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Portugal and Spain entering the Common Market: Their industrial competitiveness revisited

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PORTUGAL AND SPAIN ENTERING THE COMMON MARKET

- Their Industrial Competitiveness Revisited -

by

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Introduction

1. After more than eight years of complex and often contentious negotiations, the European Community (EC) reached, in March 1985, an agreement with Portugal and Spain about their adhesion to the Common Market. Membership is to become effective on January 1, 1986 (provided the accession treaties are ratified by the national parliaments by next December), from which time onwards the existing mutual tariff and non-tariff barriers will be gradually removed. Thus, the Iberian manufacturing industries hold the prospect of getting new outlets for their exports, but also face a rise of import competition which may call for considerable structural adjustment.

2. The purpose of this paper is to assess the overall position as well as the relative strength and weakness of the Iberian manufacturing industries within an enlarged Community. Earlier studies of the authors (Donges, Schatz, 1980; Donges et al., 1982) are up-dated and extended to cover the bilateral trade relations between Portugal and Spain. Following a recapitulation of the major trade patterns of the Iberian countries, we examine the nature of their specialization, both with regard to the EC and among themselves. The increased import competition, employment changes and the adjustment problems faced by the two countries will be analysed subsequently. The paper concludes with some considerations about an overall strategy to cope with the challenges induced by the accession.

This paper was presented at a workshop on "Iberian Integration within European Integration?", organized by the Instituto de Estudos para o Desenvolvimento and held in Lisbon on May 22-24, 1985, with financial support from the Volkswagen Foundation.

Trade Patterns and Determinants

3. Although Portugal and Spain are yet to become full members of the EC, the Common Market has been of prime importance to them for a long time, yet their weight in the Community's foreign trade is minor (Table 1). Both countries got most of their imports (of manufactures and generally) from the EC in 1970, and they continued doing so in the early eighties, although imports from the EC grew more slowly than average (Table A-1 and A-2). On the export side, the shares are somewhat lower, but also here the EC has been the single most important market. Total and manufactured exports to the EC increased faster than the respective imports from there.[1]

4. Note should also be taken of the fact that both countries increased sharply the share of manufactured exports destined for the EC in the period under consideration. The EC orientation is most pronounced in the case of Portugal, whose export industry (including foreign enterprises) presumably benefitted substantially from the removal by the EC of most of its trade restrictions against imports from EFTA countries by mid-1977 (Silva Ferreira, 1979). By comparison, the 1970 Preferential Trade Agreement between the EC and Spain provided less favourable market access conditions for Spanish manufacturers (Donges, 1976). Nevertheless, Spain made considerable headway in diversifying its export structure to include an ever-lengthening list of new, more skill-intensive products for which the income elasticity of world

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[1] The end year for the statistical calculations is 1982, as more recent data from the same source were not available at the time of this writing. In any case, the 1983 and 1984 trade patterns might not be typical due to the incidence of the soaring U.S. dollar. Note that the analysis is based on the product categories SITC 5 to 8 and thus does not consider processed food, beverages, manufactured tobacco, processed animal and vegetable oils, and petroleum products.

Table 1: Trade Matrix between the Iberian Countries and the EC-9[a]
(per cent)

Country / Year		Exports[b]		Imports[b]	
		Total	Manufactures	Total	Manufactures
Share of EC-9 in trade of Iberian countries:					
Portugal	1970	41.9	36.6	48.3	63.6
	1982	57.3	60.1	40.6	64.3
Spain	1970	46.3	34.7	40.3	60.4
	1982	45.8	42.5	31.4	62.4
Share of Iberian countries in trade of EC-9					
Portugal	1970	0.9	0.7	1.4	1.6
	1982	0.7	0.7	1.6	1.5
Spain	1970	2.1	1.5	4.1	3.9
	1982	3.5	3.4	5.2	3.7

[a]Excluding intra-EC trade. - [b]Based on U.S. dollar values.

Source: As Table A-1.

demand is above unity (Casado et al., 1982). Thus, one could expect this country to have the supply potential for exploiting whatever market opportunities may arise after accession, if it had not been for the persistent slowing down of productive investment which has taken place since 1975 (more on this later).

5. As to the bilateral trade relations between Portugal and Spain the links are weak (Table 2), although mutual trade (exports and imports, in current U.S. dollar prices) increased at an annual rate of roughly 20 per cent (all commodities) and 25 per cent (manufactured goods) in the period 1970-82.[1]

- For Portugal, Spain plays a major role as source of supplies rather than as a market for export outlets; the opposite holds for Spain.

- Moreover, Portuguese manufactured exports to Spain show a relatively high level of concentration and tend to be quite complementary to production in Spain, whereas Spanish manufactured exports to Portugal are relatively diversified and, to some degree, substitutive of production in Portugal.

- It should also be noted that Portugal has invariably run a bilateral trade deficit with its neighbouring country (both in total trade and in manufactured trade); and this deficit has been growing over time - in manufactures from $35 million in 1970 to $354 million in 1980 and $379 million in 1982, when it accounted for 19.3 per cent of Portugal's total deficit in manufactured trade (as compared to 7.4 per cent in 1970).

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[1] For further details see the studies by Rato (1984) and by Romao et al. (1985, chapter 6+7), prepared for this workshop.

Table 2: Bilateral Trade between Portugal and Spain[a]
(percentage shares)

Commodities	Year	Portugal		Spain	
		Exports to Spain	Imports from Spain	Exports to Portugal	Imports from Portugal
All commodities	1970	1.62	4.34	2.92	0.40
	1980	3.65	5.52	2.73	0.48
	1981	2.92	6.58	2.96	0.42
	1982	3.63	6.02	2.78	0.48
Manufactured goods	1970	1.00	3.83	3.15	0.31
	1980	2.06	8.41	3.04	0.51
	1981	2.01	10.04	3.24	0.54
	1982	2.89	9.31	2.90	0.72

[a]Based on U.S. dollar values.

Source: As Table A-1.

6. Though bilateral trade balances are not a criterion for trade equity, there seems to be a bias in favour of Spain due to the differing import protection schemes applied in both countries.

- Traditionally, tariff protection of the domestic manufacturing industry has been higher in Spain than in Portugal; the unweighted (weighted) averages amounted to 19.4 (16.2) per cent and 15.2 (13.4) per cent, respectively, in the mid-seventies (Donges et al., 1982, p. 93). As most Portuguese tariffs towards Spain are still specific rather than ad valorem duties (as they are, since 1980, in trade with other countries), their protective impact was reduced over time by the rapid internal inflation, for which ad hoc application of import surcharges led to a partial correction only.

- Spain has also been more prone to the use of non-tariff barriers. In the context of its system of indirect taxation, based on a multi-stage turnover tax and a number of special taxes, the country imposes on imports a compensatory levy and grants a tax refund to exporters which in some cases exceed the taxes borne by domestic producers. The hidden import protection and export subsidization will only disappear when Spain introduces the value-added tax in 1986, following accession to the EC. Furthermore, Spain not only applies import quotas to a wide range of products but also changes them frequently, whether for balance-of-payments reasons or to suit protectionist demands from troubled domestic industries. These changes in the level and incidence of non-tariff protection have presumably inflicted considerable uncertainty upon Portuguese exporters, upsetting their plans and discouraging rapid expansion. One consequence is much volatility of various Portuguese exports to Spain. But even more characteristic is the fact that Portugal's major manufactured exports to the

EC and other countries (textiles, clothing, footwear, leather products, ceramics) play almost no role in trade with Spain (illegal flows aside).

- The 1979 Preferential Trade Agreement between Spain and EFTA (of which Portugal still is a full member), which came into effect in 1980, has not yet reduced bilateral protectionism substantially. Particularly Spain seems to be reluctant to ease its quantitative import restrictions towards those Portuguese exports which are highly competitive; these are labour-intensive and Spanish firms would have difficulties withstanding Portuguese competition due to the low wages prevailing in Portugal (less than half of those paid in Spain). At the same time, the liberalization measures introduced by Portugal have allowed Spanish manufacturers to better exploit cost advantages, technological superiority and marketing expertise in order to penetrate the Portuguese market; chemicals, machinery and transport equipment are cases in point.

7. Improved competitiveness is naturally not the only factor to which an increase in exports can be attributed. Changes in demand for exports - worldwide, commodity-specific and market-specific - may also play a role. In order to account as far as (statistically) possible for different sources of export growth in Portugal's and Spain's total external trade, a Tyszynski-type constant-market-share analysis was carried out. The basic assumption is that a country's share in the world market remains unchanged over time; this means that its export demand - globally, by commodities and by regions - as well as its supply capacity develop at the same pace as in all other countries combined. Four effects were estimated using the following formula:

$$\sum_{ij} X^1_{ij} - \sum_{ij} X^\circ_{ij} = \sum_{ij} r_t X^\circ_{ij} \rightarrow \text{average demand change effect}$$

$$+ \sum_{ij} (r_i - r_t) X^\circ_{ij} \rightarrow \text{commodity composition effect}$$

$$+ \sum_{ij} (r_{ij} - r_i) X^\circ_{ij} \rightarrow \text{market structure effect}$$

$$+ \sum_{ij} (X^1_{ij} - X^\circ_{ij} - r_{ij} X^\circ_{ij}) \rightarrow \text{competitiveness effect}$$

where X^1 and X° stand for Portugal's/Spain's export value in 1982 and 1970, respectively; r represents the percentage increase in world exports, the subscript t referring to total manufacturing exports, the subscript i denoting one of the SITC commodity groups 5, 7 and 6+8 (the only level at which data are available for measurement), and the subscript j marking one of the following 14 importing areas: EC-9, EFTA, other Western Europe, Eastern Europe, USA, Canada, Japan, Australia and New Zealand, South Africa, African developing countries, Latin America, Middle East, other Asian developing countries, Mainland China and other Asian centrally planned economies.

8. The results are given in Table 3. In spite of the high level of aggregation and certain conceptual drawbacks, a clear picture emerges:

- Improved competitiveness was pervasive in the increase of Spain's exports. If Spain had shared only proportionately in the expansion of world trade (on average and in the individual commodity groups and markets), total manufactured exports would have increased by $5.3 billion from 1970 to 1982, and not by $13.1 billion as they actually rose.

Table 3: Sources of Increase of Manufactured Exports, 1970-82[a]

(per cent of total increase)

Factors	Chemicals (SITC 5)	Machinery & transport equipment (SITC 7)	Other Manufactures (SITC 6+8)	Total (SITC 5-8)
		Portugal		
1. Average demand change	107.9	67.8	115.0	104.5
2. Commodity composition	21.0	5.1	-14.3	-6.4
3. Market structure	29.1	0.3	-26.7	-14.9
4. Competitiveness	-58.0	26.8	26.0	16.8
		Spain		
1. Average demand change	39.4	38.2	42.5	40.6
2. Commodity composition	7.8	3.0	-5.4	-1.0
3. Market structure	5.2	26.1	-3.7	8.1
4. Competitiveness	47.6	32.7	66.6	52.3

[a]For method of calculation see text.

Source: United Nations, Commodity Trade Statistics and Monthly Bulletin of Statistics, various years.

- By way of comparison, Portugal appears much more as a "trend economy". But this notwithstanding it was important that competitiveness also improved here (though less than in Spain), because overall commodity composition and market structure were unfavourable to Portugal. Without the observed increase of competitiveness this country would have earned $408 million less from manufactured exports at the end of the period under consideration.

- Looking at the three product categories it can be seen that in both countries the major proportion of the increase in the exports of "chemicals" and "machinery and transport equipment" is attributable to the three factors on the demand side combined. This holds for Portugal also with regard to "other manufactures", whereas in the case of Spain the predominant influence of the competitiveness effect is remarkable indeed. Note that the market structure effect in the expansion of exports in the broad product category which includes almost all investment goods was more favourable in Spain than in Portugal.

Comparative Advantages and Specialization

9. After quantifying the competitiveness effect at an aggregated level, more light can be shed on this issue calculating the Balassa-index of revealed comparative advantage (RCA) for individual commodity groups. The following formula was used:

$$RCA = \ln \left(\frac{X_i}{M_i} : \frac{\sum_i X_i}{\sum_i M_i} \right) \cdot 100$$

where X and M denote exports and imports, respectively, and the subscript i refers to each of 35 commodity groups at the two-digit SITC level 5-8.

10. According to this formula, a positive sectoral trade balance as a proportion of the total balance of trade in manufactures is taken as reflecting international competitiveness, while a negative relative trade balance pinpoints the opposite. The higher (lower) the RCA index is, the more (less) successful is the trade performance of the industry in question. Moreover, the structure of RCA indexes is influenced by the nature of division of labour which predominates in trade relations; it narrows with increasing importance of intra-industry trade and widens when there is much inter-industry trade. It goes without saying that factors such as protective measures, transport costs, taste and traditional ties also have an incidence on the revealed comparative advantage, but their consideration is beyond the scope of this paper (and accurate quantification is difficult anyhow).[1]

11. RCA indexes have been computed for 1970 and 1982, distinguishing between Portugal's and Spain's trade with the EC, with other OECD countries and with the rest of the world (mainly developing countries and centrally-planned economies). The results are given in the Appendix Tables A-3 and A-4. Their ranking conveys three features (Table 4):

- First, Portugal underwent a more pronounced change in revealed comparative advantages vis-à-vis the Community than Spain did in the period 1970-82. The same holds for Portugal's trade with the other OECD countries, but not for its trade with the rest of the world.

- Second, the structure of comparative advantage as revealed in trade with the EC-9 and the other OECD-countries was

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[1] Empirical analyses show, however, that factor endowments theory contributes heavily to explaining trade patterns in Portugal (Moura Roque, 1983) and Spain (de la Puente, 1980).

Table 4: Spearman Rank Correlation Coefficients for RCA Indexes

Trading Partners /Years	Portugal	Spain
1970 vs. 1982		
EC-9	0.664*	0.794*
Other OECD countries	0.625*	0.727*
Rest of world	0.606*	0.584*
1970		
EC-9 vs. Other OECD countries	0.866*	0.732*
EC-9 vs. Rest of world	0.185	0.311
1982		
EC-9 vs. Other OECD countries	0.681*	0.755*
EC-9 vs. Rest of world	0.136	-0.084

* = statistically significant at the 0.1 per cent level of confidence (two-tail probability).

Source: Calculated from Tables A-3 and A-4.

more similar for Portugal than for Spain in 1970 and more similar for Spain than for Portugal in 1982.

- Third, in trade with the rest of world both Portugal and Spain exhibit a pattern of competitiveness which is distinctly different from the other structures.

12. As far as trade with the Community is concerned, Spain shows a wider range of products with a revealed comparative advantage than Portugal does (Table 5). However, competitive strength declined in most cases, including those manufactures in which Portugal increased its own competitive strength (i.e. footwear, cork and wood manufactures, clothing). These products are labour-intensive to a large extent, so that Spain was bound to loose ground in the process of its industrial advancement, and this the more so because wage cost increased sharply during the late seventies.

13. No clear pattern of revealed comparative advantage is discernible in trade between the two Iberian countries (Table A-5). Due to the protective measures mentioned earlier the RCA indexes are not susceptible to an accurate economic interpretation. This notwithstanding, Portugal's industry seems to display a solid degree of competitiveness in cork and wood manufactures, clothing and furniture (in this order), whereas its competitive disadvantage is most persistent in road vehicles, metalworking machinery, iron and steel as well as dyeing and tanning materials. Thus, differences in the factor endowment between Portugal and Spain manifest themselves at least at the upper and lower ties of RCA indexes.

14. In this context it is worth remarking the drastic change in the structure of bilateral RCA indexes which occurred between 1970 and 1982: Spearman's rank correlation coefficient is 0.265. In the course of this change Portu-

Table 5: Commodity Groups Revealing Competitiveness in Trade with EC-9, 1982

Portugal		Spain	
Commodities	Trend 1970-82	Commodities	Trend 1970-82
Footwear	+	Footwear	-
Cork and wood manufactures	+	Leather manufactures	+
Clothing	+	Cork and wood manufactures	-
Manufactured fertilizers	+[a]	Rubber manufactures	-
Textile yarn and fabrics	-	Furniture	-
Non-metallic mineral manufactures	-	Clothing	-
Furniture	+[a]	Travel goods	+
Miscellaneous chemical materials	-	Road vehicles	+
Telecommunications equipment	+	Non-ferrous metals	+
Paper and paper products	+	Manufactured fertilizers	+
Leather manufactures	+[a]	Textile yarn and fabrics	-
Office machines	+[a]	Paper and paper products	+[a]
		Miscellaneous manufactures	-
		Fabricated metal products	-
		Non-metallic mineral manufactures	-
		Iron and steel	+[a]

[a]Revealing a comparative disadvantage in 1970.

Source: Tables A-3 and A-4.

gal's RCA indexes related to trade with Spain got closer to its RCA indexes resulting from trade with both the Community and the other OECD area (Table 6). This implies that there is already a tendency for competitive strength and weaknesses of Portuguese industries to become apparent irrespective of the market orientation of trade. Iberian trade relations are now more similar to trade relations with the highly industrialized countries than they were in 1970.

15. The argumentation so far has not accounted for eventual shifts in the nature of specialization in the Iberian countries, in particular movements from inter- towards intra-industry trade or vice versa. The relevance of this issue resides in the presumption that import-related adjustment pressures can be handled at lower social costs if there is a comparable scope for export expansion in the same industry at the same time.

16. One way to approach this issue consists of measuring Finger-DeRosa-coefficients of trade overlap (TO). The following formula can be used:

$$TO = \frac{2 \sum_i \min (X_i, M_i)}{\sum_i (X_i + M_i)}$$

where X_i and M_i refer to exports and imports, respectively, of each of the 35 commodity groups i at the two-digit SITC level 5-8 and "min" defines the magnitude of the total trade in manufactures which overlaps in (dollar) value terms. The TO coefficients can vary between 0 and 1. The closer they come to unity, the more are exports of a particularly industry matched by imports belonging to the same product category, thereby indicating intra-industry specialization.

Table 6: Portugal's RCA Indexes in Trade with Spain Compared to Those with Other Trading Partners

(Spearman rank correlation coefficients)

Region of comparison	1970	1982
EC-9	0.225	0.695*
Other OECD countries	0.311	0.773*
Rest of World	0.069	0.232

*Statistically significant at the 0.1 per cent level of confidence (two-tail probability).

Sources: Calculated from Tables A-3 and A-5.

17. The results, broken down according to major trading regions, are reported in Table 7. On the whole, the TO coefficients of Portugal and Spain are still rather low, so that inter-industry specialization predominates. By comparison, the TO coefficients pertaining to the EC-9 were, in 1982, 0.983 for trade among the member countries and 0.794 for trade with the other OECD countries. In their trade relations with the Community, Portugal made only little progress towards an increase of the proportion of intra-trade, whereas Spain did. The same holds in relation to the other OECD countries. Bilaterally, the Iberian countries reveal an inter-industry specialization pattern, with a tendency to intensify in the case of Spain but not in that of Portugal. Therefore, there is a strong presumption that both Portugal and Spain face a considerable potential for increasing intra-industry trade relative to inter-industry trade, in mutual trade as well as in trade with the EC-9, once tariff and non-tariff barriers are dismantled. Rising per-capita incomes, leading to a larger size of the domestic market, might support the emergence and consolidation of a new type of specialization.

Facing Increased Import Competition

18. Once the agreements of accession become effective, the Iberian countries will have to open their markets to industrial suppliers from other EC member countries. The removal of tariffs on imports has to be made during a transition period of seven years (Table 8); prevailing import quotas and other non-tariff barriers will be phased out over a period of 3 to 4 years according to special, industry-specific arrangements. Perhaps because Spain starts from considerably higher levels and a wider coverage of protection than Portugal (Melo and Monés, 1982; Lopes Porto,

Table 7: Trade Overlap Coefficients for Portugal and Spain[a]

Trading Partners	Year	Portugal	Spain
EC-9	1970	0.226	0.368
	1982	0.389	0.638
Other OECD countries	1970	0.340	0.306
	1982	0.329	0.486
Rest of world	1970	0.185	0.266
	1982	0.493	0.222
Portugal	1970	.	0.290
	1982	.	0.262
Spain	1970	0.207	.
	1982	0.246	.

[a]Based on SITC rev. 2, two-digit groups 5-8. For method of calculation see text.

Source: As Table A-1.

Table 8: Tariff-cutting Commitments by the Iberian Countries for Manufactured Trade with the EC[a]
(reductions in per cent)

Date	Portugal	Spain
1.3.86	10	10
1.1.87	10	12.5
1.1.88	15	15
1.1.89	15	15
1.1.90	10	12.5
1.1.91	10	12.5
1.1.92	15	12.5
1.1.93	15	10

[a]Assuming that the adhesion becomes effective on January 1, 1986.

Source: Information provided by the German Federal Ministry of Economics.

1982)[1], it has to reduce tariffs faster than its neighbouring country during the first half of the transition period. The agreed tariff cuts will be applied across-the-board, which temporarily may increase the dispersion of effective rates of protection and thus cause distortions in the allocation of resources. However, given the basic trend towards a liberalization of trade, these distortions are presumably not substantial.

19. What might be substantial, is the increase of manufactured imports in connection with the future openness of markets, particularly in Spain. In previous studies, using the Viner-Meade approach to estimate custom-union trade effects, it was shown that the increase of Spain's manufactured imports could amount to about 5 per cent per annum above total imports in the chosen base year (1979) and more than 11 per cent per annum above imports from the EC-9; the corresponding percentages were expected to be 2 and 5 points lower in Portugal (Donges and Schatz, 1980; Donges et al., 1982, pp. 90-95).[2] In both countries, the lion's share of the expected rise in manufactured imports will correspond to investment goods (mainly non-electrical and electrical machinery, transport equipment, professional goods) and intermediate products (mainly industrial chemicals), the production of which is relatively human-capital intensive and thus provides a comparative advantage to the most advanced EC member countries. These estimates capture the import-expanding effects after all tariffs have been removed. The fact that a seven-year period of transition has been agreed upon, may cushion the perceived impact of the opening of markets.

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[1] The tariff cuts of Portugal will affect only about 20 per cent of this country's manufactured imports from the Community. The main product groups are machinery, electrical appliances, chemicals and petrochemicals.

[2] Alternative estimates, derived from different data sets and made with different formulas, have been provided by Feitor et al. (1982) for Portugal and by Puig i Bastard et al. (1979) for Spain.

20. However, Portuguese and Spanish firms are going to face not only increased import competition from other EC countries. The adhesion calls for additional fundamental trade policy revision by the Iberian countries.[1] They will have to

- dismantle tariff and non-tariff barriers in mutual trade;

- enter the free trade agreements which have been established between the present EC and EFTA (Portugal just changes sides);

- adopt the Community's Generalized System of Tariff Preferences on manufactured imports from developing countries (LDCs), join the Lomé Convention with African, Caribbean and Pacific (ACP) countries, and share the market access concessions made by the EC to countries of the Mediterranean basin;[2]

- reduce the tariffs, which they presently impose on imports from third countries, to the Common External Tariff (CET) levels and harmonize their still highly restrictive import quotas with the rules practiced by the Community.[3]

21. Under these circumstances it is likely that there will be a rising penetration of the Iberian markets by suppliers from third countries outside Western Europe. Not only will major trading nations such as the United States and Japan enjoy greater export opportunities, but also the newly-in-

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[1] The details were still a matter of negotiation at the time of this writing.

[2] However, imports of "sensitive" goods can be limited for a period up to 6 years. This rule can also be applied in trade with Japan.

[3] Even Portugal has been pursueing a quite protectionist trade policy towards (non-EFTA, non EC) third countries, as shown by Lopes Porto (1982). Tariffs will now have to be reduced gradually using the same formula as in trade with the EC-10; tariffs which do not exceed the CET by more than 15 per cent will be harmonized immediately after the adhesion.

dustrializing countries (NICs) whose past export dynamism is likely to continue in the future (certainly so in Taiwan, South Korea and Singapore) as well as all LDCs following outward-looking industrialization strategies will contend with Portuguese and Spanish firms for market shares. As both Iberian countries still attach relatively high weight to the production of low-skilled, labour-intensive goods (textiles, apparel, shoes and the like) a number of traditional domestic firms might be displaced from the market by new foreign competitors. Domestic demand for such products is relatively price-elastic and aggressive LCD suppliers can easily exploit advantages deriving from low labour costs. Japan and the NICs could become a source of major concern as they typically cluster their export drives in a limited number of product categories. The probably most affected producers in Portugal and Spain include those of radio and television sets, clocks and watches, motorcycles and bicycles, automobiles, iron and steel, bulk carriers and tankers, rubber products, and industrial machinery of various kinds.

22. To all this one has to add the probability of rising import-penetration ratios in Portugal and Spain resulting from a mutual opening of their markets. Given their production structure and revealed comparative advantages, Spanish manufacturers will be strongly exposed to Portuguese suppliers of non-durable consumer goods (especially textiles and apparel as well as footwear), whereas Portuguese manufacturers will face a growing Spanish competition in product categories incorporating higher-skilled labour and standardized technology (motor cars, steel, some chemicals, glass manufactures, rubber products, and various engineering goods are cases in point).[1] Though reasonable transition periods

[1] For details, see Feitor et al. (1982). Portugal's manufactured exports to Spain have been estimated to increase by 18.1 per cent above pre-accession values, whereas manufactured imports from Spain would rise by 13.3 per cent (the base year is 1978). If agricultural manufactures are included, the incremental rates of expansion are 18.0 and 15.6 per cent, respectively. In any case, Portugal will continue running a trade deficit with its neighbour country (op. cit., pp. 162-163).

may prevent an onslaught of imports, both in bilateral trade and in trade with overseas countries, Portugal's and Spain's manufacturing industries cannot but prepare themselves at once to undergo a far-reaching process of adjustment and restructuring.

Employment Effects

23. There is much concern in the Iberian countries that rising import competition would lead to job losses which are not compensated by employment gains stemming from export increases, due to weaknesses in the international competitiveness of the respective industrial sectors. It seems worthwile, therefore, to estimate these labour displacement and job creation effects, in order to clarify the dimension of the problem. Needless to say, that a precise quantification of employment changes which may emerge with accession is not possible, as neither the future trade patterns nor the firms' adjustments to the new conditions are known.

24. The following basic formula has been used to calculate the hypothetical employment changes in the manufacturing industry:

$$\Delta L = \frac{Y^* - Y}{(\frac{O}{L})}$$

where L denotes employment, Y stands for exports and imports, respectively, and O represents gross output; the asterisk marks the potential exports or import increases resulting from tariff reduction in the Iberian countries and the EC. The incremental imports have been referred to in para. 19. On the export side, the rates of expansion could be 1.5 per cent for Portugal and 5.7 per cent for Spain (Donges et al., 1982, pp. 96-98). While these incremental rates have originally been obtained for 1979, it is assumed for the purpose of the present analysis that they were still valid in 1982. We have estimated the average labour productivity in Portuguese manufacturing to have amounted to

$24,000 in 1982, and to $52,000 in Spanish manufacturing.[1]

Given these productivity levels, employment in Portuguese manufacturing would have been lower by about 8,600 persons or 0.8 per cent of total manufacturing employment in 1982, if tariffs would already have been removed by this year and domestic production been replaced by imports to the extent mentioned (Table 9, static model I). The respective figures for Spain are 16,900 persons or 0.7 per cent.[2]. At the same time, additional export demand for Portuguese products could have added 1,100 or 0.1 per cent to the persons employed in manufacturing, and demand for Spanish products could have increased employment by 6,900 or 0.3 per cent. These figures reveal that the employment balance resulting from tariff elimination would be negative both for Spain and Portugal, though by no means dramatic.

25. It may be argued, however, that in reality job creation due to increased exports will be lower and labour displacement due to increased imports would be larger because normally labour productivity is above average in export industries and below average in import substituting industries. This argument could be rejected on the ground that the bulk

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[1] At 1982 exchange rates and prices. - For both Portugal and Spain, the respective base data for output and employment have been taken from UN, Yearbook of Industrial Statistics. 1981 Edition, Vol. I. New York 1983. They are available in the case of Portugal only up to 1980, and in the case of Spain only up to 1977. Output figures at current prices for 1982 have been estimated applying indices for manufacturing production (taken from OECD, Main Economic Indicators. Historical Statistics, 1964-1983. Paris 1984) and industrial prices (from OECD, Economic Outlook. Historical Statistics, 1960-1982. Paris 1984; wholesale prices for manufactured goods for Portugal). The output figures have been converted to U.S. dollars at 1982 exchange rates. 1982 employment figures have been obtained by connecting an index for manufacturing employment (OECD, Economic Outlook, op. cit.) to the respective base year data.

[2] In 1982, Portugal employed 1,014 million persons in the manufacturing industry, Spain 2,591 million (Source: OECD, Economic Outlook, op. cit.).

Table 9: Employment Changes from EC Entry in Portugal and Spain[a]

	Portugal		Spain	
	Model		Model	
	I (Static)	II (Dynamic)	I (Static)	II (Dynamic)
Import expansion ($ million)	206	1,024	881	1,362
- Employment change (1,000 persons) at				
- Average labour productivity	-8,6	-42,6	-16,9	-26,2
- Two thirds of average labour productivity	-12,9	-64,0	-25,4	-39,3
Export expansion ($ million)	27	625	358	2,398
- Employment change (1,000 persons) at				
- Average labour productivity	1,1	26,0	6,9	46,1
- Four thirds of average labour productivity	0,9	19,5	5,2	34,6

[a]For method of calculation see text.

Source: OECD statistics as referred to in p. 24, fn. 1.

of additional imports from the EC will be concentrated on investment goods and intermediate products (para. 19), the production of which is less labour intensive than that of consumer goods, where the two Iberian countries above all might expand their own exports (Donges et al., 1982). We have nevertheless re-calculated the static employment changes, assuming that labour productivity in import substituting industries is one third below and in export industries one third above the manufacturing average. As the results reveal, the employment effects remain small (Table 9). It would leave Portugal with an absolute loss of 12,000 instead of 7,500 persons, or 1.1 per cent instead of 0.7 per cent of manufacturing employment, and Spain with a loss of 20,000 instead of 10,000 persons or 0.8 per cent instead of 0.4 per cent of employment.

26. The elimination of tariffs is, of course, not the essence of accession to the EC. The abolition of other trade barriers will be much more important for mutual trade expansion, and still more significant may be dynamic developments emerging from the integration of Portugal's and Spain's economies into the Common Market. Adequately dealing with such issues would require, inter alia, forecasts of future policies, which we felt unable to provide. Instead, we have simply assumed that both the new entrants and the present EC members will seize the opportunities which the enlargement offers, substituting cheaper foreign supplies for more expensive domestic products, and expanding own exports faster than in the past. Again, 1982 was taken as reference year, asking what employment changes by additional exports and imports in trade with the EC could have been expected for Portugal and Spain, if they had joined the Community in 1973 already and if the transition period, which is to last seven years, would have been accomplished in 1982 (and would have begun in 1974, instead of 1986, as presently planned). We assumed both imports and exports of Portugal and Spain to have increased by one third faster than actually in the

period 1975-82, which would have been a somewhat more dynamic development. This dynamic model of trade integration reveals that both employment losses and gains from trade would be substantially higher in each of the two Iberian countries than the static model suggests (Table 9). If average manufacturing labour productivity would be typical for import substituting as well as for export industries, Spain could enjoy an employment gain of roughly 20,000 persons instead of suffering a loss of 10,000 in the static model, and under the assumption of diverging productivities it would loose 5,000 only instead of 20,000 persons employed in manufacturing. For Portugal, both the average (16,000) and the above/below productivity assumptions (44,500) lead to higher absolute employment losses in the dynamic model than in the static one.[1]

27. Whatever the balance of employment changes according to the two models is, it reveals that adhesion to the EC offers neither a quasi automatic way of solving the labour market difficulties of Portugal or Spain, nor that it will substantially add to them, though one has to keep in mind that the job displacement and job creation effects would neither occur in the same industries and regions nor affect the same labour qualification groups. Yet, the models essentially rely on past trends, though modified by certain assumptions. And in the past, Portugal and Spain suffered from economic policy inefficiencies hindering them in fully exploiting their comparative advantages in the international division of labour. To a considerable extent these inappropriate policies have given rise to a variety of structural problems, which are a much more important source of unemployment and to which we turn now.

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[1] However, the absolute figures for Portugal need further interpretation. These country's exports have been much lower than its imports in the base year underlying the models, but they have grown faster. For this reason, after a certain time period exceeding the prevailing one of seven years (chosen because of the length of the transition period), the employment gains by exports would exceed the employment losses through imports.

Adjustment Requirements

28. The industry in both Iberian countries has been beset with deep structural diseases for a long time (Donges et al., 1982, ch. 2):

- On the one hand, there is excessive fragmentation of production capacities, many firms do not take advantage of scale economies, the installed equipment is frequently outmoded (especially in small- and medium-sized companies), numerous firms are over-staffed and under-capitalized, and several enterprises operate with a negative value added at world market prices.

- On the other hand, monopolistic and oligopolistic structures have emerged which involve significant "X-inefficiencies" (in Leibenstein's sense) for given plant size and factor prices. Among the high-cost producers are industries such as iron and steel, non-ferrous metals and chemicals which, because of their strategic position in the economy's input-output network, contribute to the proliferation of defective cost structures over the whole manufacturing sector and make it difficult for other firms to become more efficient. State-owned companies, most notably in Spain, show a particularly poor performance in this regard.

- Moreover, only a few Portuguese and Spanish firms are known for applying modern organizational techniques and for running R&D activities. Indicative of the nationwide neglect of R&D is the observation that in each of the Iberian countries, only about 35 people per 1,000 are engaged in research and development (against an average of 350 in the EC-9) and the R&D-to-GNP ratio amounts to only 0.3 per cent (as compared to 2 per cent in the Community).

29. These serious structural deficiencies remained largely unnoticed during the sixties and early seventies when industry in both Iberian countries was growing remarkably rapidly by any comparative standard. However, when external shocks (oil price increases along with various cyclical recessions in the world economy) occurred over the seventies, compounded by domestic distributional quarrels and frequent changes in economic policy in the aftermath of the political transition towards democracy, it became apparent that the industry was lacking flexibility just at a time when much adaptability to changing circumstances was required (Balassa, 1983; Donges, 1984). Thus, the structural shortcomings inherited from the past indirectly have become a strong contributory factor to the slackening of industrial growth in both Iberian countries.[1] Moreover, the enduring economic crisis which Spain is suffering for almost a decade, triggering a high and increasing rate of unemployment (which nowadays is about 22 per cent of the labour force as compared to 4.7 per cent in 1975), is rooted in structural rigidities to a considerable extent.

30. To overcome structural weaknesses and to adjust to a changing international and domestic economic environment, substantial modernization investments should have taken place. This did not happen, however. In Portugal, gross fixed capital formation in real terms only grew at 0.6 per cent annually in the period 1975-84, with an absolute shrinkage in 1979 (-1 per cent), in 1983 (-7.5 per cent) and in 1984 (-20 per cent). In Spain, developments were even more disappointing, as gross fixed capital formation declined by 1.5 per cent annually, with small increases only in 1980 (1.3 per cent) and in 1981 (1.2 per cent). There-

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[1] Portugal's manufacturing industry grew at an annual rate of 4.5 per cent in the period 1975-84 (in real value added terms), as compared to 6.5 per cent in the period 1960-75. The growth rates achieved by the Spanish manufacturing industry were 2.8 and 8.6 per cent, respectively (Source: National statistics).

Table 10: Investment Ratios in Portugal and Spain[a]

(per cent)

Year	Portugal			Spain		
	Gross fixed capital formation / GDP		Net capital formation / national income	Gross fixed capital formation / GDP		Net capital formation / national income
	Total	Equipment		Total	Equipment	
1970-74	25.6	11.3[b]	21.0	23.0	9.0	15.7
1975	25.9	9.1[b]	22.9	23.3	8.9	15.9
1976	25.1	7.2[b]	22.3	21.8	8.1	14.4
1977	26.5	10.9	23.6	21.0	7.7	13.5
1978	27.9	11.0	25.0	19.9	7.2	12.4
1979	26.6	12.1	23.8	18.9	6.3	10.9
1980	28.8	12.9	26.3	19.4	6.5	11.1
1981	30.7	13.7	28.8	20.3	7.0	11.7
1982	30.9	n.a.	29.5	19.7	6.6[b]	10.7
1983	28.9	n.a.	27.2	18.8	6.4[b]	9.6
1984	24.1[b]	n.a.	22.5[b]	18.0[b]	6.1[b]	9.5[b]

[a]Based on current prices. - [b]Own estimates.

Source: OECD, National Accounts, various issues.

fore, in this country the gross investment share in GDP has been declining in recent years; equipment investment was weak, too. The downward trend was most dramatic with regard to the net investment ratio, which usually reflects the national accumulation rate: it fell from almost 16 per cent in 1975 to 9.5 per cent in 1984 (Table 10). That the corresponding investment ratios apparently look more satisfactory in the case of Portugal, does not mean much, as they are mainly due to heavily capital-intensive projects implemented in petrochemicals, steel and port infrastructure, the efficiency of which still has to be proven. Moreover, Portuguese private firms reportedly have been curtailing investment plans year after year since 1980.[1]

31. There are various reasons to explain the inadequate private investment activity in the Iberian countries. In the case of Portugal, the 1974-75 wave of expropriations has had a prolonged adverse effect because the question of compensation, let alone reprivatization, is still a matter of political controversy. This wave did not spread to Spain, but there are common features to both Iberian countries:

- To begin with, real labour costs rose strongly in the years following the political transition. Though wage increases slowed down over the last few years, the cost pressure was redressed only partially and the harmful impact of the then labour cost explosion has remained appreciable until now due to severe rigidities of the labour market, inherited from the old authoritarian régimes, such as a heavy protection of employees and workers against dismissal and their entitlement to severance pay.

- Second, both countries experienced a very rapid growth of public consumption expenditure, which outstripped that of tax revenues in spite of a nearly uninterrupted rise in the tax burden and in social security contributions since

[1] See Handelsblatt, February 16, 1985.

the late seventies. The financial position of the public sector thus shifted from a (small) surplus in the early seventies to a sizeable deficit in 1984, amounting to about 8 per cent of GNP in Portugal and roughly 6 per cent in Spain.[1]

- Third, inflationary pressures were strong, with consumer prices rising at two-digit rates during almost the whole period, most persistently in Portugal. This pressure forced the national authorities time and again to tighten monetary policy, which usually entailed higher interest rates and exerted a dampening impact on domestic demand.

- Fourth, these developments have squeezed profits during many years and they have created considerable uncertainty about the viability of investment projects in the future. Though corporate profits have been improving recently, casual evidence suggests that this is essentially attributable to returns from financial investments, particularly government bonds.

32. To be sure, similar developments took place in the EC countries too, and they have retarded investment there also. But the trend was much more pronounced in the Iberian Peninsula (Table 11). This can be ascribed to the fact that the successive governments took it for granted that a consolidation of democracy would require a priority of income redistribution over efficiency improvement. In such an environment it does not come as any surprise that most of the investment which actually was undertaken in Portugal and Spain was rationalization investment aiming at substituting capi-

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[1] Source: National statistics. The figure for Portugal is probably biased downwards to a considerable extent. Silva Lopes, who was governor of the Bank of Portugal in the late seventies, recently detected important errors and omissions in the accounting of public expenditures, the inclusion of which would have brought the share of public deficit in GNP up to 17 per cent in 1983 and thus to the highest level within the OECD area (1985, pp. 5-25).

Table 11: Comparative Trends of Macroeconomic Distortions
(Average annual change 1974-84 in per cent)

	Portugal	Spain	EC-10
Wages	16.5	22.0	12.7
Unit labour costs	11.5	18.0	9.7
Public current expenditure	37.5	24.0	18.5
Public current revenue	36.5	21.5	13.7
Consumer prices	22.0	15.9	9.0

Source: IMF, International Financial Statistics, various issues. - OECD, Main Economic Indicators, various issues. - EC-Commission, Annual Economic Report 1983-84. - Own estimates.

tal for labour. The rate of capacity-enlargement and product-innovating investment remained poor, so that the ability of numerous firms to operate successfully under the new conditions of European integration is subjected to the condition that the inappropriate trends from the past be reversed and that private business confidence in future economic development be restored on a lasting basis.

33. Despite productive investment, and thus industrial adjustment, lagging behind needs, both countries achieved remarkable export results, especially in recent years. To some extent, this development can be attributed to the export orientation of foreign companies in selected sectors (textiles and electrical components in Portugal, motor cars in Spain, for instance). Also it has to be noted that numerous domestic firms used to regard exports as a substitute for weak domestic demand in order to maintain capacity utilization at reasonable levels and that they sold abroad even at unremunerative prices.

34. This notwithstanding, exchange-rate policies might have had a role in the export expansion too. The Portuguese authorities introduced, in 1977, a crawling-peg for the escudo to be depreciated more or less gradually (against a basket of foreign currencies), with major adjustments from time to time, to neutralize the impact of the faster internal inflation. In Spain, a policy of managed floating has been applied since 1974, with formal unilateral devaluations of the peseta in February 1976, July 1977 and December 1982. The real valuation of the escudo and the peseta achieved under these exchange-rate schemes are shown in Table 12.[1] In the

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[1] In effective nominal terms, the escudo depreciated by an average of 13 per cent during the period 1974-84; the decline of the escudo exchange rate against the EC currencies was in the same order of magnitude, while the depreciation against the dollar was steeper (16 per cent) and the one against the peseta was smaller (6.6 per cent). As far as Spain is concerned, the peseta exchange rate fell annually by 7.8 per cent on average, by 5.4 per cent against the EC currencies, and by 9.7 per cent against the dollar.

Table 12: Index of Effective Real Exchange Rates[a]

Year	Portugal vis-à-vis				Spain vis-à-vis		
	World	EC-9	USA	Spain	World	EC-9	USA
1974	100.0	100.0	100.0	100.0	100.0	100.0	100.0
1975	94.7	92.3	102.3	95.3	103.4	103.1	103.6
1976	97.0	93.4	98.3	96.2	98.7	101.6	97.8
1977	89.7	85.4	112.3	97.5	97.8	98.8	95.2
1978	93.5	83.3	100.5	98.5	100.1	97.1	101.9
1979	89.2	82.5	104.2	91.3	115.3	108.3	118.5
1980	80.1	75.8	95.0	86.5	112.5	106.6	114.4
1981	83.3	82.8	84.3	93.2	101.6	108.5	94.1
1982	79.2	77.1	73.1	87.9	97.0	109.2	86.8
1983	80.3	76.1	68.8	95.8	85.6	99.7	75.1
1984	81.5	74.9	65.9	93.0	86.5	105.2	73.6
Average annual change p.c.	-2.0	-2.8	-4.1	-0.7	-1.4	+0.5	-3.0

[a] Nominal exchange rates adjusted for changes in wholesale/producer prices abroad and at home. The relevant weights have been derived from the bilateral trade (exports plus imports) shares in 1980. All figures are period averages. A real depreciation (appreciation) is indicated by a decline (increase) of the indexes shown.

Sources: OECD, Main Economic Indicators, various issues, and Foreign Trade by Commodities, 1980. - Banco de Portugal, Relatório do Conselho de Administração, various years. - Banco de España, Boletín Estadístico, various issues.

case of Portugal, the overall trend was in the direction of a real depreciation of the escudo against the currencies of various trading partners. When the crawling-peg lagged behind the inflation differential between home and abroad, as it sometimes did, the deterioration of the external price competitiveness was of short length and got compensated by improvements later on. The picture looks different for Spain. The peseta also depreciated in real term on average and against the dollar, but not against the EC currencies. Moreover, the authorities even allowed a prolonged real appreciation in the late seventies, to support their attempts to bring down the rate of inflation. But in the last few years, the real depreciation of the peseta was significant (1982-83 also with regard to the EC currencies), which certainly stimulated the export expansion.

35. The maintaining of external price competitiveness by means of currency devaluations, important as it may have been in both Iberian countries on balance-of-payments grounds, bears some risk over the medium run, however. The exchange-rate devaluations usually involve a deterioration of the terms of trade and thus imply losses in national income if no adequate adjustment takes place. As a matter of fact, these policies have supported manufacturing activities for which Portugal or Spain may no longer display a comparative advantage or may lose it in a foreseeable future due to changes in the international division of labour; in the case of Spain, this holds true in particular for traditional labour-intensive industries such as footwear or clothing. When the real exchange-rate devaluations concede such industries the possibility to expand exports rapidly, while protecting them at the same time against competing imports, there is the danger that inexorable structural adjustments are deferred once more.

Conclusions and Policy Implications

36. As discussed earlier, it is likely that both countries could derive gains from increased specialization within the enlarged Community. As the future invariably is uncertain, there is no specific method for being precise about promising activities, however persistently the enthusiasts of industrial policy advocate the merits of selective government involvement to pick potential "winners". It is a genuinely entrepreneurial task to search in the market place for profitable opportunities to invest and specialize. Just for illustration, the following remarks may be in order:[1]

- Portugal's best chances for specialization should lie in its internationally most dynamic sectors (textiles, footwear and electronics) to the extent that they up-grade their products and thereby consolidate their competitive strength against suppliers from LDCs (and some NICs). The same holds for some traditional products, such as cork manufactures, wood pulp and paperboard, and industrial ceramics. Good possibilities might also exist for the manufacturing of components and accessories for a wide range of final goods, and for assembling activities as well. Moreover, it is conceivable that the country develops a distinct comparative advantage in the repair of ships.

- Spain's best chances should lie in the intermediate goods sector and in investment goods industries, whose factor requirements seem to fit with the actual and foreseeable factor endowments in this country. Machines of various kinds, electronic products, railway vehicles as well as accessories and parts for the aircraft and the motor car

[1] The reader should remind at this stage that this analysis does not include processed agricultural and fish products, in which both Iberian countries have a considerable comparative strength. See Donges et al. (1982, ch. 5) for details.

industries have even a more promising potential because of a relatively favourable international environment. The automative industry itself also faces good prospects as it already is integrated into the European production network of various multinational companies, exporting about 60 per cent of its annual production to other European countries (including Portugal).

- As far as bilateral trade relations are concerned, Portugal should be able to take advantage from the fact that wages are substantially lower than in Spain (about half, on average). Textiles and clothing, footwear, furniture, printed matter and other traditional consumer goods are therefore good candidates for a drive into the Spanish market. For Spain, the greatest specialization gains might accrue to the investment goods sector. Even industries such as steelmaking and shipbuilding, now under strain, could benefit from a closer trade relationship with Portugal, provided they undertake an effective restructuring.

37. The future pattern of specialization might be influenced also by additional inflows of foreign direct investment, provided the pertinent legislation remains favourable in both countries.

- Portugal could become, even more than in the past, a natural location for the redeployment of labour-intensive activities from the advanced EC countries, given its advantages of an elastic supply of low-priced, diligent and trainable workers. Also Spanish manufacturers of traditional consumer goods (clothing, leather- and footwear, for example) may consider to invest in Portugal and thereby strengthen their export competitiveness; moreover, Portugal's lower wage costs may induce Spanish producers of intermediate and investment goods (such as chemicals, paper, fabricated metal products, transport equipment), which have been expanding their investments in Portugal

rapidly in recent years (Molero and Buesa, 1983, pp. 71-93), to continue doing so in the future.

- Spain itself could increase its weight in the process of internationalization of production within the Community, as its rating by foreign investors based on past experience seems to be satisfactory and its potential for a rapidly growing market appears to be reasonably large. Apart from the automotive industry, prime candidates for a further foreign-capital involvement include industrial equipment, electrical machinery, chemical industry, and non-metallic mineral manufacturing.

- Besides these potential intra-Community private capital flows, it is likely that companies from non-EC countries (such as the USA and Japan as well as a number of East Asian and Latin American NICs, which are already generating their own multinational corporations) establish subsidiaries in Portugal or Spain in order to overcome the tariff and non-tariff barriers which surround the Common Market and to protect themselves against the discretionary and thus unpredictable nature of the EC's trade policy.

38. This said, neither Portugal nor Spain can expect that the entry into the EC will automatically yield substantial net benefits to them in terms of trade expansion, acceleration of economic growth and creation of new employment opportunities. For this to happen a necessary condition is that the manufacturing industry makes sufficient progress on its way to indispensable adjustments. Concrete steps by the governments to assist this process have already been taken in the last few years. Whereas in Portugal the emphasis is laid on diversifying industrial production, on proceeding cautiously with the implementation of excessively capital-intensive projects and on encouraging the settlement of foreign companies, the major concern of the Spanish government is the restructuring of ailing industries. The sectors

covered include those which have been the engines of industrial growth for decades, like shipbuilding and the steel industry (Table A-6).[1] But it still remains to be seen whether the restructuring will just consist of employment cuts and a restoration of the financial position of the companies affected, or whether it will, as it should, go beyond that and pave the way for true product innovations which would make the industry more competitive within the Community and worldwide as well. Given the regional concentration of the adjustment burden and the strong opposition by the trade unions against the envisaged reduction of employment, confidence in a completion of the restructuring plans as scheduled may be at this stage premature.

39. To be fully effective, a strategy which is to enhance the competitiveness of domestic firms following the accession to the EC must be embedded into a framework in which inflation pressures are brought under control and market forces are allowed to steer the allocation of resources. Key elements in the shaping of such a framework are, as is now widely recognized, the reduction of budget deficits, a liberalization of prices on product markets, the removal of existing labour market rigidities, the deregulation of financial markets, a reorganization and even reprivatization of public enterprises, and a strengthening of competition policies in combination with a promotion of mergers to the extent necessary to rationalize production and to reduce real costs. With such a framework, both Iberian countries would also improve their attractiveness for foreign direct investment in the manufacturing sector, in competition with other countries of the EC periphery (in particular Ireland and Greece). They thereby would not only widen the source of financing the urgently needed new investments but also have

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[1] The present EC countries have also embarked upon a process of reconversion of the steel industry. This programme, and in particular the subsidization which it implies, is to be completed by the end of 1986, whereas Spain has been given two years more to subsidize and restructure the industry.

a greater share in the diffusion of technological know-how, including the new information technologies; foreign direct investment also can bring improved management and contribute to an up-grading of labour skills (through on-the-job training), thereby strengthening the competitive position of the Portuguese and Spanish economy within the enlarged EC.

40. Some measures going in the direction indicated have already been adopted, others are planned or promised. But considerable efforts will continue to be needed. In any case, it is important that the governments show firmness and do not give way to actions dictated by short-term political expediency. Otherwise, the prospects for a substantial increase of the marginal efficiency of capital, which is a prerequisite for new productive investments, would remain bleak. The positive expectations derived from the forthcoming membership in the European Community could then easily vanish. And the chances for resuming self-sustaining economic growth and for increasing employment opportunities would be small.

Table A-1: Foreign Trade Indicators for Portugal

Commodities[a]	Exports[b]			Imports[b]		
	Annual rate of growth (p.c.)	Structure of exports (p.c.)		Annual rate of growth (p.c.)	Structure of imports (p.c.)	
		within regions and worldwide	by commodities		within regions and worldwide	by commodities
	1970-82	1982	1982	1970-82	1982	1982
	Trade with EC-9					
All commodities	16.1	100.0	57.3	14.5	100.0	40.6
Manufactured goods	19.4	76.9	60.1	13.9	83.1	64.3
	Trade with other OECD countries					
All commodities	12.8	100.0	24.5	17.5	100.0	28.6
Manufactured goods	13.5	76.6	25.6	15.4	57.4	31.2
	Trade with rest of world					
All commodities	7.7	100.0	18.2	17.4	100.0	30.8
Manufactured goods	6.4	57.4	14.3	6.4	7.6	4.5
	Trade with world					
All commodities	13.1	100.0	100.0	16.1	100.0	100.0
Manufactured goods	14.6	73.3	100.0	13.8	52.6	100.0

[a]On the basis of SITC rev. 2. Manufactured goods are those included in SITC 5-8. - [b]Based on U.S. dollar values.

Source: OECD, Foreign Trade by Commodities, various issues.

Table A-2: Foreign Trade Indicators for Spain

Commodities[a]	Exports[b]			Imports[b]		
	Annual rate of growth (p.c.)	Structure of exports (p.c.)		Annual rate of growth (p.c.)	Structure of imports	
		within regions and worldwide	by commodities		within regions and worldwide	by commodities
	1970-82	1982	1982	1970-82	1982	1982
			Trade with EC-9			
All commodities	19.4	100.0	45.8	14.7	100.0	31.4
Manufactured goods	24.4	68.1	42.5	13.9	79.4	62.4
			Trade with other OECD countries			
All commodities	14.9	100.0	15.6	14.1	100.0	22.7
Manufactured goods	16.3	70.5	15.0	12.8	54.2	30.7
			Trade with rest of world			
All commodities	22.6	100.0	38.6	21.7	100.0	45.9
Manufactured goods	23.6	81.0	42.5	15.1	6.0	6.9
			Trade with world			
All commodities	19.5	100.0	100.0	17.1	100.0	100.0
Manufactured goods	22.4	73.5	100.0	13.6	40.0	100.0

[a]On the basis of SITC rev. 2. Manufactured goods are those included in SITC 5-8. - [b]Based on U.S. dollar values.

Source: As Table A-1.

Table A-3: Revealed Comparative Advantages (+) and Disadvantages (-) in Portugal's Foreign Trade [a]

SITC	Commodities	EC-9		Other OECD		Rest of World	
		1970	1982	1970	1982	1970	1982
	Intermediate goods						
51	Organic chemicals	-272.9	-54.6	-261.0	1.6	-27.8	-126.2
52	Inorganic chemicals	-88.3	-177.7	-156.4	-44.5	224.1	2.3
53	Dyeing and tanning materials	-431.4	-398.3	-284.6	-401.4	103.3	20.4
56	Manufactured fertilizers	-35.7	213.7	13.2	-395.0	603.0	106.1
57	Explosives and pyrotechnic products	-65.5	-244.5	122.2	-609.1	456.5	375.3
58	Artificial resins, plastic materials etc.	-240.7	-166.5	-315.0	-167.5	106.1	14.1
59	Other chemical materials	171.8	67.3	76.0	-79.1	180.5	184.2
62	Rubber manufactures	-6.2	-201.9	49.7	-77.9	293.9	-12.2
65	Textile yarn, fabrics etc.	157.1	128.9	138.5	140.8	224.4	94.8
66	Non-metallic mineral manufactures	283.7	87.0	136.9	106.8	-272.8	-119.3
67	Iron and steel	-179.1	-191.6	-224.4	-137.5	93.5	-101.8
68	Non-ferrous metals	-224.1	-187.9	-199.4	-212.7	-229.3	-293.2
	Investment goods						
69	Fabricated metal products	-41.4	-45.9	3.1	99.1	211.6	178.1
71	Power generating machinery	-296.7	-114.0	-313.6	-233.3	223.1	8.5
72	Machinery for particular industries	-449.2	-318.1	-308.4	-233.5	151.3	-29.2
73	Metalworking machinery	-182.0	-322.2	-143.9	-213.1	241.2	-159.1
74	General industrial machinery	-233.4	-211.8	-126.0	-87.7	278.6	15.1
75	Office machines and automatic data processing equipment	-70.2	33.0	-27.5	9.0	138.2	-127.7
76	Telecommunications equipment	29.8	53.0	5.7	-45.7	132.6	-70.7
77	Electrical machinery	-105.1	-21.9	-40.0	-139.9	249.0	-54.8
78	Road vehicles	-288.8	-97.0	-272.9	-321.2	183.2	-20.8
79	Other transport equipment	-246.8	-140.6	-274.3	-475.2	44.8	156.4
87	Professional, scientific and controlling instruments	-165.8	-141.0	-189.1	-192.2	101.7	-121.9
	Consumer goods						
54	Pharmaceutical products	-104.2	-124.6	-133.3	-117.7	285.6	163.5
55	Essential oils, perfume materials etc.	-104.5	-119.1	-104.3	-152.3	402.4	469.4
61	Leather and leather manufactures	-95.4	40.1	-90.3	-12.2	46.0	-220.5
63	Cork and wood manufactures (excluding furniture)	469.1	474.0	455.2	469.8	207.7	300.3
64	Paper and paper products	24.6	49.7	-235.2	-1.9	553.9	188.5
81	Sanitary, plumbing, heating and lighting fixtures and fittings	-149.0	-105.0	65.7	15.8	200.7	119.0
82	Furniture	-140.9	82.7	51.3	168.6	180.9	80.3
83	Travel goods	82.5	-84.3	166.2	-54.8	-113.7	-271.0
84	Clothing	279.8	383.1	367.6	483.3	130.0	-58.6
85	Footwear	346.0	486.1	433.5	483.1	123.4	268.9
88	Photographic apparatus, optical goods and watches	-370.5	-22.7	-304.6	-103.8	59.1	-209.6
89	Miscellaneous manufactures	-139.2	-51.9	-39.2	8.0	72.0	-51.1

[a] For method of calculation see text.

Source: As Table A-1.

Table A-4: Revealed Comparative Advantages (+) and Disadvantages (-) in Spain's Foreign Trade[a]

SITC	Commodities	EC-9		Other OECD		Rest of World	
		1970	1982	1970	1982	1970	1982
	Intermediate goods						
51	Organic chemicals	-82.0	-84.9	-107.9	-41.7	-74.4	-141.2
52	Inorganic chemicals	45.4	-78.5	92.5	-9.4	-179.8	-173.1
53	Dyeing and tanning materials	-143.6	-102.2	-4.3	86.3	-127.0	-65.7
56	Manufactured fertilizers	14.2	55.4	29.3	108.8	-71.8	-40.5
57	Explosives and pyrotechnical products	22.3	-90.7	-22.0	-284.1	80.5	67.3
58	Artificial resins, plastic materials etc.	-168.0	-128.3	-36.0	45.5	41.1	192.3
59	Other chemical materials	-56.1	-121.7	-204.4	-87.3	-82.8	12.8
62	Rubber manufactures	211.4	133.8	214.4	167.0	271.7	140.8
65	Textile yarn, fabrics etc.	100.4	52.3	104.4	39.9	95.2	-28.6
66	Non-metallic mineral manufactures	20.6	11.0	49.3	138.6	95.9	132.6
67	Iron and steel	-68.2	0.7	-156.3	146.0	-216.6	59.8
68	Non-ferrous metals	56.6	67.1	-117.1	106.9	-249.1	-119.6
	Investment goods						
69	Fabricated metal products	64.6	28.3	135.0	78.9	238.4	147.2
71	Power generating machinery	-129.7	-29.1	-252.3	-175.0	205.6	179.4
72	Machinery for particular industries	-129.0	-125.4	-30.1	-78.3	143.6	112.5
73	Metalworking machinery	0.2	-99.7	6.4	12.8	15.1	192.6
74	General industrial machinery	-138.1	-97.8	-155.3	-63.2	74.6	140.0
75	Office machines and automatic data processing equipment	-58.7	-87.0	-59.5	-64.1	-49.9	-128.8
76	Telecommunications equipment	-54.5	-130.8	-151.1	-218.8	55.8	-193.9
77	Electrical machinery	-32.1	-33.5	-18.3	-92.7	168.0	-14.4
78	Road vehicles	44.9	78.6	107.3	65.3	354.3	242.6
79	Other transport equipment	197.6	-51.4	-376.5	-94.0	471.5	140.6
87	Professional, scientific and controlling instruments	-148.3	-213.3	-132.9	-275.3	15.0	29.5
	Consumer goods						
54	Pharmaceutical products	-103.1	-62.9	-173.7	-63.1	16.1	15.0
55	Essential oils, perfume materials etc.	23.4	-17.2	115.9	35.2	-9.7	50.9
61	Leather and leather manufactures	198.9	245.6	203.0	236.4	-86.1	-284.5
63	Cork and wood manufactures (excluding furniture)	318.4	226.0	254.7	159.4	81.1	6.3
64	Paper and paper products	-72.9	39.3	-152.5	-181.0	214.1	139.7
81	Sanitary, plumbing, heating and lighting fixtures and fittings	113.5	-9.9	277.8	66.7	88.0	111.7
82	Furniture	185.4	118.8	311.6	134.3	129.4	46.2
83	Travel goods	79.4	95.3	412.2	299.4	-12.4	-185.9
84	Clothing	149.3	99.8	341.9	137.4	28.3	-164.8
85	Footwear	355.1	310.1	588.1	474.8	242.9	-63.9
88	Photographic apparatus, optical goods and watches	-201.7	-118.0	-245.5	-188.8	-62.8	-300.0
89	Miscellaneous manufactures	79.1	38.6	114.6	45.0	121.3	-55.1

[a]For method of calculation see text.

Source: As Table A-1.

Table A-5: Revealed Comparative Advantages (+) and Disadvantages (-) of Portugal in Trade with Spain[a]

SITC	Commodities	1970	1982
	Intermediate goods		
51	Organic chemicals	0.2	139.5
52	Inorganic chemicals	b	-265.0
53	Dyeing and tanning materials	-152.5	-262.6
56	Manufactured fertilizers	146.1	-221.3
57	Explosives and pyrotechnical products	-83.1	b
58	Artificial resins, plastic materials etc.	-216.9	-81.7
59	Other chemical materials	-19.5	-62.5
62	Rubber manufactures	-273.9	-111.3
65	Textile yarn, fabrics etc.	77.4	154.5
66	Non-metallic mineral manufactures	-16.8	-60.3
67	Iron and steel	-5.0	-208.5
68	Non-ferrous metals	-361.6	-295.9
	Investment goods		
69	Fabricated metal products	32.1	132.5
71	Power generating machinery	25.5	-138.3
72	Machinery for particular industries	-207.2	-183.1
73	Metalworking machinery	-1.7	-208.5
74	General industrial machinery	-94.9	-92.3
75	Office machines and automatic data processing equipment	55.5	-41.1
76	Telecommunications equipment	-44.8	57.2
77	Electrical machinery	-129.5	-41.6
78	Road vehicles	-229.8	-121.5
79	Other transport equipment	189.0	b
87	Professional, scientific and controlling instruments	-6.0	-67.3

(continued)

(continued)

SITC	Commodities	1970	1982
	Consumer goods		
54	Pharmaceutical products	101.6	-200.4
55	Essential oils, perfume materials etc.	-73.5	-84.3
61	Leather and leather manufactures	-109.8	-125.5
63	Cork and wood manufactures (excluding furniture)	403.9	403.1
64	Paper and paper products	-273.0	291.2
81	Sanitary, plumbing, heating and lighting fixtures and fittings	27.6	110.0
82	Furniture	23.4	315.6
83	Travel goods	b	b
84	Clothing	25.5	375.6
85	Footwear	-115.0	207.7
88	Photographic apparatus, optical goods and watches	-37.9	276.5
89	Miscellaneous manufactures	-75.7	27.5

[a]For method of calculation see text. - [b]Indetermined.

Source: As Table A-1.

Table A-6: Government-guided Industrial Restructuring in Spain: Employment Implications

Sector	1981 Restructuring scheme			1983 Restructuring scheme		
	Employment[a]			Employment[a]		
	Total Dec. 1981	Planned reduction 1981-85		Total Dec. 1983	Planned reduction 1984-86	
		Total	% Change		Total	% Change
Footwear	55,000	3,100	-5.6	50,000	3,100	-6.2
Textiles and clothing	420,000	68,000	-16.7	400,000	11,900	-3.0
Home appliances	19,400	4,527	-23.3	19,400	5,314	-27.4
Iron and steel	71,100	17,494	-24.6	70,100	12,545	-17.9
Shipbuilding	39,000[b]	9,838	-25.2	41,400	17,368	-42.0
Copper manufacturing	4,300	979	-22.8	-	-	-
Paper	-	-	-	20,400	1,500	-7.4
Fertilizers	-	-	-	10,000	1,180	-11.8
Electrical parts for cars	8,000	1,713	-21.4	5,000	460	-9.2
Electrical equipment	3,400[a]	134	-3.9	15,000	3,100	-20.0
Telecommunications	-	-	-	17,000	3,200	-18.8
Machine tools	-	-	-	8,300	2,000	-24.1
Individual companies	47,700	13,369	-28.0	9,688	1,836	-19.0
TOTAL	667,900	119,154	-17.8	666,288	63,503	-9.5
In per cent of manufacturing employment[c]	29.2	-	-	31.5	-	-

[a]Differences in total employment between December 1983 and December 1981 are mainly due to an extension of companies included in the scheme, apart from delays in the implementation of the first plans.

[b]End of 1982. - [c]Own estimantes.

Source: Ministerio de Industria y Energía, El Libro Blanco de la Reindustrialización, Madrid 1983, p. 55. - OECD, Economic Surveys 1983-1984: Spain, Paris, May 1984, p. 47.

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