

46420

ADVANCE STUDY PAPER

RAC READING ROOM

19990121 042

~~"DTIC USERS ONLY"~~

NATO

Problems and Prospects

May 7-8, 1964

THE CENTER FOR STRATEGIC STUDIES
GEORGETOWN UNIVERSITY

WASHINGTON, D. C.



Reproduced From
Best Available Copy

J End 46420

**NATO AND
THE ECONOMIC PROBLEMS
OF THE WESTERN ALLIANCE**

by

Lawrence B. Krause

The Brookings Institution

Advance Study Paper No. 11

APRIL 1964

~~"DTIC USERS ONLY"~~

NOTE

This is a preliminary working paper only, and may not be quoted or cited without the written permission of the Center for Strategic Studies, Georgetown University.

The opinions expressed in this paper are those of the author and do not purport to represent the opinions of the trustees, officers, or other staff members of The Brookings Institution.

THE CENTER FOR STRATEGIC STUDIES

Georgetown University
Washington, D.C.

Authors of Advance Study Papers

NATO—PROBLEMS AND PROSPECTS

*Conference of The Center for Strategic Studies,
Georgetown University, 7-8 May 1964*

Maurice Allais

Professor
Institut de Statistique de
l'Université de Paris

André Beaufre

Général, French Army (Ret.)
Director, Institut Français
d'Études Stratégiques, Paris

Kurt Birrenbach

Foreign Affairs
Committee of the Bundestag
German Federal Republic

Karl Brandt

Director
Food Research Institute
Stanford University

Hendrik Brugmans

Rector
College of Europe
Bruges, Belgium

W. Randolph Burgess

United States Permanent
Representative to NATO,
1957-1961

Milorad Drachkovitch

Senior Staff Member
Hoover Institution on
War, Revolution, and Peace

John W. Holmes

President
Canadian Institute of
International Affairs

Henry A. Kissinger

Professor
Center for International Affairs
Harvard University

Klaus Knorr

Director, Center of
International Studies
Princeton University

Lawrence B. Krause

Senior Staff
The Brookings Institution

James E. Moore

General, USA (Ret.)
Chief of Staff SHAPE, 1959-1963
Presently with Research Analysis
Corporation

Hans J. Morgenthau

Director, Center for the Study
of American Foreign Policy
University of Chicago

Philip E. Mosely

Director
European Institute
Columbia University

Friedrich Ruge

Vice Admiral, FRG (Ret.)
Former Chief of the German Navy
Presently at University of Tübingen

Sir John Slessor

Marshal of the Royal Air Force
Vice President, Institute of
Strategic Studies, London

Robert Strausz-Hupé

Director, Foreign Policy
Research Institute
University of Pennsylvania

Pierre Uri

Director of Studies
Atlantic Institute
Paris

These advance study papers will form the basis of the two-day discussion and debate. The papers will not be presented formally at the conference, but will be available prior to the conference through the Center. After the conference, revised and updated papers, with the conference discussion, will be published in book form.

NATO AND THE ECONOMIC PROBLEMS OF THE WESTERN ALLIANCE

Introduction

The need for collective defense that gave rise to NATO in order to face the threat of Soviet expansionism in Europe has implications beyond the domain of military policy. A unified military posture demands coordinated diplomatic positions on matters not military in the narrow sense. Furthermore, international diplomacy is related in a very intimate way with international economic problems. It is thus from derived importance that international economic problems have a bearing on NATO.

It is worthwhile noting that intimate economic relations among the NATO countries is not a goal in itself. The *economic* gains from harmonious economic relations among the NATO partners are no different from those that can be obtained from similar relations with Japan, Australia, Sweden, Switzerland, or indeed South Africa, the Soviet Union, Communist China, or Cuba. The fact that we draw diplomatic and military distinctions between these countries that carry over into economic policy should not hide the realization that no *economic* end is being served by these distinctions. Neither should we forget that when economic disputes occur among NATO countries, no special importance should be attached to them unless they have diplomatic or military implications.

The desire to keep economic relations distinct from diplomatic and military ties of the NATO countries has been recognized, and a report to that effect was issued in 1956. Not only is there no great

advantage to combining economic functions within NATO — there would be an economic and political loss in discriminating against all non-NATO countries, many of whom are close friends to the alliance. But we must return to the reality that economic relations do have a bearing on our military position and cannot be excluded in an examination of NATO unity.

Changes in the Western Alliance

One need not be very observant of world affairs to recognize that the Western alliance has changed and is in the process of changing further. In military matters, diversity has replaced what once appeared to be a monolithic structure. Serious questions have been raised by the French as to the effectiveness of collective defense for the security of individual countries.¹ Indeed the Cyprus issue has made two NATO countries wonder whether the most immediate military threat to them is to be found outside or within the alliance. Diplomatic changes have also been very marked. Recently, France has extended recognition to the Communist Government of China and thereby withdrawn recognition of Nationalist China without prior consultation in NATO.² While diversity on diplomatic questions has always been greater than on military issues within NATO, open differences on crucial East-West questions have been avoided in the past. The changes on the economic front have been just as great, although they do not appear as spectacular because they evolved more slowly over time. These changes have many implications for the unity of the alliance. Change by itself is neither good nor bad, but must be evaluated as to consequences. In economic matters as well as military and diplomatic ones, the changes have some elements that can be generally welcomed and others that seem less desirable.

The changes that have occurred can be traced to two sets of forces,

one external and one internal. The Western alliance, particularly in its military and diplomatic aspects, is primarily a defensive alliance that owes its existence to the threat of Communist — mainly Soviet — power. The fact that this external threat is or appears to be less severe today than it was in years past has reduced the need for the alliance and, as a result, the individual members feel they can indulge themselves in the luxury of diversity. Another source of change has been the marked revision in the relative economic strengths of the member countries of the alliance. Europe has experienced what is surely the most remarkable period of sustained economic growth in the history of mature capitalist countries. The standard of living within this area has increased to the point where they can carry a much larger share of the economic burdens of the alliance and rightly insist on a greater role in leading it. This change is not due to the fact that the United States has stagnated while Europe has advanced. To the contrary, the United States since the war has achieved better than average growth by its own historical standard. The difference has been solely the result of the exceptional economic dynamism in Europe which has allowed them to narrow the gap with the United States.

The evaluation of the military and diplomatic as well as the economic changes requires detailed study individually and this has not been attempted. The first impression that one gets from viewing the military situation is that it is hard to recognize any advantages in diversity, but easy to see potential dangers from the weakening of NATO unity. A careful and critical re-examination of strategic planning is desirable, and to the degree that this would not have occurred otherwise, the crisis within NATO has improved our defense. However, the weakening of NATO may have seriously undermined our military posture if it has made us appear less resolute in the face of Communist pressure or if it has increased the chances of nuclear accidents.

The possible advantages from diversity of diplomatic positions among the members of the alliance are easier to contemplate. It is frequently difficult for a single country to amend a diplomatic position once taken, and this may be particularly true for the United States. But diplomatic positions should be changed if the conditions upon which they were predicated no longer exist. When the path to an improved position is embarked upon by a friendly country, it is then possible for other countries to follow without giving the appearance of a retreat in the face of hostile pressure. This allows the alliance to be flexible without being irresolute. There are real dangers to diversity, however. When an important member of the alliance takes a new diplomatic step, it will necessarily weaken the old position adopted by the alliance. If a great deal of power is required to reach the new position and the member making the diplomatic overture does not possess this power, then the alliance position may be weakened without a realistic alternative being presented in its place.

In contrast to military and diplomatic changes, the new economic situation would appear to have only desirable consequences. The general dictum that when one country advances economically, all countries gain would seem to apply in this case. Indeed, the economic advancement of Europe is an important goal of U.S. policy and has been due in some measure to Marshall Plan aid extended by the United States. The most important single outcome of the economic resurgence of Europe has been the creation of the European Economic Community (or Common Market) which has had the unswerving support of Washington. Nevertheless, our applause must be tempered with some caution for even a desirable change can frequently be improved upon and there are many features of the European Common Market that are less than optimal.

European Economic Community and the Unity of the West

The approval of the Treaties of Rome by the parliaments of West Germany, the Netherlands, Belgium, Italy, Luxembourg, and France can properly be regarded as a major victory for a group of European statesmen who were not only visionary thinkers but also practical politicians. This major step toward turning the idea of European unity into reality reflected past successes such as the European Coal and Steel Community and also past defeats such as the still-born European Defense Community. Yet the form of the EEC as specified in the Rome Treaty was not considered to be an ideal, but merely a beginning toward economic and political integration of all of Western Europe. It is clearly this larger purpose which was the basis for U.S. support.³

The motivations that can be identified as being of some importance in the creation of the Common Market are in the main compatible with and in part identical to the goals of NATO. Of primary importance was the desire to prevent a reoccurrence of conflicts in Continental Europe. By immersing West Germany and her neighbors in an all-embracing institutional structure, it was hoped that independent aggressive action by a single country would no longer be possible. Certainly the cold war gave a sense of urgency to this desire since it became clear that West Germany would not only have to be rearmed, but would soon have the strongest conventional forces in Western Europe. Furthermore, it was hoped that the Common Market could help alleviate some of the problem caused by the East-West division of Germany. While the major goal of reunification could not be served -- and might even be hindered -- by the formation of the EEC, the Common Market could ease some of the frustration of division by giving the Germans an achievable goal in the form of a unified Europe. This would provide an outlet for German nationalism without exacerbating the cold war struggle. Economic motives also played a part in kindling enthusiasm for the Common Market.

It was thought that by combining the separate markets of the member countries into one gigantic market, substantial economic benefits could be obtained. All of these motives were in keeping with United States interests and with the U.S. view of an integrated Europe.

There was a further motive involved in the formation of the EEC that might be called the desire for independence and self-respect. It was all too apparent that only two real powers survived the Second World War, the United States and the USSR. In the face of this power, the individual European countries could make little impact on the world scene. The reduced diplomatic role of Europe was graphically illustrated during the Suez Crisis when the United States refused to support the steps taken by France and Great Britain. A follower role is never very satisfying, and for countries previously at the center of world affairs, the role may be thought to be intolerable. While there was no hope for any single European country ever reaching superpower status, enough economic recovery and advancement had occurred in Europe by the mid-1950's to indicate that an amalgamation of European nations would achieve this position if true political unity could be developed. The independent or third force idea has subsequently been most closely associated with President de Gaulle, but he is not the only Frenchman who feels this way, nor is France the only country in Europe where nationalism survives.⁴ Jean Monnet avers that unity in Europe will not develop into a nineteenth-century type superstate and that the Common Market was developed in order to avoid nationalism.⁵ But political unity in Europe will create power and how that power is used will depend on the desires of those political leaders able to direct it. President de Gaulle sees a unified Europe as a power base for spreading European — mainly French — influence throughout the world.

From the point of view of the United States, European independence has two faces. On the one hand, independence means that Europe will shoulder a much larger share of the costs of defense, will provide

greater resources for the "have-not" nations, and will in general take on more of the responsibilities of the free world. On the other hand, independence also means a rejection of U.S. leadership and all that this implies.

The EEC and the Cleavage of Europe

The conflict of interest between the EEC and the United States stemming from the creation of the Common Market was overshadowed in the first instance by the cleavage within Europe itself among member and nonmember countries. The EEC included only six European countries, not because the members wanted to keep the club exclusive, but because the other European nations did not wish to join. Great Britain showed indifference to the customs union idea and great hostility to institutional arrangements which impinged upon its national sovereignty. The decision by Britain to stay out precluded Norway and Denmark from seriously considering joining themselves. The European neutrals — Sweden, Switzerland, and Austria — felt their military status prevented them from participation. For the other European countries, either the weakness of their economies or their peculiar political position (or both) inhibited them from seeking membership. However, the Six recognized that the nonmember countries of Europe might someday change their minds and they included a provision in the Treaty of Rome for accepting new members.

When it became obvious that the EEC was going to become a reality, the implications of its existence for intra-European trade began to attract attention within the OEEC. In February 1957, the British Government unfolded a plan to prevent the trade split within Europe through the creation of a free trade area in which the EEC would be one member. The proposal accommodated all of Britain's needs by closing the trading breach without sacrificing Commonwealth preferences or the British agricultural system, and without the sacrifice of national sover-

eignty to a supranational organization. In this form, the proposal did not generate much support, either within the EEC or from the United States. The United States saw the free trade area as a means of spreading discrimination against U.S. exports and also as a means of weakening the movement toward political unity in Europe, both of which it opposed.

The EFTA Solution

Even though the free trade area proposal was modified during the negotiations to overcome some of its weaknesses, the basic objections of the EEC remained and the negotiations failed. The failure, unlike subsequent ones, was marked by a lack of very strong feeling. The nonmember countries which are most dependent on the EEC, Austria and Switzerland, accepted the failure almost with indifference. Nevertheless, a conference was called at Stockholm and eventually a rival trade organization was born, the European Free Trade Association. The purposes of EFTA were threefold: to provide an economic offset to the member countries for the loss that they might suffer from not being a member of the Common Market, to demonstrate the technical feasibility of the free trade area technique, and to provide a bargaining counterweight to the EEC. Actually, the bargaining power provided by EFTA is usable only in multilateral trade negotiations or in negotiating a wider free trade area, but not in negotiating for membership in the EEC as Britain found out subsequently.

Both the EEC and EFTA have proven to be successful and, on some grounds, more successful than could have been expected. For the Common Market, economic gains have been outstanding. Intra-community trade has expanded at a fantastic rate which has contributed to and resulted from the rapid pace of economic growth of the member countries. This has enabled the accelerated removal of the barriers to intra-community trade and the beginnings of a common agricultural policy.

The EFTA has also made substantial progress in reducing trade barriers and increasing trade among its members, but, of course, has not resulted in the complete reorientation of the trade of those member countries dependent on the EEC. In addition, EFTA has scored an important diplomatic victory by negotiating the association of Finland to its group and thereby re-establishing the economic unity of Scandinavia, while at the same time staying clear of cold war problems.

The success of the two groups, however, made the economic cleavage of Europe more ominous. The more they succeeded in directing the trade of member countries toward other member countries, the greater became the welfare loss of trade diversion. Furthermore, the possibility of an aggressive trade war within Europe that might accompany a cessation of economic expansion was enhanced. Since NATO countries are found in both groups, the military and diplomatic consequences of overt economic hostility had to be recognized. Finding a bridge between the Six and the Seven became an important goal.

British Membership in the EEC

At this point Great Britain once again took the initiative. Having faced up to the fact that only a major proposal could succeed, Britain took the bold step and applied for membership in the EEC. This move was quickly followed by applications for membership or association from all the EFTA countries (except Portugal and Finland) plus other European countries then affiliated with neither group. It was clear from the start that the negotiations would be very difficult. Britain had trade commitments to the other EFTA countries and to the Commonwealth which would be undermined by membership in the EEC unless special provision was made for them. Furthermore, Britain enjoyed a special relationship to the United States, particularly with respect to the shar-

ing of nuclear secrets. If the political side of the Common Market was to have meaning, then this special relationship could not remain unaltered. The negotiations became protracted with both sides bargaining very vigorously. Tentative settlements were reached on a number of technical points, usually following a British concession, but many difficult problems remained to be decided when the negotiations were abruptly halted in January 1963 by the unilateral action of President de Gaulle.

The De Gaulle Veto of Britain

It is difficult to know all the factors that went into de Gaulle's decision but certainly the issue of nuclear armaments played a part. When the United States canceled the Skybolt missile project, a crisis developed for British strategic planning as they were counting upon this missile as part of their nuclear weapons delivery system. The choice made by Prime Minister Macmillan at Nassau was to accept continued dependence upon the United States by agreeing to rely on polaris-type missiles. President de Gaulle interpreted this move as a choice by Britain for collaboration with the United States at the expense of Europe and was reported to be personally angered because he thought Macmillan had agreed to consider a "détente nucléaire" with France.⁶

The ending of the Brussels negotiations led to a great deal of bitterness among the participants and most of it was directed against France. Many observers in Britain felt that the talks were on the road to if not on the verge of success. They interpreted the de Gaulle veto to mean that France simply did not want Britain as part of the EEC and had been bargaining in bad faith. Certainly the Conservatives lost the election issue on which they hoped to be retained in office. Within the EEC, anger against France was directed especially toward the method by which the talks were ended. Unilateral action — particularly a pro-

nouncement in such a form as a press conference — struck at the very heart of the Community spirit and therefore robbed the Common Market of the necessity for agreement. Without the "will to agree," all the basic weaknesses of the institutional procedures whereby decisions are made in the EEC came to the fore. A crisis of confidence resulted and is still having its effect on the operations of the Community.

The breakdown of the Brussels talks can be evaluated in terms of its possible consequences on economic policy of the European countries and its effect on relations among the Atlantic countries and the free world in general. On the surface, calm has returned to the diplomatic scene. The British economy survived the shock and expanded at a rapid pace during 1963 without excessive pressures from their balance of payments. While discussion of joining the EEC has ended in Britain, the public reaction to the failure was not so great as to prevent a subsequent attempt at entry after a reasonable time lapse. Official British statements have indicated that they have not turned their back on European unity, although future initiatives for joining the EEC will be much more cautious. Periodic discussions between the EEC and Britain have continued under the aegis of the Western European Union (WEU) which has kept a channel of communications open, though nothing of substance has resulted as yet. Even in Brussels a sense of normalcy reigns, but there certainly has not been a return to the *status quo ante*. Progress has been made on some of the problems facing the Community by working out carefully balanced programs to meet some of the needs of all of the countries. The "synchronization" approach, however, is slow and cumbersome and many important issues have yet to be dealt with. For the United States, the rejection of Britain by the EEC was a real disappointment; however, no obvious shifts in U.S. policy resulted from it.

Insight as to the importance of these recent developments can be gained by examining the major economic policy areas individually in

order to relate them in general to the problem of the unity of the West. There are five areas of economic policy that can be indicated as of importance:

- 1) trade of industrial products,
- 2) trade of temperate agricultural products,
- 3) international monetary mechanism,
- 4) international transmission of inflation and recessions, and
- 5) the relations of developed countries to less developed countries.

Trade of Industrial Products

Much progress has been made since the war in liberalizing restrictions on the flow of industrial products among the developed countries of the West. Quotas and dollar discriminations that were so much a part of the early postwar scene have all but disappeared. Tariffs have been reduced substantially through tariff bargaining in GATT. However, in a competitive world, even moderate tariffs can be quite protective. The creation of the EEC and EFTA also raised the importance of the tariff barrier to trade since the tariffs of these trading groups are levied only against nonmembers, while trade amongst the members themselves are (or will be) free of restraints. Despite the need for further tariff reductions, the traditional mechanism for bringing this about, item-by-item bargaining, had reached the limit of its usefulness. The United States was particularly constrained in its ability to carry on fruitful tariff negotiations because of the limitations imposed on it by the Reciprocal Trade Agreements legislation under which it operated and especially by the "no injury" philosophy that it contained.

Recognizing the situation, President Kennedy proposed and the U.S. Congress accepted a new approach to tariff bargaining contained in the Trade Expansion Act of 1962. Under the new act, the United States can bargain for large tariff reductions on whole groups of products, the linear method, and the only item negotiations needed would be over

those products whose tariffs were not to be reduced. This legislation was passed primarily as a tool for negotiating with the Common Market, since at the time of its enactment it was generally believed in the United States that the EFTA countries would in the main be absorbed within the EEC. However, the most-favored-nations principle was to be maintained, so all GATT countries would benefit from any tariff reductions negotiated and therefore would be urged to take part in the negotiations themselves as in the past. Even the method of tariff bargaining was patterned after that followed so successfully by the EEC in pursuing their internal tariff reductions.

When de Gaulle vetoed British entry into the EEC, the Trade Expansion Act became much more important. While it could not be used to heal the breach between the Six and the Seven, it could lead to substantial lowering of tariffs all around which would ease much of the pain of the separation. It also gave the EEC an opportunity to prove what they had long proclaimed, namely that they were liberal-minded with respect to trade with nonmembers. Being the largest trading bloc in the world — greater even than the United States — the importance of the commercial policy of the EEC for the prosperity of all countries is second to none.

The need for a new round of tariff negotiations was recognized by all of the GATT countries and in May 1963, a resolution was adopted at the GATT Ministerial Meeting calling for preparations to be started for such a negotiation, named the Kennedy Round, to be held the following year (1964). Since that time, very little has been accomplished by way of agreeing to rules which would ensure the success of the Kennedy Round. A major controversy has involved the rules to be used for cutting industrial tariffs. While the Common Market had found the linear method suitable for cutting their internal tariffs to zero, they had reservations concerning the fairness of the method for use externally when a

reduction to zero was not contemplated. The U.S. tariff is highly differentiated with many high and many low rates, and a 50 per cent cut of all rates would still leave some tariffs quite high. The EEC external tariff in contrast has little dispersion and a 50 per cent cut would bring almost all of its rates to a moderate level which they feared would not be protective enough to induce further rounds of tariff negotiations. Thus, even though the average tariff level of the United States and the EEC is identical, an equal cut was feared by the EEC because some U.S. tariffs would remain high and they would have no bargaining power to get them reduced.

Attempts to find a solution to the disparity problem have been complicated because a number of technical details are involved and because of the internal politics of the EEC itself. The characteristics of a good solution would be one that all parties felt was equitable, that did not unduly reduce the over-all level of the tariff reduction, that did not so complicate the negotiating procedure as to be unworkable, and that did not work a hardship on innocent third countries. Such a formula is conceivable and one has already been worked out. All that remains is the agreement to accept it. Solving the disparity problem will not insure the success of the Kennedy Round, but failure to reach an agreement will certainly cause a failure.

If the negotiations get scuttled on this or some other technical issue, it will only be because there is no will for success. It is not clear that all countries do want the Kennedy Round to succeed. One gets the view that France is very reluctant and will agree only if forced to by her Common Market partners. If this is true, then one must contemplate what failure might mean. The fragmentation of the West into trading blocs would take on added meaning in the event of a failure of the Kennedy Round. It would sharpen the split, partly because of the disappointment of expectations and partly because of the drift toward protectionism

that might well occur in the absence of a major step in the other direction. The drift toward protectionism between rounds of tariff reductions has appeared in the past and is going on at present.⁷ It is almost certain that the disappointment would sour diplomatic relations and possibly military relations among the NATO members.

The form in which the bitterness might be expressed could be an attempt to isolate the country or countries whose policies caused the failure. If the country was France, then she might react by becoming more obstructionist and less committed to NATO. Alternatively it could force the United States to reconsider its policy of nondiscrimination in international trade and lead to the return to the conditional form of the most-favored-nations principle. The hint of such a suggestion was contained in a report by the Joint Economic Committee of Congress.⁸ In any event, a failure of the Kennedy Round would shake the NATO alliance just when it might need strengthening.

Trade in Temperate Agricultural Products

International trade in temperate agricultural products has not benefited from the liberalization measures taken since the war. Codes of conduct long since deemed inappropriate for industrial products are still permitted in agriculture. Many agricultural products are still state traded (even in free enterprise economies), they are subject to import licensing and quotas, they are besieged by discriminatory health and mixing regulations, and their export is often subsidized. Nevertheless, the volume of agricultural products entering international trade has increased.

The trading situation merely reflects the position of the agricultural sector in the domestic economies of the Western countries. Methods of agricultural production have been improved to the point where an output revolution has occurred. These increases in output have been achieved

with a labor supply that has been constantly shrinking. Despite these trends, economic rewards to agricultural pursuits have not kept pace with those in nonagricultural work. Under these circumstances practically all governments have policies to supplement farm incomes. These policies have led to a great deal of governmental involvement in the business of agriculture and the interference in international trade is just another manifestation of this trend.

Before the advent of the EEC, agricultural protectionism in Europe was kept within reasonable limits. While few countries showed much restraint in stimulating increases in output of particular crops up to the point of self-sufficiency, most countries refused to continue artificial stimulants beyond this point. Further output could only be disposed of in foreign markets with export subsidies which would cause a substantial drain on their treasuries. While these policies closed many markets to the efficient world exporters, many other traditional markets remained open to them and they grew in size. The adoption of the Common Agricultural Policy by the EEC, however, threatened the market of two of the most important of the traditional importers, the Netherlands and West Germany. What was needed was an agricultural policy for the group that was *more* responsible than any of the countries had followed individually (except the Netherlands) because the power of the EEC to create mischief in world agricultural markets was greater than the sum of the powers of the countries separately. Instead the EEC adopted a policy of complete agricultural protectionism that in theory and possibly in practice can isolate the EEC markets entirely from international competitive forces.⁹

The first major clash over the new EEC policies occurred in 1963 in the now famous chicken war. The United States had developed a lucrative and expanding export trade in frozen poultry to West Germany. The Common Agricultural Policy when applied to poultry tripled the tariff

on American chickens entering Germany and proved to be an insuperable barrier. The United States felt that the increase in tariff was unjustified, particularly in view of an explicit agreement to the contrary. The United States protested in vain and finally took steps within GATT to seek redress, which was finally obtained. The controversy raised tempers beyond what the importance of the product would justify because it was fought over an issue of principle and because of what the EEC action portended for other agricultural products.

The United States and other agricultural exporting countries came to the belief that agriculture could no longer take a back seat in international negotiations. The interests of agricultural producers are being threatened and they are insisting that agriculture be treated on the same basis as industrial products in the Kennedy Round.

Agricultural trade is important to all the Western countries (despite the fact that many of them are highly industrialized with small farm populations, in percentage terms) because of the magnified political importance of this group. Even the figure of President de Gaulle is not enough to calm the French peasants when they are angry over economic issues. This makes international negotiating very difficult because domestic political considerations limit the area of maneuver for all participants. Yet as difficult as the negotiations may be, the problem must be faced because there is probably no other economic issue that could poison the diplomatic relations of the Western countries more quickly than a wrangle over agriculture.

International Monetary Mechanism

The experience of currency markets in the 1930's was not a happy one; values were very unstable due to private speculative capital movements and attempts by governments to alleviate domestic unemployment through competitive depreciations. Recognizing that chaos in currency

markets inhibits international trade and investment, the postwar monetary mechanism was designed to maintain fixed exchange rates to the greatest degree possible. The present system, the gold exchange standard, was patterned after the gold standard of the late 1920's and early 1930's but with the addition of the International Monetary Fund to aid in adjustment problems and as it developed, with a greater role for key currencies, primarily the U.S. dollar.

It was hoped that the system would combine the advantages of the stability of the gold standard while avoiding its disadvantages. Domestic money supplies were not to be tied to gold and occasional changes in currency values were to be allowed to correct fundamental disequilibria in the balance of payments. The system seemed to work quite adequately in the early postwar years as alterations in the exchange rates of developed countries were infrequent and the U.S. dollar was able to supplement the small increases in new gold for official reserves. Before 1958, the U.S. dollar was really the only international currency since all others were technically inconvertible and the dollar was as fully acceptable or was considered preferable to gold.¹⁰ After the major European currencies were returned to convertibility, however, the situation changed. Not only did European currencies become more desirable, the U.S. dollar became less so because of the very large balance-of-payments deficit that the U.S. developed beginning in 1958.

With the changing status of the dollar, questions began to be raised as to the efficacy of the gold exchange standard itself.¹¹ It was recalled that an essentially similar system collapsed in 1933 and our current system is not free of defects. Critics of the gold exchange standard claim that it combines the worst features of a gold and non-gold standard. It does not contain a quick acting adjustment mechanism, does not provide enough liquidity to allow slow adjustments, and permits exchange rate changes only as an act of desperation leading to harmful speculative capital movements.

As the continued U.S. balance-of-payments deficit exposed the weaknesses of the system, attempts were made to strengthen it by improving the liquidity-creating mechanism. The resources of the International Monetary Fund were increased and special standby borrowing rights were created for it. A number of bilateral agreements were made between the United States and other developed countries to shore up the key currency status of the dollar. New borrowing instruments were created so as to enable the U.S. to limit its short term liabilities without a loss of gold. All of these measures, however, are of the nature of a rescue operation and have not added much basic strength to the system itself.

There is probably no other economic issue on which the basic interests of the Western countries correspond so closely as with the desire to improve the international monetary mechanism. The International Monetary Fund is studying methods to improve the system as is the Committee of Ten.¹² The interests of the countries while close are not identical. If agreement cannot be reached on this issue, then it is a very bad omen for the unity of the West. On the other hand, the spirit of cooperation that could be kindled from a successful attack on this problem could carry over into other areas.

The International Transmission of Business Fluctuations

During the Great Depression, all countries learned the meaning of common destiny as economic distress was spread from one country to the next through the network of international trade and capital movements. After the war, most governments became committed to preventing large-scale unemployment and Keynesian economic policies offered them the instruments to bring this about. However, Keynesian economics does not provide a means of insulating domestic economies from changes in foreign business conditions. In the postwar period, inflations rather than depressions have been the major worry. If a rapid inflation begins

in one country, it will quickly spread to other countries. To resist the inflation requires a country to allow its resources to be shifted abroad through involuntary foreign investments which it may be unwilling to do. Thus, the problem is still worthy of consideration.

It is certain that the science of economics will not develop in the near future to the point where economic growth can always be prevented from leading to inflation or economic constraint from bringing unwanted unemployment. Moreover, even if economics did always give the right answer, it is uncertain that the political will to take unpopular policies will be present. It is therefore of international concern that some countries will be going into excess in one direction or another. This concern can be harnessed for positive good if it can lead to better economic analysis and if it could bolster the will of governments to take proper actions. Some steps have been taken in this direction. In the framework of the OEEC and its successor, the OECD, the economic situations of the member countries are examined and governmental policies reviewed. This confrontation procedure imposes no obligations on countries deemed to be following improper policies, but the confrontation itself may be beneficial.

This problem does not present a critical issue for the West since countries can continue to adjust to the excesses of other countries as they have in the past. It is an area, however, where great benefits could be obtained if international cooperation ever developed to the point of allowing meaningful consultations. This is a field of preventive medicine which promises reductions in balance-of-payments worries and help in achieving sustained economic growth if perfected.

Relations of Developed to the Less Developed Countries

The NATO alliance is directed at the East-West controversy, but another area of difficulty may have equally upsetting implications for

the political stability of the world, the so-called North-South controversy. Within recent years the less developed countries have found that a slow attack on poverty is today not politically acceptable at home and therefore they are impatient to take rapid steps up the economic ladder. This they recognize cannot be done without foreign help. From the point of view of the "have-not" nations, the United States looks much like the Soviet Union, and West Germany like East Germany; they are all rich countries not doing very much for the poor ones. Discontent in these countries can lead to internal revolutions or aggressive external actions. These conflagrations cannot be easily contained and quickly take on cold war characteristics as witnessed in the Congo, Cuba, Lebanon, and elsewhere. Issues involving the LDC's have also frequently led to squabbles among the advanced Western countries themselves.

Primarily what is involved is the desire by the LDC's for better conditions for their trade of goods and services, greater and more liberal grants of aid and loans, and some LDC's desire larger receipts of foreign investments and technical aid. The United Nations Conference on Trade and Aid convened in April 1964 for the purpose of giving the LDC's a forum for expressing their desires in the hope that joint expression would bring concessions from the richer countries. It is apparent that there is a difference of view among the Western advanced countries on how help should be extended to the LDC's. On the one hand there is the method typified by the association of certain African countries to the EEC. Through this agreement grants and loans are extended and preferential treatment is given to the products of the associated LDC's when entering the Common Market. In contrast is the method of extending general aid without trying to tie the recipient country to any special arrangement to the donor country. This latter approach is preferred by the United States, balance of payments permitting. These different approaches have their counterpart in suggestions made at the U.N. Conference: one plan would extend preferential trading opportunities in ad-

vanced countries to the LDC's and they would be differentiated by degree of poverty; and the other plan would call for the general reduction of tariffs by the advanced countries on products of importance to LDC's without seeking compensation from the LDC's.

There is no need to coordinate Western policy to the point where only identical terms are being offered the LDC's and a substantial loss might be involved in doing this. It is the diversity of the West combined with competition for the markets of the LDC's that makes the West a much better commercial area for the LDC's than do the Communists. Competition insures that the LDC's will get the most for their resources today and in the future. Yet there would be benefit from agreeing on a code of behavior that would discourage certain practices that could be quite detrimental to the Western alliance. Policies that further the economic development of one poor area at the expense of another poor area cause political animosity in the area being discriminated against. They may also bring resentment in the favored area if the arrangement yields commercial benefits to the advanced countries. Preferential trading arrangements are of this type and should be discouraged. Furthermore, any arrangement that ties an LDC in a special way to an advanced country, particularly if it mirrors a former colonial tie, may someday be the target of nationalist extremists in the LDC's as being a form of neo-imperialism. This may be an issue over which moderate leaders in the LDC's could be defeated to the detriment of the stability of the world. It would be naive to suggest that each developed country treat all under-developed countries equally, especially when traditional patterns have been established by reason of a common culture and the dictates of geography. However, it is only when traditional ties are not institutionalized in restrictive agreements that they can appear natural and desirable in the long run to the less developed countries.

Conclusion

Walter Hallstein has characterized NATO as an alliance that has demanded the highest degree of responsibility from one member and from the others the highest degree of trust.¹³ In order to convert this nonsustainable position into one of lasting benefit, methods must be found of sharing responsibility and spreading mutual trust. It is clearly in the area of military policy and particularly with respect to nuclear weapons that the best opportunity exists for doing this. However, the NATO countries have economic and nonmilitary diplomatic relations which also can play a role in the transformation. Many economic problems have been discussed where differences if compromised could aid in the process. If in contrast the economic problems create lasting differences, NATO is unlikely to be undermined, but it certainly will be hurt.

The NATO alliance has lasted for fifteen years, which is long as military alliances go, but is still too short to have stood the test of time. The NATO alliance could end and if its *raison d'être* were to cease, the demise would be the object of endless happiness. However, NATO could end as an effective alliance without a diminution of the Soviet threat. Under these circumstances any joy that was expressed in the West would be short lived. The seeds of NATO's destruction have already been sown. Mistrust and resentment are powerful poisons. Change must come and should be aided wherever possible.

Footnotes:

¹ Pierre M. Gallois, "The Raison d'Être of French Defense Policy," *International Affairs* (October 1963) and General Paul Stehlin, "The Evolution of Western Defense," *Foreign Affairs* (October 1963), pp. 70-83.

² Apparently there was also no consultation between Paris and Bonn on this issue. This makes one wonder what the meaning of the 1963 Franco-German Treaty may be when an issue of such great importance to both governments was not included within it.

³ Max Beloff, *The United States and the Unity of Europe* (Washington: The Brookings Institution, 1963).

⁴ In a speech before the National Press Club, March 23, 1964, Gaston Defferre, the Socialist candidate for president of France, criticized President de Gaulle for the way that he attempts to assert French independence but not for the substance of his moves.

⁵ Jean Monnet, "A Ferment of Change," *Journal of Common Market Studies*, Vol. 1, No. 3, pp. 203-11. Reprinted in *The Common Market: Progress and Controversy*, edited by Lawrence Krause.

⁶ Hal S. Nieburg, "Nuclear Exclusion and the Common Market," *Midwest Journal of Political Science*, VIII (February 1964), pp. 55-74.

⁷ Since the Dillon Round of negotiations we have seen the carpet and glass controversy, the chicken war, the movement toward agricultural protectionism in Great Britain as well as the EEC, and the raising of steel tariffs by the ECSC.

⁸ U.S. Congress, Joint Economic Committee, *The United States Balance of Payments*, 88th Congress, 2d Session, 1964.

⁹ Lawrence B. Krause, "The European Economic Community and American Agriculture," *Factors Affecting the United States Balance of Payments*, U.S. Congress, Joint Economic Committee, 87th Congress, 2d Session.

¹⁰ The British pound and the Swiss franc also played an international role but much reduced from that of the dollar.

¹¹ Robert Triffin, *Gold and the Dollar Crisis* (New Haven: Yale University Press, 1960).

¹² The United States, Canada, Belgium, the Netherlands, West Germany, France, Italy, the United Kingdom, Sweden, and Japan, with the cooperation of Switzerland.

¹³ Walter Hallstein, "NATO and the European Economic Community," *Orbis*, VI (January 1963), reprinted in *The Common Market: Progress and Controversy*, edited by Lawrence Krause.

The articles and books cited above form the author's bibliography in addition to the following:

Field H. Haviland, Jr., "Building an Atlantic Political Community," *International Organization*, XVII (Summer 1963).