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A FREE WORLD COMMUNITY

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BY

HENRY S. REUSS

LETTER OF TRANSMITTAL

WASHINGTON, D.C., *November 1, 1961.*

Hon. HALE BOGGS,
Chairman, Subcommittee on Foreign Economic Policy,
Joint Economic Committee, Congress of the United States.

DEAR MR. BOGGS: I am grateful to the Subcommittee on Foreign Economic Policy of the Joint Economic Committee for the opportunity to include "The Task for 1962: A Free World Community" in its series of studies on foreign economic policy.

The paper outlines my views on the kinds of cooperative action which the principal industrial countries must take if the free world is to grow toward economic and political cohesion. The greatest challenge to U.S. policy now comes from the threatened division of the West by the European Common Market. I have, therefore, not only suggested a proposed course of action, but set forth my reasons for urging that steps be taken in 1962.

Sincerely,

HENRY S. REUSS,
Member of Congress.

THE TASK FOR 1962: A FREE WORLD COMMUNITY

"There is a tide in the affairs of men, which, taken at the flood, leads on to fortune; omitted, all the voyage of their life is bound in shallows and miseries."—"Julius Caesar," act IV, scene 3.

The United States must take the lead, now, to form a free world community dedicated to the liberal exchange of goods, the mutual protection of their currencies, and the sharing of aid for developing areas.

In such a community, countries distinguished by advanced industry, political democracy, and free institutions—such as most of Western Europe, Canada, the United States, Australia, New Zealand, and Japan—would cooperate to strengthen themselves and to help the countries of Asia and Africa and Latin America.

The tide of history will flow very fast in the months ahead. The Common Market and the United Kingdom will be deciding on their terms of association. The Reciprocal Trade Agreements Act will expire next June. Everywhere in the free world, immobilized and fascinated by Communist threats at Berlin and elsewhere, voices are being raised calling for a new initiative by the West.

Taken at the flood—if the challenges and opportunities immediately ahead are constructively seized for united free world action on trade, payments, and aid—the tide can indeed lead on to fortune. But if the challenges and opportunities are not taken, or are postponed out of calculations of tactical advantage, there is a good chance that we shall be "bound in shallows and miseries"—new recession and protectionism and isolationism at home; abroad, a fractured free world for Khrushchev to divide and conquer.

Let us look at the three central economic problems of the free world—trade, payments, and aid—and see how they may best be solved by sovereign nations working together.

TRADE

The Common Market—France, Italy, West Germany, Benelux, and perhaps Greece—is booming along. As matters now stand, the Common Market will have eliminated its internal tariffs and will have a common external tariff by December 31, 1965.

Meanwhile, the countries of the European Free Trade Association, led by the United Kingdom, are seeking, or are about to seek, association with the Common Market.

Both the Common Market proper, and its current enlargement, have been major objects of U.S. foreign policy.

The immediate-run advantages to Western Europe of a vast customs union are great.

Economically, it enlarges the domestic market, at the same time as it introduces the efficiency-stimulating effects of duty-free imports from within the area.

Politically, the Common Market can insure that Western Germany remains at peace with France, and firmly with the West.

Historically, the hope of European unity goes back to Charlemagne, the Holy Roman Empire, the grand design of Henry IV, the pan-European movement of Aristide Briand, and all the impulse toward European integration following World War II.

But, ironically, the Common Market, particularly as enlarged, encourages a European particularism at just the time when what is needed is a free world generalism. If we let the Common Market erect its external tariff wall, and stop there, we shall have split the free world into enclaves at just the time when we should have been moving toward a free world community.

As the Common Market reduces its internal tariffs toward zero, and works toward a common external tariff, it cannot help but hamper exports from the United States and the rest of the free world outside the Common Market. Common Market producers will benefit from lower costs and greater efficiency, the result of larger markets and greater competition.

The United States and other third-country exporters are going to find the booming Western European market increasingly difficult to infiltrate. Moreover, Western Europe may well find that its lower costs will enable it to obtain a larger share of the world export market outside Europe, at our expense.

Expanding U.S. exports is the best way to bring our international payments into balance. Yet the loss to U.S. exports by reason of the Common Market, as enlarged, has been conservatively estimated at $800 million a year.

Currently, our exports are running at the rate of roughly $20 billion a year, and our imports at the rate of $15 billion. If we are ever to balance our payments, we must expand our exports. Yet the Common Market is more likely to contract them.

A particularly discouraging feature of the discriminatory Common Market external tariff is that it will hurt our exports in their fastest-growing area. U.S. exports to Western Europe rose from $2.7 billion in 1953 to $3.2 billion in 1954, to $4 billion in 1955, to $5 billion in 1956, to $5.5 billion in 1957, and—after a mild decline because of the European recession of 1958–59—to $6.2 billion in 1960.

But, from here on out, we will have to contend against a higher external tariff, with substantial tariff increases for low-tariff countries like Benelux and Germany, as well as against the discriminatory preferences granted internally by the Common Market. We can lead a Spartan life in the United States, keep wages and prices stable, and make admirable productivity gains, yet see our export trade gobbled up by countries to which the Common Market accords a sweeping discriminatory advantage.

The Common Market's adverse effect upon our exports will not be evenly spread throughout the United States, but will be concentrated in a few places. Unhappily, it may well penalize some of our most efficient industries: those that do well in export trade.

Here are some examples of the tariff discrimination under which we will be staggering. Our tariff on automobiles is 8½ percent. The proposed Common Market tariff is 29 percent against the United States, contrasted with an internal tariff of zero against auto imports from France, Germany, Italy, and other European member countries.

The Common Market external tariffs on radio and TV sets will be 20 percent; automatic dishwashers, 18 percent; electric washing machines, 19 percent; most clothing, 20 to 22 percent; sheep leather, 10 percent; varnishes and lacquers, 19 percent; putty, 11 percent; oil burners, 14 percent; knitting machines, 13 percent; metal lathes, 10 percent; and office and calculating machine parts, 14 percent.

Once again, it should be emphasized that the discrimination against us and the rest of the free world will be the difference between these percentages and zero, the tariff barrier affecting other Common Market members. Moreover, in many cases the Common Market external tariffs will be considerably higher than the preexisting tariffs of Germany and Benelux, the low-tariff countries which have been such good export customers of ours.

In agriculture, the Common Market proposes a highly restrictionist policy. For many important farm products sold by the United States, Canada, Argentina, and other producing countries, stringent import quotas and a system of varying tariff levies are proposed. Revenue from the tariff levies will be used to subsidize present and expanded farm production in Europe. Secretary of Agriculture Freeman recently pointed out that Common Market plans will seriously affect American wheat, corn, tobacco, poultry, and soybean oil exports, which now represent about $250 million annually in farm income.

The question, then, is whether it is necessary to let the Common Market, as enlarged, divide the free world in two—Western Europe and its dependencies on the one hand, and the rest of the West on the other. The question is whether it is necessary to let the Common Market discriminate against the United States at just the time when it is vitally necessary that we increase, rather than contract, our exports in order to overcome our balance-of-payments deficits.

Happily, there is a way in which Western Europe can have the advantages of more active competition and of a large free market, and in which Germany can be bound to the West, without setting up a discriminatory Western European enclave. That way is for the United States and its leading industrial free world partners to establish a common market which will not divide and discriminate—a common market not for a dog-in-the-manger grouping, but for the whole free world. For example, each adhering member could agree in principle to cut tariffs on industrial goods 10 percent a year for the next 10 years, down to zero. Consistent with GATT provisions, privileged arrangements for the developing countries could be made. By thus generalizing to the whole free world the presently discriminatory tariff reductions of the Common Market, we could at one stroke retain the good of the Common Market and get rid of the bad.

As with the present Common Market, agricultural goods are another matter, and there the goal should be painstaking and steady negotiation to move away from autarchy and toward comparative advantage in free world farm policy.

The United States has much more to gain than to lose by greatly reducing industrial tariffs to zero in concert with other countries.

In the first place, the Common Market external tariff will undoubtedly average at least as high as the approximately 11 percent which is the present average U.S. tariff on the value of dutiable imports. We have cut our tariffs to almost one-fifth of what they were—80 percent—when we started tariff cutting in 1934. The last 20 percent of the way is where we can get some reciprocal mileage.

In the second place, obtaining reciprocal tariff cuts from the Western European countries is doubly advantageous to us in a day when they are allowed to discriminate against us, as they are under the Common Market and EFTA. For example, if we can get France, among others, to reduce the external Common Market tariff by 50 percent, she will by the same reduction reduce by 50 percent the German tariff advantage over us in France which comes from the elimination of internal Common Market tariffs.

Generalizing the customs union feature of the Common Market to the free world would by no means require that this country, or any other country so minded, would have to subject itself to the complicated political superstructure of the Six. All the coordination necessary could be supplied by GATT and OECD, to which we already adhere.

To be sure, a liberal trade policy will necessitate shifts in American production—shifts to be cushioned by trade-adjustment legislation. But the West European countries have managed to shed their fears of a hugely expanded area of competition among countries with greatly different wage levels and habits of doing business. They have all gained as a result.

Today, when our Western European partners in the free world are engaged in taking a major economic step forward, the United States stands to lose its leading position as a world trader if we content ourselves with traditional thinking on commercial policy. The dogmas of the relatively quiet past are indeed insufficient for the stormy present in world trade.

The momentum to trade liberalization given by the Common Market must be seized by us and directed to the benefit of the whole free world.

PAYMENTS

A free world policy of liberal trade requires bolstering by an accompanying policy of mutual support against payments crises—like the gold flurry in London and Zurich which endangered the dollar in October 1960, and the sterling crisis of March 1961.

The countries of the free world today hold their monetary reserves partly in gold and partly in convertible currencies. The great bulk held in currencies is in the form of either dollars or pounds sterling, the two "key reserve" currencies in the world.

Gold available for international reserves has increased very slowly. Thus, for many years after World War II other countries were content to accumulate dollars (and pounds) instead of gold. Today, foreign official and private holders have short-term dollar claims of about $17.5 billion, and $10.5 billion in similar sterling claims. The stability of the dollar and the pound are, therefore, essential to the monetary stability of the free world.

Monetary reserves are necessary because no country can have a continuous balance in its international transactions with the rest of the world. The amounts needed increase as trade expands and, particularly, as it becomes ever easier to transfer money freely from one country to another. When a country's payments exceed its receipts over a period as long as a year, its balance of payments is said to be in deficit.

Until the mid-1950's, the United States held to a deliberate policy of incurring deficits so that the rest of the free world could buy from us and also build their own monetary reserves. Since 1958, we have had larger deficits, but for a variety of reasons. For one thing, while we have almost always sold more goods to others than we have bought from them, this merchandise trade surplus narrowed in some years. At the same time, we continued to make large expenditures for defense and for foreign aid. In 1960 and 1961, our trade surplus rose substantially, but there is concern that we shall not be able to maintain it. Exports to Western Europe may not continue to rise as new tariff barriers are raised against us and as American firms do more and more of their manufacturing inside the Common Market tariff walls. And imports will rise as the U.S. economy gathers steam, since the great bulk of our imports consists of fuel, ores, and other raw materials.

No major step which a country could take to eliminate a payments deficit, by itself and quickly, is appropriate or desirable in the case of the United States.

We could attempt to reduce the prices of our export goods by highly deflationary domestic economic policies. But with 7 percent of our workers unemployed already and much of our industrial capacity idle, we need to expand and not to deflate our economy.

If we raise our own tariffs in order to shut out imports, we would only be starting a beggar-thy-neighbor contest which could wreck the free world.

If we devalue the dollar, we would betray countries which have elected to keep a relatively large portion of their reserves in dollars. Moreover, this would shatter the foundations of our present international monetary system.

For the sake of the free world as well as for ourselves, we could not abruptly cut down our military expenditures abroad or shut off foreign aid.

If, therefore, the United States is to balance its payments in a way which will not injure free world interests, it needs, in cooperation with the other industrial countries, to take constructive measures to eliminate its deficit. One of these measures, for example, would be through the expansion of U.S. exports to Western Europe. Another would be through larger contributions by Western Europe and Japan for foreign aid. Still another would be a redistribution of the burden of military defense.

Above all things, these constructive measures will take time, for they must be undertaken in cooperation with the other developed countries of the free world. Meanwhile, an iron lung must be provided so that balancing our payments may take place in an atmosphere free from "dollar crises."

What is needed is an agreement by the leading industrial countries of the free world to lend substantial sums to each other, through the International Monetary Fund, if any of their currencies came under pressure.

The Subcommittee on International Exchange and Payments of the Joint Economic Committee, in its August 23, 1961, report, posed certain essentials of such an agreement. Funds would be borrowed by the IMF from participating countries having adequate or redundant reserves and strong balances of payments and lent to other participants experiencing payments deficits. Countries owning these IMF obligations would be permitted to use them in international payments, along with their gold and foreign exchange reserves. Credits should be made promptly as needed. The size of the credit in relation to the deficit should be governed by the nature of the deficit: if the deficit is caused by "hot money," the bulk of the outflow should be financed by the credit; if the deficit is "structural" (i.e., of the type which requires correction through accelerated industrial modernization), credit might be granted to cover a significant fraction of the deficit over a period of several years; if, however, the deficit is caused by inflationary policies on the part of the deficit country, credit should be given for only a short period and only if the deficit country agrees to take adequate remedial measures.

Our leading free world partners approved such an agreement "in principle" at the IMF meeting in Vienna in September 1961. It is important that the agreement, to be presented to Congress in 1962, not be watered down in negotiation. The best guarantee against any such watering down would be the announcement of a free world decision to move toward community, on a "one for all, all for one" basis, in trade and aid as well as in payments.

AID

Since World War II, the United States has lent or given $85 billion in foreign aid. Of this total, $56.5 billion has been in purely economic aid, and $28.5 for direct military aid or economic aid to areas in which we have a direct defense interest. Nearly half of the $85 billion in both economic and military aid has gone to Western Europe, and the other half to the rest of the free world, to Russia for a short period after World War II, and, in relatively small amounts, to certain East European countries since that time. In the present 1962 fiscal year, the United States will again lend or give a total of nearly $4 billion in economic and military aid.

Such a sum is not nearly enough for the development needs of the free world. The United States alone cannot provide for these larger needs.

It is economically, politically, and morally sound that the prosperous Western European countries and Japan increase their contributions in a measure commensurate with their international reserve and payments positions and their level of total production. In economic aid, the United States now contributes between $2.5 and $3 billion, about six-tenths of 1 percent of our gross national product. The United Kingdom also contributes in roughly this ratio. France contributes more, but its contribution is to Algeria and connected with its military expenditures there. Germany, Italy, and Japan contribute three-tenths of 1 percent or less. Important conversations are now underway in the Development Assistance Group (DAG) of the Organization for Economic Cooperation and Development to persuade these countries to increase their participation in aid. Again, a Free World Community offers the best chance of persuasion.

The Free World Community here proposed requires no loss of U.S. "sovereignty." The agreements for trade, for payments, for aid involve no yielding to a supranational agency, but simply the use of cooperative agencies to which we already belong—the OECD, the GATT, the IMF.

The Community requires no lessening of congressional power. What is needed are renewed and imaginative exercises of often-used congressional powers over reciprocal trade, payments arrangements within the IMF, and development aid.

Congress in the future may well wish to name delegations of Senators and Representatives to sit in consultative session with fellow parliamentarians of the other free world members of the OECD. Cooperation can thus be achieved on the legislative as well as on the executive level.

The Free World Community would bring many benefits.

Such a Community could ease our balance-of-payments difficulties in the only constructive ways available: by sharing out our development aid responsibility, and by giving U.S. exporters access to indispensable overseas markets.

To the free world, the accomplishment of the Community would provide the economic and political solidarity necessary to meet Khrushchev's challenge of competitive coexistence. Above all, it would give the West the spark, the elan, the drive which it needs.

Many in the free world have a vague suspicion that the totalitarians *are* moving ahead. We need the sense of forward motion which a 10-year drive for a Free World Community could generate. What better occupational therapy could there be for a free world plagued with crises?

The time to announce our goal of a Free World Community is now. If we let 1962 slip by, we may never have as good a chance. Once the EFTA countries are locked into a divisive European Common Market, interests will vest which will be difficult to dislodge; extending the Common Market principle to the rest of the free world could well be blocked. If our recovery in the United States should peter out, or if we should let the Reciprocal Trade Agreements Act expire, the new isolationism and protectionism might prove irresistible. Most dangerous of all, the free world is most likely to shake apart when its only goal is the negative one of containing each new Communist threat.

Congress operates by committees. The Committees on Ways and Means, and Finance, handle foreign trade; Banking and Currency, payments agreements; Foreign Affairs and Foreign Relations, development aid. Fragmented, and without public understanding and support, a Free World Community program has little chance of passage.

Fitted together, explained to the public, supported by the Nation, the program could become a reality in 1962. A new Reciprocal Trade Agreements Act, with adequate authority to develop a free trade area as broad as the free world, could be enacted. A sensible payments agreement could be approved. A coordinated aid program could be developed.

But the task of public education will have to start at once. If public support cannot be developed by June 1962, despite the best work of leaders in the administration and the Congress, at least there will be a foundation on which to build in 1963. And our friends abroad throughout the free world will at least know that America has begun to understand her role as leader of the free world.

HENRY S. REUSS.