

# **The EIB and the Italian Economic Integration in the EEC: from its birth to the early eighties**

(Donatella Strangio - Paolo Tedeschi)<sup>1</sup>

*Extended abstract without tables – Do not quote*

## **1. Introduction: Topics and Aim**

The significant monetary imbalances at the end of the WWII were obviously largely due to the lack of cooperation between states in working to solve economic and financial problems. This experience led to a new way of thinking about the world economy and the problems of international economic relations and to the belief that the solution consisted in coordinating the economic policies of foreign governments. The result of this was the establishment of international organizations as supranational bodies which in fact, would influence both the reconstruction and the development of the economy in the following decades. This represented a historically significant step indicating growing governmental awareness of the need for international collaboration.

The first objective was to safeguard the hard-won peace, as well as improving standards of living, promoting economic and social development in backward regions, establishing global economic and monetary stability, rebuilding areas devastated by war, removing obstacles in the relationships between individual states, boosting production, reaching full employment and facilitating credit.

As Douglass North said, "institutional change influences the evolution of society over time and is the key to understanding history." The central idea of institutional analysis is the belief that economic activity is so dependent on institutions that it cannot be analysed without prior knowledge of the nature and trends of those institutions, whose functioning is the framework of action for both individuals and groups. Institutions are important because the development of organizations that create an environment conducive to cooperative solutions in the complex context of trade is the basis of economic growth. At the centre of everything there is cooperation, in the sense of the competition of actions that allows economic systems to reap the benefits of trade, as posited by Adam Smith. The aim of institutions is to create a stable structure of social relations that can reduce uncertainty.

The aim of this work is, therefore, twofold: firstly, to analyse the historical reasons that led European countries to embark on a common path of integration not only with the help of the literature, but also through some important archival sources that are to be found mainly in the Historical Archives of the Bank of Italy and the European Investment Bank (EIB), such as reports,

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<sup>1</sup> Donatella Strangio – Associate Professor in Economic History – University of Rome La Sapienza – Department Memotef – E-mail [donatella.strangio@uniroma1.it](mailto:donatella.strangio@uniroma1.it) ; Paolo Tedeschi – Associate Professor in Economic History – University of Milan Bicocca DEMS - Email: [paolo.tedeschi@unimib.it](mailto:paolo.tedeschi@unimib.it)

economic reports, speeches of some influential politicians of the time. And secondly, to give special attention to the relationship between integration and Italy and, in particular, between Italy and the EIB, whose establishment goes directly back to the origins of the European Community, namely the Treaty of Rome in 1957. In particular the analysis will examine the EIB's management and fundraising, the area of its jurisdiction and its work at every level (in particular, in the depressed areas of the South of Italy – indicated as Mezzogiorno in the EIB's analysis).

The paper illustrates the credit policy followed by the EIB both in principle (as it emerges from official documents and from archival research) and in practice (by examining statistically the nature of all the loans granted to Italy). Using the principal literature the paper also fits within some strands of discussion that have been identified by the 'Besançon group' of academics working on counter-discourses on Europe, which led to the creation of an international network known as the Observatory of Discourses on Europe. This allows to see who supports European integration, and evidently who does not help the process of European social and economic integration.

Please note that the focus is on the period that goes from its birth in 1958 to the early eighties: so the paper concerns the "golden age", the oil shock and the first enlargement of the European Economic Community (EEC) and it arrives at the birth of the European Currency Unit (ECU) and the entry of the Greece. The investigation is extended over the long run for some specific aspects only: in fact EIB's Archives are not fully available for the eighties and they are not available for the following years.

## **2. The role of the EIB in the EEC**

The EIB was born in 1958, with the signing of the Treaty of Rome. The EIB was founded with the task of contributing to the balanced development of the Common Market, by supporting initiatives to reduce imbalances. Nowadays, it is a modern international institution, financing investment projects to many countries, even outside European borders.

The institutional configuration that the Bank assumed when it was created was the result of an intense debate and of a comprehensive set of proposals made since the late forties in the OEEC countries. In this debate and in defining the initial organizational characteristics of Bank, Italian representative plays a major role. The Bank was, in the idea of Italian negotiators, the necessary *"compensation for... economic backwardness that the country asked for acceding to the trade liberalization imposed by the process of European integration"*: greater trade openness must come with financial support for the solution of regional disparities that could worsen as a result of accession to the Community.

The Article 130 of the Treaty stated: “The task of the European Investment Bank shall be to contribute, by calling on the capital markets and its own resources, to the balanced and smooth development of the Common Market in the interest of the Community. For this purpose, the Bank shall, by granting loans and guarantees on a non-profit-making basis, facilitate the financing of the following projects in all sectors of the economy:

(a) projects for developing less developed regions;

(b) projects for modernising or converting enterprises or for creating new activities which are called for by the progressive establishment of the Common Market where such projects by their size or nature cannot be entirely financed by the various means available in each of the Member States;

(c) projects of common interest to several Member States which by their size or nature cannot be entirely financed by the various means available in each of the Member States.

The reasons for this downgrading were well described in the Minutes of the Board of Directors and were connected with the fundamental task of the EEC Treaty, that was to favour the full realization of the Common Market. In this respect, as it was noted by the Board of Directors, many sectors still benefited of institutional incentive mechanisms (coal, steel). Secondly, the effects of the Single Market and the situation of the companies were so uncertain at early stage that EIB preferred to wait and see: *"if the single market would have brought itself to convergence, the action of the EIB would have been more conveniently addressed to the other two tasks"*.

As it emerged from the debates within the Board of Directors, the structural problems that could exist in certain industries could be due only exceptionally to the opening of the borders: *"... the difficulties of the sector are reconnected to the general problems ... and hence is not the effect of the Common Market"*. Thus, the EIB's action did not have to interfere with the unfolding of the competition of the newly formed European Economic Community. The intervention of the EIB might be even detrimental to the market by financing sectors where there existed a production capacity in excess, dooming them to a subsequent necessity of being rescued.

This theme also emerged from the earliest meetings of the Board of Directors. At the meeting of 26 February 1959, the President Pietro Campilli announced that the Cassa per il Mezzogiorno<sup>2</sup> had submitted to the EIB and the International Bank for Reconstruction and Development (IBRD) a list of investment projects to be carried out in southern Italy in the fields of energy, industry, water supply, agriculture, railway transport: so in the history of the EEC, the EIB brought the legacy of the IBRD which, between 1951 and 1960, had granted 7 loans to Italy used to finance electrical,

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<sup>2</sup> The Cassa del Mezzogiorno was an Italian public body created to finance industrial projects aimed at economic development of southern Italy, in order to bridge the gap with the Northern Italy. It was established by law 10 August 1950 n. 646; it was designed by Pasquale Saraceno and his collaborators. The institute wanted to copy in the Mezzogiorno the US development agencies operating during the New Deal.

industrial and irrigation projects. The representatives of the two banks jointly decide to make a financing transaction totalling \$ 40 million to be distributed on two projects: the exploitation of lignite deposits in Basilicata for the production of electricity, the construction of a large petrochemical complex in Sicily. The comments (shared by the members of the Board Directors and by the representative of the EEC) focus on two points. After stressing that the intervention in the two sectors could certainly help to improve the local economy and to reduce the unemployment (an issue that will be discussed later), they pointed out how it will be appropriate, in the choice of the projects in future, to consider the total capacity of production in the Common Market with regard to the danger of financing sectors where an excess of production capacity could prevail. So financing had to take into account the developments of the common market: the Bank lent accordingly, making sure not to finance those activities where productive capacity was already in excess or those who already suffered from competition from foreign competitors and had little prospects of development. So the EIB financed new technological sectors (for example the chemical plants working with oil and/or producing plastic) or enterprises having a good market and high possibilities to expand it in particular in the country where they operated (for example, during the 1960s, the enterprises of the dairy sector and in general of the food industry which took profit of the great increase of the consume and of the baby-boom). On the contrary less funds were addressed to industrial plants for the production of paper, where the industry of European cellulose, was affected by the difficulties of competition with the Scandinavian countries. Finally, to show that the EIB was not in competition with the main European banks, the EIB's loans arrived at 50 per cent maximum of the project and this allowed the main banks to participate (and to earn) at the building of the new Europe of the six.

A further theme which occupied a special place in the early debates concerning the credit policy, was the impact in terms of employment. The reasons for seeking an increase in employment was a clear choice of economic policy in Italy, the cornerstone of the development plan (known as Vanoni Plan) that was also at the heart of the Protocol concerning Italy, annexed to the Treaty of Rome. The economy and life conditions in the EEC members could be enhanced only if there was a serious competition of bodies encounter any difficulties to the solution of national economic development. It was argued that for France and Italy had to do much more than what has been done until now to solve their problems management "du territoire". So it was necessary to give a new impetus to national policies of regional development, but at the same time the EEC had to create, with its own

bodies and their own policy coordinated with national policies, a new equitable distribution of investments<sup>3</sup>.

### **3. The EIB and its role in the Italian social and economic development**

Considering the EIB's aims is not a surprise to discover that during the sixties the EIB in particular financed projects which wanted to improve the per capita income and the quality life in the cheapest regions of the EEC, and in particular in Italy. The EIB's aims clearly explained why, during the sixties, the half of financed projects and the half of the total EIB's loans concerned Italy and in particular the Southern Italy. They were normally related to the building of new infrastructures and the creation new industrial poles, that is the tools that EEC had chosen to help the process of harmonisation between the EEC members' economies. The EIB was primarily established to realize this and it was in fact indicated in the part of the Treaty of Rome concerning the social and economic cohesion.

For the "fathers of the EEC" the development of the poorest areas allowed to strongly reduce the number of jobless and people emigrating, to avoid social and political problems (that is no riots and less possibilities for communist party to win the election), to create a new market for the local enterprises but also for those of the richest regions of the EEC. So the EIB had to contribute to the effort of the Italian government to close (or at least to strongly reduce) the gap between the North and the South of the Country and between Italy and the other EEC members. The EIB in fact had to represent the most relevant testimony of the importance of institutions and of a policy of cooperation between EEC members. The EIB's activity had to encourage them to pursue an increasingly strong policy of cooperation and to strengthen the idea of a more united Europe.

The EIB, together with the European Social Fund, represented the main tools designed to solve the problems of regional economic disparities and to help those countries that could further exacerbate their conditions after the creation of the common market. The fathers of the Europe knew that the existence of the less developed regions among European countries (with obsolete industrial structures, low levels of income per capita and inadequate infrastructures) could create a lot of problem. In heterogeneous economic area as the EEC was in the early days of its creation, the main fear was represented by a possible increase, with the establishment of the Common Market, of the economic distances between countries, some of whom had deep structural imbalances. In negative social and economic conditions the appeal of alternative ideologies, in particular those

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<sup>3</sup> Please note that when the EIB was born, the President Campilli wrote to the CEO of the main European banks: he assured them that EIB wanted to collaborate with them and that European institutions were not in competition with European financial *milieux*. Besides he communicated that the EIB deposited a part of its money in these banks.

related to the USSR, could be very strong and this could strongly decelerate (and perhaps definitively avoid) the building of the new Western Europe of the Six.

The EIB and the ESF had to be considered victories of the Italian diplomacy. The demand for these institutions represented a crucial point for Italy behind a precise plan of economic policy, that of the Vanoni Plan. The EIB was an Italian idea and started its activities with an Italian president, Pietro Campilli, who remained in office for two years. After him another Italian took over the presidency of the Institute, that is Formentini who left an important sign because of his strong personality and his intellectual brilliance mark the first 12 years of history of EIB.

Even if the aims which were underlined in the preamble of the Treaty: (as *reducing disparities between different regions and the backwardness of the least favored*) were not followed by providing a specific Community regional policy, they were entrusted to the ESF and in particular to the EIB: so they depended on the success of a fund and a bank. This last, from a purely quantitative point of view, quickly became one of the most important financial instruments of the EEC (even if the EIB did not insist on the EEC budget and all funds were obtained by collecting resources on the capital markets), and the size of his resources represented a point of reference for member countries firms and institutions for all the sixties, in particular for those operating in the Mezzogiorno.

During the seventies the EIB policy partially changed but it always remained in line with its statutory provisions: it in fact reduced its loans for Italy because of the effect of enlargements (and the arrival of other backward regions) and economic conditions (in particular the effects on all EEC members of the oil shock and the related great increase of the inflation and the arrival of the stagflation). However the EIB always maintained a particular attention and continued to give an important contribution to the development of the Mezzogiorno and, by the building of the infrastructures (new railways and free-ways) relaying it to the other EEC members, to the improvement of the communication between Italy and its partners.

The effects of the EIB's loans during the seventies were less relevant than before. In the Mezzogiorno the EIB in particular financed the creation of new industrial poles which had to improve the quality of the life of citizens: however a lot of new industries became inefficient and obsolete after 1973 because they were built following the hypothesis of an increase of oil price of 20 per cent max., while this last was of 400 per cent in a year. Besides, face to the devaluation of European currencies which started in 1974, the EIB decided to lend money only in strong currencies (as Swiss Franc, German Mark, etc.) and this got more difficult for Italian enterprises to reimburse the loans<sup>4</sup>. Even if this means that a part of the development of the less developed regions of

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<sup>4</sup> The end of the "gold exchange standard" on 15 August 1971 and the first oil crisis in 1973 obliged all financial institutions to change their strategies in order to guarantee the real value of their loans: the financial

Europe was financed by making them pay the cost of their monetary weakness, it is important to note that all EEC members knew that EIB's loans in strong currencies were offered at rates "impossible" to obtain from other financial institutions (especially for borrowers from countries with weaker currencies). For a country with a weak internal market and which had to be competitive on the world market, the cost the state was exposed to was regarded as less important than the overall advantages derived from the implementation of project financed by the EIB and the possibility of using strong currencies at favourable rates for the import of raw materials. So the Italian country, which guaranteed the loans, had to pay for them and this means that after 1973 the EIB's real help was strongly inferior to those showed by reports and statistics. In any case the EIB's activity advantaged the Italian economy, but paradoxically it was positive moreover for the Northern Italy which benefited of the new infrastructures and also owned enterprises more flexible face to the crisis, in particular the small-medium ones<sup>5</sup>.

The range of instruments that the EIB used to achieve its purposes was progressively expanded (currently, the Bank uses many tools as loans and guarantees, technical assistance, venture capital) and promotes a wide range of interventions). Italy was, over the period 1958-1972, the largest borrower of the EIB. The amount of loans in real values grew until 1984 and after they showed a contraction. On average, the share of funds granted to Italy over total EIB financing was, until the early seventies, 60 per cent of the total, with peaks in some cases exceeding 80 per cent for some particular sectors. Since the mid-1980s, the weight of loans granted to Italy was reduced following the entry into EEC of new countries as Greece, Spain and Portugal which had some regions in precarious social and economic conditions.

Until the mid-seventies the EIB loans financed mainly infrastructures and the development of large industrial plants. Since the early 1980s, there was a rise of loans toward initiatives aimed at financing small and medium enterprises through loans intermediated by banks, with a parallel

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institutions in fact had to face the rising inflation and exchange rate fluctuations. New serious risks progressively added to the "traditional" risk related to the failure of the debtors (which obviously increases during the negative economic trend). If a currency strongly devaluated a loans which was regularly reimbursed with all interests could become, converted in the *European unit*, in a partial loss. If the inflation was not correctly foreseen and the interest rate was fixed, a high rate of inflation could provoke a relevant reduction of the "real" capital and interest received at the end of the loans. Italy (as France, Ireland and the UK) owned one of the weakest currency and so quickly left the "monetary snake". So the EIB changed the strategy that it had been applying to the loans granted in those countries. Thus, to avoid the risks of devaluation, the EIB used strong and stable currencies such as the Deutsch Mark or the Swiss Franc, which protected the real value of its loans.

<sup>5</sup> Italy had to guarantee the projects and was liable for exchange risk losses. Italian laws 876/73 (concerning the Mezzogiorno) and 956/76 (regarding central and northern Italy) regulated the funding mechanisms for loans granted by the EIB: the borrower (Italy) chose the [strong and stable] currency to be used for the loan and was itself liable for the cost of covering the exchange risk. Italy therefore was paying to guarantee the granting of EIB loans to its project and was providing assistance to the companies concerned.

decrease of direct loans to industry. Lending to SMEs companies has totally accounted for 34.1 percent of loans in the South and 38.3 percent in the North Central regions (38.8 per cent in Italy). The weight of direct loans to industry on total loans in Italy has been only 6 percent between 1994 and 2007, but it was 45.8 per cent between 1958 and 1972 and 15.9 per cent over the whole period compared with a share global loans for small and medium enterprises of 21.5 percent. The ratio of loans to total infrastructure is equal to 61.2 percent with reference to the entire period and to 52.6 percent between 1958 and 1972. In particular, funding for the energy sector accounted for 20.6 per cent (6.8 per cent in the first years), the shares of loans to transport and telecommunications amounted respectively to 14.7 and 12.1 percent (29.1 and 10.7 percent between 1958 and 1972). For projects of water supply was allocated 6.6 percent of total loans (5.2 percent in the first fifteen years). For the Mezzogiorno it is possible to make an attempt of evaluating the contribution of EIB to the growth of per capita GDP in those provinces where EIB granted its loans. From 1952 to 1970 their per capita GDP tripled: EIB intervention probably contributed to a share of 6.4 per cent of the total growth (that is 14 percentage points of growth over a total growth of 215 percentage points).

The financing activities in the South was done entirely through the Cassa per il Mezzogiorno until the early seventies. Not all the demands forwarded by the Cassa were subsequently financed. The EIB made a selection because it obviously wanted to allocate its funds in the best way. It is also evident that, by the selection of projects, the EIB tried to influence the policy for the development of the Mezzogiorno. The EIB “simply tried” because Italian governments sometimes financed with other funds the projects that EIB refused. Furthermore, it was very difficult for the EIB to resist at the political pressures of the governments of the EEC members which asked for the financing of “national interest projects”, so some projects were financed and, in the following years, the EIB had to communicate that some projects did not have reached their targets. In any case, as the EIB had the obligation to maintain in pair its balance, a particular clause obliged the EEC country whose enterprises benefited of the financing to guarantee the reimbursement of the capital and the interest. So the real problem was the Italian citizens who had to pay for the failure of worse projects, that is the failure of the idea of the fathers of the EEC: they in fact wanted to oblige each country to be attentive at the behaviour and strategic choices of people and enterprises involving in the projects which were financed; when there was a serious mistake, the country paid.

**Very important:**

When EIB only financed 50 per cent, it obliged the country to finance an important part of the project: so the country had to prepare a project to develop. Besides, it allowed other banks to participate at the financing of the project: so EIB was not in competition with them but it collaborated with them. Finally, to avoid an impact of EIB's activity on the exchange rates between



EEC member countries, the EIB's loans were paid in all EEC currency excluding the currency of the country where the project was developed.

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