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How to fill a dollar gap? Observations on the liberalisation of West Germany's external trade and payments 1947-1958

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- How to Fill a "Dollar Gap"? -
Observations on the Liberalisation
of West Germany's External Trade
and Payments 1947-1958*

by

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Abbreviations:

ECA	Economic Cooperation Agency
EPU	European Payments Union
ERP	European Recovery Program
GATT	General Agreement on Tariffs and Trade
IMF	International Monetary Fund
JEIA	Joint Export Import Agency
OEEC	Organisation for European Economic Co-Operation
U.S.	United States of America

I. Introduction

The first attempt at European economic reconstruction after 1945 culminated in the economic crisis of 1947 (Tumlrir, La Haye 1981). Due to state control over prices and production and the lack of sound money for both internal and external transactions, Europe had, to a large extent, returned to the stage of barter trade. This paper addresses the strategies chosen to overcome the shortage of international liquidity, the so-called "dollar gap", during the second and successful attempt at European economic reconstruction from 1947 onwards. It focuses on those aspects which relate directly to the transition from bilateral barter to multilateral trade involving money, i.e. on the liberalisation of trade and payments. Since most early steps to remove restrictions on external trade and payments in Germany and Europe were initiated by the U.S. and implemented on a Western European level, this paper discusses these first measures in a European context before the emphasis shifts to the question why West Germany became a genuine pacemaker for the liberalisation of cross-border transactions from 1953 onwards. As a first step towards a more ambitious study, this paper provides an - admittedly theory-laden - description of some major aspects of the chosen subject rather than an in-depth theoretical analysis or a thorough evaluation of all historical evidence available.

II. Strategic Choices

In the first two years after the war almost all European economies were subjected to plans and regulated prices, and the importance of money prices as indicators of relative scarcities and the role of money itself as a safe store of value were further diminished by open inflation in countries like France and "repressed inflation" (i.e. fixed prices in a state of excess liquidity) in other areas like occupied Germany. Cross-border transactions in Europe and elsewhere were severely hampered by the lack of international liquidity. The emergence of this "dollar gap" can be explained as

follows: Any money - for exchanges within and between countries - has to be based on the trust in the future acceptance of this money by one's future partners in exchange. After the war only the dollar played this role for international transactions at the existing exchange rates. Trade and payments figures (and the fashionable "dollar shortage" talk which usually did not even address the question of price, i.e. of the exchange rate) point to a gross undervaluation of the dollar in the postwar period. At the going exchange rate, no other major currency looked sound enough to be trustworthy or even be credited with some expected revaluation. Consequently, every country had an incentive to refuse to accept any currency but dollars in exchange for its goods. Due to a severe shortage of money that could be used in transactions between currency areas, the world outside the dollar area turned to barter trade, i.e. a network of bilateral agreements specifying in detail the quantities and values of goods to be exchanged in order to make sure that no partner ended up with any deficit that would have had to be settled in scarce dollars¹, or at least with no bilateral deficit exceeding a fixed limit called "swing".

Bilateral agreements of this kind do not necessarily impede the growth of trade volumes in the beginning. They may even facilitate the abolition of protectionist measures. Any exporter whose sales are actually restricted by a foreign country's quota can easily identify which import controls of his own country would have to be relaxed in order to pave the way for a balancing of bilateral trade on a higher level. Thus, exporters can effectively lobby for import liberalisation. However, these bilateral agreements distort trade flows, hinder a specialisation according to comparative advantages, and impede a truly multilateral system of exchange.

Besides the countries of the dollar area, occupied Germany was a major exception to the rule of bilateral trade, at least until 1948. At the end of the war the Allies had assumed complete control of cross-border contacts and exchanges². The Anglo-American decrees (notably Joint Export Import Agency - JEIA - No. 1, 1947) according to which the trade of the two major Western zones of

occupation was to be conducted in dollars had two major consequences: while Germany's customers discriminated against her exports, the terms of trade for the very tiny volume of Germany's imports and exports looked rather favourable (Tables 2, 7).

In the first years after the war, the Americans in effect dealt with the transatlantic payments imbalance by providing aid to prevent "unrest and diseases" in Europe. Meanwhile, they used the leverage that this aid gave them over European countries to pursue the idea of an international economic order. This order was supposed to be characterised by liberal trade practices on a non-discriminatory basis (to be supervised by the envisaged International Trade Organisation), some credit facilities for countries in the process of reconstruction (World Bank), and stable exchange rates (International Monetary Fund). But the organisations which were actually established from 1944 onwards were - at least at that time - far too weak to deal with any major problem. In face of the ongoing American protectionism and of the actual state of disintegration of the world economy due to the shortage of liquidity, this American approach might - in very drastic words - be called a strategy of "benign reluctance" to face the fundamental problems of the time.

The crisis of 1947 in Europe marked the end of the first attempt at European economic reconstruction after the war. Disruptions in production due to the lack of energy (mainly coal), widespread hunger attributed to a bad harvest which was caused by a hard winter and a lack of fertilizers, and a host of other problems pointed to the major defect of the approach chosen so far: the lack of a mechanism providing for an efficient allocation of resources. The crisis of 1947 was a crisis of the means necessary for the coordination of a complex pattern of division of labour rather than a genuine crisis of production. Regulated relative prices had failed i.a. to indicate a shortage of equipment for the transport of goods (most of all coal), and the lack of sound money had inhibited the chance to allocate essential commodities between places and uses according to relative scarcity.

Shocked by the crisis and scared that parts of Western Europe might become communist (or at least not be of much help in an eventual conflict with the Soviet Union) and amidst fierce debates within the American administration about the appropriate course of action, the U.S., the only country capable of shaping the international economic order, turned towards an increased involvement in economic decision-making in Europe and decided to focus on the abolition of the bilateral trading practices³ (Tumlrir, La Haye 1981).

In principle, the problem of the "dollar gap" underlying the bilateral trading practices could have been dealt with in any of the following ways, at least for some time:

- (1) by more aid;
- (2) by severe restrictions on currency movements involving dollars (currency inconvertibility) and on transactions that give rise to currency movements (import quotas, discrimination against dollar imports in general);
- (3) by a revaluation of the dollar in terms of gold or a corresponding devaluation of most other currencies in terms of dollars;
- (4) by relative disinflation in Europe; or
- (5) by a worldwide change in preferences away from dollar imports.

With the announcement of the "Marshall Plan" in 1947 - which turned into the European Recovery Program (ERP) - and with the foundation of the Organisation for European Economic Co-Operation (OEEC) in 1948 (in which the three Western zones of Germany were initially represented by the Allied Authorities) the Americans made their choice plain. They opted for (i) maintaining the severe restrictions on transatlantic exchanges, (ii) providing Europe with aid financed imports of capital goods and with some liquidity necessary for the conduct of intra-European trade on a multilateral basis, i.e. without the need to balance trade bilaterally, and (iii) pushing for the removal of restrictions on intra-European exchanges. In effect, the U.S. decided to wait for a change in the structure of European import demand away from dollar imports and to "close" the dollar gap provisionally by more aid and a

continuation of administrative controls for the time being. This U.S. approach was in general supported by European governments who favoured an increase in American aid over a devaluation of their currencies, which would have raised the price of the socially sensitive agricultural imports from the U.S. From this perspective, American efforts to liberalise intra-European trade and to re-integrate West Germany into the European economy can be seen, apart from their political significance, as an attempt to speed up the change in the structure of European import demand away from dollar imports. Such a change did actually occur to some extent in the 1950s as the increased agricultural output in Europe, the supply of high quality capital goods by Germany, and the general progress of European reconstruction did reduce the postwar dependence on imports from the U.S..

It is remarkable that the U.S. did use the leverage they had over Western Europe to promote European economic integration instead of, say, a far-reaching liberalisation of dollar imports or a thorough currency realignment. However, at the going exchange rates the U.S. would have had to pay the bill for increased European dollar imports by extending more aid, and a revaluation of the dollar would at least in some respects have had the same consequences as the chosen path of maintaining trade restrictions: it would have hurt American exports. Obviously, at least as far as international trade and payments were concerned, the U.S. and Europe in the late 1940s still preferred a state rationing of quantities at artificial prices to a rationing via the price mechanism. Although a currency realignment would also have reduced the scope for the growth of American exports, at least for the time being, it remains an odd feature of postwar economic policy that the U.S. actually did pay Europe to erect a trade system based on the continuing discrimination against dollar imports.

Incidentally, American pressure to liberalise intra-European trade and payments eventually initiated a step in the right direction. Faced with (i) OEEC demands for an increasing element of multilateralism in the settlement of payments balances in Europe (Erhard

1954) during a time when the British foreign exchange position was deteriorating rapidly and (ii) with American-inspired discussions in the IMF over a (mild) devaluation of Sterling, the British devalued their currency by 30.5 % in mid-September 1949. This move led to a wave of devaluations against the dollar throughout the world. Some European countries like the Netherlands exactly copied the British example, other countries devalued their currencies by a smaller percentage (20.6 % in the case of Germany) while Switzerland and a few others kept their dollar exchange rates stable.

Although some high inflation countries in Europe actually devalued their currencies vis-à-vis the dollar more than once, these changes in parities were not sufficient to close the "dollar gap". However, they did reduce the potential scope for intra-European payments imbalances and thus facilitated moves towards regional multilateralism. These moves began in earnest with the decision of the OEEC-countries in late 1949 to remove quantitative restrictions on 50 per cent of intra-European trade as of December 15, 1949, and with the initiation of talks on a European Payments Union in the same month (Triffin 1957).

III. The Role of the European Payments Union

A. The Clearing Mechanism

The European Payments Union (EPU), which replaced the first timid attempts to introduce regional multilateralism in Europe⁴ in mid-1950, was to a large extent the brainchild of the U.S. Economic Cooperation Agency (ECA). Having won a fierce debate with the U.S. Treasury, which had advocated a strengthening of the IMF (Triffin 1957, p. 136), the ECA initiated negotiations over a regional multilateral clearing mechanism in Europe. As a supplement to the OEEC which applied pressure on European countries to liberalise intra-European trade, the EPU was designed to advance European economic integration in two ways: (i) under the EPU regime, all

intra-EPU payments were to be settled monthly on a strictly multi-lateral basis, thus reducing the overall need for transaction balances in transferable currencies (i.e., the dollar) and eliminating any need for a bilateral balancing of trade in the area covered by the EPU; (ii) the EPU was to provide for the automatic extension of limited balance of payments credits from countries with net surpluses in intra-EPU exchanges to net debtors, with the credits being backed up by an initial infusion of \$350 million of ERP-aid. In the EPU agreement, which was signed on September 19, 1950 and covered intra-EPU payments from July 1, 1950 onwards, the contracting parties specified the details of this credit mechanism in the following way: every member country was allotted a quota amounting to roughly 15 % of its 1949 trade volume with OEEC members. Within the limits set by these quotas 60 % of net deficits or surpluses with the Union were to be settled by the extension of credit and 40 % in gold or dollars⁵. In case the net cumulative deficit of a country surpassed its quota, the difference had to be settled entirely in gold⁶.

The EPU was more than a merely intra-European organisation. The clearing mechanism encompassed European payments balances with the entire monetary areas of the OEEC countries, including overseas territories and all members of the sterling area such as India, Pakistan, and South Africa. All in all, the EPU area accounted for 57.4 % of world exports and for 61.7 % of world imports in 1950. The actual clearing operations were carried out by the Bank for International Settlements in Basle, while the administration of the EPU was laid into the hands of a Paris-based managing board operating under the supervision of the OEEC Council, which in turn had the exclusive authority to take all major decisions.

B. The "German Crisis"

Viewed from a German perspective, the European Payments Union seemed to be set for a good start. In June 1950, the last month not covered by the EPU, the balance of payments problems following

the 1949 realignment of currencies and the subsequent removal of quantitative restrictions affecting roughly 50 % of private imports from OEEC countries in late 1949⁷, had been all but overcome. The overall trade deficit had narrowed to \$45 million in June, with exports rising rapidly (63 % up on the monthly average of the second quarter of 1949, Table 5, Table 6) while imports stagnated. Vis-à-vis the EPU countries, the monthly trade deficit was down to \$7 million. These figures may explain why the German balance of payments crisis that developed in the first month of the Korea-boom took the German authorities and the EPU management by surprise. By the end of September 1950, i.e. within three months of regional multilateral clearing via EPU and before the EPU directorate had even met for the first time, West Germany had exhausted almost 60 % of her quota, while all other member countries (or currency areas, respectively) exhibited hardly any deficit at all (Denmark came a distant second with a deficit of some 10 % of her quota). The deterioration of the German EPU position accelerated in October. Following the implementation of the OEEC decision to raise the percentage of "liberalised" private imports from OEEC countries to 60 % in early October (with the emphasis on raw material imports), the German monthly trade deficit with the EPU area went up to a record \$71 million. This development was mostly due to the run on raw materials from overseas and to purchases of consumer goods from the metropolitan EPU area (member countries excluding their overseas territories). To combat this surge in imports, the German inter-ministerial import committee ("Einfuhrausschuß") and the central bank undertook i.a. the following actions in the second half of October 1950: outstanding import licences, for which contracts had not been signed, were cancelled (Wallich 1955, p. 236); applicants for new licences were obliged to deposit 50 % of the value of the desired imports until the goods had actually entered the country (25 % as of December 23); banks were subjected to a host of measures including outright credit restrictions and an increase in minimum deposit requirements with the central bank by 50 % (on average for the various categories of bank liabilities); and the discount rate was raised from 4 to 6 % (BIS 1951, p. 50f). The main emphasis of these

actions was to dampen the growth of internal demand and, thus, imports. Trying to build up a reputation as a liberal trader and trustworthy member of the OEEC, West Germany was eager to avoid the reimposition of quotas on previously liberalised imports. The exchange rate was not altered although the Advisory Council to the ministry of economic affairs had strongly advocated a devaluation (Wissenschaftlicher Beirat, 5.11.1950).

The discussion of the German crisis by the EPU directorate and the OEEC council was based on the report of two independent experts, Alec Cairncross and Per Jacobsson, who, having scrutinised the West German economy, came up with the conclusion that the patient was basically healthy (Cairncross and Jacobsson 1950). On November 14, when Germany's cumulative deficit had already surpassed her quota, the OEEC council decided to extend a special credit of \$120 million designed to cover up to two-thirds of the German EPU deficit in the months until April 1951, provided the West German government submitted a credible program for the restoration of external balance. This condition was formally met by the German government in early December, although the parliamentary debate on tax increases, the core of the proposed measures, did not start prior to March 1951 (BIS 1951, p. 50ff).

Meanwhile, the October measures did show some effect. The trade deficit with the EPU area went down to an average of \$40 million for the months of November to February. However, even a reduced deficit still implied a deterioration of the German cumulative balance with the EPU. At the end of January 1951 the "Bank deutscher Länder" enacted new credit restrictions, and on February 22, when the German cumulative balance with EPU surpassed a deficit of \$450 million, the import committee suspended the previous relaxation of quantitative controls and temporarily ceased to issue new import licences six days later. In spite of grumblings about a German return to "Schachtian" trade practices in some Western European countries (Erhard 1954), the EPU directorate accepted the German measures, thus barring other member states from retaliating against German exports. In the following months, the German

overall balance of trade (Table 5) and her EPU position improved dramatically, with Germany repaying the special assistance credit in May - five months ahead of schedule - and turning into a net creditor to the EPU by November 1951, a position the country continued to hold until the EPU was abolished in late 1958. In compliance with requests by the EPU directorate and under the supervision of a mediation group of three independent experts appointed by the OEEC council, the "Einfuhrausschuß" had gradually resumed issuing new import licences since spring 1951, though quantitative restrictions were not lifted prior to January 1952 (for 57 % of private OEEC imports, a share that increased to 76 % in April and to 81 % in August 1952).

The speed of improvement in the West German payments position gives rise to the question how severe the crisis had actually been in the first place. For a thorough evaluation the following points have to be considered.

- (i) The run on imports, especially on raw materials, initiated by the war in Korea had led to a substantial worsening of Germany's terms of trade - on top of the already severe deterioration in the wake of the currency realignment in late 1949 (Table 7). The OEEC price index for raw materials reached its peak in the first quarter of 1951, just at the time when Germany suspended liberalisation (Table 7). With Soviet troops located on her eastern border, hoarding of raw materials (and consumer goods) was more pronounced in West Germany than elsewhere. However, the accumulation of stocks would not have gone on indefinitely, while higher import prices were bound to dampen import demand anyhow, although with a J-curve type delay.
- (ii) The terms of payments for West Germany's foreign trade had changed for the worse. Germany's customers delayed payments for exports, while imports had to be paid for immediately. According to the Bank for International Settlement this change alone accounted for a shortfall of foreign exchange receipts

of \$65 million vis-à-vis the EPU area in the second half of 1950 (BIS 1951, p. 48). However, payments were not likely to be delayed indefinitely unless war did actually break out in Europe, and the "Bank deutscher Länder" had already taken an important step to halt this hidden flight of capital by raising interest rates in October 1950. In the first half of 1951 the terms of payments for Germany's foreign trade normalised.

- (iii) Prior to the Korea-boom capacity utilisation in West Germany had been lower than in other industrial countries. Consequently, West Germany had more scope for the expansion of production which by necessity implied a surge in raw material imports in advance of any substantial increase in production for internal and external markets. At least some imported raw materials were likely to find their way into export products eventually.
- (iv) Even the notion that imports were expanding ahead of exports does not hold without some qualifications. Germany's overall trade deficit in 1950 (\$60 million/month on average) was actually smaller than the 1949 deficit (\$93 million respectively). If imports had remained at their October 1950 level (or even if they had been higher by, say, \$30 million/month) for the rest of the year, the West German balance of trade would still have shown a remarkable improvement over the year 1949 (the same holds for a comparison of the corresponding quarters of these years, Table 5).
- (v) Except for January 1950, a month in which imports were extremely high due to the removal of quantitative restrictions on roughly 50 % of private imports from the OEEC area, exports had been rising much more rapidly than imports in terms of their annual percentage change throughout 1950 and 1951 (Table 6). As exports grew from a lower level, this discrepancy of growth rates in favour of exports could go along with a temporary balance of trade deterioration in late 1950 - an imbalance that would soon have corrected itself, provided that no

major change of trend had occurred. The development of export and import volumes confirms this optimistic view. In the fourth quarter of 1950 imports (in constant prices) were up 33.5 % on the last quarter of the preceding year, while export volumes had grown by 142 %.

(vi) The most striking feature of German trade in 1950 was the change in the breakdown of imports by regions of origin. In 1949, 45 % of German imports had come from countries that were to become part of the EPU area, 38 % from North America. Due to

- the drastic decline of imports financed by U.S. aid (from \$96 million/month in 1949 to \$40 million/month in 1950),
- the intra-European liberalisation measures of late 1949 and mid-1950, and
- the chance to increase raw material imports from the non-metropolitan EPU countries,

the share of imports originating in the EPU areas went up by 13 percentage points to 68 %, while the share of imports from the U.S. and Canada declined correspondingly (Table 1). Almost the reverse happened to West German exports: the share of exports to the EPU area went down by 8 percentage points to 77 % in 1950 (which can be seen as part of a normalisation process as the percentage of exports going to the currency areas of Western European countries had been extremely high in the post-war years). This redirection of trade and the delay in payments for exports mentioned above account to a large extent for the rapid exhaustion of the West German EPU quota at the time of an export boom.

All in all, the changes in the West German balance of payments in late 1950 and early 1951 hardly deserve the label "German crisis". While the restrictions on the expansion of internal credit may have been justified to check the rise of prices during the Korea-boom, the suspension of import liberalisation was certainly not justified by the actual development of trade. However, this criticism can hardly be directed at the German authorities, whose

foreign exchange reserves were running out. Rather, it points to a deficiency of the international payments system apart from the fact that exchange rates were fixed, namely to the lack of an adequate source of credit on commercial terms for a rapidly and healthily growing country. The EPU quota, based on 1949 trade figures which had been rather small for West Germany, was certainly not sufficient. Acknowledging this fact, the EPU raised the German quota to \$500 million in late 1951. Still then, the lack of an international capital market remained a potential obstacle to growth.

C. Stages of Liberalisation

In spite of the German deliberalisation in early 1951, the handling of the German crisis and the rapid improvement in the German payments position in the same year thoroughly enhanced the prestige of the EPU and the OEEC. The measures adopted by Germany and the EPU set a precedent for other crises to come. By means of (i) extending temporary balance of payments credits and (ii) by making sure that no member country could legally retaliate against a country whose import deliberalisation the EPU had deemed temporarily justified, the EPU and the OEEC council enticed those debtor countries about to exceed their quotas to adopt more restrictive monetary and fiscal policies and to relax any reimposed import control within a short period of time. The negotiations over the terms of renewal of the EPU, that were held every year since the initial agreement on each country's financial obligations to the EPU had expired in 1952, endowed creditor countries with some leverage over net debtors who were afraid of losing a convenient source of credit. Creditors effectively used this leverage to nudge debtors towards a more liberal trade and payments regime. On the other hand, countries accumulating claims on the union in excess of their quotas were themselves urged by the EPU to further liberalise their imports.

Roughly speaking, the abolition of impediments to trade and payments proceeded in the following stages:

- (1) Initially, the emphasis lay on liberalisation in the narrowest sense, i.e. the removal of quantitative restrictions on trade in goods. In July 1950, even before the EPU agreement had been worked out in detail, the OEEC countries agreed to raise their percentage of OEEC imports free from quotas to 60 % as of October 4, 1950 for each of the broad categories of goods (food and feeding stuffs, raw materials, and manufactured goods) and to increase the share of these liberalised goods in their total private imports from the OEEC area to 75 % on average for the various categories of commodities as of February 1, 1951. On January 14, 1955, this overall percentage was further increased to 90 % (EPU 1951, 1955; BIS 1955). While member countries had initially been free to choose the goods they wanted to liberalise within the three categories of goods, the OEEC eventually passed a "common list" as a minimum requirement for all members as of August 15, 1951. The removal of quotas on imports originating in non-OEEC countries covered by the EPU (i.e. countries belonging to a member's currency area) and in other countries outside the dollar area lagged slightly behind the liberalisation of intra-OEEC trade, while the first substantial steps towards freeing dollar imports were taken by the United Kingdom and West Germany in early 1954, a move which most other members imitated in late 1954 and early 1955.
- (2) In the years 1953-55 the emphasis shifted somewhat to invisible trade. Following some initial steps dating back to the years since 1950, the OEEC decided in June 1955 that, subject to some limitations and escape clauses, all invisible transactions and transfers on current account between OEEC members should be free of restrictions (EPU 1956, p. 27). However, liberalisation of invisible trade did not imply free competition between suppliers of services in Western Europe. It merely meant that expenditures for and incomes arising from cross border transactions in services became convertible into the desired European currency.
- (3) In the same period (1953-55), member countries made remarkable

progress on their way to full convertibility of currencies. In May 1953, authorised banks in eight major member countries were permitted to set up multilateral arbitrage arrangements for spot (and later for forward) transactions in any of the eight currencies involved. In early 1954, the United Kingdom, still hoping to reestablish sterling as a widely accepted world currency, took the lead in extending convertibility for her currency beyond the EPU area to (almost) every country outside the dollar area, an example that was followed by Germany in late 1954 ("Beko-Mark") and by most other OEEC countries in the following year. Furthermore, at the insistence of countries with mounting cumulative surpluses, above all Belgium and West Germany, the terms of deficit and surplus settlement were "hardened". On June 30, 1954, the initial gold-free tranche for debtors was abolished and 13 months later the share of gold (or dollars) in any future settlement was increased to 75 %. The importance of these moves towards a higher degree of convertibility was, however, diminished by corresponding increases in all quotas which made sure that the maximum amount of automatic and - in fact - permanent credit available still amounted to 60 % of the original quota. Given the fact that prior to these changes deficits in excess of the quota had to be settled in gold anyhow unless the OEEC council had granted special assistance credits, the net effect of this "hardening" was felt only by countries who had not already exhausted their original quotas. Unlike these changes in payments provisions and quotas there was another agreement concluded in mid-1955 which turned out to be of considerable importance, although with a long delay: after protracted negotiations between debtor and creditor countries, the OEEC members agreed to terminate the EPU as soon as members holding more than 50 % of the quotas had made their currencies fully convertible into dollars. According to this European Monetary Agreement signed on August 5, 1955, a European fund was to become the new provider of temporary balance of payments credit in Europe (besides the IMF who played an increasingly active role in Europe in the 2nd half of the 50s). However, due

to a series of balance of payments crises from mid-1955 onwards, it took three-and-a-half years until member countries holding a majority of EPU quotas finally agreed to replace the EPU with the European Monetary Agreement as of December 27, 1958.

All in all, the liberalisation of trade and payments followed a peculiar pattern. Most major steps on the European level, i.e. the removal of 50 % of existing quotas in late 1949, the raising of this percentage to 75 % and the introduction of the EPU, both agreed upon in mid-1950, the measures undertaken in the years 1953-54, and finally the restoration of full currency convertibility for non-resident holders at the end of 1958, were initiated - though not always enacted - in times of comparatively slow growth of output and trade or in the initial phases of an upswing (the 1955 measures being the exception to the rule). This runs counter to the belief that liberalisation is easiest in times of rapid growth. The reason for this specific feature seems to be that in the 1950s the attainment of balance of payments equilibrium at a given exchange rate was closer to the heart of European policy-makers than outright protectionism. Given a system in which exchange rates are fixed, existing imbalances tend to get worse in times of rapid growth of both imports and exports, while they abate in times of relative stagnation. Furthermore, imports reacted more strongly than exports to changes in the relation between aggregate demand and supply⁸, making it easier for deficit countries to consent to a further liberalisation of imports in times of comparatively slow growth. In times of most rapid growth and in the immediate post-peak phase of cyclical booms, i.e. from late 1950 to the end of 1951 and from mid-1954 to mid-1957, the EPU tried to hold the line, offering assistance to extreme debtors in exchange for promises to act on internal demand rather than to restrict imports, while urging creditor countries to relax remaining impediments to the free flow of trade and payments for current account transactions.

A simple rule of thumb goes a long way towards explaining why which members tended to get into what kind of serious imbalance during upswings. Low inflation countries usually accumulated huge claims on the union while high inflation countries tended to suffer from recurrent balance of payments crises. Evidence presented in Table 9 suggests that the divergences in the development of major member countries' cumulative balances with the EPU can, at least to some extent, be attributed to inflation rate differentials (with Switzerland, a country which had not devalued her currency in late 1949, being the major exception to the rule).

From late 1955 onwards the EPU turned into an almost bilateral affair, with low inflation Germany accumulating high surpluses in excess of her quota (accommodated for by quota extensions called "rallonges"), forfeiting dollar payments she would have been entitled to receive from the union, and extending credit via the EPU-mechanism to high inflation France, whose position with the EPU deteriorated rapidly. This increasing imbalance was bound to bring down the EPU eventually. In late 1958, following a cyclical downswing and the drastic change in French policies (de Gaulle's rise to power, two devaluations in 1957 and 1958, and the adoption of an austerity program called "plan Rueff" approved by the OEEC and the IMF), France finally agreed to replace the EPU with the European monetary agreement as of December 27, 1958. With the exception of Greece (who followed in May 1959), Iceland, and Turkey, all OEEC members restored external convertibility for non-resident holders of their currencies on this date.

D. Evaluation

The European Payments Union was meant to close the "dollar gap" and to enhance economic growth in Europe by distorting the pattern of trade flows in favour of intra-European exchanges for a limited period of time. It is remarkable that this European discrimination against dollar imports was actually not perpetuated but gradually reduced, and that the EPU itself was dissolved in late 1958 to be replaced by a more liberal regime. Although the transition to full

convertibility took considerably longer than anticipated in 1950, the fact that it actually happened has to be counted as a success. In terms of the objectives laid down in the Preamble to the EPU Agreement in 1950 (EPU 1950, 1959), i.e. (i) the removal of quantitative restrictions on the basis of non-discrimination in Europe, (ii) further moves towards full convertibility, (iii) increases in foreign exchange reserves, and (iv) the attainment of independence from U.S. aid, the EPU members made remarkable progress during the years in which the EPU operated.

In terms of "trade creation", the EPU seems to have been a success as well, at least at first glance. The shares of the metropolitan EPU countries in both world imports and world exports rose significantly in the years 1950-58, from 35.3 to 41.8 % for exports and from 41.8 to 43.6 % for imports respectively (Table 4). These figures point to a considerable reduction of the combined trade deficit of the metropolitan OEEC countries and to a rapid increase in trade at the same time. However, this growth of shares in world trade can be attributed to one single factor: the re-emergence of West Germany. The Federal Republic took 4.6 % of world imports in 1950 compared to 7.5 % eight years later and increased her exports from 3.6 to 9.4 % of world exports at the same time, almost attaining the shares held by the much larger German Reich in 1937 (8.2 % for imports and 9.8 % for exports respectively, Table 4). The other metropolitan OEEC countries barely increased their slice of world exports (32.6 % in 1958 as opposed to 31.7 % in 1950 and 32.6 % in 1937), while their share of world imports declined from 37.1 % to 36.2 % (1937: 43.8 %). Although the EPU may initially have facilitated the German re-integration into the world trading system and may have given the Germans the chance to promote their trade by extending export credits to France and others via the EPU mechanism, the comparison with other EPU members⁹ shows that this institution can hardly be credited with the German success.

Another way of looking at the effects of the EPU is to examine the change in the breakdown of trade flows by regions. The standard theory of customs unions suggests that both "trade creation" and

"trade diversion" would lead to an increase in internal trade relative to external trade in any (regional) grouping that lowers its trade barriers for members more than it does for outsiders, thus discriminating against the latter. Neglecting Germany for the moment, the experience of the other metropolitan OEEC countries fits into this picture (see Table 8). For these countries the share of imports coming from metropolitan OEEC countries went up from 35.2 % in 1949 to 39.3 % the following year and reached 46.4 % in 1958 (1937: 37.7 %). The rise in the corresponding export share was less pronounced, it went up from 43.8 % (1949) to 47.2 % (1950) and to an average of 48.5 % in the years 1955-58 (however, the share was down to 47 % in 1958). The relative importance of trade (i) within monetary areas, (ii) with overseas regions covered by the EPU mechanism in general, and (iii) with other developing countries, notably in Latin America, decreased while exports to the U.S. and Canada grew slightly faster than average, thus contributing to the tendency towards balance in cross-Atlantic trade.

Data on the divergence of regional trade patterns between members sheds another light on European economic integration from 1949-58. Taking the share of intra-OEEC trade in overall trade as the relevant indicator, it appears that the countries became slightly more similar (once again neglecting Germany for the moment): the amount by which individual countries deviated from the average decreased in this period, for exports more so than for imports (see Table 8). This move towards more similar patterns of trade was most pronounced in 1950, i.e. following the abolition of quotas on 50 % of intra-OEEC trade.

Once again, West Germany was a special case in point. The figures for Germany, although they do reveal a tendency of trade patterns moving towards the OEEC average, do not indicate a growing relative importance of intra-European trade. A look at the striking regional imbalance of German trade in the early post-war years helps to explain this feature (see Table 1). In 1949, only one-third of West German imports originated in the metropolitan OEEC area (up from 21 % in 1947), while 78 % of her exports went to

these countries (1947: 95 %). These figures for the early post-war years reflect i.a. the importance of aid-financed food imports from the U.S. and of raw material exports to neighbouring European countries. In 1950, the share of OEEC imports increased by 17 percentage points to 50 % (see chapter III. B.), significantly exceeding the OEEC average. During the following years, the share of OEEC imports decreased by 43.7 % in 1958 (3.7 percentage points below OEEC average), contradicting the development in other OEEC countries. At the same time, Germany's regional trade pattern became more balanced, with the share of exports to OEEC countries declining to 68.9 % in 1950 and to 57.1 % in 1958 (5 percentage points above the 1937 figure for the German Reich). Correspondingly, Germany increased her share of the North American market more rapidly than the rest of the OEEC. With less inflation, a relatively far-reaching and rapid liberalisation of imports and a faster growth of productivity than in most other EPU countries (OEEC 1955, p. 70; OEEC 1956, p. 26), Germany outpaced her OEEC partners in terms of export and import growth and gained market shares overseas while other European countries became slightly more dependent on intra-European exchanges. Röpke's apprehension that the EPU would severely distort Germany's traditional trade pattern, i.e. surpluses with Europe compensating for deficits in overseas trade (Röpke 1950), turned out to be overpessimistic. From 1951 onwards, Germany was once again running a surplus in intra-European trade while the trade balance with overseas countries exhibited the traditional deficit (Table 1).

All in all, the evidence presented above is consistent with the following hypotheses. The first steps towards freer trade in Europe, i.e. the removal of quotas in December 1949 and October 1950 and the founding of the EPU, significantly and lastingly enhanced the economic integration of Europe, reducing the relative importance of (aid-financed) dollar imports and of exchanges within monetary areas. For the following years in which the further liberalisation of intra-European exchanges was paralleled by first measures to remove quotas on imports from other regions, the evidence reveals neither a major additional amount of trade creation

within Europe nor increasing trade diversion to the detriment of outsiders. It rather indicates some tendency towards an intra-industry type of division of labour within Europe and across the Atlantic, replacing trade with the (former) colonies in the south. Thus, apart from the initial effects and as far as conclusions can be drawn from trade data at this level of aggregation, the EPU can neither be credited with trade creation on a grand scale nor can she be blamed for massive trade diversion.

In order to come up with a well-founded judgement, the EPU has to be compared with the likely effects of feasible alternatives. Via the EPU, the U.S. did provide some international liquidity necessary for the transition to regional multilateralism, and the EPU facilities did offer incentives for the removal of barriers to cross-border transactions. However, the same might have been achievable with less initial discrimination against dollar imports by a similar payments union including the dollar area, i.e. by a reformed and more active IMF. It is at least conceivable that under such a regime which would necessarily have focussed on the transatlantic payments imbalance, the U.S. might have liberalised their imports more rapidly, while the European countries might have been under increased pressure to devalue their currencies. Under the EPU regime, the U.S. and Europe waited until, at the end of the reconstruction period in the mid-50s and with the re-emergence of Germany as a major supplier of capital goods, Europe's special post-war need to import from the dollar area had been reduced before Europe liberalised imports from the region which, at least at that time, could offer the most advanced technology.

Unfortunately, the alternative option of flexible exchange rates was not even seriously considered by most policy-makers in the late 1940s and early 1950s¹⁰. Milton Friedman first presented his - by now famous - "Case for Flexible Exchange Rates" in a memorandum written in late 1950 (Friedman 1953, p. 157). However, he did not convince policy-makers and fellow economists for the time being that any shortage, be it the lack of a commodity or the lack of international liquidity, would correct itself if the relative

prices concerned were allowed to move freely according to relative scarcities. Lower exchange rates vis-à-vis the dollar, be they determined by the market or be they the result of a devaluation in a regime of otherwise fixed parities (as the Advisory Council to the German Ministry of Economic Affairs had advocated, Wissenschaftlicher Beirat 27.4.1952) would have made Europe attractive for foreign investors. Provided that restrictions on the free flow of capital had been relaxed accordingly, this inflow of capital would have shortened the time needed for reconstruction and the partial catching up with the U.S.. At the same time, a higher dollar would have subjected the American economy to more competitive pressure. Under such a regime, productivity could have increased at an even more rapid rate on both sides of the Atlantic.

IV. Determinants of West Germany's Liberalisation Policy

A. Removal of Administrative Controls

In spite of the traditional importance of Germany's foreign sector the development of trade on commercial terms lagged even behind the initially sluggish reconstruction of West Germany's internal economy in the post-war period. This can be attributed (i) to the fact that foreign trade had become an Allied government monopoly in 1945 (which was rather reluctantly and slowly dismantled from August 1947 onwards), (ii) to the Allied decision that Germany's trade had to be conducted in dollars at artificially high exchange rates¹¹, and - most of all - (iii) to the lack of any appropriate incentive to go beyond the export obligations imposed by the Allies. Apart from a minor foreign exchange retention quota introduced in Bizonia in September 1947¹², German firms were paid in almost useless Reichsmark for their exports while local markets offered at least opportunities for profitable barter transactions. Thus, the relaxation of internal price controls coupled with the currency reform in June 1948, i.e. the re-introduction of sound money for internal use, provided a significant stimulus to engage

in international trade as well. However, foreign trade continued to play a rather minor role for the time being as external transactions were still tightly controlled by JEIA. This agency was finally dissolved in October 1949.

West Germany's subsequent gradual progress towards less government interference into external transactions to complement the internal liberalisation of June 1948 roughly resembles the pattern described above in Chapter III for the EPU members as a whole, the main difference being that, from 1953 onwards, Germany undertook most steps earlier than most other EPU members. For the period from late 1949 to early 1953, liberalisation almost exclusively meant the removal of quantitative restrictions on imports from the EPU area and, with a slight delay, from other non-dollar countries. The motives behind these early measures (including the reliberalisation after the "German Crisis") can be summarized as follows:

- (i) Trying to become a respected member of the Western world, Germany took great pains to comply with the rules conceived by the ECA and laid down by the OEEC.
- (ii) The liberalisation was meant to ensure reciprocal concessions from fellow OEEC members and - with respect to countries that had entered into bilateral agreements with Germany - to widen the scope for the growth of exports, a scope given by the sum of German imports from the country concerned and the respective swing credit.
- (iii) To enhance the growth of output in general and of exports in particular, the removal of quotas on imports of raw materials and other "essential" goods not produced locally was given top priority, notably vis-à-vis countries outside the dollar area.
- (iv) And at least by some economists like Röpke (1950), integration into the world market was - correctly - seen as a powerful tool to prevent a recartelisation, an issue which in the early post-war years had dominated the thinking of many Americans calling for a new and thoroughly liberal Germany.

In the years after 1952, the reasons underlying the German liberalisation efforts changed. Policy-makers were faced with growing trade and current account surpluses. The corresponding influx of

foreign reserves endangered the policy of tight money as the Bundesbank could not go on buying foreign currencies and selling domestic assets indefinitely to keep the money supply stable. Thus, the desire to promote price level stability and to keep the inflow of reserves in check by relaxing import restrictions became an important determinant of Germany's trade and payments policy. As a low inflation country piling up the largest cumulative surplus relative to her quota within the EPU, Germany turned into a pace-maker for European liberalisation, taking unilateral steps ahead in times of cyclical upswings while some debtor countries temporarily re-introduced severe restrictions to trade at the same time. The almost permanent pressure brought upon West Germany by the OEEC helped to overcome internal resistance against these measures.

In the years 1955-57, amidst a swelling influx of reserves, Germany tried to use the relaxation of administrative controls as a substitute for a revaluation of her currency. In this sense, Germany's almost dogmatic adherence to the principle of fixed parities facilitated her integration into the world market. However, the liberalisation of imports (and the gradual restoration of some degree of freedom for capital outflows which had started in 1953 and continuously outpaced the removal of restrictions on capital inflows) is no adequate substitute for a revaluation in the long run. Even under a regime of fixed exchange rates, liberalisation tends to promote export growth, directly by reducing the internal price of imported raw materials and intermediate products and indirectly by enhancing productivity growth and putting downward pressure on wages, albeit with a delay. Thus, the cyclical downturn in the U.S. and in Europe in late 1957 and 1958, which reduced foreign demand for German exports, did more to relieve the pressure on the German Mark than all measures directed at imports.

In the revaluation debate, the Advisory Council to the Ministry of Economic Affairs strongly demanded a realignment of currencies, albeit with a difference: the Council argued for a devaluation of other European currencies rather than for a revaluation of the

Mark (Wissenschaftlicher Beirat, 30.4.1957). Trade figures support the rationale behind this view: Germany was running a huge trade surplus with Europe and a small deficit with the rest of the world while the other OEEC countries combined exhibited massive deficits both vis-à-vis Europe and the rest of the world. In August 1957, France actually devalued her currency de facto by 20 %. This move slightly eased the French balance-of-payments problems. However, it was insufficient to arrest the deterioration in the French position with the EPU and to correct the fundamental imbalances in intra-European trade.

The unwillingness of other European countries to devalue their currencies and Germany's reluctance to revalue the Mark¹³ implied that Germany had to maintain restrictions on capital inflows and to accumulate unproductive foreign exchange surpluses at the same time. She thus forfeited a chance for an even more efficient allocation of resources.

However, this is not the only dark spot in German foreign economic policy in the '50s. Up to this point, this paper has presented the German liberalisation efforts as if they had hardly been affected by any kind of protectionism. As a matter of fact, protectionist pressure groups were quite active and, in some cases, remarkably successful. While the freeing of raw material imports posed no major obstacle, the removal of quotas on imports of foodstuffs encountered fierce resistance from the influential agrarian lobby. As most of the expected benefits from liberalisation (e.g., more price level stability and less pressure on the German mark) did not critically depend on the adoption of measures affecting all kinds of imports in the same way, the German authorities yielded to these pressures, although at least Ludwig Erhard, the Minister of Economic Affairs, was aware of the distortions implied. As quotas on imports of raw materials and most industrial goods were abolished, the effective rate of protection for the non-liberalised goods increased. Table 3 shows that the liberalisation of agrarian imports lagged behind consistently. However, Table 3 actually understates the extent of quantitative restrictions on food

and feeding stuff imports. Even in the '50s, the markets of many agrarian products were so tightly controlled by "orderly market regimes" ("Marktordnungen") in Germany that trade in these products was not counted as "private trade" by the OEEC and, thus, not included in the official liberalisation statistics.

B. Tariff Policy: Tearing Down Self-Erected Barriers to Trade

In the first three years after the war tariffs certainly exerted no influence on the tiny volume and the structure of German imports. Until the end of 1946 tariffs were hardly ever collected at all in the three Western zones of occupation; and even the reenactment of the prewar tariff in the Anglo-American bi-zone in early 1947 and in the French zone a few months later scarcely affected German consumers as internal prices were fixed by the Allied Authorities anyhow. Although the introduction of a unified exchange rate (0.30 \$/Mark) in May 1948 and the abolition of price controls on most goods in the wake of the currency reform of June 20, 1948, did create some link between import duties and internal prices in West Germany, these tariffs were largely irrelevant in face of the all encompassing system of administrative import controls. However, by the time tariffs actually started to play at least a minor role for the volume and structure of imports, i.e. after the removal of quotas on 50 % of private imports from the OEEC countries at the end of 1949, the debate about German tariff policy had already begun in earnest, both between competing local lobbies and between the German authorities on the one hand and the Allies on the other hand.

In the years 1948 to 1949, the Allies had set the stage for the debates to come. At the first round of GATT negotiations in Geneva, the U.S. had succeeded in ensuring that West Germany, without being a party to the General Agreement on Tariffs and Trade, was granted "most favoured nation" (MFN) treatment by 13 of her most important trading partners on September 14, 1948. This was a remarkable step. After World War I, the victors had obtained MFN treatment from the Reich without granting a reciprocal concession

(Möller 1981). Nevertheless, a subsequent allied decision of August 8, 1949, that Germany was to extend MFN treatment to all countries regardless of the beneficiaries policies towards Germany ("statement of Annecy") was considered a "unilateral servitude" by many Germans, including liberal-minded Ludwig Erhard, the future Minister of Economic Affairs (Erhard 1954, p. 210). The chance for the German authorities to reshape the future structure of tariff protection came a few months later. As a preparation for the third round of GATT negotiations in Torquay (England) in 1950 and 1951, the specific tariff dating back to 1902, the "Bülow-Tariff", which had been reenacted in 1947, had to be replaced by an ad valorem tariff specifying products according to the 1948 "Brussels nomenclatura". On October 11, 1949, four weeks after the foundation of the Federal Republic, the Federal Government appointed a committee including representatives of industrial and agricultural organisations and the trade unions to work out a new tariff schedule. In the hearings before and the discussions within this committee representatives of industry argued for low tariffs in general (except for fertilizers, other chemicals, electrical products, and some other commodities) and for a far-reaching reduction of tariffs on agricultural products in particular in order to (i) ensure admission into the GATT to the benefit of German exports, (ii) to lower the cost of imported raw materials, and (iii) to reduce prices for essential goods as a means of moderating wage demands. This point of view was largely supported by the Ministry of Economics and the trade unions, while many conservative politicians lent an ear to the agrarian lobby who argued for high tariffs on agricultural goods (and low tariffs on fertilizers correspondingly) (Jerchow 1979, Lohse 1958).

The tariff that emerged out of this debate over effective rates of protection for different sectors of the economy was a compromise biased in favour of agricultural interest. The new tariff was expressly designed to give German negotiators in Torquay considerable bargaining power and scope for reciprocal tariff reductions (Erhard 1954). The rates proposed by the tariff committee were in general considerably higher than the corresponding rates in the

old Bülow Tariff, although Germany had been invited to the Torquay conference under the condition not to use the introduction of a new tariff schedule to increase import duties. As a consequence, the Allied High Commission did in fact demand substantial reductions of the proposed duties on many agricultural products, on chemicals, fertilizers, electrical goods and some other commodities (Jerchow 1979). However, when the German parliament turned out to be very reluctant to yield to this pressure, the Allies dropped most of their demands in 1951.

Meanwhile, Germany negotiated in Torquay on the basis of a proposed tariff that had not yet been approved by parliament and the Allies. In the course of these negotiations, the Germans made "concessions" (i.e. the reduction or at least the binding of tariff rates), on 32 % of her 3646 tariff positions. Still, the new import duties finally enacted on October 1, 1951, were according to some calculations on average three times as high as the Bülow rates (Rittershausen 1955, Lohse 1958). The lowest tariffs were levied on imports of raw materials and intermediate products (Erhard 1954) while agriculture was protected most thoroughly. For the time being Germany assumed a middle position between high tariff-countries like the United Kingdom, France and Italy on the one hand and low-tariff countries like Belgium, the Netherlands, Sweden and Switzerland¹⁴ on the other hand.

In Torquay, Germany had achieved her overriding goal: admission into the GATT (which had actually been put in jeopardy twice, first by an initial Czech objection against the participation of the "non-sovereign" Federal Republic, and second - and more seriously - by a quarrel about German seasonal tariffs on the imports of some vegetables from her Western neighbours). However, while the representatives of German agriculture were content with the Torquay results, many German industrialists and Ludwig Erhard were somewhat disappointed. Germany had obtained fewer "concessions" from her partners than the export oriented branches of industry had hoped for - and had in turn reduced fewer tariffs than her negotiators had been willing to (Ehmann 1958, Erhard 1954). The

very fact that the Germans had previously increased tariff rates to obtain bargaining chips helps to explain this partial failure. Assuming that Germany would reduce these tariffs anyhow, her partners at the negotiation table were reluctant to offer "concessions" in exchange (Erhard 1954, p. 219). Indeed, on October 10, 1951, Germany first reduced some of her left-over bargaining tariffs unilaterally.

As quantitative restrictions were gradually relaxed in the years 1952 to 1958, tariffs reassumed their role as the classical instrument of commercial policy, and the debate on German tariffs remained rather vigorous, both internally and between West Germany and her trading partners. Erhard who advocated linear tariff reductions (i.e. reductions affecting all goods alike) was - on this point - usually supported by the export industries, many social democrats, the trade unions, and even housewives' associations (Ehmann 1958) who demanded a farreaching reduction of agricultural tariffs in particular. The agrarian lobby, on the other hand, which tried to resist any changes that would not have increased the effective protection of German agriculture, was in most cases backed by the Ministry of Agriculture, the parliamentary committee on agriculture, many Christian Democrats and some Free Democrats (Tudyka 1978).

Erhard's position was strengthened by pressure from abroad, most notably from the OEEC and the GATT, to reduce German tariffs unilaterally as a means to dampen the rise of Germany's export surplus. As a matter of fact, most tariff reductions enacted by Germany in the years 1953 to 1958 were made on a unilateral basis. The agreements reached during the 9th and the 10th round of GATT negotiations in 1955 and 1956 hardly went beyond a prolongation of previous "concessions". With less American leverage to nudge their trading partners into "concessions", the "free-rider" element inherent in unconditional MFN treatment became increasingly relevant: every country has an incentive to abstain from serious negotiations and wait for others to exchange "concessions" that are

automatically extended to the abstaining countries without any reciprocal "concessions".

Although external pressure on West Germany increased in line with Germany's trade surplus, internal considerations gradually became the prime mover in West Germany's commercial policy. With the argument that a lowering of import duties would help to ease upward pressure on internal prices (and would reduce the balance of payments surplus that gave rise to an influx of foreign reserves) Erhard secured a series of unilateral tariff reductions in the years from 1954 onwards. However, Erhard did not succeed in lowering all tariffs alike. Tariffs on agricultural products were mostly exempt from these measures (or reduced by a smaller margin than levies on other goods). Thus, although Germany gradually turned into a low-tariff country, the effective protection of agriculture remained high (and may even have increased for some products due to relatively lower tariffs on inputs).

In most respects, West Germany's tariff policy from 1951 to 1958 (the last year of the period considered) resembles that described above for the removal of quantitative restrictions, the main difference being, however, that newly independent West Germany had erected most of her tariff barriers herself in 1950 to 1951, while she had inherited the system of administrative controls of trade quantities from the Allies and the late German Reich.

V. Conclusions

After World War II Europe took the long road to currency convertibility. Due to a reluctance on both sides of the Atlantic to revalue the dollar or to devalue European currencies respectively, the lack of international liquidity, the "dollar gap", retarded the removal of barriers to trade and payments for more than a decade. Instead of realigning currencies sufficiently, the U.S., the hegemonial power, and Europe simply opted to wait for Europe's postwar needs to import from the U.S. to abate over the course of

time before they took decisive steps to liberalise European imports from the technologically most advanced area. American pressure for the economic integration of Europe can, apart from its political dimension, be seen as an attempt to hasten the change in the regional structure of European import demand by removing intra-European barriers to trade and payments and by integrating West Germany into the European economy. As far as the peculiar German experience is concerned, the Allies have to be credited with initiating the first German steps away from wartime autarchy after 1947. However, the four overriding imperatives dominating West Germany's foreign economic policy after 1949, namely (1) the integration into the Western world, (2) the promotion of exports, (3) the maintenance of internal price level stability, and (4) the adherence to the principle of fixed exchange rates, turned Germany into a pacemaker for liberalisation for endogenous reasons. With less inflation than almost everywhere in Europe, Germany started to accumulate huge balance of trade surpluses, and the argument that a removal of barriers to trade is good for keeping prices stable helped the liberal-minded Minister of Economic Affairs, Erhard, to push for liberalisation. At the same time, Germany outpaced other countries in terms of growth of exports, output, and productivity, while her liberalisation policy enabled her to buy goods where these were cheapest, i.e. improved her terms of trade (Wallich 1955). Unfortunately, West Germany's liberalisation efforts were partly made ineffective by the government's willingness to yield to pressures from the farmers' lobby for high rates of effective protection for agrarian products.

Table 1: West Germany's Foreign Trade

I. Regional Structure								
	1937 ^a	1947 ^b	1949	1950	1952	1954	1956	1958
Total Exports ^c	198	26	94	165	336	438	613	734
Percentage share of exports to								
- EPU	60	97	85	77	72	71	71	69
. Met. OEEC	52	95	78	68	63	61	60	57
- \$ area				12	11	12	13	13
. North America	4.1	1.5	4.7	5.7	7	6.4	8	8.5
- Others				11	17	17	16	18
. Eastern Europe	9.2		3.8	3.8	1.2	1.5	3	3.1
Total Imports ^c	183	71	186	225	321	383	555	618
Percentage share of imports from								
- EPU	52	23	45	68	62	63	60	60
. Met. OEEC	36	21	34	50	45	47	45	48
- \$ area				22	23	18	23	23
. North America	6.3	71	38	16	19	14	17	17
- Others				10	15	19	17	17
. Eastern Europe	10.2		4.1	2.5	1.4	1.9	3.2	3.9
II. Commodity Structure ^d								
	1936 ^a	1948 ^b	1950	1952	1954	1956	1958	
Exports								
- Food and feeding stuffs		2.0	2.7	2.3	2.2	2.3	2.7	2.4
- Raw Materials		10.5	25.1	14.0	7.6	7.7	5.6	4.6
- Semi-finished Products		9.6	29.9	18.8	15.1	13.1	12.4	10.5
- Finished Products		77.9	42.3	64.9	75.1	76.9	79.1	82.2
Imports								
- Food and feeding stuffs		34.5	57.7	44.1	37.4	37	31.5	30.2
- Raw Materials		39.5	23.1	29.6	34.8	28.4	29.4	24.7
- Semi-finished Products		17.4	14.3	13.8	14.6	18.0	18.7	16.9
- Finished Products		8.5	4.9	12.5	13.2	16.6	18.7	27.3
III. Balance of Trade ^c with								
	1937 ^a	1947 ^b	1949	1950	1952	1954	1956	1958
World	15	-45	-93	-60	15	55	58	117
- EPU countries	23	9	- 5	-27	42	71	104	133
. Met. OEEC	37	10	10	- 0.5	66	88	118	123
- Others	- 8	-54	-88	-33 ^e	-27 ^e	-16	- 56	- 16
. Dollar countries				-28 ^e	-38 ^e	-18	- 48	- 45
North America	- 4	-50	-66	-28 ^e	-36	-24	- 44	- 41
Bilateral countries				0 ^e	12	2	- 12	29

^aGerman Reich; Figures on Commodity Structure: Western Regions of German Reich

^bBizonia;

^cMonthly averages in million dollars at current prices; exports f.o.b., imports c.i.f.; balance of trade: exports minus imports

^dPercentage Shares

^eBdL figures

Sources: OEEC, Foreign Trade, Statistical Bulletin, 1950-1959; Erhard 1954; Motz 1952; Bank deutscher Länder (BdL), Monthly Report 12/57; BdL figures differ slightly from OEEC figures due to a stricter exclusion of transshipment in BdL-Statistics.

Table 2: West Germany's Foreign Trade: Volume Indices and Terms of Trade (1953 = 100)

	1936 ^a	1947 ^b	1949	1950	1952	1954	1956	1958
Export Indices ^c								
- Volume	64	5	24	56	86	124	165	195
- Average Value			89 ^d	81	107	96	101	103
Import Indices ^c								
- Volume	66	21	56	75	89	126	171	205
- Average Value			89 ^d	94	114	96	102	95
Terms of Trade ^e	108	(140) ^f	100 ^d	86	94	100	99	108

^aGerman Reich^bBizonia^cFor 1936 and 1949-54 items are weighed with 1950 and for 1956 and 1958 with their 1954 shares in totals.^d2nd half of 1949 only.^eAverage value of exports divided by average value of imports.^fCalculated on the basis of volumes and average prices given in table 7 (items weighed with 1948 shares). Due to the difference in base years between the 1947 and the other figures, to the multiplicity of exchange rates governing Bizonia's trade in 1947, and to the general unreliability of the data for the early postwar period, this figure is a rough indicator of magnitude rather than a precise number. Bizonia's terms of trade would have looked even more favourable if her coal exports had not been priced below world market level until mid-1947.

Source: OEEC, Foreign Trade, Statistical Bulletin, 1949-1959; own calculations.

Table 3:

Percentage of Private German Imports Free from Quantitative Restrictions

Breakdown by product categories

	Imports from Metropolitan OEEC countries ^a						Imports from ^c North America	
	31.12.1949 ^b	01.01.1952	31.12.1954	30.09.1956	01.07.1957	30.06.1958	01.07.1957	01.01.1958
Weighed mean	57	56.8	90.1 (83)	91.5 (86.8)	92.6 (89)	94.0 (94)	91.0 (61)	94.0 (84)
- Food and feeding stuffs	53	51.3	79.4 (79.3)	81.3 (82.4)	81.3	85.4	85.8	92.4
- Raw materials	64	60.0	97.8 (91.6)	98.0 (93.7)	99.3	99.3	96.3	96.3
- Manufactures	52	59.8	93.7 (78.2)	96.2 (82.6)	98.2	98.2	88.5	93.8

^aItems weighed by their 1949 share in private imports from metropolitan OEEC countries^bSeptember/October 1949 share^cItems weighed by their 1953 share in private imports from the U.S. and Canada

(): OEEC average

Sources: Bank for International Settlements, Annual Reports 1952-1959;

European Payments Union, Annual Reports 1952-1959.

Table 4:

Percentage Shares in World Trade

	1937	1947	1949	1950	1952	1954	1956	1958
Exports f.o.b.								
- Metropolitan OEEC	42.4	27.3	34.3	35.3	37.2	38.7	39.5	42.0
. Germany	9.8	0.66	2.05	3.6	5.6	6.9	8.0	9.4
. Others	32.6	26.6	32.2	31.7	32.6	31.8	31.5	32.6
- Rest of EPU				22.1	20.6	19.7	18.1	17.3
- United States	13.6	29.8	21.8	18.3	20.8	19.7	20.5	18.8
Imports c.i.f								
- Metropolitan OEEC	52.0	41.3	40.7	41.8	40.8	42.8	44.0	43.6
. Germany	8.1	1.8	3.7	4.7	4.9	5.8	6.9	7.5
. Others	43.8	39.5	37.0	37.1	36.0	37.0	37.1	36.2
- Rest of EPU				19.9	21.4	19.3	18.4	19.0
- United States	12.4	11.8	12.0	15.1	13.6	13.0	12.9	12.9

Source: OEEC, Foreign Trade, Statistical Bulletin, Series I, 1949-1959; own calculations.

Table 5:
"German Crisis": Export and Import Values^a 1950 to mid-1951

	10-12/49	1/50	6/50	8/50	10/50	11/50	12/50	1/51	2/51	3/51	4/51	6/51
Exports to												
All countries	95	104	155	178	214	232	241	217	231	260	275	297
- EPU	75	84	118	134	153	167	177	155	171	197	202	211
Met. OEEC	69	76	108	121	137	143	155	134	148	175	177	178
- North America	5	5	6.5	11	17	18.5	17	15	17	19	21	24
Imports from												
All countries	211	230	190	205	312	287	314	295	290	299	257	255
- EPU	101	146	125	149	224	207	216	202	211	202	148	135
Met. OEEC	77	109	87	116	166	152	151	140	151	143	88	87
- North America	71	57	36	25	44	34	44	40	41	53	55	59
Balance of trade with												
All countries	-116	-126	-45	-33	-98	-55	-73	-78	-59	-39	+28	+42
- EPU	-26	-62	-7	-15	-71	-40	-39	-47	-40	-5	+54	+76
Met. OEEC	-8	-33	+26	+5	-29	-9	-4	-6	-3	+31	+89	+91
- North America	-66	-52	-29.5	-14	-27	-15.5	-27	-25	-24	-24	-34	-35

^a Monthly average in Million dollars at current prices

Source: Compiled from OEEC Foreign Trade, Statistical Bulletin, 1950-1952

Table 6 :
"German Crisis": Growth Rates^a of Export and Import Values

	1/50	6/50	8/50	10/50	11/50	12/50	1/51	2/51	3/51	4/51	6/51
Exports to											
All countries	22	63	78	125	144	154	109	106	86	115	92
- EPU	15	39	51	104	123	136	85	88	76	100	79
Met. OEEC	12	40	55	99	107	125	76	78	68	88	65
- North America	0	62	100	240	270	240	200	240	217	250	269
Imports from											
All countries	54	- 4	10	48	36	49	28	74	53	45	34
- EPU	128	44	67	122	105	114	38	82	44	18	8
Met. OEEC	137	43	76	116	97	96	28	86	42	2	0
- North America	-11	-53	-64	-38	-52	-38	-30	28	56	83	64

^a Percentage change on corresponding month of previous year, for 1950: change on corresponding quarter of 1949. Source: see table 5

Table 7:
"German Crisis": Trade Volumes^a and Terms of Trade

	1947	1948	1949:				1950:				1951:			
			I	II	III	IV	I	II	III	IV	I	II	III	IV
Exports:														
- Volume	20	54	83	95	104	129	167	199	241	313	307	335	360	352
- Growth Rate ^b		(170)	(53.7)	(75.9)	(92.6)	(138.9)	101.2	109.5	131.7	142.6	83.8	68.3	49.4	12.5
- Average Price	1.29	1	1.02	1	0.96	0.73	0.71	0.71	0.72	0.73	0.77	0.84	0.89	0.91
Imports:														
- Volume	75	130	149	199	193	251	238	211	268	336	302	227	272	278
- Growth Rate ^b		(73.3)	(14.6)	(53.1)	(48.5)	(93.1)	59.7	6.0	38.9	33.9	26.9	7.6	1.5	-17.3
- Average Price	0.94	1	1	1	0.96	0.84	0.83	0.82	0.83	0.91	0.98	1.12	1.16	1.09
Commodity Terms of Trade	1.37	1	1.02	1	1	0.87	0.86	0.86	0.86	0.8	0.79	0.75	0.77	0.83
OEEC Index of Raw Materials Prices														
- Food		81.6		73.7			82.1		89.9		108	102	94	95
- Crude Materials		94.0		84.6			91.1		94.6		100	102	99	98
- Mineral Fuels		65.8		60.3			72.9		89.8		119	104	87	89
- Base Metals & Ores		99.2		87.8			90.0		91.7		99	99	100	101
		81.6		76.8			80.0		88.3		98	99	100	103

^a Monthly averages in million dollars at 1948 prices

^d 1951 average = 100

^b Percentage change of export or import volume on average of previous year, for 1950 and 1951: change on corresponding quarter of previous year

^c Average price of exports divided by average price of imports. Source: see table 5

Table 8:

Selected Measures of European Economic Integration

Exports to/imports from Metropolitan OEEC countries in per cent of all exports/imports

	1937	1947	1949	1950	1952	1954	1956	1958
Export shares								
- OEEC ^a								
Mean ^b	49.1	44.6	43.8	47.2	45.6	47.9	49.1	47.0
Standard Deviation ^b	17.6	15.6	17.4	16.7	17.2	15.9	16.5	16.3
Variation Coefficient ^c	0.355	0.350	0.398	0.354	0.377	0.332	0.337	0.347
- West Germany	52.0 ^d	71.2	78.0	68.9	62.8	61.2	60.3	57.1
Import shares								
- OEEC ^a								
Mean ^b	37.7	29.3	35.2	39.3	39.1	44.0	44.8	46.4
Standard Deviation ^b	16.1	14.1	14.8	15.2	18.3	18.5	17.1	17.7
Variation Coefficient ^c	0.426	0.482	0.419	0.387	0.467	0.422	0.382	0.382
- West Germany	36.2 ^d	21.1	33.6	50.3	45.3	47.1	45.4	43.7

^aMetropolitan OEEC countries excluding West Germany

^bWeighed by actual exports/imports of the individual countries

^cStandard deviation divided by mean

^dFor 1937: German Reich

Source: OEEC, Foreign Trade, Statistical Bulletin, Series I, 1949-1959; own calculations

Table 9:

Prices and Payments Positions of Major EPU-Members

	Price ^a Increase 1950-58 (%)	Relative Payments Position with the EPU ^b	Cumulative Balance with EPU 12/58 in Mill \$	EPU Quotas (late 1951) in Mill \$
Switzerland	11.9	0.1	+ 20	250
Belgium	17.5	3.6	+1192	331
Germany	22.5	8.9	+4473	500
Denmark	29.8	-1.3	- 255	195
Netherlands	31.3	1.6	+ 557	355
Italy	35.6	-2	- 420	205
United Kingdom ^c	46.3	-1.3	-1396	1060
Norway	47.5	-1.7	- 342	200
Sweden	52.2	0.5	+ 137	260
Austria ^d	52.2	-0.9	- 61	70
France	62.9	-4.7	-2900	620

^aConsumer Price Index.

^bCumulative balance 12/58 divided by the respective EPU quota.

^cPayments figures understate the British balance of payments problems due to the inclusion of the Sterling area in these figures.

^dDevaluation of 18 % in 1953.

Source: EPU, Annual Reports 1950/51-1958; BIS, Annual Reports 1950-1959; own calculations

Notes

¹In some cases bilateral deficits surpassing the "swing" were accommodated by the extension of additional credits even in the early postwar period.

²Since the 1945 Potsdam Agreement on a joint administration of Germany had miscarried due to French resistance to any measure treating Germany as a unit, the trade monopoly of the military government meant in fact that every occupying power had almost complete freedom of action in her own zone. In the Western zones, the French used this power to extract as many goods as possible out of their slice of Germany, the British made sure that exports of coal (and other raw materials) reached high levels while, for protectionist reasons, they showed less enthusiasm for the promotion of exports of German manufactures, and the Americans generously supplied food imports while the debate on the desired future for Germany between late adherents of a watered-down Morgenthau plan in Washington and pragmatists like General Clay, the Commander of the U.S. Forces in Germany, went on. The beginning of 1947 marked a turning point. The Joint Export and Import Agency (JEIA) of the Anglo-American bizonie (founded on January 1, 1947 at the insistence of the U.S.) made some efforts to promote exports and even to reduce red tape, albeit with rather limited success. The relaxation of internal price controls in the wake of the currency reform in June 1948 gave a first significant stimulus to private cross-border exchanges, a development which was enhanced by the JEIA decision to restrict its role to a mere ex post control of private trade contracts for most products as of December 1, 1948. Six months after the trade agency of the French zone (OFICOMEX) had (at least on paper) been merged with JEIA in mid-April 1949, JEIA was finally dissolved. Her functions were taken over by the authorities of the just established Federal Republic, although Germany's commercial policy remained subject to Allied control until her admission to the General Agreement on Tariffs and Trade (GATT) in October 1951.

³Incidentally, the Joint Export Import Agency of the Anglo-American bi-zone started to conclude the first minor bilateral trade agreements on behalf of Bizonia in 1947 in order to expand the tiny volume of German trade. However, the bilateral agreements concluded between JEIA and 20 foreign countries in 1947 and 1948 were much too rigid to be of great practical significance (Erhard 1954, p. 85).

⁴The first Agreement on Multilateral Monetary Compensation concluded by the Benelux countries, France and Italy on November 18, 1947, and extended to Bizonia shortly thereafter, had hardly any significance at all. No country was obliged to participate in any operation which would have increased her net deficit vis-à-vis any other country. The turn-over of intra-European compensations increased from October 1948 onwards when all OEEC countries except Switzerland and Portugal were enticed to participate by a link between the settlement of trade balances and ERP aid. Under the two Agreements for Intra-European Payments and Compensations

(October 1948 to June 1950) fixed amounts of this aid were earmarked for imports from specified European countries only. These bilateral drawing rights were periodically determined in advance on the basis of the expected bilateral payments positions. Deficit countries gained from this procedure while surplus countries were, in effect, forced to donate part of their ERP aid to their debtors. Consequently, countries systematically overstated their prospective bilateral deficits and even discouraged exports in some instances. The problems were exacerbated by inadequate forecasts of actual payments positions. Due to this biased mechanism, not even the conversion of one-quarter of these bilateral drawing rights into multilateral means of exchange in July 1949 sufficed to make this system workable. All in all, no more than 4 % of the bilateral positions which could have been settled under an effective multilateral scheme were actually cleared by the multilateral mechanisms established in Europe under these agreements (Triffin 1957, p. 149).

⁵To be precise: beyond an initial gold free tranche amounting to 20 per cent of the respective quota for both debtors and creditors, 50 per cent of net surplusses were to be settled in gold while countries with a net deficit had to pay gold (or dollars) on a rising scale (EPU 1959, p. 19).

⁶Independent of the quotas, the Economic Cooperation Agency fixed initial balances for countries presumed to be in serious payments imbalances in the initial period. Presumed creditors (Belgium, United Kingdom and Sweden) were allotted initial debts totalling \$215 million, while supposedly "weak" countries (Greece, Iceland, Netherlands, Norway and Austria) were granted initial credits totalling \$279 million. These initial positions were not repayable. They amounted to a donation from the Union to the latter group of countries, while the members of the former group - having received corresponding amounts of conditional Marshall-plan aid - were obliged to donate their respective initial positions to the EPU.

⁷On October 30, 1949 West Germany unilaterally abolished quotas on 37.4 % of private imports from OEEC countries (base period: first half of 1949). Furthermore, bilateral trade agreements with Switzerland (27.8.1949), the Netherlands (7.9.1949), Norway (19.9.1949), Austria (30.9.1949), Belgium-Luxembourg (16.11.1949), Denmark (24.11.1949), and Sweden (26.11.1949) provided for the removal of most quantitative restrictions on German imports from these countries, subject only to a global quota in the case of Switzerland and the Netherlands (Bundesanzeiger 3.11.1949; Brzosniowsky 1950). In the subsequent negotiations with the OEEC, West Germany took the stance that she had thus already fulfilled her obligation to remove 50 % of quantitative restrictions vis-à-vis OEEC members by December 15, 1949, a claim which was valid if only the second half of 1949 and not the entire year was taken as the base period for the calculation of the share in liberalised imports. However, this debate became obsolete in early 1950 by the liberalisation of imports from France (trade agreement of 10.2.1950), the revision of the German "free list" (30.4.1950) and

by the fact that most other OEEC countries were even further behind their liberalisation schedule than Germany.

⁸Incidentally, this pronounced pro-cyclical behaviour of European imports may - to some extent - be due to the belated effects of import restrictions enacted by debtor countries at the peak of booms.

⁹The following facts may further illustrate this point: In 1958, the final year considered in this paper, exports of goods and services amounted to 25 % of West Germany's GNP as compared to 8 % in 1949, while imports of goods and services went up from 11 % of GNP in 1949 to 21 % in 1958 (BIS 1959, p. 37). The growth of the external sector was much more pronounced in Germany than in France and the U.K., two industrial countries of comparable size (U.K.: ratio of visible and invisible exports to GNP: 20 % in 1949, 23 % in 1958; corresponding import ratios: 20 % in 1949, 20 % in 1958; France: ratio of visible and invisible exports to GNP: 9 % in 1949, 15 % in 1958; corresponding import ratios: 14 % in 1949, 16 % in 1958 (BIS 1959, p. 37)).

¹⁰Even Ludwig Erhard who turned into an advocate of flexible exchange rates in the early 1950s (Erhard 1953, p. 133; Erhard 1954, p. 83; Deutsche Zeitung, 18.10.1952) did not press this point in the international policy debate.

¹¹Initially, the Allies fixed the dollar exchange rate at \$ 0.10 per Reichsmark for purchases of the Armed Forces ("Militärmark"), while the minimal volumes of cross-border trade were governed by a chaotic multiplicity of product-specific exchange rates supposed to equate the fixed internal price of a product to the corresponding price on the world market (\$ 0.24 - 0.80 per Reichsmark). As a corollary to the currency reform and the relaxation of internal price controls in June 1948, the exchange rate was (almost completely) unified and fixed at \$ 0.30 per Reichsmark in May 1948. This rate was at that time justified by Erhard as a means to expose German industry to severe competitive pressure from abroad (Erhard 1954), but it was deemed far too high by his advisory council (Wissenschaftlicher Beirat 1949).

¹²The 10 % foreign exchange bonus was split evenly between imports of inputs (bonus A) and imports of goods to be distributed to the workers (bonus B). Bonus B expired in July 1948, bonus A in February 1949 (Motz 1954).

¹³The dollar parity remained fixed at 4.20 Marks per dollar throughout the '50s except for some experiments with retention quotas for foreign exchange proceeds which amounted to multiple exchange rate practices. The most striking example is the 40 % dollar quota initiated in 1952. This scheme allowed exporters to sell 40 % of their dollar proceeds to importers of certain goods at a negotiable price. The practical usefulness of this dollar quota was diminished by severe restrictions on the list of permissible imports. It was abandoned in May 1953 in compliance with a

request from the International Monetary Fund (IMF) (Wallich 1955, p. 250).

¹⁴The new German tariff immediately invoked heavy criticism from Switzerland whose government had not participated in the GATT talks. Swiss threats to discriminate against German exports induced a series of negotiations. In the end, Germany made considerable "concessions" which affected 165 out of her 3646 tariff positions (Lohse 1958).

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