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Customs Union Theory, Political Economy, and Tiers  
Monde Reality: A Critique Toward a Revision of Economic  
Integration Analysis\*

Why does the theory of economic integration as it now stands appear largely irrelevant to actual economic union proposals and institutions, particularly to those outside Eastern Europe? To what extent does its abstraction from socio-political concerns and its potentially simplistic assumptions about the nature of governmental concern with economic policy limit its usefulness? To what extent are these weaknesses the result of a faulty analytical approach, of inappropriate institutional and structural assumptions, and to what of incompleteness rather than error or unrealism?

The examination of these questions is not, as may appear at first glance of purely academic (or pedagogic) interest. The reformulation of economic union theory to create more useful applied analytical tools will be much sounder if the lack of cutting power and gaps in the present tool list are better understood. Moreover, given the substantial body of theoretical - analytical formulations existing to start a nouveau without any attempt to see what concepts and lines of attack are useful or usefully modifiable would be misplaced inventiveness of a high order.

The theory of economic integration arose as a branch of Vinerian tariff and neo-pigivian welfare economics. Despite fairly extensive recent refinement, it retains many of the more limiting and artificial characteristics of its origins. Four of the most crucial of these are: use of comparative static and marginal, not dynamic and structural, analysis, assumption of a negative (permissive) rather than a positive (directive) role for economic policy, adoption of a functional rather than institutional policy evaluation framework, and explicit or implicit use of assumptions based on the "special case" of industrial economies.

Use of semi-comparative static analysis contrasting the situation with and without economic union at a given time has the result of placing emphasis on gains or losses from static efficiency and resource allocation considerations. To the extent the gains (or costs) from economic union arise out of increased rates of growth either in resource utilization or in production efficiency they tend to be overloaded or treated as side effects. At best one has the median taxonomic approach to marshallian comparative statics which is highly cumbersome and certainly ill adopted for considering growth as an integral part of models.

Moreover, the limitations of this approach are increased by the use of a modified Ricardian - or simplistic Ohlin - model in regard to comparative advantage. Advantages in production are assumed either to result from basically unchanging factor endowment characteristics or from economies of scale. Given the standard assumptions of perfect competition and mobility of the location of production, these will be

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\* This paper is one of three attempting a reformulation of economic integration analysis in terms more relevant to non-industrial economies. The first (EDRP 81) provides a tentative formulation of the potential relevance of economic unions to achieving and sustaining rapid growth under african economic conditions. The third will attempt specific application of the approach set out in the initial pair to East African economic union questions.

be mutually reinforcing within a common market. Specialization - and intramarket trade flow - will increase on the basis of natural comparative advantage determined location of optimal production units.

Entirely apart from questions as to the validity of the comparative and mobility assumptions this approach fails to face the question of whether and to what extent comparative advantage (even if based on factor quality and supply as defined by Heckscher and Ohlin) is created rather than inherent. If it is created then productive location within a common market will have a decided tendency to reinforce historic patterns of created advantage whether these are optimal in a real resource utilization or growth sense or not. Further the acceptance and reinforcement of historic created comparative advantage as a basis for allocation of production is likely to increase both income level and growth disparities within the economic union. Free movement of labour and investment within the common market - as assumed in the model - would increase the polarizing tendencies regionally, albeit possibly damping them on a per capita basis.

Finally, the analysis implicitly assumes changes in the market structure of production and consumption - though possibly not of extra market trade - will be marginal. The same real resources are to be allocated more efficiently resulting in higher outputs but not in any great change in the distribution of output by sector or industry. In other words one has virtually a Walrasian equilibrium type growth in which all the output figures are multiplied by a fixed coefficient. Alternatively, the result could be viewed as an input-output system in which a more or less uniform reduction in input coefficients allowed a consistent expansion of output.

When combined with the standard assumptions of factor mobility between uses in any one of the uniting economies and of mobility of labour and capital among them, this Walrasian equilibrium approach totally abstracts not only from questions of changed production or demand patterns for the union as a whole, but also from adjustment and factor redeployment problems in the smaller units.

This approach is not inherently unreasonable for flexible economies with broadly based structures of production. Changes in total output are likely to be marginal for the economic union and the increase in output per head not such as to alter the patterns of demand. The instantaneous adjustment assumption is unrealistic but given probable changes in location of productive activity, the redeployment problem would not be severe in a growing economy with a reasonably flexible and mobile labour force.

However, this analysis does not deal with the case in which a major proposed gain from economic union is the creation of a market adequate to support new lines of activity. Under these conditions the structure of production will alter substantially if the market unification proves successful. Such structural alterations are likely to have substantial effects both on utilization of resources and on growth rates. The first of these problems is abstracted from in the Walrasian equilibrium approach which assumes both continuous full employment and totally (or predominantly) intra-market financing of investment. Analytical concerns have tended to be permissive rather than directive in that the operational framework for economic policy

assumed or implied has been Marshallian neo-laissez faire. The approach is negative in the sense of removing barriers to efficient private utilization of resources rather than positive in the sense of creating possibilities more effective planned or directive resource allocation.

Several conditions are necessary for this approach to be relevant. First the economies must be basically private sector in orientation with public economic policy and expenditure supporting and national planning indicative and inducive. Second there must be workable competition (however defined) to ensure that resource reallocation does take place and that economies of scale are realized.\*\* A stricter formulation of this condition is that whatever divergences from perfect competition exist must not be such as to alter materially the optimum resource allocation (post union) which would result under perfectly competitive conditions. Third the changes in production and productive location required must be consistent - in scale and time horizon - with private resources and decision making outlook (either initially or subject to secondary state inducement and support programmes). Fourth private and public costs and benefits accruing from union induced changes must be not only in the same direction but substantially equivalent.

Whether these conditions are met in any particular case is a matter of fact. It is worth noting that the third and fourth are more likely to be satisfied if the changes entailed by union are marginal and the required adjustment period short. To the extent the first condition is not met analysis assuming it is likely to be irrelevant while to the extent the others are not met actual results are likely to diverge from those analytically projected \*\*\*

The neo-laissez faire characteristic of economic union analysis leads both logically and practically to a functional (or specific) rather than a structural (or comprehensive) view of economic policy. In practice - albeit with considerably less logical justification - this characteristic appears to hold true of most CMEA oriented socialist analytical work.

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\* Clearly this characteristic is not relevant to CMEA (COMECON) oriented analytical writing. However appear to be very few serious pieces on the basic purposes and operations of an economic unifying or coordinating body among socialist economies. What articles the author has seen are extremely tentative and limited precisely because they tend to think of economic union as implying common "free" market and therefore inconsistent with central planning. Realization that the presumptive parallel to a Common Market among "free market" economies is a Common Plan among centrally planned economies is apparently recent and incomplete. In any event CMEA and its literature have had minimal impact on analytical formulation, proposals, and policies for tiers monderegional economic cooperation and unification.

\*\*EEC's attempts to unify and bolster anti-cartel legislation and the British Conservative interest in EEC membership as a competitive spur to efficiency are examples of policies and concerns consistent with and to some extent deriving from this analytical point.

\*\*\*The European Iron and Steel Community illustrates such divergence. The combination of national planning (and employment) imperatives, cartellization, and the scope of changes both in resources and time required has resulted in substantially slower and lesser alterations in productive location and scale and lower gains in efficiency than would have been the case had the four assumptions been fully met.

Since policies are regarded as aimed at removing particular obstacles to, or providing certain incentives for, private action within a basically private, workably competitive, market economy they are seen as limited in scope and specific in orientation. This outlook is, of course, reinforced by the assumption that the changes with which the market and its component economies are faced are marginal and the resource redeployment problems limited in amplitude and period.

If the conditions for a neo-laissez faire analytical framework are not met there is a strong case for a comprehensive approach to policy and institutional effects of an economic union. This case is logically irrefutable if the economies involved are, in fact, basically public plan rather than private market economies\* Economic integration would then be regarded as a process designed to attain certain ends and an overall optimal institutional and policy framework would be formulated for the purpose of their attainment. Specific policy and institutional additions and alterations would be designed to adjust the present framework to that envisaged as most appropriate for the desired operation of the economic union.

The structural and institutional assumptions underlying economic union analysis are those of what Dudley Seers has aptly termed "the special case", the developed industrial economies. Some of these assumptions - more often implicitly the explicitly formulated - have been noted above. Four additional structural assumptions are usual. First, relationships among different sectors of the economy are taken to be numerous, quantitatively significant, and substantially more important than international linkages. Second, substantial economic flexibility in use (or mobility) of factors of production both geographically and among different economic units or activities is assumed. Therefore even substantial alteration of production to meet changes in demand or relative costs is possible without radical price shifts, severe and lasting bottlenecks, or substantial long term unemployment. Third, the pattern of production is taken to be roughly balanced in relation to national demand. Obviously, autarchy is not assumed, rather that the bulk of the output of all major economic sectors and most individual lines of production is home market directed while the bulk of national demand for most products and all major sectors is met from national output. Fourth, output levels and growth rates are viewed as primarily internally generated and internally sustainable in the sense that national demand is central in calling forth both short run use of productive capacity and long run investment in additional capacity. Furthermore, growth is substantially domestically sustainable in the real sense because of the existence of substantial intermediate and capital goods production capacity and of corporate and public savings flows sufficient to sustain high levels of productive investment.

In short the uniting, economies are assumed to be nationally integrated, flexible, and capable of self generated and self sustained growth. These assumptions are largely appropriate for at least most European economies, the United States, Canada, and (with rather more qualifications) China.

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\* This definition is admittedly imprecise. The mere presence of a "plan" does not make an economy planned. The degree of state control over specific private economic decisions - in particular investment and output levels and international transactions - and the relative share and role of public investment, especially in large scale directly productive activities, are probably the critical criteria.

They are likely to lead to faulty conclusions when applied to economies dependent on primary product export proceeds for a substantial share of their national product, investible surplus, command over manufactured products and/or supplies of machinery and investment goods.

II.

The particular analytical emphasis of economic union theory are closely related to its special characteristics and assumptions. These are global welfare effects (i.e. the relative effects of trade creation and distortion), static resource allocation and scale economies, and particular policy modifications necessary for effective operation of a common market. Two more recent concerns - often vaguely if at all, linked to the remainder of the analysis - have been growth reinforcement and vertical integration of primary producing units with a central industrial common market.

The welfare analysis has tended to be either neo-pigovian or in terms of the Scitovsky "bribe potential" criterion. A common market is held to be justified if gains in welfare (measured in terms of additional real consumptive capacity) to the uniting states exceed losses to the rest of the world. In other words if total world output - physical - is increased then it is accepted that the common market has increased global welfare because (given the basically unchanged productive structure of the union) transfers to losing states equalling their losses could be made out of common market member gains. No assumption that such transfers will take place is made and no attention is paid to questions of the union's effect on equality of global union distribution.

Evaluation of the conditions under which the conditions for a net gain will be met has centered on trade creation vs trade diversion. In general, the criterion is that if the gains on trade created among union members (new trade value times average saving per unit) exceeds the loss on trade diverted from outside sources to market members (diverted trade value times average loss per unit\*) the global welfare (output) effects will be positive. As may be noted this assumes full employment of factors of production throughout both in the common market and in outside economies.

Even at this level, certain ambiguities - or cases assumed to be of secondary importance and mentioned at best in passing - arise. Trade diversion cannot be costed (or quantified) in terms of total imports shifted because of tariff discrimination times pre-union cost differences. Post union costs for the market member exporter and pre-union for the outside must be used to evaluate added "diverted trade" cost. Otherwise the analysis will abstract from economies of scale which might substantially reduce costs in the union member expanding production and raise them in the market losing outsider. Especially if the joining economies are both individually small (say each under \$1 billion money sector national product) and relatively far from outside sources of supply, the scale effect may swamp the apparent pre-union data

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\* The "loss" on some of the "diverted" imports might be negative. This would be true if higher pre-union tariffs against union members had, in fact, diverted imports to outsider sources. A number of such cases might well arise in West Africa were the Anglophonic and EEC Associate states to form a common market. For example a number of Nigerian exports including beer, confectionery, and probably cement, shoes, plastic goods, and plywood and finished lumber are kept out of Cameroonian markets by the tariff structures heavy preference to EEC and Associate suppliers.

based diversionary effect. Unfortunately in this case, "diverted trade" cost does not represent global gains or losses. Nor will the gains or losses of the market and outsiders necessarily be equal and opposite, indeed both could lose or the market gain and the outside suffer no loss if it suffered no economy of scale losses and could immediately redeploy its resources to equally productive uses. Assuming full employment and efficient resource allocation throughout, formulas for computing market added real resource cost ( $DC_M$ ), outside added real resource cost ( $DC_O$ ) and global added resource cost ( $DC_g$ ) can be written:

$$1. DC_M = T_D (C_{M2} - C_{O1}) - D_1 (C_{M1} - C_{M2})$$

$$2. DC_O = D (C_{O2} - C_{O1})$$

$$3. DC_g = DC_M + DC_O$$

$DC_M$  and  $DC_g$  can be  $\geq 0$

$DC_O$  can be  $>$

$T_D$  = trade diverted

$C_{M1}$  = market pre-union unit cost

$C_{M2}$  = market post-union unit (scale effect)

$C_{O1}$  = outsider pre-union unit cost

$C_{O2}$  = outsider post-union unit cost (scale effect)

$D_1$  = market pre-union output of goods affected by trade diversion.

$D$  = outsider pre and post union output for home use and non-market export of goods affected by trade diversion

To the extent that  $D_1$  is large relative to  $T_D$  and/or  $C_{M2}$  is substantially below  $C_{M1}$ ,  $DC_M$  is likely to be small or negative.

To the extent that  $D$  is large relative to  $T_D$  and/or  $C_{O2}$  is substantially above  $C_{O1}$ ,  $DC_O$  is likely to be large.

Ceteris paribus the larger  $D_1$  and  $D$  are in relation to  $T_D$  the less the  $C_2$  will diverge from the  $C_{1s}$ .

The smaller  $D_1$  is to  $T_D$  and  $D$  the greater the relative change of the  $C_M$ 's is likely to be in relation to that of the  $C_O$ 's.

Operationally, this suggests that a union among small economies with substantial (protected) inefficient production and imports substantial relative to that production (but not to supplier output) may well result in a negative  $DC_M$  and an insignificant  $DC_O$  even though the computed "trade diversion" cost is positive and large. This conclusion - which is of evident relevance to Africa - is strengthened if the market results in net resource inflows or fuller employment of existing resources in the market economies while not substantially effecting employment levels outside. These conditions are likely to be met if the market members are small relative to their trading partners and have import levels largely determined by export plus resource transfer flows not by national income levels per se.

This is in fact, the position of African states vis a vis their external trading partners.

Similarly the evaluation in terms of trade creation and diversion tends to place little emphasis on income effects. If market members joint product is substantially higher after union then a spillover trade effect benefitting outside economies is almost certain. This would certainly reduce - and might reverse - the initial diversionary effect costs.\* This can be viewed as a secondary trade creation effect. On the other hand if the resource redeployment in the outside economies results in lower real output after union then a "trade destruction" effect will increase the diversion losses. As a first approximation it seems true that the relative sizes of the positive and negative income effects are likely to be proportional to the direct trade creation - diversion gains and losses as modified to take scale considerations into account. Again, however, the smaller the market in relation to its outside trading partners the more likely its redeployment gains are to be substantial and the partner redeployment losses minimal and, therefore, the net real income effects on trade resulting from static redeployment and scale changes are to be positive.

As the foregoing partial amendments to standard trade diversion - creation analysis indicate, two frighteningly unrealistic assumptions remain. First, by assuming full employment in all economies throughout, the possibilities both of creating factor employment possibilities and of facing unemployment of former export producing factors in the market and outside economies respectively is ignored. Second, by taking a comparative static view of output and trade levels the effects of economic union on growth rates both of national product and of trade is left outside the analysis although they could completely alter the static gain and loss calculations within a relatively short period.

The next stage in the analysis has usually been to determine what pre-union production patterns are likely to result in predominantly trade diversionary and predominantly trade creating patterns. Here substantial confusion has arisen partly, perhaps, because of the basically static and marginal approach to productive structures. There is general agreement that the union of complementary economies, will maximize the share of diverted trade in total intramarket transactions while uniting competitive economies will tend to maximize the share of created trade. Both trade diversion and trade creation will be lessened to the extent the uniting economies were their own major trading partners before as well as other common market creation. Somewhat ironically this suggests that ceteris paribus a globally beneficial common market will result in less added-market trade and minimal impact on market - outside trade. Admittedly this probability reinforces the appropriateness of the marginal change assumption noted earlier. One difficulty with this presentation of complementarity and competitiveness is that it does not specify whether the member production structures are competitive before or after equilibrium. Further it fails to distinguish whether competitiveness - and to lesser degree or irrelevant nature. If the production structures of the uniting economies are dominated by export commodities not substantially consumed in any of the market members the

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\* It seems unlikely to reverse them assuming full employment before union. To do so would require very large gains in efficiency in the common market and more productive average resource utilization in the outside economies so long as one holds total resource employment constant.

complementarity or competitiveness is irrelevant as no substantial intra-market trade can result unless the total market structure of production is altered by union. Proposed unions of primary export dominated economies are cases in point, the diversity or homogeneity of member country's export patterns is quite irrelevant to the potential gains from intra-union trade.

The more recent position is that substantial gains are likely if the economies joining are initially competitive but will, after union, become complementary. In other words this formulation recognizes that significant gains are possible only if intra-market trade and individual economy alterations of productive structure are relatively large. However this statement still assumes significant pre-union trade among the economies. If this is absent, the condition for substantial market gains is that the union results in significant intra-market trade in goods not previously produced in the market economies or in significantly lower costs of production for goods previously produced for national markets behind very high protective tariff walls but now produced at substantial economies of scale for the joint market. The former conditions are particularly relevant in Africa or Southeast Asia and the latter in Latin America. Global gains are likely if the market's external trade level is not significantly below that of its pre-union component states. However, this means that the new output represents not only a relative shift in the structure of production but also substantial expansion of certain lines of production without countervailing contractions to release resources. Therefore either pre-union full employment or the absence of significant outside - market resources flows must be relaxed. This is scarcely a surprising conclusion as one of the basic arguments for protection - whether national or regional - is that it allows previously unemployed (or unemployable) resources to be utilized while attracting complementary resources from abroad. Equally, it is quite consistent that it should be of particular significance in the case of small primary export specialized economies with sluggish dependence on external capital sources.

Curiously enough, distribution of gains and losses within the common market has received substantially less analytical attention. Either it is assumed that gains and losses will be so distributed that all members will automatically benefit or that some redistribution mechanism - whether in terms of factor movements or fiscal transfers - will result. While admittedly consistent with a neo-laissez faire economic framework these assumptions appear to be unrealistic. Both the experiences of widening regional disparities within long united economies, e.g. the Appalachian Region in the United States, the Mezzogiorno in Italy, the Northeast in Brazil, and of common market operational difficulties e.g. EEC, East Africa suggest that what Hicks' terms centrifugal or centralizing tendencies are likely to be dominant in an economic union. It will be pure chance if each member has an equivalent (to GNP before union) share of the centres. Especially in a union which is relatively small, involving radical changes in the joint (as well as member) structure of production, substantial intervention in regard to location of production or significant income transfers are likely to be necessary for each member to have net gains much less for gains to be equivalent (either in relation to national product or to population) in each member.

The second concern of analysis has been the nature of the static gains resulting from a common market. These are seen as falling under the broad category of specialization in production with more complete adherence to real comparative advantage and economies of scale the significant sub-categories.



The limitations involved in the Ricardian or simplistic Heckscher - Ohlin type definition of comparative advantages in factor use as natural and permanent have already been noted. Similarly attention has been drawn to the inadequate consideration of scale effects on gains and losses within (and outside) the common market.

Analysis of the pattern of particular policy changes needed to permit the efficient operation of competitive forces within a common market has proceeded on a taxonomic basis. Perhaps predictably the initial - and in many respects still the best - treatment is that of J.E. Meade, Problems of Economic Union. There is broad agreement on the need for harmonization of taxation and labour payment levels and of joint action to further competition and increase factor mobility. Divergences arise on the degree of specific tax, wage, social benefit, and competition inducing unification required exist but appear to be of secondary significance.\* Two critical points which do emerge - albeit in some studies blurred by the myriad particular cases treated - are that broadly parallel economic legislation over a wide range of major areas and substantial faith in the future actions of partners (including continued adherence to the common market) are essential for the viable functioning of even a neo-laissez faire economic union.

Growth stimulation or reinforcement has become an analytical concern because of its significance among the considerations leading to the Treaty of Rome and the apparently substantial impact EEC has had in this regard. The difficulty of integration of this aspect into the basically static analytical model has tended to be sidestepped by considering the change as a once for all increase in growth rates resulting from more efficient resource allocation and economies of scale. The reasons posited are that lower costs increase competitiveness of output in world markets and therefore export growth as well as raising profits creating both higher marginal efficiency of capital and the investible surpluses to carry out the longer desired investment programme. The profit effect will tend to be self-fulfilling in that higher expected profits will lead to higher desired investment as well as increased foreign capital inflows (if for no other reason to protect established markets as re US and UK firms' additions to production capacity in the Six) and thus increase ex post demand as well as capacity. This line of analysis requires relaxing the continuous full employment assumption as well as the negligible market - outside productive capital flows assumption. In most forms it also implies an expected shift in the basic market - outside balance of trade position which is - apparently assumed to be both stable and in balance before and after union in the main body of analysis.

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\* EEC experience is on the side of those who argue broad equivalence in broad areas rather than specific policy uniformity.

Analysis - or rationalization? - of the effects of union between a central industrial economy common market and a group of peripheral primary producers also received substantial stimulation from EEC and its Associate member policies\*, Eurafrican and related proposals have sought to develop on analytical base showing mutual gain through lower cost primary product supplies and stronger export markets to the centre and higher primary product prices and larger investment flows for the periphery.

The inconsistency in regard to primary product prices is obvious but secondary. The union of a group of industrial and a group of primary producing economies in a common market is the classic case of dominance of trade diversion effects with negative global welfare effects. Primary exports cannot benefit except by discrimination against lower cost outside producers. Neither can industrial exports within the market be expanded except at the expense of lower cost outside industrial economies and the primary producers. The classic hothouse protection case arises. If gains and losses are divided equally both the centre and the periphery are likely to lose by the resultant inflated cost structure and by a clear reduction of competitive pressures for greater efficiency either at any given time or over time.

In practice, one would not expect the losses to be shared in a ratio equivalent to national products but to fall more heavily on the peripheral members (or Associates). Their trade to monetary product ratios are likely to be higher and their bargaining power less. Moreover the union - even with safeguards - is likely to reduce their ability to develop lines of production competitive with those of the centre economies, especially if these are their chief sources of investment funds.

EEC - Associate experience does little to challenge the appropriateness of these analytical conclusions. The special provisions built in to the arms length Greek and Turkish Association agreements as opposed to their relative absence from the ex-colonial ones strongly suggests that the latter are net losers from Association except to the extent it augments their global capital importing capacity. Admittedly Association with EEC did widen the range of "Economic union" import sources from the ex-colonial power to the Six but, by the same token, this was a less advantageous change than would have resulted from - say - a most favoured nation tariff policy.\*\*

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\* It can be argued quite plausibly that much of the literature on the economics of imperialism deals precisely with this topic. However, both the assumptions and the areas of special concern tended to be different e.g. dynamic growth effects, unemployment and employment changes, and investment flows were always significant in colonial-imperial analysis. Moreover socio-political considerations and the actual institutional patterns of the colonial periphery received rather more attention. On the other hand, the analysis itself was often loose or shoddy and often e.g. Hobson, Luxemburg quite inadequately supported by the data cited. Only since 1955 has there emerged any substantial interaction between analysis of industrial centre - colonial or dependent periphery economic relations and that of economic union.

\*\* In any event, the loss of French import subsidies on primary products entailed by the lower EEC protective duties against outsiders more than offsets this gain. At the same time, it lowers the centre's loss from the union albeit by raising that of all members except France.

The analytical model appears even less relevant to any proposed Asian economic union. With the exception of India (Japan and China do not figure in any of the proposals) the economies are basically irrelevantly competitive and/or complementary.\* For an economic union not involving India to have a significant impact, massive changes in the union structure of production are needed and the gains from union would arise if, and to the extent, it made possible and resulted in development along these lines. In India were in the union, special problems would arise as in a laissez faire common market virtually all large scale industry would tend to gravitate to her larger base market and much more advanced industrial foundation.

Africa is nearly a pure case of non-applicability of the institutional-structural assumptions. Certainly neither the continued existence of the East African Common Market nor the creation of any additional or broader one will depend significantly either on global gain and loss considerations or on static resource allocational efficiency within basically unchanged productive structures. Nor - given even joint market sizes - can competition be viewed as a very hopeful prime mover even in the economies with loose or ineffectual planning mechanisms.

A number of the analytical limitations can be removed either by substituting more appropriate structural and institutional assumptions or by adding specific consideration of dynamic effects. Indeed, the previous discussion of the existing theory has pointed to a number of instances in which such additions or modifications appear to involve relatively minor effort.

Before proceeding with an attempt to apply, and in the process to modify, the analytical apparatus to African economic union considerations, it is necessary to re-examine the relationships between economic union and broader economic aims as well as the socio-political ends toward the attainment of which economic programmes are presumably (and properly) means.

Standard customs union analysis is based on the promise that maximization of current national product through more efficient resource use is the dominant (or only) goal. In so doing it abstracts from growth rate, trade balance employment and unemployment, and structural or institutional change which are often significantly more important from a national policy formulation viewpoint.

Further, by assuming continuous trade balance with imports determined by the size of national product and continuous full employment of factors, the analysis is able to define trade diversion as unambiguously harmful and its minimization as a goal. In the case of economies dependent on capital imports for much of their domestic fixed investment and with substantial resources unemployed or unemployable in existing lines of pre-union production trade diversion may in fact have positive global and market effects on real output.

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\* There is, in fact, substantial intra- ECAFE trade even excluding Japan. Apart from Indian manufactured goods exports, however, it consists predominantly of Burmese and Thai rice exports. The reasons why economic union might effect these are rather different from those posited in the standard analysis.

Examination of the primary concerns of economic union analysis, in summation, bears out Raymond Mikesell's judgement:

By and large the theory of customs unions has been confined to consideration of welfare gains and losses arising from a disturbance of the existing patterns of trade.

Moreover, it has done so in a static frame. Neither resource supply and utilization, market productive structure, nor dynamic growth rate effects have received more than peripheral attention.

### III

Considered in its own terms, the present body of economic union theory seems of doubtful relevance to any economic union except one among neo-laissez faire industrialized economies. Even for such a union its abstraction from resource employment and unemployment, dynamic efficiency, transitional, and period, and intra-union income distributional effects would appear to render it seriously incomplete.

These limitations are least for EEC. However, what sketchy computations exist suggest that static allocation and scale economy efficiency gains cannot be very substantial relative to national product even in this case. The more recent "growth reinforcement" case with its recognition of non-full employment considerations, institutional influences on investment decisions and international investment flows seems of substantially greater explanatory power.

EFTA - which is in any event a loose free trade area rather far from becoming a thoroughgoing common market - is a special case because its existence and policies are largely reflex reactions to EEC. Use of existing analysis would suggest EFTA's economic impact is minimal - a conclusion in accord with empirical evidence.

None of the institutional and neo-laissez faire framework assumptions hold for CMEA (COMECON). Certainly its effects are most unlikely to be the result of freely operating competitive market forces. Furthermore, there is a very substantial divergence in the basic characteristics of the member economies from predominantly industrial Czechoslovakia and economically massive Soviet Union to primary product dependent, economically small Bulgaria. However, potential static efficiency and scale considerations are almost certainly considerably more relevant in CMEA's case than in EEC's.

Latin American economies fit neither the structural nor the institutional assumptions of the analytical frame. They are heavily primary export dependent - at least for financing capital and industrial input goods - and the major ones are neo-mercantilist rather than neo-laissez faire. Moreover, the range in economic size and structure of production between e.g. Brazil and Paraguay is far greater than the model assumes. However, as with CMEA the scope for increased static allocational and scale efficiency gains is large albeit less significant than the possible growth creating effects of market unification.

If the uniting economies pre-union imports were determined by primary export levels plus capital transfers rather than national product levels per se., the entire concept of trade diversion becomes ambiguous. While the import pattern of the union will diverge from that of its pre-union members, imports from outside economies are likely to rise not fall because additional capital inflows induced by the new internal economic opportunities add to import capacity. Traditional export proceeds (and their growth) are unlikely to be substantially determined by the rate of growth of new sectors of production in the early stages of structural changes because there is relatively little direct competition for scarce factors of production.\*

Global welfare analysis presupposes both direct one to one comparability of national gains and losses and global concerns on the part of policy makers. At least in the case of economic unions among poor countries both are fallacious. An addition to African (or Asian or Latin America or Middle Eastern) national product "balanced" by an equal loss to Europe and North America would represent a clear gain in global welfare terms under any reasonable weighting of equity or marginal utility considerations. Further a substantial e.g. 10% gain to Africa totally at the expense of outsiders would mean only 1/5% loss to outside economies because of their far greater absolute magnitude. A 1/5% loss in national product is of an order of magnitude easily handled by national economic policy and indeed is swamped within one year by any plausible growth rate.\*\*

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\* This may no longer hold once a substantial industrial sector is established especially if wage rates rise. Certainly it is not argued that faulty import capacity allocation may not harm primary export sectors but such allocation is neither unique to economic union nor inherent in it. On the other hand, the rate of growth of extra-market export proceeds will be a significant determinant factor in the rate of structural change as well as of extra-market import growth. Comparative South Asian studies by Dr. Pauw and by the author show, success in raising and sustaining traditional export proceeds is closely correlated with achieving development based on structural change vide the cases of the Philippines, Malaya, and Thailand vs those of Burma and Ceylon. The latter's failure to expand their export bases has largely contributed to their failure to attain structural change despite protectionist policies verging on attempted neo-autarchy and certainly far more draconic than those pursued by the achievements in both the primary export and industrial sectors.

\*\* The impact on particular industries will of course be larger, however even here the maximum plausible losses will be smaller than those routinely faced from internal technological shifts or even minor recessions.

A 10% gain foregone is a very different matter. Moreover, as noted above both the market and outside effects are likely to be positive.

Whatever the force of global welfare considerations on trade policy formulation by rich economies - and the history of GATT, IMF, EEC, UNCTAD, and various agricultural subsidy and declining industry employment protection measures leave one distinctly sceptical, not to say cynical - it is both unrealistic and unreasonable to expect African - or other tiers monde - economies to give them any substantial weight. National economic policy is determined on the basis of (real or assumed) national (or politically powerful sectoral) economic interests subject to outside pressures. Global welfare is significant only if a national economy is so massive that the secondary feedback of its policy measures affecting the economies of other states is quantitatively large. Certainly this is true of no African state and - except for a limited number of commodity markets - would not be true of Africa as whole.\*

More broadly the global gains and losses approach inherently views customs unions as generalized - and, if increasing global welfare, rationalized forms of bilateralism. Common market creation is, in short, seen from the member point of view as an exercise in optimum tariff cum bilateral discrimination formulation and from the global standpoint as an inferior "second best" substitute for free trade.

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\* A stronger case can be made for intra - tiers monde welfare effects. For example, industrialization through import substituting against other poor economies is undesirable if regional solutions are possible. Massive diversification by all primary producers into each other's staple exports is - pace the IBRD! - likely to be mutually disastrous. In fact, tiers monde economies do recognize these sub-global welfare considerations at least to the extent of seeking means of mitigating or reversing them vide the UNCTAD "75" and ECA, ECLA, and ECAFE discussions.

This is hardly the way any African state views, or can reasonably be expected to view, economic union.\*

No general assault on the value of analysis based on simplified or special assumptions is intended. Such analysis can: (a) isolate the working of a particular force, (b) provide a clearer understanding of a simple (simpliste) form of an issue from which a broader view can be built by relaxing assumptions; (c) serve as a pedagogical device. However, to believe one can proceed to direct application of such an analytical model to specific problems in political economy is rather analogous to a person attempting to apply the action conclusions of a logical, but not totally realistic, cosmos such as Tolkien's to his daily life.

Governments are rarely, if ever, interested in economic policy as an end. Economic policy and projects are seen as means to attaining social and/or political ends.

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\* If two conditions were met there might well be a good deal to be said for the analytical viewpoint. However, to state the preconditions, is to illustrate just how far reality - present or probable - diverges from them:

1. World tariff policy would be such as to give equal access to processed and finished products based on raw materials as to the unprocessed raw materials themselves. In support, infant economy preferences would be extended to encourage the growth of comparatively advantageous lines of processing and manufacture in present primary export economies;
2. National "full employment promoting" monetary policies would be extended to the international level so that otherwise viable development would not be choked off or distarted by foreign exchange bottlenecks inherently beyond national control loans (which would in the end flow back in lender exports to borrowers) would not be viewed as "aid" any more (or any less) than national deficit financing or credit easing policies to combat recession one viewed as "aid" to the otherwise unemployed workers or semi-employed plants.

African (and other tiers monde) states have, of course, argued for such international trade and finance structural changes. However, despite the support of an growing number of applied as well as theoretical economists in the "industrial world", the likelihood of their speedy adoption is nil. So long as the economically larger and richer states decline to pursue global welfare oriented policies of this vonuity, the "second best" world is the only one in which African states can operate. Or rather they can operate in "second best" or worse, descending to the "best" of stagnant, semi, subsistence neo-autarchy a'la Haiti or (perhaps) Burma.

For example the rate of growth in the standard of living of the groups to which politicians belong, or from which they derive their support, is often of more intrinsic concern to them than the rate of growth of national product as a whole.\* This is not to say that politicians or civil servants are uninterested in, or unwilling to support, economic policies and programmes shown to be relevant to the attainment of socio-political objectives. If a government feels reasonably assured of a long term of office (for whatever reason), it will be willing to consider policies entailing short term sacrifices and unpopularity if it is convinced the medium and long term effects will be fuller attainment of its socio-political ends and greater long run support. Development plans calling for higher short run investment out of national savings - public or private - and slow expansion of private and public consumption are of this type e.g. Ghana, Tanzania.\*\*

If economic integration is to be accepted and promoted by politicians it must be and be shown to be relevant to their socio-political goods. As it happens, economic integration may be vaguely "supported" because it is a handy argument for some other desired end e.g. Malaysian or West Indian political federation with no real idea of what economic possibilities or pre-requisites for attaining them exist. Such an approach is quite as unlikely to lead to political or economic union as is an unexamined grasping for economic unification without any very precise idea as to what might be gained, at what cost, and under which conditions.

There are three reasons why these comments - which apply to applied economic programmes and policies in general are especially relevant to serious economic union.\*\*\*

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\* This statement is not intended as a value judgement. Such concern may mean a concern with greater equality of income distribution, broader economic participation and national integration necessary for long term growth. The soundest defense of the Kenya Plan follows these lines. On the other hand, a mass based government may engage in populist largesse while destroying the bases - political as well as economic - of growth vide Peron and Goulart while a government responsive to a narrow politics-economic elite may follow policies useful to them - at least in the short run - but against any logic for long term growth of the national economy vide Nigeria, Liberia, Gabon, and probably the Ivory Coast.

\*\*If an "economic union" is purely or largely a paper one e.g. the West African Customs Union or not likely to have major effects for some years e.g. Cameroon - Equatorial customs union, it may be very easy to keep "operating" harmoniously. No major conflicts of interest will arise and no state will walk out - except perhaps from boredom. Similarly, peculiar pseudo - unions e.g. Sahel-Benin Entente which have very limited objectives and a single dominant state (Ivory Coast) have very different and less broad conditions for viability than e.g. the East African "Common Economy".



First, the range and scale of the impact of true economic unification is much wider than that of almost any other economic policy - other than the acceptance of serious quantitative planning cum implementation. This, more than incidentally, implies that it is essential for member plans to be harmonized or united if an economic union is to work successfully. Economic policy must be based on clear assumptions as to the limits of the relevant economic unit and as to what is external to it. Moreover, if economic unification is meaningful, it will involve concentration on fewer projects of greater scale and efficiency made viable by increased specialization and higher trade flows within the union. (To balance gains and losses in an economic union by dividing up industries, balancing trade at the level of the lowest intra-market exporter, and increasing the exceptions to the free flow of goods may "preserve" the market in name but minimizes its value to all participants collectively, and maximizes it for none individually.)

Second, economic integration, once established to a significant degree, is not easily or cheaply reversible. To separate a unified economy into its component territorial units (especially if the breakup is less than amicable) is at least disruptive and potentially catastrophic for some or all of the units.\* The serious economic problems still faced by Senegal and Congo Brazzaville flowing from the division of the French West and Equatorial African Federations, the economic crisis ensuing on the collapse of the Mali Federation, and the dimming of Southern Rhodesia's industrial sector outlook at Zambian withdrawal from federation illustrate this point.

Third, economic integration movements - when effectuable - are usually (always?) part, and often a secondary part, of broader socio-political movements.\*\* The "European Idea" and EEC are integrally related (if separable) and the connections between varying expressions of (and support for or antipathy to) political and economic Pan-Africanism are even closer. This argument, of course, works in both directions. A political union with no economic relevance is unlikely to provide substantial enough gains in other fields to be viable. Economic integration once it builds up a body of political support is likely - at the least - to reinforce existing cultural and political forces working for union.

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\* If the economic union was exploitative in operation then some of the members may gain e.g. Zambia and Malawi on Central African breakup. However, even in these cases, a more equitable restructuring of the union could leave all members economically as well or better off than under dissolution.

\*\* The possible exceptions lie in Latin America. On the other hand the weaknesses both of LAFTA and the Central American Economic Union may stem in large measure from the very inchoate nature of "Latin" or "Central" Americanism. Per-contra their rise to the level of serious attempts parallels the growth of a real - if often vague - Latin American feeling of joint interests and desire for joint policy at least in the external policy realm.

If economic programmes and institutions can secure and maintain political approval and support only when seen to be relevant to the goals of government and other power wielding groups, a summary examination of African national socio-political goals and the economic policy means posited for their attainment is appropriate at this point:

1. Economic reconstruction in the sense of reducing dependence on any one export, market, or firm, increasing national production of locally used products, and creating a more national economy in terms of ability to take public economic decisions on the basis of national interests and goals rather than primarily in response to foreign economic interest group pressures;
2. Economic expansion especially in the fields of modernized agriculture and of industrialization;
3. Modernization in terms of acquiring distinctively modern capital cities, industrial plants, agricultural machinery, and transportation equipment;
4. Augmented standards of living and (although the linkage is not always clearly made) of increased output per head to support them;
5. Better and more broadly available social services particularly education, health, and urban housing;
6. Lessening "economic distance" between African and industrial (capitalist or socialist) states. A somewhat lesser number of African states specially stress lessened economic inequality between individuals and regions within African states and within Africa.

One need not take all the professions at face value or assume a high level of operational efficiency in programme implementation to attribute meaning to this set of goals. A majority of African governments actively seek them; the others either passively agree with them, or feel forced to espouse them lest they follow in the paths of Abbe Youlou, President Maga, and King Farouk. In any event, a far reaching proposed economic programme will have little or no chance of serious considerations, much less acceptance, unless it serves and/or appears to serve the rapid attainment of these ends.

The first economic prerequisite for the attainment of each of these ends is very easy to define (even if not to attain): rapid and sustained expansion of real output, defined as production for domestic use plus the import purchasing power of exports. In short Africa is a relevant case for Dudley Seers' dictum:

"The proponents of any major economic policy measure in an underdeveloped economy are under an obligation to show how this measure will stimulate growth."

To which one could well add, and to outline a framework of attainable institutions and implementation programmes capable of achieving the potential economic growth gains. To be attainable the institutions and programmes must be consistent with basic socio-political goods - unlike recurrent studies pressing a "free enterprise", private sector development policy on the Ghana government - and

must not lead to levels of socio-political unrest which will halt or hamstring all government policy or lead to a change of government.\*

Economic integration as a serious policy proposal in Africa, Asia, the Middle East or Latin America must stand or fall on its ability to satisfy this set of criteria.

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No government will knowingly adopt an economic programme whose consequences include its own overthrowal (and presumptively the reversal of the programme). If a programme is rejected on this count even though its long run effects are desired, the economic civil servant or economists' duty is to attempt to find a way to alleviate short run sacrifices consistent with rescuing as much as possible of the long term objectives. Utter failure of nerve by politicians and unimaginativity by economic proposal formulatørs is likely to lead to short run stagnation and a worsening basic economic situation making needed initiatives over more draconic and politically dangerous. A particularly appalling example is Ceylon which - as a result - has from 1945 to date dissipated its reserves, failed to develop a viable economic diversification programme, and begun to face massive unemployment cum falling real investment, import capacity, and income per head.

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