of course conceal larger rises in certain countries—particularly France, the Netherlands, Norway and the United Kingdom—as well as in certain sectors, such as the building industry, and in foodstuffs. There were also important differences in the timing of price inflation.

9. At the same time, unit costs of output increased fairly generally. This was mainly a result of the rising trend of wages which followed the price increases and derived its strength from the tightness in the labour market, where overtime work at increased rates became a widespread phenomenon in most countries. In 1956 wage-rates or earnings in a number of countries rose by 8 per cent or more, and this tendency persisted in the following year despite the easing in demand pressures.

2.1.2. External imbalances

10. The initial phase of economic expansion up to mid-1955 was accompanied by a rising volume of trade —both intra-Eufopean and with the rest of the world—-without the appearance of serious imbalances. The expansion in trade was partly the result of rising activity, but largely also of the increase in intra-European liberalisation from 64.7 per cent at the end of 1952 to 86 per cent at the close of 1955, and a simultaneous increase in dollar liberalisation from 11 per cent at the beginning of 1953 to 54 per cent at the beginning of 1956. Trade liberalisation was accompanied by substantial moves towards greater freedom of payments and a hardening of the EPU rules of payments settlements.

11. Even during the following inflationary phase Europe as a whole continued to be roughly in balance on current and capital account with the outside world, although there was some deterioration as the trade deficit continued to increase more than net receipts from invisibles and military transactions. Nevertheless, during this phase severe payments imbalances developed for some major European trading countries, largely as a consequence of disequilibria in intra-European trade balances. The most persistent of these were the large current surplus of Germany and, from early 1956, the large French deficit, but payments difficulties occurred also for the United Kingdom, the Netherlands, Denmark, Norway and Austria.

12. In part, these imbalances were unquestionably the result of differences as between European countries in the strength and the timing of demand pressures. But it is also clear that imbalances on trade account were frequently severely aggravated by short-term capital movements engendered by fear of inflation. This was particularly evident in the exchange crisis of September 1957 when the preceding de facto devaluation of the French franc gave rise to doubts concerning the stability of exchange rate parities.

13. The progress towards freer trade and payments was in general interrupted during the inflationary phase of the boom but, with the exception of France which was obliged to reimpose controls for practically all imports in August 1957, payments difficulties were not as a rule met by measures to restrict trade. Indeed, just before the French devaluation, intra-European trade liberalisation stood at a record level of 89 per cent.

2.1.3. Anti-inflationary policies

14. It has been pointed out that the expansion that started in 1953 was confined to the civilian (private) sector and that, although it was not in general markedly affected by Government expenditure, it was in various other ways deliberately encouraged by Governments. As demand pressures started to affect payments positions and generate inflationary price movements, Government policy gradually shifted toward restraint. Restrictive action was thus taken, principally for balance-of-payments reasons, as early as 1954 in Denmark, and in the following year also in the United Kingdom, Norway, Sweden, Germany and Austria. In 1956 and 1957 almost all OEEC countries resorted to or reinforced restrictive policies.

15. While major emphasis was placed on measures designed to reduce the overall level of demand, some countries—in particular the United Kingdom, the Netherlands, Norway and Sweden—made considerable use of selective measures to restrain specific categories of demand such as house-building, certain types of fixed investment and hire purchase of consumers' durable goods. While these and other forms of controls rapidly produced the expected effects they were not, of course, able to or designed to reduce overall demand.

16. The outstanding—and for the postwar period—novel feature of policies in this phase was that governments, in combating inflation, placed their main reliance on general monetary policies. In particular, most Governments made extensive use of the traditional weapon of increases in official discount rates— both to squeeze the liquidity out of the banking system and to prevent short-term capital movements from aggravating the payments position. This was frequently combined with open market operations and changes in the legal reserve requirements of banks. In a number of countries the authorities also had recourse to formal or informal directives to the credit institutions to restrict specified types of credit.

17. On the whole, the Report points out, Governments did not use fiscal policy as a major instrument to combat inflation. Government expenditure was on the whole prevented from adding to overall demand, but no attempts of any importance were made to reduce Government spending during the boom.

18. Summing up its analysis of the anti-inflationary policies, the Report concludes that most countries had only very limited success in restraining the boom. This is ascribed partly to the reluctance of Governments to check an expansion of private productive investment which was in itself highly desirable from a long-term point of view, especially in a period of important technological changes. It was, however, evident, that in many cases the policies applied were too weak and applied too late and that the monetary restraints which were principally used to the neglect of other instruments of stabilisation policy proved to be relatively ineffective once inflation got under way. In certain countries where the external payments position was sound enough to have permitted a marked rise in imports, thereby absorbing excess purchasing power without increasing the strain on domestic resources, this method of combating inflation appears not to have been used sufficiently.

2.2. The present standstill

2.2.1. Industrial output levels off

19. From mid-1957 there were signs that the boom had come to an end. In most countries this was first reflected in the volume of industrial output and trade and only somewhat later in rising unemployment and price stabilisation. Simultaneously the foreign balances of most countries improved rapidly.

20. The countries that experienced the most significant fall in industrial output (exceeding 10 per cent from peak to trough) were Belgium and Norway, followed by the Netherlands and the United Kingdom. With regard to the United Kingdom, the decline which set in dui'ing the second and third quarters of 1958 was small, but it should be observed that industrial activity in that country had slowed down as early as 1955. On the other hand, Austria, Italy and Sweden experienced little or no actual decline and in Germany industrial production

after a brief halt even continued to increase, though at a slower pace. In France, too, industrial production continued to increase until about mid-1958 but has since declined steadily even after most other countries again began to record slight increases towards the end of 1958.

21. In almost all countries the slackening in activity has been concentrated on manufacturing industry, particularly textiles, clothing, leather and shoes, and on the coal, and iron and steel industries. The situation in the coal industry, with increasing pithead stocks, is very serious—even though it is partly attributable to continued large-scale imports from the United States—because there are indications that the trend towards increased use of other forms of energy which was checked during the Suez fuel crisis was resumed again in 1958. British and German crude steel production fell 16 and 11 per cent respectively between the third quarter of 1957 and the same period in 1958, partly under the influence of large inventory reductions. At the same time capacity has continued to expand although there are signs of late that investment in this industry may be lower in 1959 in the Community countries than it was in 1958. By and large, declines in these sectors were offset by continued expansion in others, mainly the motor-car industry, chemicals and foods. In most countries, non-residential fixed investment levelled off by early 1958 and new housing, which reacted more rapidly and markedly to the interest rate rises in 1957 has in most countries declined; in some countries quite substantially.

2.2.2. Unemployment reappears

22. Inevitably, the levelling-off in output since mid-1957 has been accompanied by a general easing of conditions on labour markets. This, naturally, first affected overtime work and unfilled vacancies, and it was not until the first and second quarters of 1958 that a fairly general but modest rise in unemployment was recorded. The most significant changes appear to have taken place in the Netherlands, Belgium and the United Kingdom, but unfilled vacancies were fewer and unemployment greater in 1958 than in 1957 in all countries except Germany.

23. While unemployment has not assumed very serious proportions in any country and has not in all sectors followed the decline in output, (which suggests that there has been a tendency to hoard labour or decrease output per man), quite important changes in the employed labour force took place in the industries that have contracted most, particularly in the building industries in Belgium and the Netherlands, and in some countries regional pockets of unemployment have emerged, as in certain coal-mining districts in Belgium.

24. In France, where industrial expansion continued longer than elsewhere, unfilled vacancies started to decline in 1957 but unemployment hardly increased at all and remained very low until the end of 1958. In Germany unemployment after a brief rise early in 1958 again fell to an all-time low in the third quarter of 1958. In the United Kingdom unemployment rose slowly but steadily during the twelve-month period xip to the end of the third quarter of 1958.

2.2.3. Trade declines

25. As demand pressures slackened and output levelled off in Europe after mid-1957, the rise in intra-European trade which had accompanied the boom rapidly flattened out and in the first half of 1958 gave way to a decline of 4 per cent compared with a year earlier. The decline in intra-European trade came later than the general slackening in world trade which had made itself felt since 1956 but ante-dated, and was stronger than, the decline in Europe's trade with the rest of the world that set in in the second half of 1958. The decline in intra-European trade was partly an effect of the general fall in output and activity, but to a large extent also the direct result of the import restrictions which were reimposed by France in August 1957 and the measures taken in the Netherlands to correct a growing external imbalance. Member countries' exports to France and the Netherlands thus decreased by 14 and 17 per cent respectively in the first six months of 1958 as compared with a year earlier. In value the fall in exports to these two countries totalled about $360 million or about 20 per cent of the total trade decline. The two countries most severely affected by these and other contractions in European imports were the United Kingdom and Belgium-Luxembourg, United Kingdom exports to France falling by 30 per cent in the fourth quarter of 1957 compared with a year before and its exports to member countries combined declining by 18 per cent in the first half of 1958. Obviously, changes of this order in exports to Europe in turn affected output levels in the countries concerned. On the other hand, Germany's imports from member countries combined increased in this period while its European exports remained relatively stable.

26. The decline in Europe's trade with the rest of the world set in later and almost exclusively affected imports, whereas exports remained almost stable. However, to a considerable extent the fall in European imports from third countries reflected price falls of primary products, which were initially induced by the fall in U. S. imports of such materials during the U. S. recession.

27. Contrary to what happened during the two earlier post-war American recessions, European exports to the United States were well maintained throughout the recent United States recession. Whereas in 1954 total European exports to the United States fell by more than 10 per cent they remained practically unchanged from 1956 to 1957. This was largely due to a continued increase in U. S. imports of finished goods, particularly motor-cars, from Europe. On the other hand, European imports from the U. S. fell quite substantially in the first half of 1958 compared with a year earlier. As a result Europe's trade deficit with the United States over this period fell from $1.6 thousand million to $0.7 thousand million and this change contributed substantially towards the large payments surplus of almost $1.5 milliard which Europe netted in its transactions with the U. S. from the first half of 1957 to the same period in 1958.

2.2.4. Foreign balances improve

28. The net effect of the trade developments summarised here was at once a spectacular improvement in the payments position of Europe as a whole—shared by almost all member countries—and an appreciable improvement in the balance of trade between member countries. In the eighteen months following mid-1957, foreign exchange reserves of member countries have thus risen by S3.5 milliards. This was, however, also partly the result of a substantial fall in the outflow of European capital to other parts of the world, which had been running at the rate of SI.5 milliard a year from mid-1955 to mid-1957.

2.2.5. Policies shift

29. The remarkable improvement in external payments positions and the easing of pressures on internal prices gradually led governments to relax the severely restrictive policies which had been put in force in the autumn of 1957. In most countries these relaxations have been cautious. So far the emphasis has again been on easing monetary restraints, but official discount rate reductions, most of which were made as late as in the summer of 1958, were usually ineffective, since market rates had already fallen as an automatic effect of the accumulation of foreign exchange reserves and the decline in demand for finance. Similarly, quantitative credit controls were allowed to lapse as they became inoperative.

30. The more selective measures which have been applied in certain countries have been aimed at checking the rise in unemployment in particular sectors rather than to raise overall demand. As in the preceding boom, Government budgets have not been brought to play as an instrument of anti-cyclical policy, nor have countries, generally, taken specific steps to stimulate private consumption; and in some countries, it seems, certain restrictions on consumption, such as hire-purchase limits, have not been fully abolished.

3. The Prospects

31. The fact that industrial output in Western Europe as a whole has not declined since the boom ended in mid-1957—decreases in output in certain countries being compensated by a standstill or some continued increases in others—and that unemployment levels are still on the whole relatively modest does not make less true the general conclusion that the European economy in the last eighteen months has been stagnating. That a period of readjustment was called for after the inflationary excesses of the boom is unquestionable, and the Tenth Report clearly establishes that the slow-down in economic activity and decline in intra-European trade were largely the result of the policies adopted to re-establish internal and external financial stability. But eighteen months is perhaps rather too long a period of readjustment, particularly if one considers that foreign balances improved very quickly and that inflation has in most countries been brought under control for some time. One is thus led to enquire whether the present standstill is not also due to other, more deep-seated causes.

32. This impression of stagnation in the European economy is somewhat reinforced if one examines the prospects of a revival in the immediate future and of resumed expansion in the longer term. As the following account will show, while there is certainly no cause for alarm, there is definitely no justification for complacency.

33. There are two main factors of stability. First, as the Tenth Report stresses, there is the continued buoyancy of private consumption. As noted earlier, wages generally went on rising for some time after output ceased to increase and trade started to decline. Further, the decline in earned income which has taken place

as a consequence of higher unemployment has, of course, been partly compensated by unemployment benefits. Nevertheless, the considerable decrease in overtime work and the fact that the employment force has for various reasons declined or ceased to increase as much as before cannot be disregarded and was, in fact, reflected in some short falls in estimated Government revenue in 1958. An important element of stability, it should be added, lies in the strenght of the trade unions and the confidence that wages and salaries will not be allowed to fall.

34. The second factor which should contribute to stability and facilitate a revival of economic activity is that conditions on the money and capital markets have been eased quite considerably more recently. The full impact of this development has perhaps not yet made itself felt—although liquidity is already high—owing to the fact that the effects of monetary policies on economic activity and especially investment are as a rule rather delayed. This, of course, also applies to the recent and so far modest increases in Government expenditure and in public and semi-public investment.

35. On the other side of the ledger the first thing to note is that the signs of revival of economic activity are generally weak. Although some countries are expected to pick up steadily but slowly in the coming months, others are likely to experience some further slackening of activity.

36. Industrial investment, it is true, is still running high in many industries in spite of lower levels of industrial output. On the other hand, there is little evidence that the easier conditions on the money and capital markets have produced stimulating effects outside house building. Investment in manufacturing industry—except the moto-car industry—appears to be more for replacement and, in some lines, for long-term modernisation than for immediate expansion. Indeed, in many industries—among them the steel industry—capacity built up during the boom is in excess of the relatively lower demand levels which are to be expected in the near future. The existence of excess capacity in a number of sectors of European industry is also likely to make private investment less responsive even to more specific stimuli than easy money conditions. Moreover, as the Report points out, the uncertainties concerning intra-European commercial policies and the resulting pattern of trade are also affecting investment decisions.

37. While inventory policy is not so decisive a factor in business conditions as in the United States, it has been shown that it has nevertheless played quite an important role in Europe, both at the beginning of the recent boom and in ending it. Considering the already low levels of stocks, particularly for certain raw materials, further stock depletion should not be expected to worsen conditions. At the same time it is unlikely that there will be a reversal to stock accumulation until the outlook for sales and profits has improved. Profit margins having been squeezed for some time as a result of receding demand and international competition, a marked return of confidence in a revival of economic activity may be needed before dealers' orders start to mount again over and above levels required to maintain present turnover.

38. A further factor that clouds the outlook is the slackening in export demand in Europe and in the rest of the world. As regards intra-European trade, forecasts are, of course, particularly difficult in view of the uncertainties concerning the effects of the operation of the Common Market and the deadlock in the negotiations for a European Economic Association. The re-liberalisation of French imports is undoubtedly a positive factor in the situation, although too great hopes should perhaps not be attached to it, in view of the fact that industrial output in France is still declining. Another positive factor is the continuing economic expansion in Germany, but here again the beneficial effects could easily be reversed if renewed German export surpluses were to exert pressure on the payments positions of other European countries.

39. With regard to the propects for Europe's exports to the United States, the Report notes that in view of the upward movement of business activity in the United States and in the light of present trends of trade, it does not seem likely that Europe will suffer from any delayed direct repercussions of a substantial nature. Considering that one of the main causes of the high level of imports from Europe during the United States recession was the fact that consumer incomes and spending in the United States were well maintained despite the decline in industrial activity, as also that European exports to the United States have levelled off after the end of the American recession, it would in all circumstances be unwise to bank on a continuance of the large increases in European exports experienced during the boom. In any case it should be recalled that Europe's commodity exports to the United States amount to only one-seventh of its total exports to the rest of the world and to about 1 per cent of the total output of member countries combined. In fact it would appear more likely that European imports from the United States will pick up faster than its exports, as a result of the further liberalisation of dollar trade that may be expected in the near future in consequence of the move to convertibility in Europe.

40. Nor is any support to activity levels in Europe to be expected from export demand in third countries. True, primary producers' earnings on exports to the United States should start rising again in 1959 with a continued recovery in American demand, but this cannot make up for the much more substantial decline which has taken place in their exports to Europe in the last two years, since Europe represents an export market twice the size of the American market for these countries. Indeed, the Report remarks that the export earnings of third countries may not yet have reached their trough. While not all third countries are in balance-of-payments difficulties, some countries such as Japan have already been obliged to take remedial action and India—Europe's most important third country market—,New Zealand, and certain South American countries, have recently cut imports drastically. Unless international lending increases further in the near future a number of other countries may also be forced to restrict imports.

41. The decision to increase the lending power of the Bank for International Reconstruction and Development by 50 per cent is an encouraging sign that this problem is receiving attention. By itself, however, public international finance cannot reverse the trend, in the absence of resumed demand in Western Europe and in face of declining capital exports from Western Europe.

42. In short, export demand in the U. S. and third countries cannot be counted upon to provide substantial stimuli to economic expansion in Europe. Just as this slackening in activity in general originated not from outside influences but from domestic developments, Europe will be obliged to generate within itself the main forces of its own expansion. The most serious feature for the long-term prospect is therefore the apparent absence of any spontaneous expansionary force in the European economy comparable with the reconstruction needs in the first post-war period and the accumulated demand for consumers' durables that started off the recent boom.

43. The unavoidable conclusion is that the rate of growth in the next few years, if things are left to themselves, is likely to be lower than that achieved in the post-war period up to mid-1957. This conclusion of the OEEC Tenth Report is also shared by the Economic Commission for Europe in its recently published Economic Survey of Europe for 1958. The fact that both these reports stress that in the longer run the resumption of an adequate rate of expansion will depend on new advances in private investment and consumption serves as a warning, since it would appear that it is precisely here that forces for expansion are lacking.

4. Policies for Expansion

44. The review of the situation up to the end of 1958 indicates that the initial policies for expansion have been timid and largely ineffective. The present discussion of the policies that appear to be called for will therefore start by examining whether the policy lines for the near future, as set out in the first part of. the Tenth Report, reflect a change in the thinking of the Governments of member countries.

4.1. Present OEEC Policies

45. The need for a reversal of economic policies from restrictions on overall demand to stimulating economic activity was recognised by the Council of 0. E. E. C. as early as July 1958, when it adopted a recommendation with regard to the economic situation in which Member Governments were urged to "now pursue policies encouraging sustainable economic growth". However, the recommendation runs on as follows : "In so doing they should guard against any renewal of inflationary pressures and avoid endangering the balance of payments".

46. Although nine months have elapsed between the adoption of this recommendation and the publication of the Tenth Report, it would seem that, while economic growth is certainly the keynote of the Report, equal emphasis is still placed on the other restraining element. The need for economic growth is once again qualified by adding that the objective of economic policies should be to stimulate a rate of economic growth that is sound, i.e. that can be sustained without giving rise to inflation and balance-of-payments disequilibrium.

47. Having declared, as the first of its conclusions (Chapter I, para. 10, pages 9-10), that "policy must generally be focussed on the need to stimulate an adequate rate of economic growth" (point (i)), the Report goes on to say that "it is equally essential that the measures adopted should not be such as to lead to a rate of growth of demand which gives rise to inflation and balance-of-payments disequilibrium and which cannot therefore be sustained" (point (ii)).

48. In the two following points the Report indicates the main lines of expansionary action. Greater emphasis should be laid on increasing consumption (point (iii)). A revival of international trade is further needed; in particular it is essential that further action should be taken to stimulate trade by reducing the remaining barriers to trade both between member countries and between member countries and the rest of the world (point (iv)).

49. These considerations are counterbalanced by three points stressing the need for internal and external stability. In the first (point (viii)) the Report warns that it is necessary that strains in particular sectors or industries be prevented early in an expansion by appropriate measures to limit demand and to expand supply; further, (point (ix)) excessive overall demand must be avoided and (point (x)) also cost inflation.

50. Within this balanced framework of growth and stability the Report emphasises (point (vi)) the special responsibility of the countries in a stronger economic position, particularly (point (vii)) towards the countries which are in course of development, and, which rely heavily on agricultural exports, and (point (v)), emphasises also that countries should so far as possible act in concert since isolated efforts could quickly produce balance-of-payments difficulties in the new payments situation introduced by convertiblity, which increases the need for greater co-ordination of national policies.

51. Finally, considering that countries are committed to the maintenance of high levels of activity and that price increases have become almost irreversible, the Report stresses (point (xi)) that Governments should make the best possible use of all the appropriate instruments of stabilisation policy and (point (xii)) improve the collection of current information on economic developments.

52. The Tenth Report thus leads to the general impression that Governments still lay equal stress on growth and on stability.

53. This attitude is undoubtedly largely connected with the general move towards non-resident convertibility on current transactions, a move that must be considered an important measure of economic progress inasmuch as it furthers a more rational international division of labour. Governments are hence required to observe stricter discipline in their economic policies so as to ensure that total demand is kept within the limits of total resources. Convertibility inevitably makes countries more sensitive to price movements both at home and abroad, particularly in a group of countries such as the West European countries which have very close commercial relations with each other. Nevertheless, your Rapporteur is convinced that the present situation calls for a holder approach to the problems of expansion. It is a fact that existing resources, both industrial capacity and foreign balances, are substantially in excess of present demand levels. They could therefore well sustain some increase in overall demand and governments should consider it their urgent duty to take the necessary measures to ensure the fullest possible use of available resources in a process of self-generating growth.

54. As rightly emphasised in the Tenth Report, this will require the use also of instruments of economic policy other than general monetary policies. Admittedly, the greater reliance placed on general monetary policies is also connected with the move to convertibility. But, while the wider use of general policies should be heralded as an improvement on earlier quantitative, and necessarily ai'bitra-ry, controls, and as a step towards a more rational allocation of national resources in response to world market conditions, this should not deter Governments from taking other measures to stimulate expansion where it is apparent that monetary policies are inadequate.

4.2. Co-ordination of policies

55. The Tenth Report is emphatic in stating that "insofar as the newly introduced non-resident convertibility contributes to increased liberalisation of trade and capital movements, divergences in member countries' internal situations and policies will in general be reflected more directly than hitherto in their external payments. It is, therefore, all the more essential that they should improve the co-ordination of their policies. If the expansionary policies are not effectively coordinated, and if differences in the degree of demand pressure on resources again become j marked, new balance-of-payments difficulties ! could arise and the advantages of the recent I international co-operation in the monetary j field soon be sacrifieel". Your Rapporteur's | view that the present need is for a more deter- j mined shift toward policies designed to encou- I rage a revival of economic activity and a j fuller employment of resources and particu- : larly of the labour force lends added strength to this argument. For it is obvious that if, as advocated here, member countries should push economic expansion as near as possible to the limits of total resources, the more indispensable will it become to ensure the closest possible co-ordination of policies, based on regular, indeed almost continuous, reviews of the development of trade, payments and indeed, the whole complex of national policies.

56. In making its recommendation concerning policies for sustained economic growth in July 1958, the Council recognised "that the problem of effective co-ordination of economic policies had by no means been resolved" [2]. The repeated plea for closer co-ordination of economic policies made in the Tenth Report indicates that this is still the case. This is not to deny that over the ten years of the O. É. E. C.'s existence member countries have evolved habits of co-operation which have been and remain most valuable. The most long-standing of the 0. E. E. C.'s methods of promoting the co-ordination of general economic policies has been the well-known procedure of the annual reviews which have created an opportunity for regular and frank discussions of all problems of policy, including that of the impact of an individual country's policy on the economies of other member countries. The principal organs of the 0. E. E. C. involved in reviewing national policies have been the Managing Board of the E. P. U. (now replaced by the Board of Management of the E. M. A.—European Monetary Agreement), the Steering Board for Trade and the Economic Committee. Moreover, in 1956, the Council decided to set up a Ministerial Working Party, assisted by senior officials, which meets from time to time as the situation requires; a working party composed of independent experts is also assisting the 0. E. E. C. as a guide on economic policies.

57. Among recent instances of policy decisions in member countries that have been the result of consultations in the 0. E. E. C. one might mention the steps taken by the German authorities to increase imports and the outflow of capital. The concerted move to convertibility is another instance, as is also the fact that despite the payments difficulties experienced during the boom, trade liberalisation was generally maintained.

58. Unquestionably the past experience of the 0. E. E. C. in the co-ordination of economic policies provides a foundation for future progress, and in stating that the co-ordination of policies is still not adequate to meet the demands of the current situation, the aim is not to belittle the results achieved or the difficulties ahead, but to urge Member Governments to overhaul and make the existing OEEC machinery for policy coordination more effective. There can be no doubt that this is the most urgent task of all for the 0. E. E. C. at the present juncture.

4.3. A Programme for Expansion

59. The difference between the views developed in the present paper and those set out in the Tenth Report is in the last analysis a matter of emphasis. It is no less important for that. The shift from a continuation of present policies, which despite the recognition of the problems of economic growth facing Europe appear to be dictated largely by fears of future unfavourable developments of the payments position, to a determined and concerted effort to raise production and employment levels, may mean the difference between continued stagnation for some time, with the dangers this entails, and the more rapid realisation of higher living standards not only in Europe but in large areas of the free world.

60. How near the danger-line of inflation member countries should steer the economy will, of course, always remain to some extent a matter of political opinion which it is for national Governments to settle with their parliaments and public opinion. What Governments, parliaments, and public opinion alike must realise more clearly than ever is that the decisions taken in these matters, which determine levels of output, employment and prices, are indissolubly linked—via the channels of trade and the payments mechanism—-with corresponding policies in neighbouring countries.

61. With the many politically determined rigidities built into our societies, on the one hand, and their sensitivity to economic fluctuations abroad on the other, the problem of sustaining a desirable level of economic growth, while maintaining stability in the economy, is virtually impossible to solve unless there is effective co-ordination of national policies in an international framework.

62. Such co-ordination of policies, however, today requires more than consultations and confrontations. To achieve the necessary high rate of economic growth, the European countries must develop a constructive programme for expansion within the coordinating machinery of the 0. E. E. C. It will be recalled that 0. E. E. C. did something-similar in 1951 when it launched a programme for the achievement of a 25 per cent increase in production in five years. The economic situation is, of course, entirely different today, and the 1951 programme is only mentioned to show that there exist precedents for the type of co-operative effort to increase output which is proposed.

63. As suggested in the Tenth Report, one of the objectives of a programme for expansion should be to revive intra-European trade, as a stimulus to economic recovery, by reducing remaining trade barriers, particularly quantitative restrictions and especially in the agricultural sector. The principal task, however,

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2. Tenth Report, para. 113.

should be to co-ordinate policies designed to stimulate consumption and overall demand by all the means at the disposal of Governments, including fiscal inducements and public investment where necessary. A third element should consist in a long-term concerted programme of aid for the economic development of the less industrialised member countries, as well as of other less developed regions. This would involve increased expenditure of public funds as well as the encouragement of private capital exports. Fourthly, a determined effort should be made to improve the collection and standardised presentation of significant economic data to provide better instruments for economic diagnosis and short-term forecasting on the lines that are being developed in the European Economic Community.

64. Whatever is clone to revive production, employment and trade, the fact should finally be stressed, as the Tenth Report itself emphasises, that the main responsibility for turning the economic tide towards renewed expansion lies with the four largest countries, France, Germany, Italy and the United Kingdom. Without the support of economic expansion and increased demand in the larger economies, the smaller countries are severely handicapped, indeed crippled, in their individual policies for full employment.

65. A last, but important word. A European programme for expansion should be seen in the context of the Common Market and the difficult negotiations of a European Economic Association. We must face the fact that these efforts to integrate Europe will be very deeply affected by the economic climate in which they develop; a healthy rate of expansion will do as much to facilitate as continued stagnation to endanger their realisation. But it is also vitally important to demonstrate the determination of European Governments to ensure an expansion of their own output and consumption, and thus to foster a revival of world trade, in order to strengthen confidence abroad in the free economy and to allay the fears which the present economic situation in Europe and the European integration projects themselves have understandably given vise to, particularly in the less developed countries which depend so heavily on their earnings from exports to Europe if they are to raise the low living standards of their populations.

66. Your Rapporteur desires to record his appreciation of the great assistance he has received from the Secretariat in the preparation of this report.