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Security, Commercial and Monetary Policies

by Hugh Corbet, London*

This article discusses the frustrations both sides of the Atlantic regarding security, commercial and monetary policies. It suggests, however, that with the European Community, Japan and the USA all in difficulties together they might now possess the political will to arrest through negotiations a threatening return to discriminatory policies.

In the aftermath of the October war in the Middle East, as the industrial countries grapple with the energy "gap" they had not expected for another decade, there is not room any more to cavil at the inter-relationship between security, commercial and monetary policies, as happened when it was bluntly invoked by John Connally during his stewardship of the United States Treasury.

The emphasis then was on the inter-relationship — on a global plain — between commercial and monetary negotiations. These last have been pushed into the background by the enforced shortages, and the increased costs, of oil from Middle East sources.

Deep Frustrations

Precisely how adverse the implications of the energy crisis will be for world production, international trade and economic diplomacy remains to be seen¹. But with the European Community, Japan and the United States all in economic difficulty together, they might now possess the political will to arrest, through negotiations, an even more threatening return to the autarkic and discriminatory policies which characterised the 1930s. It is not wholly irrelevant therefore still to be trying to clarify the inter-relationships between the policies that must form the basis of a new international order.

George Shultz, as Mr Connally's successor, removed at the 1972 meeting of the International Monetary Fund (IMF) a major if somewhat incredible misunderstanding of the American view of the inter-relationship between commercial and monetary arrangements. He firmly asserted that

currency reforms did not have to wait on "specific trade negotiations" — not that the United States had ever meant any such thing. Much is left to be understood, though, about the inter-relationship, in spite of nodding acceptance everywhere nowadays of its existence.

The misunderstanding arose largely out of European suspicion of American motivations during the 1971 monetary crisis. And European suspicion of American motivations appears to have been just as rife during the 1973 military crisis². Without going into details, there are plainly deep frustrations on both sides of the Atlantic, resulting in part from inflated expectations about how soon the new Europe could assume in international affairs a role of leadership and responsibility commensurate with its size and importance as the world's largest trading block.

American Efforts for Trade Liberalisation

Ever since the Kennedy Round of tariff-cutting negotiations ended in mid-1967, the United States has been preparing — as remarked several times before in this journal — for the next phase in the movement towards an open world economy³. More than that, the agencies in Washington concerned with the various aspects of economic policy, being deeply conscious of rising protectionist pressures at home, have been seeking abroad to maintain the momentum of trade liberalisation by getting the European Community in particular, but also other countries, to engage in further multilateral negotiations under the General Agreement on Tariffs and Trade (GATT) on outstanding tariffs, non-tariff barriers and agricultural-support policies⁴. Unfortunately the Common Market was only interested for a long time in its *achèvement, approfondissement et élargissement*.

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¹ For a discussion of the issues see C. Fred Bergsten, *The Threat from the Third World*, in: *Foreign Policy*, New York, December, 1973.

² European behaviour over the American "general alert" during the Middle East war is succinctly dealt with in Lord Kennet (Wayland Young), *Some Unnerving Lessons for Britain from the Nuclear Alert*, in: *The Times*, London, October 27, 1973.

³ The preparations, and the role of independent policy research, is discussed in Corbet, *The Formation of Foreign Economic Policy*, Moorgate and Wall Street, London, Spring, 1973.

⁴ See Harald B. Malmgren, *The New Posture in US Trade Policy*, in: *The World Today*, London, December, 1971.

Americans have been discovering that the new Europe they had encouraged from the outset is capable of effectively denying them support in the maintenance of the international economic order. But the decision-making process in Brussels has not developed enough for the European Community to be able to speak with a single voice. Increasingly it has become apparent, in the words of Curt Gasteyger, that the Common Market is suspended between economic power and political impotence⁵. It seems incapable of subsuming internal differences to take external initiatives of any consequence.

The Fate of Nixon's Trade Reform Bill

How have these frustrations affected the inter-relationship between the politico-security and economic aspects of international relations? Take the course of President Nixon's Trade Reform Bill in the Congress of the United States. Unless it is passed the Tokyo Round negotiations will not be able to proceed.

The bill has been passed by the House of Representatives, but with the *help* of amendments to Title IV dealing with East-West trade. In the Administration, however, there is strong opposition to the amendments. Under the amendments, inspired by the Jackson amendment to earlier East-West trade proposals, the United States would be prohibited from granting (a) most-favoured-nation (MFN) treatment to imports from, and (b) credits or credit guarantees on exports to, (in effect) the Soviet Union until such time as the latter liberalises its emigration policies. These last have prevented the departure of Jewish families for Israel and elsewhere.

What has concerned the Administration is that if the amendments became American law they could jeopardise the *détente* in relations between the United States and the Soviet Union. Yet an understanding between the super-powers is necessary to a lasting settlement of the hostilities between Israel and the Arab countries. And, in any case, American legislation has no extra-territorial effect. Other ways have to be found for bringing about changes in Soviet policies⁶.

It took a while, however, for the Administration to be convinced that a compromise could not be reached on the amendments until the bill went to the Senate. If the Congress was to pass the Trade Reform Bill with the Title IV amendments intact, President Nixon has indicated that he would veto the whole measure⁷, although in present circum-

stances — at home and abroad — this may seem improbable.

The fate of the amendments is very much in the hands of the Senator from the State of Washington. For it is with Senator Jackson that the Administration has to negotiate. The Senator and his main supporters acknowledge though that a threat to deny MFN treatment and credits can only serve its ends as long as it remains a threat. Once the Congress has acted with finality its leverage will be lost and, what is more, the Soviet Union might then impose an even harsher emigration policy. It is thus widely thought on Capitol Hill that the prospects for a compromise on the amendments are good.

Readiness in the Senate to compromise on the amendments will be influenced by the readiness of the Soviet Union to cooperate on a Middle East settlement. If the fabric of *détente* turns out to be a flimsy affair there is likely to be Congressional resistance to any compromise. But the course of the bill is going to be determined by much else besides the state of American relations with the Soviet Union.

For the prospects for the bill as a whole depend, in the end, on developments in American relations with the countries of Western Europe, both as members of the European Community and as members of the North Atlantic Alliance. Foreign policy considerations are critical to the Trade Reform Bill and, as recognised in the American Constitution, the Senate speaks with special authority in the field of foreign affairs.

Unless steps are taken to repair matters, the serious deterioration in Atlantic relations, which came to light as a result of the Middle East war, could produce in the Congress a general consensus that trade negotiations and economic cooperation between the United States and the European Community are becoming less and less relevant. After all, the spirit of the Trade Reform Bill is based on the economic and political interdependence of the industrialised countries of the world. If that underlying assumption is called into question the bill will lose its force and logic.

Monetary and Trade Objectives

So much, then, for the connection between security and economic relations, at least where the Trade Reform Bill is concerned⁸. Assuming the bill is passed, what of the connection between the negotiations on the reform of the trade and

⁵ Curt Gasteyger, *Europe and America at the Crossroads*, Paris (Institut Atlantique), 1971, p. 35.

⁶ See the text of President Nixon's letter to Carl Albert, as Speaker of the House of Representatives, published by the United States Information Service, December 4, 1973.

⁷ President Nixon's letter to Carl Albert, op. cit.

⁸ An exhaustive discussion of the politics of international economics and the economics of international politics can be found in Charles P. Kindleberger, *Power and Money*, London, 1970. Also see Richard N. Cooper, *Trade Policy is Foreign Policy*, in: *Foreign Policy*, December, 1972.

monetary systems. To isolate the connection the principal objectives of the Tokyo Round and the Committee of Twenty should be considered separately.

With the latter there are three issues. First, there is the provision of international liquidity, including proposals to link special drawing rights on the IMF to economic assistance to developing countries. Second, the composition of international reserves has to be discussed, along with what is to be done about the dollar "overhang" and dollar convertibility. Third, there is the central question of balance-of-payments adjustments between countries, involving provisions for changes in exchange rates and for pressures on economies in persistent deficit or surplus⁹.

With the Tokyo Round negotiations there are four issues. First, there is the question of eliminating substantially all tariffs on industrial products traded among developed countries, largely impelled by the need to ease political tensions over the proliferation of preferential agreements. Second, non-tariff distortions of international competition, popularly called "non-tariff barriers", have become more significant as tariffs have been reduced. Some measures, such as public procurement policies and government subsidies, are overtly trade-distorting. Others have trade-distorting side-effects that are incidental to non-trade objectives to do maybe with public health or safety¹⁰. Fourth, if trade is to be further liberalised the safeguards against "market disruption" will have to be improved; that is, temporary "escape clause" protection probably ought to be made more liberally available, but under stricter conditions¹¹.

Monetary Issues and Trade Problems

The first two monetary issues are highly technical, having little bearing on trade problems, and the safeguards mechanism and incidental non-tariff distortions have little bearing on monetary problems. But the third monetary issue, how the inter-

national adjustment mechanism is to function, will influence the course of the negotiations on overt tariff and non-tariff protection of industrial and agricultural production.

Under the Bretton Woods system fixed exchange rates for the currencies of the major trading countries resulted in close attention always being paid to the effect on a country's balance of payments of concessions made in a multilateral trade negotiation. With little scope for parity changes, countries in persistent deficit frequently resorted to restrictions on trade and services, even if they were ultimately obliged to devalue. At the other end, countries in persistent surplus were not prevailed upon to assist international adjustment, by either trade or monetary measures. In the absence of flexibility for exchange-rate changes, governments have been disposed to insist on full reciprocity in trade negotiations in order, it has been argued, to avoid deflationary effects on their domestic economies.

Thus if greater flexibility in exchange rates could be written into the international monetary system, it would be easier for trade negotiations to be geared towards the optimisation of investment decisions and economic efficiency through the expansion of world trade. To bolster the role of monetary policy in achieving international adjustments, governments have been urged not to undertake the use of restrictions on trade and services to correct their balances of payments, even temporarily¹².

Greater exchange-rate flexibility would provide a counter to the deflationary effects of trade liberalisation. This in turn would reduce the need to set so much store by achieving full reciprocity for trade concessions. Indeed, the domestic pressures for unilateral concessions, from such interests as consumer organisations, would be encouraged. Moreover, the inclination of countries in persistent surplus to liberalise trade controls, rather than revalue, in order to fight off "imported inflation" would also be strengthened.

⁹ See European and American Interests in the Negotiations on International Monetary Reform, Staff Paper No. 2, 1973, and Harry G. Johnson, Neglected Aspects in the Discussions on World Monetary Reform, Staff Paper No. 4, London (Trade Policy Research Centre), 1974.

¹⁰ See inter alia Ingo Walter and Jae W. Chung, The Pattern of Non-tariff Obstacles to International Market Access, in: Weltwirtschaftliches Archiv, Kiel, Band 108, Heft 3, 1972.

¹¹ Jan Tumliir, Proposals for Emergency Protection against Sharp Increases in Imports, Guest Paper No. 1, London (Trade Policy Research Centre), 1973.

¹² High-level Group on Trade and Related Problems, Policy Perspectives on International Trade and Economic Relations, Rey Report, Paris (OECD Secretariat), 1972.

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