

The Economics of European Integration



Chapter 7

Growth Effects & Factor Market Integration



Growth Effects

- European leaders have long emphasised the pro-growth aspects of European integration.
- These operate in a way that is fundamentally different from the way allocation effects operate;
- They operate by changing the rate at which new factors of production – mainly capital – are accumulated,
 - Hence the name ‘accumulation effects’.

Verbal logic of growth

- Growth in income per worker requires more output per worker.
- Nation's labour force can produce more goods and services year after year only if they have more/better 'tools' year after year.
 - 'tools' means capital broadly defined:
 - physical capital (machines, etc.),
 - human capital (skills, training, experience, etc.) and
 - knowledge capital (technology).
- ERGO, rate of output growth is linked to rate of physical, human and knowledge capital accumulation.
- Most capital accumulation is intentional and it is called investment.
 - Thus: European integration affects growth mainly via its effect on investment in human capital, physical capital and knowledge capital.

Verbal logic of growth: summary

- European integration (or any other policy) → allocation effect → improved efficiency → better investment climate → more investment in machines, skills and/or technology → higher output per person.
- * Medium run effects eventually fade out.
 - Growth returns to its long-run rate.
- Long run effects raise long-run rate forever.

Some facts

Table 7-1: European Growth Phases, 1890-1992

Period	Real GDP	Real GDP per capita	Real GDP per hour
1890-1913 Belle epoque	2.6	1.7	1.6
1913-1950 2 nd 30 yr war	1.4	1.0	1.9
1950-1973 Golden era	4.6	3.8	4.7
1973-1992 Prod'ity slowdown	2.0	1.7	2.7
Whole Period			
1890-1992	2.5	1.9	2.6

Some facts

Growth in the WWII Reconstruction Phase.

	The Set-Back: (Pre-war year when GDP equalled that of 1945)	Back-on-Track Year (Year GDP attained highest pre-war level)	Reconstruction Growth (rate 1945 to col. 2 year)
Austria	1886	1951	15.2%
Belgium	1924	1948	6.0%
Denmark	1936	1946	13.5%
Finland	1938	1945	n.a.
France	1891	1949	19.0%
Germany	1908	1951	13.5%
Italy	1909	1950	11.2%
Netherlands	1912	1947	39.8%
Norway	1937	1946	9.7%
Sweden	These nations grew during WWII		
Switzerland			
UK			

Some facts

GDP per capita & Rankings, 1950 and 1973 (1990 international dollars).

	1950 GDP (1990 \$)	European Rank 1950	Change in Rank 1950- 1973	GDP Growth Rate
EEC average	4,825	8.0	+ 1.2	4.2
EFTA average	6,835	3.6	-1.4	3.0
France	5,221	7	+ 2	4.0
Germany	4,281	9	+ 5	5.0
Italy	3,425	13	+ 2	4.9
UK	6,847	2	-5	2.4

Some facts

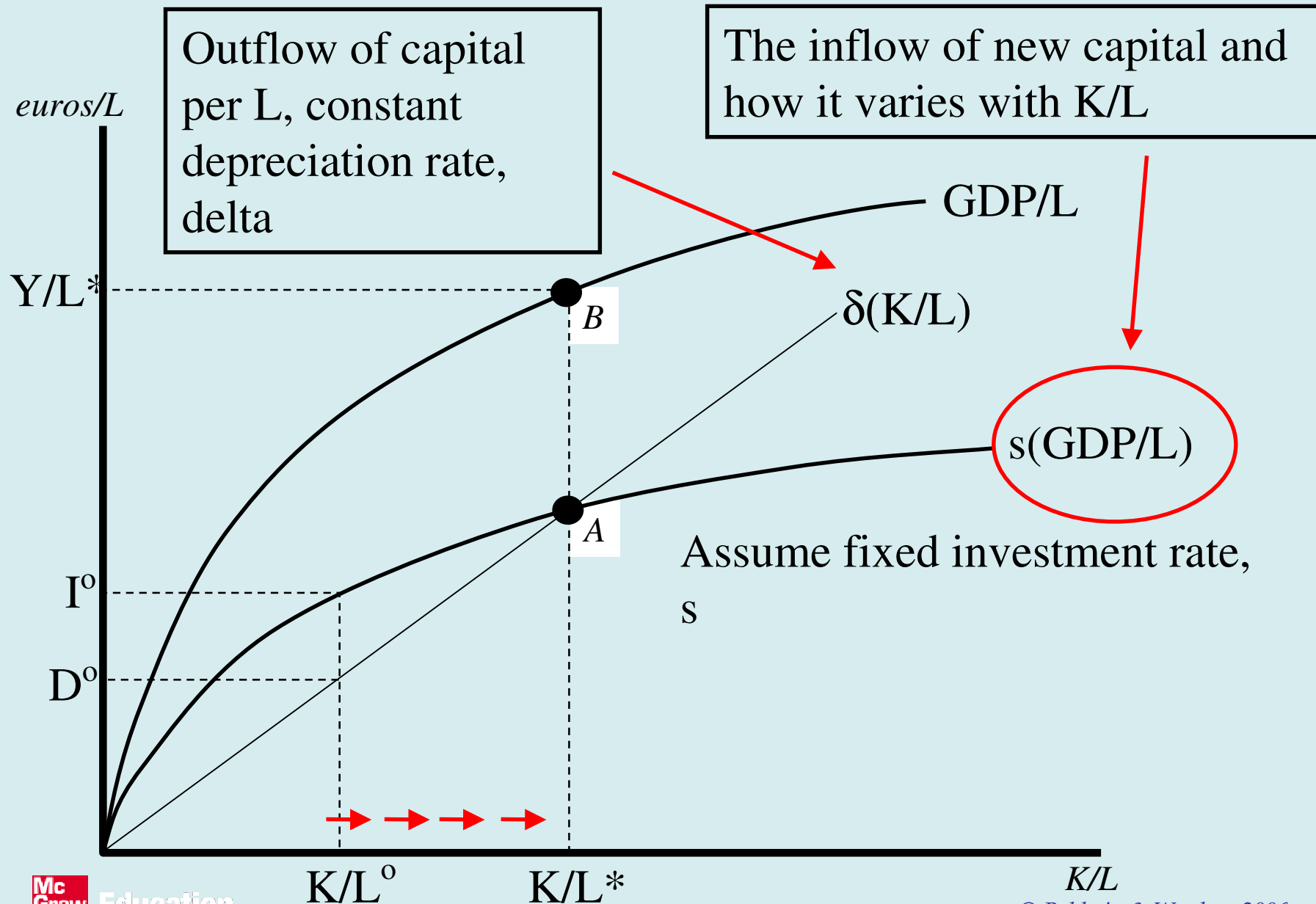
Complete table

	1950 GDP (1990 \$)	European Rank 1950	Change in Rank 1950-1973	GDP Growth Rate
EEC average	4,825	8.0	+ 1.2	4.2
Netherlands	5,850	5	-1	3.4
Belgium	5,346	6	-2	3.5
France	5,221	7	+ 2	4.0
Germany	4,281	9	+ 5	5.0
Italy	3,425	13	+ 2	4.9
EFTA average	6,835	3.6	-1.4	3.0
Switzerland	8,939	1	0	3.1
UK	6,847	2	-5	2.4
Sweden	6,738	3	+ 1	3.1
Denmark	6,683	4	+ 1	3.1
Norway	4,969	8	-4	3.2
Finland	4,131	10	0	4.2
Austria	3,731	11	+ 2	4.9
Others average	2,401	14.3	-0.3	5.2
Ireland	3,518	12	-3	3.1
Spain	2,397	14	+ 1	5.8
Portugal	2,132	15	+ 1	5.6
Greece	1,558	16	0	6.2
For Comparison USA	9,573			2.4
Japan	1,873			8.0

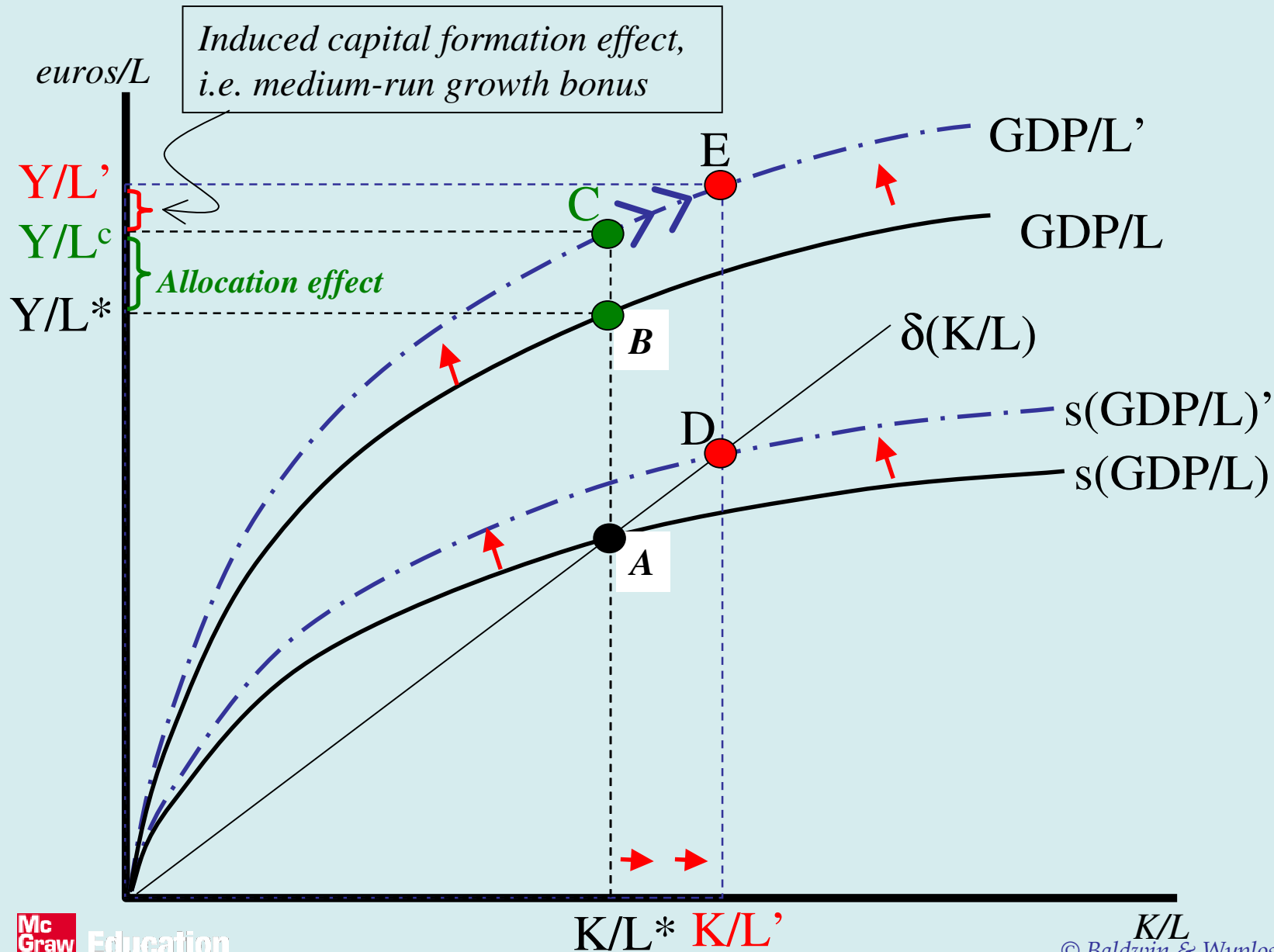
Solow diagram

- Show medium run growth effects in simple diagram.
- To simplify, start with whole EU as a single, closed economy with fully integrated capital and labour markets and the same technology everywhere.

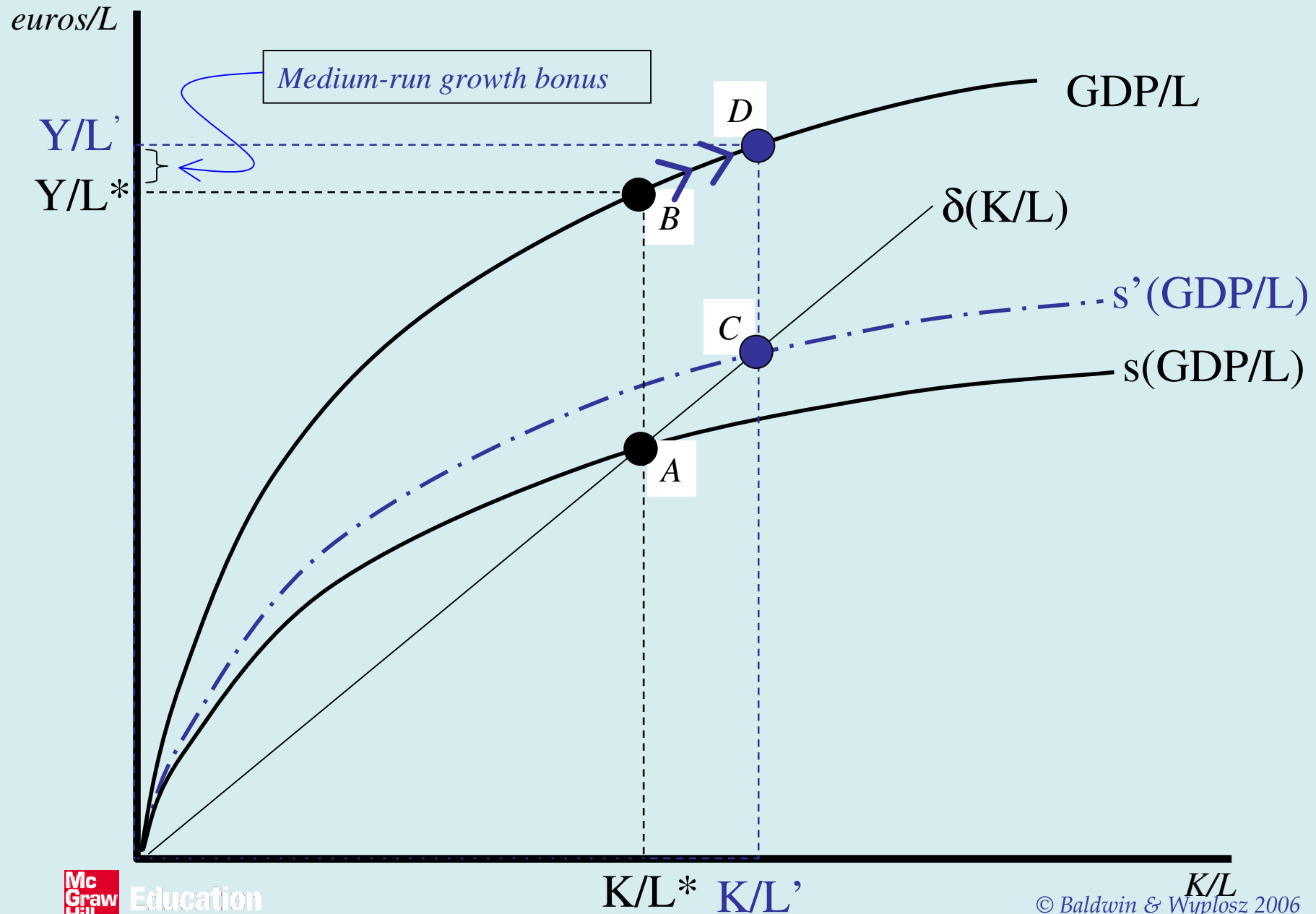
Solow diagram



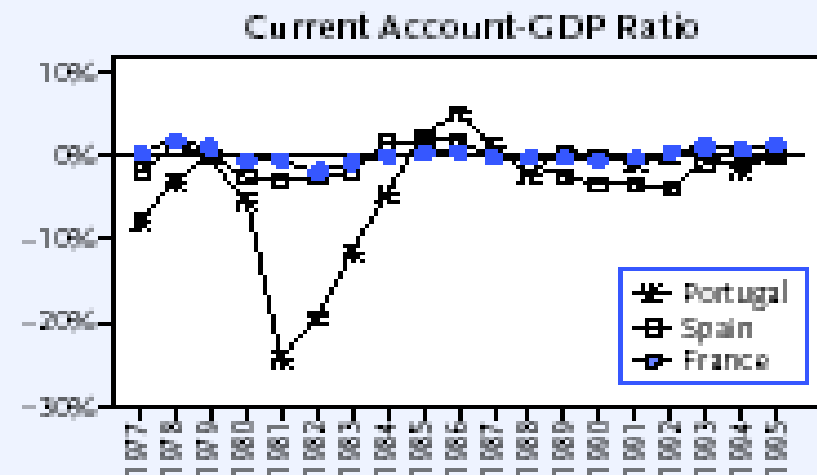
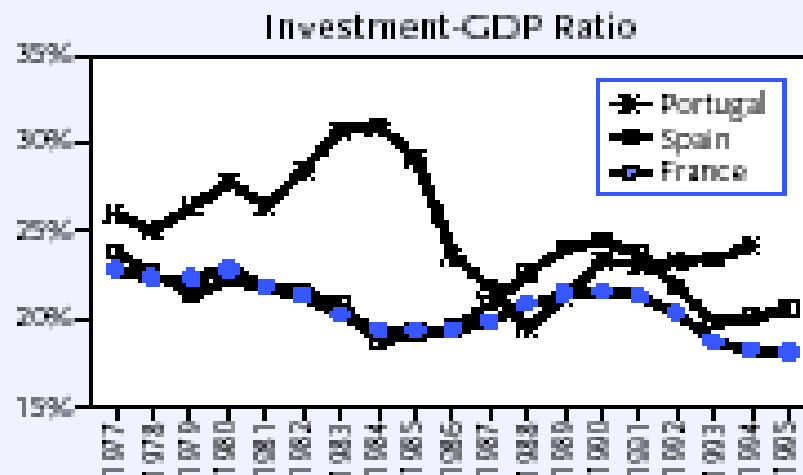
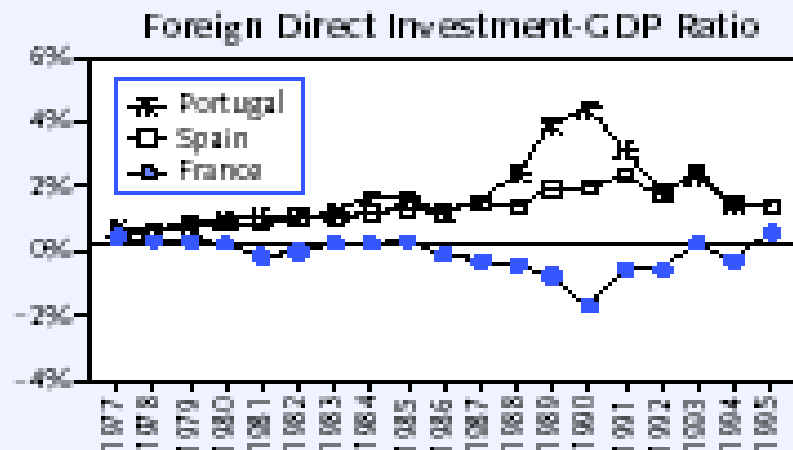
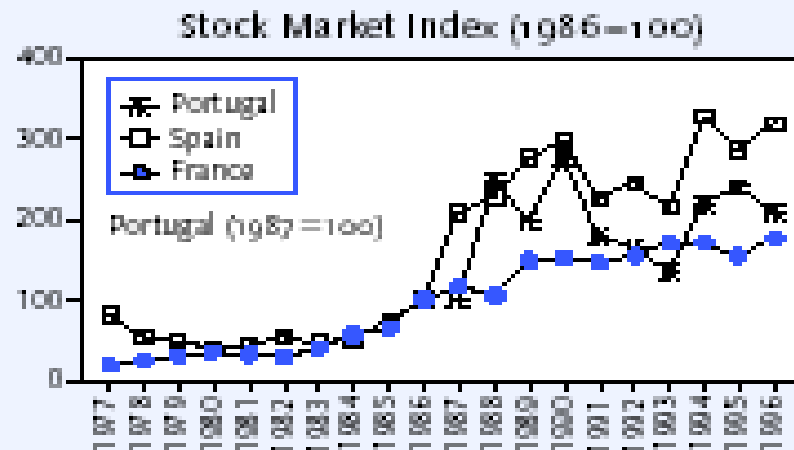
Induced capital formation



Integration induced investment rate rise

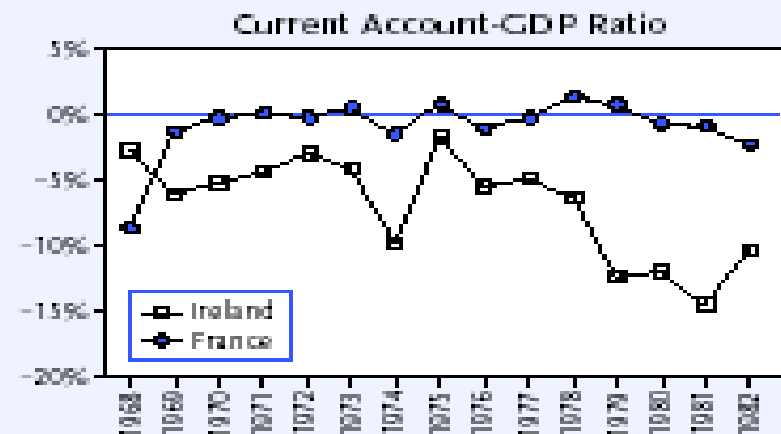
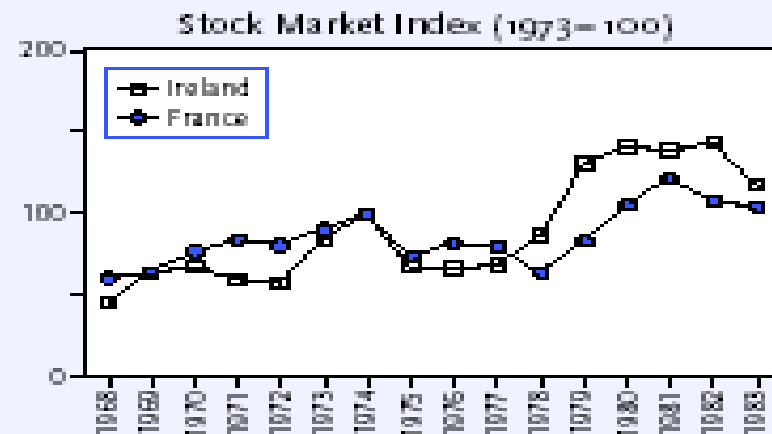
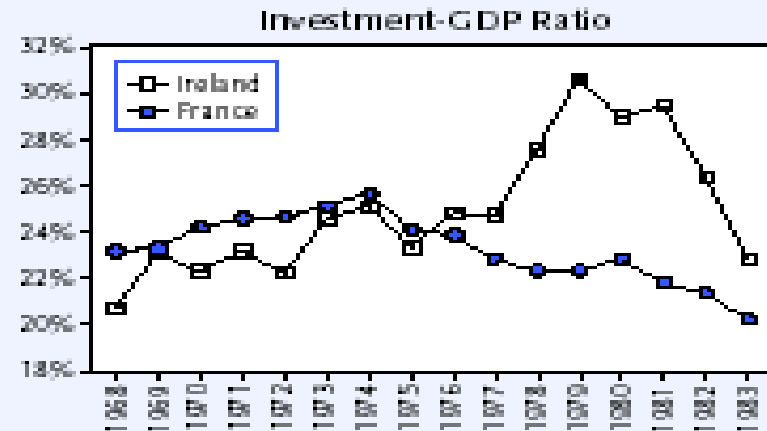
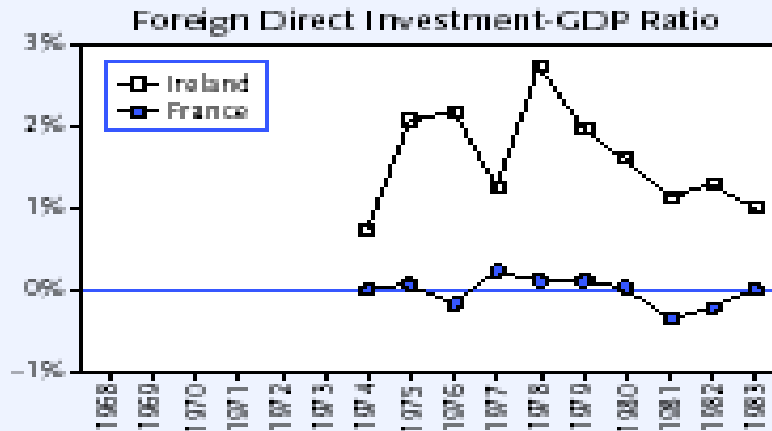


Other MR growth effects: investment rate. Experience of Spain & Portugal



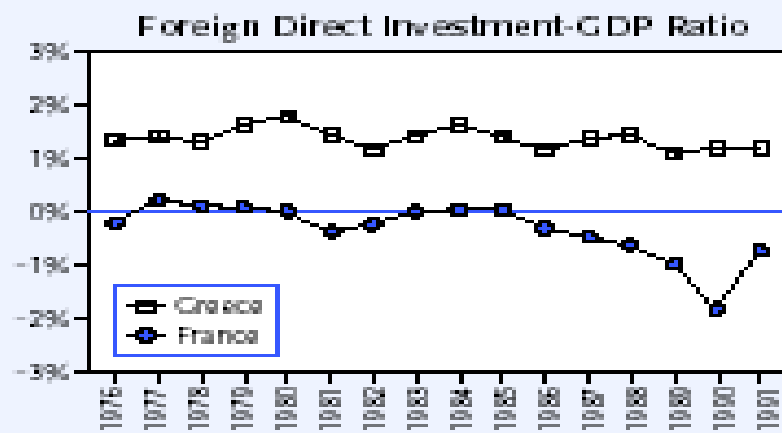
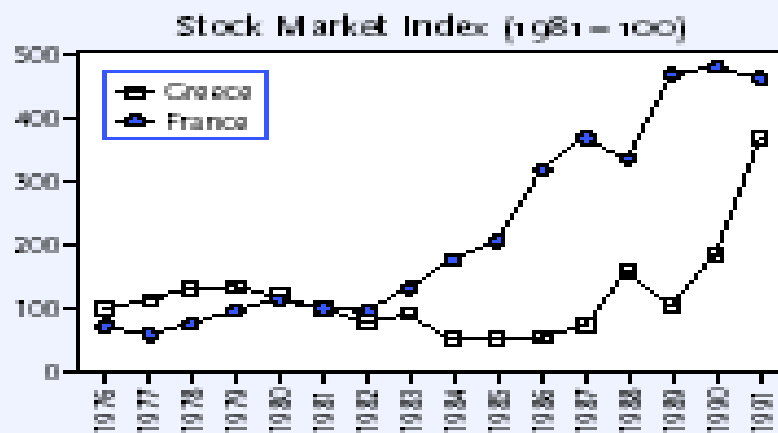
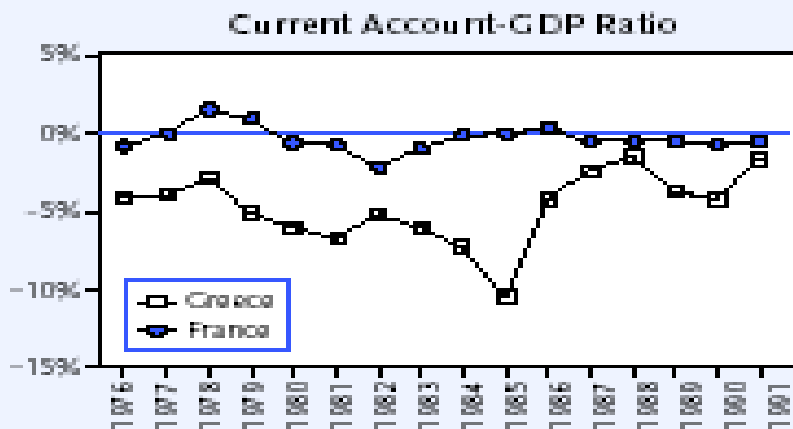
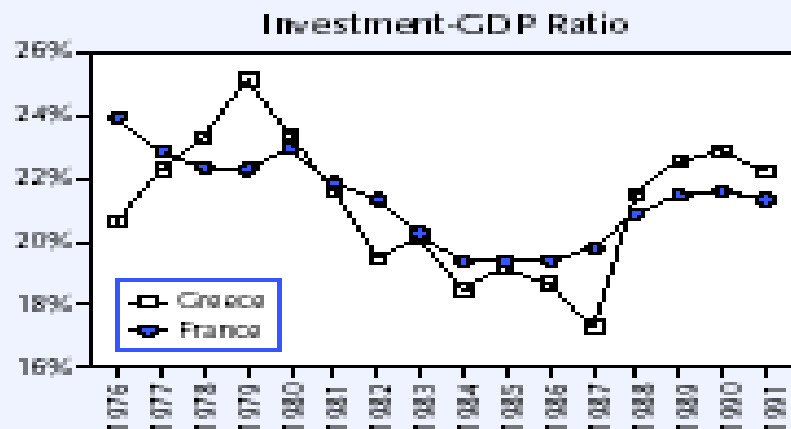
source: Baldwin and Seghezza (1998).

Other MR growth effects: investment rate. Experience of Ireland



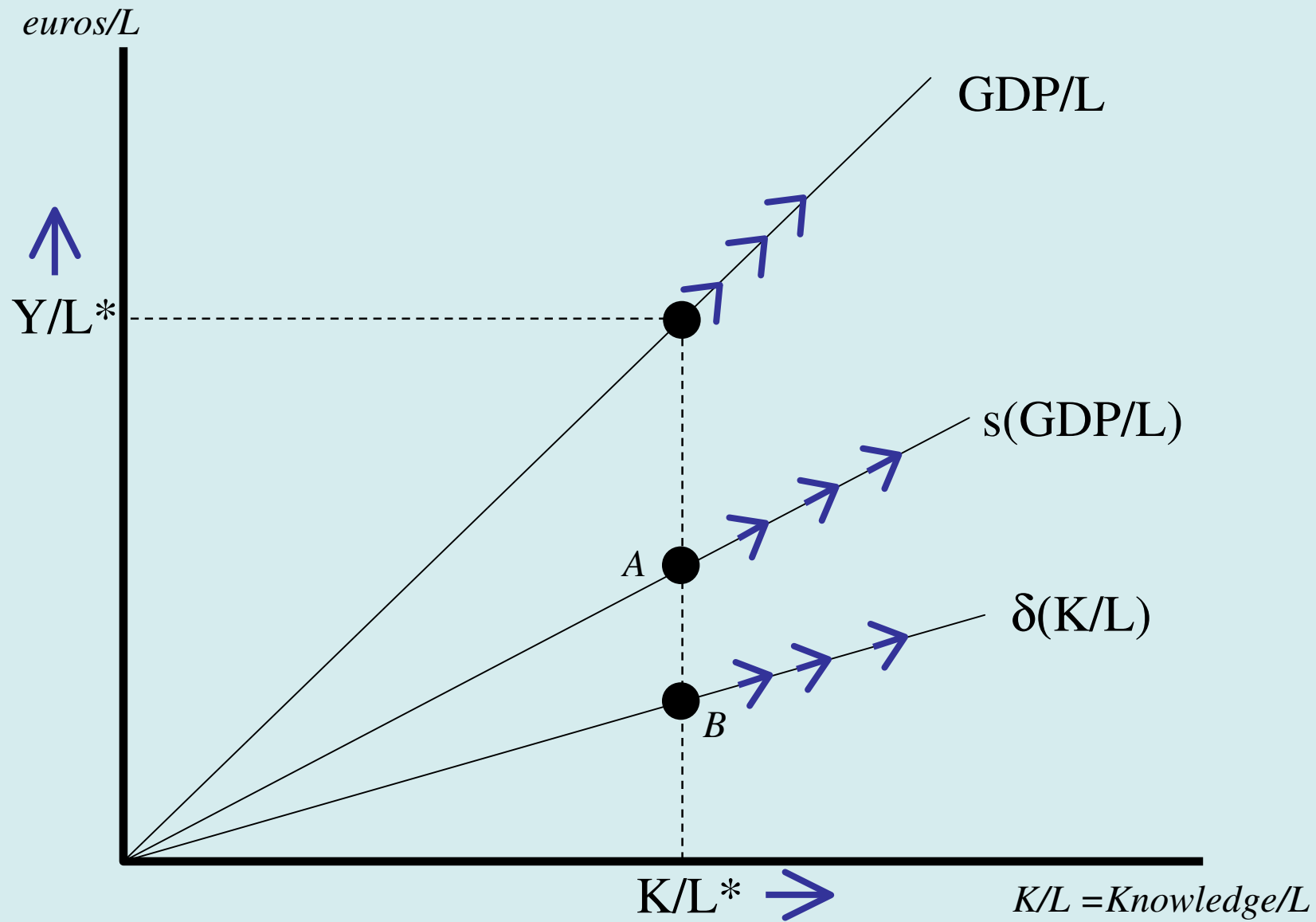
source: Baldwin and Seghezza (1998).

Other MR growth effects: investment rate. Experience of Greece



source: Baldwin and Seghezza (1998).

Long-term growth in Solow-like diagram



Long-term growth impact of integration

Integration improves efficiency → improves investment climate → higher investment rate (s rises to s') → faster growth (knowledge capital accumulates more rapidly)

