

stability to consumption which would have been lacking in their absence; this in its turn contributing to the confidence which favoured investment.

Public works expenditure was not, in the early postwar period such an important part of total demand as might be supposed. Its magnitude in most countries was varied to allow for the large size of other items and outlays on roads and infrastructure tended to lag behind the needs of the economy. Nevertheless, the existence of large waiting programmes of public-works expenditure served to bolster confidence in full employment since such programmes could always be begun in the event of flagging demand elsewhere.

Even from the foregoing brief review of the main factors influencing demand and supply in the industrial countries it is evident that almost all worked towards expansion, full employment and growth. Indeed, for a concomitance of such favourable influences, modern economic history has no parallel. Yet, thus far, we have examined only the domestic influences, common to the industrial countries. Another and perhaps the greatest force was trade, which in the fifties and sixties grew and exerted its influence on the growth of its participants.

(ii) TRADE

Although restrictions on trade were great and lingered on, in the postwar period, until 1960, the total value of the trade of non-communist countries rose from \$53.3 bln in 1948 to \$112.3 bln in 1960 – an average annual rate of growth of 6 per cent.⁷ Not all countries shared equally in this growth. The industrialised countries of Europe, North America and Japan increased their relative share of world exports from 61 to 70 per cent. Other developed countries (Australia, New Zealand, South Africa and some smaller European countries outside the OEEC) saw their share fall from 9 to 7 per cent. The share of the developing countries fell from 30 to 23 per cent.

By the mid-fifties world trade, both in primary commodities and in manufactures, was expanding faster than world production. Between 1953 and 1960 (inclusive) world production increased by 44 per cent in volume with agricultural output growing by 22 per cent. During the same period the volume of manufactured exports rose by 83 per cent and of primary products by 44 per cent. This increase in the foreign trade proportion⁸ continued into the sixties and in 1963 it was about 25 per cent higher than in 1953. It should be noted, however, that even by the latter date the proportion fell short of its 1913 and 1928 values.

At the heart of the increase in world trade was Western Europe which in

⁷ This is the more impressive in that prices of traded commodities were approximately the same in 1960 as in 1948.

⁸ The ratio of trade to GNP.

1960 accounted for 38 per cent of world exports. From 1948 to 1962 the index of export values (1958 = 100) rose from 40 to 138. Between 1948 and 1962 exports and imports of European countries grew at an annual average rate of about 7 per cent while GNP grew at an annual average rate of about 4 per cent. Moreover, European trade grew faster than that of the world as a whole. The index of exports of European countries by volume rose by 275 per cent between 1948 and 1962; for the world as a whole the increase was 230 per cent. In value terms for the same period European exports rose by 200 per cent and world exports by 150 per cent. Tables 5.4 and 5.5 show the relative importance of country groups in world trade in 1960 and the country rates of growth of exports for leading countries. Table 5.6 shows clearly that by 1960 two-thirds of the world's trading was done by the developed countries and that nearly half of such trade was with other developed countries. Time comparisons of the data from which Table 5.4 is compiled show that the trade growth of the industrial countries was at the expense of the developing countries. Moreover, the industrial countries provided by far the largest market for the products of the developing countries.

Tables 5.5 and 5.6 illumine the export performance of the trade leaders. The former shows the great difference in the rates at which countries increased their trade during the fifties. Seven countries had growth rates for exports in excess of that for the world as a whole and for at least three of these (Germany, Italy and the Netherlands) the rise in exports must have been a powerful factor in demand and a stimulus to the growth of their economies. Perhaps the most outstanding feature in Table 5.5 is the very low rate of growth of U.K. trade – making her the only country in which exports grew less than total output.^{9, 10} This poor performance has been variously explained but never very satisfactorily. A number of hypotheses are: high pressure of demand for output drawing goods to the home market; fitful domestic demand policies born of the British desire to preserve sterling as a reserve currency; diminishing competitiveness due to long delivery dates and poor after-sales service; a concentration on commodities for which world demand was relatively stagnant; failure to concentrate export effort in the fastest-growing markets – but it is impossible to assign weights to these causes, all of which probably played some role in what was certainly a dramatic relative decline for a great trading nation.¹¹

Turning to Table 5.6, we find that, with three exceptions, the trade shares

⁹ For Canada the rates of growth of output and exports were the same.

¹⁰ If we relate the level of British exports of manufactured goods to gross domestic product (at constant prices) the ratio is very stable. Between 1956 and 1966 it varied only within the range 13.8–14.3. Manufactured exports account for three-quarters of total exports. Imports varied within the range 4.1–7.9. Since the import/GNP ratio rose, the constancy of the export ratio implies a progressive deterioration of the British merchandise trade balance.

¹¹ For a good analysis of Britain's deteriorating trade position in the fifties and sixties see L. B. Krause, 'British Trade Performance', chap. v of *Britain's Economic Prospects* (Washington: Brookings Institution, 1968).

TABLE 5.5
Rate of Change in the Volume of Exports

	Average annual percentage growth, 1950-60
Belgium	7.7
France	7.2
Germany	15.8
Italy	11.8
Netherlands	10.0
Sweden	5.5
Switzerland	7.8
United Kingdom	1.9
Western Europe	7.0
Canada	3.8
United States	5.0
World	6.4

Source: A. Maddison, 'Growth and Fluctuation in the World Economy, 1870-1960', *Banca Nazionale del Lavoro Quarterly Review* (June 1962)

TABLE 5.6
Trade Shares of Some Industrial Countries, 1937-60

	Percentage of World Exports		
	1937	1950	1960
United Kingdom	20	20	14
France	7	10	9
Germany ^a	16	6	15
Other Western Europe ^b	20	20	21
Canada	8	9	7
United States	23	32	28
Japan	6	3	5
	100	100	100

^a The geographical difference between prewar and postwar Germany affects the comparability of these figures.

^b Belgium, Luxemburg, the Netherlands, Italy and Sweden.

Sources: IMF, *Direction of Trade, 1960-64*; A. G. Kenwood and A. L. Loughheed, *Growth of the International Economy, 1820-1960* (London: Allen & Unwin, 1971) p. 286.

of the major industrial countries were remarkably stable over the period 1937 to 1960. The first exception was Germany, which, for obvious reasons, dropped her share in the immediate postwar period and increased it

spectacularly in the fifties. The second exception was the United States, which increased her share in the immediate postwar period because of her temporary position as almost sole supplier of a wide range of manufactured goods. The third exception was Britain, which continued in the postwar period a secular decline in her share of world trade which began in the nineteenth century.¹²

Finally, a glance at the commodity composition of world trade is necessary. Table 5.7 shows the changes over the same period as the last three tables in the shares of commodity groups in world exports. Manufactures increased in relative importance; primary products, both food and raw materials, declined. Within these broad classifications and not discernible in Table 5.7,

TABLE 5.7
Commodity Groups in World Exports, 1937-60

	Percentage of Total Exports		
	1937	1950	1960
Food	23	23	18
Raw materials	40	34	29
Total primary products	63	57	47
Manufactures	37	43	53
Total trade	100	100	100

Source: D. W. Slater, *World Trade and Economic Growth: Trends and Prospects with Applications to Canada* (Toronto: Queen's Printer, 1968) p. 29.

there was a shift in the manufacturing group away from textiles and in favour of machinery and transport equipment. Chemicals continued a long upward trend. Thus, capital-goods trade accounted for much of the expansion in manufactures at the expense of consumer goods. The relative decline in food as a trade element in the 1950 to 1960 period can no doubt be attributed to a growing drive for self-sufficiency by the former large importers and a natural relative decline in the food element in expenditures in the rich countries as incomes rose. Within the raw-materials group, both agricultural and mineral products declined from 1937, despite notable increases within the minerals group reflecting rising world demand for fossil fuels.

The picture that emerges from scrutiny of the world, country and commodity trade of the period up to 1960 is one of spectacular growth

¹² Care should be taken in assigning too much significance to trade shares. It is, of course, quite conceivable that a country whose share of world trade is declining may still have a satisfactory balance-of-payments position even over a run of years. This is particularly true if the declining share is a share of a swiftly growing total. In the case of Britain, however, the fall in the trade share is usually taken as corroborative evidence of a deep-seated deterioration of the British trade position.

among the industrial nations in trade in their own products and of only modest growth (and declining relative importance) in the trade of the primary producers both with each other and with the industrial countries. Since the division of countries into industrial and primary producers is similar (but not precisely the same) as that between developed and developing countries, we come near to concluding that in this period the rich countries were getting richer, the poor were becoming relatively poorer. This unevenly distributed growth of the world economy, spanning as it has done more than a quarter-century, has been one of the most influential economic forces in our time, producing a great gap, politically, economically and strategically between the developed and the developing countries.

It remains in this discussion of the great trade resurgence to consider a number of general considerations which arise. The first of these lies in a discrepancy which exists, or appears to exist, between the trade growth which has occurred and the theory by which we are supposed to explain changes in real trade flows. On the basis of the pure trade theory of the thirties and of predictions made by some economists on other grounds, the great growth of intra-industrial trade, particularly in capital goods, in the fifties and sixties was anomalous.

The most widely accepted theory of international trade in the thirties was based on the so-called Heckscher-Ohlin theorem, a development by two distinguished Swedish writers¹³ of the earlier Ricardian theory of comparative costs. By this theory trade was based on the country-to-country variation of factor endowments. The greater the differences in (a) factor quantities and (b) the intensity of factor use, the greater the volume of trade. With great precision the older theory of comparative costs, a mere elaboration of international division of labour, was extended. Differences in commodity values were the basis of trade, and differences in such values were the result of varying factor endowment. While some empirical investigations of the fifties somewhat clouded the purity of this ingenious analysis, it still holds its ground in the pure theory chapters of the international trade textbooks.

But the theory carried an evident corollary. If trade was indeed caused by unequal factor endowments, with time and economic development, trade itself would ensure that the more mobile factors, labour and capital, would cross frontiers and that in the long-run factor endowments (except unique land or climate) would tend to equalise and trade would diminish. This, however, clearly did not happen. Not only was there in the postwar period a strong secular growth in trade, but most of this change lay in increasing trade between the industrial countries of which the factor pattern was fairly

¹³ See Bertil Ohlin, *Interregional and International Trade*, rev. ed. (Cambridge, Mass.: Harvard University Press, 1967); Eli Heckscher, *Ekonomisk Tidskrift*, vol. XXI (1919) pp. 497-512. The latter work, an article originally in Swedish, is reproduced in abridged form and in English in *Readings in the Theory of International Trade*, ed. H. S. Ellis and L. M. Metzler (Homewood, Ill.: Irwin, 1949) chap. 13, pp. 272-300.

uniform. Trade between the mature and the developing countries where factor patterns differed greatly was declining relatively. As interpreter of the postwar trade pattern, the Heckscher-Ohlin theory performs badly.

In such a situation one may abandon the theory and seek more plausible explanations or one may attempt to save the theory by attributing events to temporary aberrations not accommodated within the model. Neither of these courses will be followed here. To the writer the Heckscher-Ohlin theorem has always appeared more elegant and ingenious than useful in historical interpretation and empirical evidence and the wind of change may, therefore, blow where it listeth. In any event this narrative is concerned with historical facts and their interpretation rather than with fitting theory to the real world. It would seem that forces more powerful than differences in factor endowment took command of trade after the Second World War. What were these forces?

Probably the greatest was the progressive restoration by 1960 of a system of relatively free trade between major industrial countries. This change was confined to the industrial countries, but restrictions on trade in the rest of the world were not sufficient to retard the trade growth. In Western European countries trade in the immediate postwar period was severely constrained by bilateral trading and payments agreements. Not until 1948 did production make exportable surpluses available and at that time the Marshall Plan provided finance for higher levels of imports. Within Europe, the code of liberalisation of OEEC established targets for trade liberalisation while in 1950 the European Payments Union made European currencies convertible, not only with Europe, but through sterling in the sterling area and through the franc in the franc area. Thus, bilateralism withered away and was replaced by area convertibility and relative trade freedom. The areas of trade freedom became wider. Ultimately, in the late fifties, they were united and virtually the whole of the non-Communist industrial world was free from direct controls on trade and payments.

There were also tariffs. Progress in lowering these was modest upto the mid-fifties. GATT and the application of the most-favoured-nation clause was responsible for some alleviation. But in 1957 there was a big step forward. The Treaty of Rome of 1957 provided for progressive removal of tariffs within a customs union which accounted for a sizeable part of continental Europe. The European Free Trade Area (EFTA), set up in 1959, accounted for much of what remained and provided for internal tariff reductions which matched those of EEC. Somewhat later, in 1962, the 'Dillon Round' of GATT negotiations resulted in a general reduction of tariffs of 20 per cent in the industrial countries. The tariff reductions of the fifties and sixties were modest in amount but coupled with the disappearance of non-tariff trade barriers the stimulus to trade was considerable. It should be noted, however, that this stimulus was confined to the mature, industrial countries. The non-tariff barriers were considerable in the developing countries and lingered long after they had disappeared in the OEEC group, while tariffs against the exports of

manufacturers by the developing countries were reduced little, if at all, by the industrial countries. Moreover, the effective rates of such tariffs in most cases exceeded the nominal rates and constituted a very considerable barrier to entry.

A second influence on the postwar trade pattern was that of the terms of trade. These, with the exception of a brief interlude during the Korean War, were uniformly in favour of the industrial countries. Such trade terms might have been expected to reduce the demand of primary producers for industrial products and to have thereby reduced the trade of the developed countries. In fact, it does not appear to have done so. Probably foreign aid and tied lending served to maintain such exports. In any event the steep rise in industrial imports by the industrial countries from one another was the mainspring of export expansion.

A third factor propelling trade expansion was the steady increase in *per capita* incomes in the rich countries. This ensured that the sophisticated products of such countries found ready markets in similar rather than in less-developed countries. Certainly the products of both capital and consumer goods industries were avidly exchanged by the rich countries, the exchange seeming to rest upon a fine differentiation of product lines rather than upon factor endowment or the intensity of factor use. Thus, between Britain, France, Germany and Italy, all having large automobile industries, trade in cars increased steadily. The same might be said of a wide range of consumer durables. All this was only possible because rising incomes provided expanding markets in all the industrial countries. There was also the general macroeconomic effect of rising GNP levels. Even if marginal propensities to import did not increase the amount of imports would rise fastest in the countries whose income rose fastest. Since these were the West European countries, it is evident that there was a constant trade impeller for such countries. In certain countries, where exports were the leading sector, trade itself was a main growth-force, in others income growth sprang from domestic causes pulling trade in its wake. In any event it is clear that the fastest-growing areas tended to generate trade increases and this was undoubtedly the case with Western Europe in the fifties.

Finally, technological change played a considerable role in trade expansion. Innovations and particularly their application to new-product lines conferred upon the innovating countries and on firms and industries within them, significant competitive power and potential for new market penetration. Technical innovations were not only cost-saving in the productive process; they were, when they led to new products, a generator of the new specialisation which lay behind much of the boom in industrial products in the fifties. Moreover, the larger European countries provided domestic markets large enough to nurture new industries producing such products and allowed them to grow to a scale at which they could operate economically.

All this was true of the early and later fifties but it soon became apparent

that for many firms the growth potential was greater than the domestic market alone could sustain. In automobiles, civil aircraft, chemicals, synthetic textiles, electronics and (in the sixties) computers, the necessary scale of operations overspilled frontiers and generated trade either through the build-up of export markets or by trade-creating disintegration of production on an international basis.¹⁴ The picture which emerges is one of growth industries, which through innovations, research and development on a great scale and early exploitation of market opportunities, added to national outputs and, soon outgrowing their home markets, expanded by export sales and ultimately by direct investment spread their activities over several countries.

(iii) THE AGE OF INFLATION

Despite its greater scale the price effects of the Second World War were somewhat less than those of the First World War. Table 5.8 summarises the price records of a number of countries over the war period and in the first decade of peace. If we compare prices in 1945 or 1946 with those in 1938 or 1939 we may divide countries into groups according to the steepness of increase of their price levels over the period. In the first group, Canada, United States, Australia, South Africa and Venezuela had increases between 30 and 45 per cent; in the second group, the United Kingdom, New Zealand, Switzerland, Denmark, Ireland, Argentina, Norway, and Sweden had increases between 50 and 100 per cent. In a third group, consisting of the Netherlands, Portugal, Spain, Mexico, Belgium, Chile, Brazil and Egypt, the increase was two- to fourfold. In Japan, prices increased tenfold, in Italy, twentyfive fold, and in Hungary, Greece, Romania and China there were hyper-inflations.

In most countries price inflation coming from war expenditures, consumer-goods scarcities and large pent-up consumer demand lasted well into the postwar period. Unlike after the First World War, there were no purposive deflations and prices tended to level out or take on more gradual rates of increase once the sharp rises of the immediate postwar period (1946-8) were spent. Countries which had succeeded in controlling their price levels well during the war (United States and Canada) removed some or all of the controls in this period allowing prices to rise. Those which had had very high wartime inflation rates, such as Germany, resorted to currency reforms, while a third group deferred decontrol until supply caught up, or nearly caught up,

¹⁴ It seems probable that the scarce factor of efficient management, which economic theory tells us limited the optimum capacity of firms, was stretched in the fifties and sixties as firms grew ever larger. No doubt the techniques of scientific management, the advances in instant communication, the use of the computer and mechanised accounting processes all made this growth possible. That it also brought with it great new concentrations of economic power was also soon apparent.

country would have to defend its balance of payments by frequent recourse to direct controls and discriminatory measures was widespread. After a hostile debate on the principles of the Charter in the House of Commons it was decided to defer a decision on its ratification until the United States had ratified. Thus, abandoned by its original architects, the formal edifice of trade planning collapsed.

(iii) THE GATT - A MODIFIED APPROACH

With the end of ITO co-operation in commercial policy continued at a more modest and practicable level. Many countries, including Britain and the United States, were committed to the Protocol of Provisional Application of the General Agreement on Tariffs and Trade.⁷ The GATT originally intended as an interim arrangement had now to serve in default of ITO and it was imperative that the less grandiose principles implicit in GATT should not be lost.⁸ In 1949 at Annecy, 1951 at Torquay and in 1956 and 1961 at Geneva the agreement was greatly amplified and enlarged.⁹ The original membership of 23 countries was increased to 37 (accounting for 80 per cent of international trade) by the conferences at Annecy and Torquay. By 1970 participation had grown to 91. The result of all this has been a loosely knit 'organisation', not operating with a constitution and membership, but an Agreement whose contracting parties meet periodically to review the working of the Agreement, if possible to extend it and to apply it. A small secretariat located in Geneva was added to organise the almost continuous tariff negotiations and in 1960 a permanent Council of Representatives was created. The result has been an international agency less ambitious in aim

⁷ The General Agreement in its present form includes most of the commercial policy amendments which were added to the draft charter at the Havana meeting. It does not include the wider planning objectives of ITO, e.g. 'Employment and Economic Activity'; 'Economic Development and Reconstruction'; 'Restrictive Business Practices' and 'Inter-Governmental Commodity Agreements'. Equally, it does not include the original Charter's organisational and procedural provisions.

⁸ The best book on the GATT is Kenneth W. Dam, *The GATT* (Chicago, 1970). A fairly detailed account of the negotiations for the Havana Charter will be found in Richard Gardner's *Sterling Dollar Diplomacy*, 2nd ed. (Oxford, 1969). The best direct source material is in the Annual Reports of GATT published by the Secretariat in Geneva. The Agreement itself is to be found in *The General Agreement on Tariffs and Trade and Texts of Related Documents* (Washington, D.C.: US Department of State, Government Printing Office). Raymond Vernon's *American Foreign Trade Policy and the GATT* (Princeton: International Finance Section, 1954) is a good examination of GATT's first phase, while Dam's book is an excellent review of the institution from a legal and organisational standpoint.

⁹ The so-called 'rounds' of GATT have been seven in number and were as follows: 1947 at Geneva; 1949 at Annecy; 1951 at Torquay; 1956 at Geneva; 1960-2 at Geneva - the so-called 'Dillon Round'; 1964-7, the Kennedy Round, at Geneva; and 1978, the so-called Tokyo Round at Geneva.

and scope but with considerable flexibility and influence and at least vestigial of the original conception of the ITO.

The Agreement has two main components. It comprises a lengthy schedule of specific tariff concessions for each contracting party - a series of tariff rates which each country has agreed to with its partners. By the mid-sixties, when the membership of GATT had risen to include over sixty countries, this schedule covered many thousands of commodities and tariff concessions had been made on approximately two-thirds of the total imports of GATT countries. The second component of the Agreement comprises a set of general principles for the conduct of international trade. These provide for unconditional most-favoured-nation treatment, the removal of direct quantitative restrictions on trade, uniformity in customs regulations and an obligation by any member to negotiate for tariff remissions at the request of another. GATT deals with tariffs, quotas, preferences, internal controls and regulations affecting trade, customs regulations, state-trading and government subsidies. Its goal is a multilateral and free system of trading.

One problem which was not foreseen by the original draftsmen of the Agreement was that of accommodating within it the regional tariff arrangements of the customs unions and free trade areas which came to be dominant features of the postwar world in the late fifties. In spite of GATT's hostility to discrimination and its emphasis upon the most-favoured-nation principle, it does not preclude the formation of customs unions, the very nature of which is discriminatory. The only proviso is that the formation of a customs union must involve no net over-all increase in barriers against countries outside the union and that, although such a union may require to establish itself by stages, the transition period should not be prolonged. This latter condition secures that a supposed customs union may not die still-born and leave a web of discriminatory tariffs to linger on in perpetuity.

With this view in mind the concern of the draftsmen became that of distinguishing between regional groupings, which GATT approved, and preferential arrangements, which it abhorred. One of GATT's most complex and deceptive provisions, Article 24, was the result. It was under this Article that all subsequent arrangements with the European Common Market and the European Free Trade Association were accommodated.

When we turn from tariffs to direct restrictions on trade (a formidable feature in GATT's early days), it should be noted that GATT's jurisdiction extends only to quantitative restrictions on imports. Exchange controls and restrictions on payments are the responsibility of the IMF. The initial hope of GATT was that all restrictions on trade except tariffs would be removed, but in the economic climate of the forties and early fifties this proved impossible. Countries could not and would not abandon direct supports to their balances of payments. As balances of payments improved in the later fifties quantitative restrictions were considerably reduced, particularly among the industrial nations.

The General Agreement includes a general prohibition on the use of quantitative restrictions except in specific circumstances. The major exception is when a country is in balance-of-payments difficulties. Quotas may then be applied as necessary 'to forestall the imminent threat of, or to stop, a serious decline in its monetary reserves', or 'in the case of a contracting party with very low monetary reserves, to achieve a reasonable rate of increase in its reserves'.¹⁰ GATT members who invoke this waiver are required to consult the IMF as to the degree of adequacy of monetary reserves and if the Fund determines that the country concerned no longer needs to protect its monetary reserves, the country loses the right to the waiver.

Another exception to the anti-quota principle lies in the provision for a country to protect a new industry by the use of import quotas. In this case, however, there is not, as in the case of balance-of-payments difficulties, a general waiver but each individual case has to be submitted by members for approval. This exception was made in deference to the wishes of the developing countries who were anxious to support industrialisation policies by some measure of direct protection.

Yet another exception to the prohibition of quotas is in the case of agricultural products. Where these are the subject of support programmes within a country, quotas may, subject to certain conditions, be used to prevent imports from impairing the domestic support programme.

When quantitative restrictions are used under any of these waivers they must not be discriminatory. Import quotas allotted to countries must be based on typical quantities in some previous period. For a time after the war and during the period of dollar shortage, countries using quotas, under the balance-of-payments waiver, were permitted to discriminate against imports of countries whose currencies were for the moment scarce to them. This was necessary in order to allow GATT to conform to the principle implicit in the Scarce Currency Clause of the IMF. The passing of the dollar shortage, the end of widespread use of currencies with limited convertibility and the fact that the Scarce Currency Clause of the Fund Agreement has never been invoked, make this tolerated infringement of the principle of non-discrimination of historic interest only.

Thus far in this description we have been concerned with the regulatory framework within which GATT has worked. We must also glance briefly at the record of achievement. Foremost in this has been the successive rounds of tariff negotiations in which each contracting party negotiates with others on the tariffs for commodities of which they are suppliers. Seven such rounds of tariff negotiations have so far been completed under GATT auspices. If two negotiating countries agree upon a concession, this concession is extended to all other contracting parties. Such a concession may not always be a tariff remission but may be a commitment to continue

¹⁰ See Article 12.

duty free treatment or not to increase the present tariff rate. The first round of negotiations at Geneva in 1947 set the precedent. At this the United States negotiated with 22 countries, some of which also negotiated with each other. Negotiations were thus conducted bilaterally on a product-by-product basis, the results embodied in schedules which were appended to the General Agreement and made applicable to all the contracting parties. In the early sessions of GATT progress in tariff reduction appeared impressive and member countries seemed surprisingly ready to reduce or remove tariffs. But, at this stage, many of the agreements were in respect of rare goods or of goods which, even in the absence of duty, rarely entered into trade. Some reductions were, however, planned concessions to be conceded for reciprocal concessions. By the early fifties these deliberate concessions had already been used up. As discussion moved towards those duties on goods which were important to member nations progress was slower, either because tariffs on goods were the subject of legislative enactments¹¹ or because members were unwilling to make reductions. It seems there is, for every nation, a hard core of tariffs which it is difficult for GATT to touch or upon which the attitude of members is implacable.

During the period with which we are concerned in this chapter, 1945-55, GATT established itself as a flexible international agency with a growing participation and acceptance of its usefulness within its modest limitations. It provided a forum for trade bargaining and it preserved the idea of international consultation on trade matters at a time when ideas and policies were changing and being moulded by new events and influences. The year 1955 is a suitable date to interrupt this account of its activities. Not only was a reassessment of its role undertaken in that year, but in the sixties, with the rise of the European Common Market and with the new Dillon Round of tariff negotiations it was to face problems and needs qualitatively different from those of its early career.

(iv) CONCLUSION

Taking stock at the midpoint of the fifties several of the important economic developments of the postwar international economy were clearly visible. First, the American drive for multilateral trade in a world economy steered by international agencies was over. Some of the agencies were in being and

¹¹ GATT has no power to make member countries dismantle controls or amend duties which are legislatively sanctioned in their own countries. Thus, it cannot force countries to abandon existing preferences. In this respect GATT falls short of the defunct Havana Charter. Had this been ratified, and the principles of ITO been accepted, member legislatures would, by such ratification, have given their sanction to changes in duties and/or practices even provided for by their own legislation.

functioning, others had perished along the way. The ideal of 'One World' had faded in face of the Cold War and the divisive economic problems of recovery. American foreign economic policy was moving towards *ad hoc* interventions in strategic areas. The political and military realities were taking precedence; economic policies were seen as buttressing American strength and influence. Into this pattern fell the Marshall Plan, support for the economic plans of Western Europe embodied in the Treaty of Rome and American aid policies for what were now euphemistically called the 'developing countries'. Thus the earlier conception and its creations had been too grandiose to be abandoned entirely. There was much debris lying around. The Bretton Woods aims were half accomplished and might yet come to full operation. But in 1955, with many currencies still inconvertible and with exchange controls and discriminatory trade and payments arrangements still rife, judgement was suspended.

Second, the world was at last emerging from the shadow of the war. The industrial economies were growing, trade was growing, and, except among the developing countries, balances of payments were more stable. In particular the dollar problem, in the shape of a chronic scarcity of that currency outside North America, was passing, although in 1955 it was still impossible to discern what it was giving way to. Perhaps most surprising of all, although perhaps ascribable to the new orthodoxy of Keynesianism, the formerly much-feared resumption of widespread unemployment had not taken place. Rather there was misgiving that creeping inflation would replace unemployment as the supreme macro-policy problem of the age.

Finally, it was increasingly apparent that a redistribution of economic power and political influence was taking place. It was too early as yet to discern the emergence of West Germany and Japan as industrial giants, but it was clear that, in the poor and economically less-endowed countries, mainly located in the southern hemisphere, there was an economic grouping whose potential demands for a larger share in world trade and for massive transfers of development capital from the mature economies were to be an increasing force in the next decade.

5

Growth, Trade and Prices in the Industrial Countries

(i) GROWTH IN THE DEVELOPED COUNTRIES

The Second World War marked many changes. In a broad perspective none is more striking in the economic field than the beginning in 1948 of a long period of unprecedented economic growth for the industrial countries. Although somewhat obscured in its early phase by the effects of the war this strong growth trend emerged clearly in the late forties and was continued through the fifties and sixties, in varying degree for countries and at varying rates over time, but always strong and apparent – a dynamic background to the economic history of the period. Table 5.1 gives some indicators of this growth.

Although this economic growth has been described by one writer¹ as 'high and smooth' it had its discernible phases. The first phase was short and consisted of the first few years of postwar recovery, during which demobilisation of armies and switches of factors from war to peace production took place. Not surprisingly the neutrals (Sweden and Switzerland) were quickest to get on the growth path. They were followed by that group of countries in Western Europe which had been lightly damaged by the war and which could make their factor-switches relatively quickly. Germany, France and Italy, all heavy sufferers by war-damage and social and political upheaval, were slow to recover. From 1948 the tempo quickened in all countries. The currency reform in Germany in 1948 marked the beginning of sensational recovery for that country. France, although still suffering inflation and financial instability, increased her national product sharply in 1948 and Italy followed a year later. The Marshall Plan in 1948, the 44 per cent devaluation of the French franc in January 1948, and the 30 per cent devaluation of sterling in September 1949 all worked in favour of European recovery, which was well under way by 1950. Even the Korean War in 1950, although it had unsettling effects on prices and world trade, did nothing to impede economic growth, but rather stimulated output, particularly in the United States.

The period 1953 to 1957 brought a quickening of growth rates and a strong period of economic development in which swift growers – France, Germany,

¹ See M. M. Postan, *An Economic History of Western Europe, 1945-64* (London: Methuen, 1967) Part 1.

mercial presence in foreign markets. Consumer services are provided directly to retail customers by such businesses as restaurants, hotels, and travel agencies and tend to be produced, sold, and consumed within the same market. Producer services—banking, securities trading, insurance, law, advertising, accounting, data processing—are used in the intermediate production of manufactured goods and other services and are more frequently traded internationally.

By the late 1970s, services in the United States accounted for two-thirds of the GNP and for more than 50 percent of the GNPs in twelve other developed countries. Within the service sector, producer services experienced particularly rapid growth. As the economies of the developed countries matured, services came to play an ever greater role in the production and distribution of goods.⁸⁸ During the 1970s and 1980s, services also became a major factor in international trade among developed countries.⁸⁹ The liberalization of goods and capital markets created business opportunities for firms trading in services, while the revolution in telecommunications and computer technologies made possible the rapid transmission of data at long distance and enabled services to be offered across national boundaries. By 1986, for example, U.S. exports of services amounted to \$148.4 billion, equivalent to 39.8 percent of U.S. exports.⁹⁰ Because of problems both in defining services and collecting data, worldwide exports of services are difficult to quantify with any degree of certainty. Many estimates put this figure around \$600 billion.⁹¹ Services account for between 20 percent⁹² and 30 percent⁹³ of world trade.

Services trade has grown despite widespread nontariff barriers. Many service industries, such as telecommunications, banking and insurance, and law and accounting, are highly regulated and often involve state-owned industry. Frequently, such regulation discriminates against foreign services providers by denying access to national markets or by imposing constraints on activities of foreign firms operating in domestic markets. Such barriers include discriminatory treatment of foreign firms in licensing and taxation; policies through which a section of the market is reserved for domestic industry; investment performance requirements; discriminatory government procurement; and government monopolies.⁹⁴ Barriers to trade in services have not been subject to the process of liberalization, because services are not covered by the GATT regime. Although there have been efforts to establish liberalizing rules for such services as insurance in the OECD, by and large services have been outside the international trade regime.

As services grew in importance in the developed countries, service industries, particularly those in the United States and the United Kingdom, began to organize to press governments for adaptation of the trading regime to cover services. In the United States, for example, the service industry successfully pressed for a change in U.S. trade law to make trade rules and remedies applicable to services as well as goods.⁹⁵ As a result, services

barriers began to receive greater attention in bilateral U.S. trade relations. The service sector in the developed countries also sought to make the inclusion of services in the GATT a goal of the Uruguay Round of multilateral trade negotiations.

Intellectual property is another new trade issue.⁹⁶ The comparative advantage of many of the most competitive industries of the developed market economies has become increasingly dependent on their advanced technology, which is expensive and time consuming to develop. Such technology can sometimes be easily and quickly copied and used to produce products at a much lower cost than that incurred by the developer, thus undermining the competitive ability of the firm that developed the technology. The cost of computer software, for example, derives largely from developmental costs. Yet such software can often be easily copied and sold at a price far below the cost to the developer. Similarly, the cost of developing pharmaceutical products is high, while drugs can be easily copied, produced, and sold below the cost to the developer.

For this reason and to encourage the development of technology, most developed countries protect the developer of technology through patent, trademark, and copyright laws. However, intellectual property protection differs among the developed countries and frequently is nonexistent in developing countries. As high-technology firms have increased in importance in trade and as their concern about intellectual property has increased, they have argued that such pirating undermines their ability to compete internationally and, thus, disrupts trade. Because efforts to standardize and expand protection for intellectual property through the World Intellectual Property Organization (WIPO) have not led to common rules and dispute settlement procedures, they and their governments argued that GATT should be broadened to cover intellectual property.

Finally, some developed countries also pressed for GATT rules to eliminate trade-restrictive and trade-distorting effects of government investment policies and practices.⁹⁷ Trade-related investment measures (TRIMs) include local content requirements, which require domestic sourcing; licensing requirements, which stipulate that an investor license production locally and often limit the amount of royalties; product mandating requirements, which oblige an investor to supply certain markets with specific products; trade-balancing requirements, which mandate arbitrary export or import levels; and export-performance requirements, which oblige an investor to export a percentage of its production.

The Tokyo and Uruguay Rounds

The Tokyo and Uruguay Rounds—the seventh and eighth rounds of multilateral trade negotiations—attempted to respond to the changed international trading system, to reform the postwar system of trade management

by developing rules in new areas, and by addressing nontariff barriers to trade. The Tokyo Round, begun in 1973 and completed in 1979, started the process of trade reform.

The Tokyo Round of Multilateral Trade Negotiations (MTN) was the result of a U.S. initiative launched after the dollar crisis of 1971. Begun in 1973 in the midst of the oil crisis, deep recession, and rising protectionism, it took place in an economic and political environment less propitious than that of earlier trade negotiations. Nevertheless, its goals were more ambitious than those of earlier rounds. Previous negotiations sought to lower quotas and tariff barriers, primarily on nonagricultural products, and to implement GATT goals and rules. The Tokyo Round continued the pursuit of tariff reduction and also tried to regulate uncharted areas of international trade such as nontariff barriers; safeguards (i.e., the use of unilateral measures such as voluntary export restraint agreements); tropical products, which were of interest to developing countries; agriculture; and several sectors in which there were still unresolved problems.

In April 1979—six-and-a-half years after the first meeting in Tokyo—the multilateral trade negotiations were concluded.⁹⁸ Some of the goals of the participants had been achieved: tariffs on manufactured products were reduced; codes on certain nontariff barriers (NTBs) were drawn up; and changes were made in the application of GATT rules to the LDCs (see Chapter 7). Other efforts collapsed, including the liberalization of trade in agriculture and, most critically, the effort to regulate safeguards.

The most important outcome of the Tokyo Round was the progress made on regulating nontariff barriers to trade. The Tokyo Round agreement included several new codes that significantly modified the GATT system by extending trade management to nontariff barriers to trade. For example, the Code on Subsidies and Countervailing Duties was a step toward dealing with national industrial policies. The code recognized subsidies on manufactured products (but not raw materials) as nontariff barriers to trade. It allowed countries unilaterally to impose countervailing duties when a subsidy led to a material injury in the importing country and, with authorization from the other signatories, to impose such duties if subsidies led to injury to exports in third markets. A dumping code established comparable rules for anti-dumping measures. The Code on Government Procurement recognized government purchasing policies as NTBs and set rules for giving equal treatment to both national and foreign firms bidding for contracts from official entities. Although the number of government agencies covered by the code was small, it established an important precedent. Other codes covering product standards and customs valuation and licensing established rules for regulating these NTBs. The NTB codes not only established rules but also provided for surveillance and dispute settlement mechanisms. Each code set up a committee of signatories, some of which had powers only to consult (i.e., to oversee) and some of which were given dispute settlement authority.⁹⁹

Despite the new departure signified by the NTB codes, there remained important limits to their effectiveness. Because the NTB codes apply only to the signatories, they diverged for the first time from the GATT principle of most-favored-nation status (MFN) or nondiscrimination. Whereas the developed countries signed and ratified the MTN codes, most of the developing countries were not convinced of their value and chose not to sign, thus leaving themselves open to discrimination that is legal under GATT's rules. The codes are also incomplete. The Code on Subsidies and Countervailing Duties, for example, does not specify which forms of government intervention beyond direct export subsidies are to be considered trade barriers.¹⁰⁰ Even more serious was the failure to reach agreement on a safeguards code to bring rapidly proliferating VRAs under multilateral management. The pivotal, unresolvable issue in the safeguards negotiations was selectivity, the desire of some GATT contracting parties, most importantly the EC, to target safeguards measures instead of applying them on a MFN basis.¹⁰¹

The efforts to extend trade management to include agriculture also met with little success. The negotiations were unable to reconcile two opposing views of the purpose and nature of international control in agriculture. The United States, because of its competitive advantage in agriculture, advocated liberalization of agricultural trade including the modification of the European Community's CAP. The EC, on the other hand, urged the use of commodity agreements to stabilize world prices and long-term supply and refused to negotiate on the fundamentals of CAP. Japan was also unwilling to liberalize trade in agriculture. The result was thus minimal: an agreement to consult about certain agricultural problems, including those connected with meat and dairy products. The sectoral negotiations yielded only one important result: an agreement on civil aircraft that liberalizes trade in this industry. Finally, only limited progress was made on improving GATT's dispute settlement mechanism. Thus, although the MTN was an important step, it was only a limited one,¹⁰² and it was to prove inadequate to stem the burgeoning protectionist pressures of the 1980s.

Following the Tokyo Round, pressures on the GATT system increased. Departures from GATT rules, such as voluntary export restraints, grew; the agriculture trade war erupted; and trade conflicts became more frequent and more heated. Nevertheless, the postwar political consensus supporting open trade remained alive, if not well. The leaders of the developed countries used summit and OECD meetings to reiterate their commitment to open trade principles and to resolving specific conflicts, even as they negotiated managed-trade agreements. New forms of international dialogue were tried. Bilateral meetings, most notably between the United States and Japan, were used to try to resolve specific trade conflicts, and multilateral meetings, such as regular quadrilateral meetings of the United States, Japan, the European Community, and Canada, were begun to try to resolve systemic issues.

The precarious nature of the multilateral trading regime was revealed in 1982, when GATT held its first ministerial meeting since the 1973 meeting that launched the Tokyo Round. The agenda of the meeting was ambitious: a review of the Tokyo codes on NTBs; action on GATT dispute-settlement procedures; continuation of the negotiations on a safeguards code; efforts to bring agriculture under the GATT regime; and consideration of new codes on trade in high technology and services. The meeting ended in failure. The ministers made virtually no progress on any issues under discussion and could pledge only to "make determined efforts" to ensure that their countries' trade policies were consistent with GATT's rules.¹⁰³ Perhaps the most positive result of the ministerial meeting was the widening recognition that the international trading system faced collapse.

The following year, the Reagan administration, aided by the economic recovery in the United States, supported by Japan and the GATT secretariat, began a campaign to launch a new round of multilateral trade negotiations. Initially the EC, confronted with severe unemployment and recession, argued that the time was not right. However, in 1985, the world's trade officials agreed to launch a new round of multilateral trade negotiations and established a committee to develop an agenda. In September 1986, a special session of the GATT contracting parties meeting in Punta del Este, Uruguay, officially launched the negotiations, which came to be known as the Uruguay Round and set a target date of 1990 for their completion. The Uruguay Round negotiations began in 1987.

The ministerial declaration issued at Punta del Este instituted a standstill on new trade-restrictive or distorting measures and called for the elimination by the end of the Uruguay Round of measures inconsistent with the provisions of the GATT. The trade ministers also established fifteen negotiating groups that fell into four broad categories.

Some groups focused on issues that had been taken up in earlier negotiating rounds, including those (such as tariffs) that had long been on the GATT agenda as well as others (such as subsidies and safeguards) that had not been resolved satisfactorily in the Tokyo Round. Most important, and perhaps most difficult, among these issues was safeguards. As we have seen, GATT rules on safeguard actions have been ineffective and relatively easy to circumvent through new protectionist measures, such as voluntary restraint agreements (VRAs). The success or failure of the Uruguay Round on the safeguards issue will, in large part, determine whether the GATT will retain influence over the international trading system as protectionist measures continue to multiply outside of GATT disciplines. Although the 1986 ministerial declaration called for "a comprehensive agreement on safeguards," the political difficulty of reaching such an agreement remained significant. As in the Tokyo Round, the central conflict centered on selectivity. The EC insisted on the need for selectivity. The United States advocated safeguard actions taken either on a most-favored-nation or "consen-

sual selectivity" basis. The developing countries—for whom the safeguards negotiations were a top priority in the Uruguay Round—strongly advocated the most-favored-nation position.

A second set of negotiations focused on concerns of developing countries, such as tropical products, natural resource-based products, textiles, and clothing. Due to the increasingly active role of the developing countries in the GATT, successful completion of these negotiations was essential to their continued involvement in the GATT system (see Chapter 7).

A third set of negotiating groups had mandates to reform existing GATT rules or mechanisms. Dissatisfaction with existing GATT dispute settlement mechanisms had been mounting for years. Countries were able to delay or block resolution of a dispute; there was no effective mechanism for enforcing decisions or overseeing their implementation; and protection of third countries affected by the dispute was inadequate. The ministerial declaration at Punta del Este instructed the negotiating group on dispute settlement to "improve and strengthen the rules and procedures of the dispute settlement process." Negotiations moved rapidly in this negotiating group due to broad agreement on the need to expedite dispute settlement procedures and to the absence of any significant North-South division. By the end of 1988, negotiators had agreed on several measures to streamline procedures and speed up decisions in the dispute settlement process. These reforms were implemented on a provisional basis in 1989.

The negotiations on the functioning of the GATT system (FOGS) were intended to strengthen the role of GATT as an institution. The negotiating group focused on ways to enhance GATT surveillance of trade policies and practices; to improve the overall effectiveness and decision making of the GATT by involving ministers; and to strengthen GATT's relationship with the IMF and World Bank. Because there was a significant degree of consensus on what needed to be done, negotiations on FOGS proceeded smoothly. By the end of 1988 agreement was reached on the establishment of a new trade policy review mechanism to examine and publicize national trade policies on a regular basis. Negotiators agreed to begin implementing this mechanism in 1989 rather than wait until the conclusion of the Uruguay Round.

Finally, some groups sought to broaden the scope of the GATT to cover nontraditional areas. One of the most significant and controversial decisions made at Punta del Este was the agreement to include the so-called new issues—services, intellectual property rights, and investment—in the round. The opposition to their inclusion was led by a small group of developing countries, which feared that GATT rules developed for the new issues could be used by the industrialized countries to overwhelm their fledgling industries and to undermine domestic policies that the developing countries considered critical to their national economic development. They argued that the Uruguay Round should concentrate instead on unfinished

business from the Tokyo Round and on reform in areas where the GATT had clearly failed to impose adequate international discipline, such as safeguards, textiles, and agriculture. They also insisted that GATT was not the appropriate forum for the new issues that, they argued, came under the purview of other organizations, such as WIPO for intellectual property or the United Nations for investment.

The industrialized nations stressed the need to modernize the GATT by broadening its scope to deal with new areas of trade. As in previous GATT rounds, the United States took the initiative in pushing aggressively for the inclusion of services, intellectual property rights, and investment in the Uruguay Round. The EC and Japan supported the U.S. position, but they were not entirely convinced of the wisdom of increasing the burden of the GATT at a time when so many longstanding problems had yet to be resolved. They also shared some of the concerns of the developing countries about the extent to which GATT rules in the new areas might impinge on their sovereignty in domestic regulation and government policy. In the case of investment in particular, they questioned the appropriateness of using GATT as the forum for management. Finally, while there was a consensus among the developed countries about the principles that would cover some of the new issues (especially services and intellectual property), it proved difficult to come to agreement on specific details of the application of those principles.

The issue that is most likely to determine the ultimate success or failure of the Uruguay Round, however, is not a new issue but an old one: agriculture. As we have seen, agriculture has been treated as an exception in the GATT. Agriculture remains a highly controversial issue, largely because it is so deeply imbedded in the domestic politics of most nations. Although the United States, the EC, and the key agricultural producers have agreed on the need for reform, there is no agreement on how to go about it. The United States ambitiously proposed phasing out all direct farm subsidies and farm trade protection within a decade. The Cairns group—a coalition of fourteen smaller producing nations (including Australia, Argentina, Hungary, and Canada among others)—advocated a similar approach. The EC accepted the need to reduce subsidies, but viewed the U.S. proposal as highly unrealistic, advocating instead an approach that would allow it to maintain its Common Agricultural Policy. Japan was also unenthusiastic about the U.S. proposal, but generally tried to keep a low profile.

Conclusion

The Uruguay Round will thus be a major test for the multilateral trade regime. The challenge is great. New rules and techniques must be developed to constrain the new protectionism. GATT must be expanded to cover new

sectors. In the process, GATT must be expanded from a fragile dispute settlement regime and periodic international negotiation to an effective international organization capable of resolving conflicts, containing protectionist pressures, and promoting liberalization in both old and new sectors. If the Round can make headway in achieving these goals, it will make possible the continued vitality of a multilateral, liberal system.

If it fails, the stage is set for increased reliance on managed trade and a breakdown into regional blocs. As we have discussed, the European Community is forming its own separate trading system that could turn inward. The United States and Canada have signed a free-trade agreement that is intended to complement the GATT but which, without a vital multilateral system, could become the basis for a separate North American market. If such regional systems begin to emerge, there will be severe pressure on Japan to secure market access. Some have proposed a free-trade agreement between the United States and Japan. Others conjecture that, instead, Japan may turn to Southeast Asia as its central trading system. Such managed trade and regionalism bear dangerous resemblances to the blocs of the 1930s.

The continued vitality of a multilateral liberal system will also depend on the development of plurilateral management. Economic power is now more evenly dispersed. The United States as the largest (although no longer the dominant member) will have to continue to provide leadership for the system. This will be possible only if the United States can redress its trade imbalance and revitalize its competitiveness. At the same time, Europe and Japan must define new, more active roles in trade management. Europe will have to find the appropriate balance between looking inward towards the creation of an internal market and its need to look outward to the multilateral trading system. Because of its size and its role in world trade, reestablishing a reasonable balance between Japan and its trading partners, as well as integrating Japan into the management of the international trading system, will be a central challenge for the remainder of the century. Finally, as development outside the developed market economies proceeds, all will need to address the new role, first, for the newly industrialized countries and, then, for other developing countries.¹⁰⁴

NOTES

1. E. E. Schattschneider, *Politics, Pressures and the Tariff* (Englewood Cliffs, N.J.: Prentice-Hall, 1935). See also: Robert A. Pastor, *Congress and the Politics of U.S. Foreign Economic Policy, 1929-1976* (Berkeley and Los Angeles: University of California Press, 1976) and Stefanie Ann Lenway, *The Politics of U.S. International Trade: Protection, Expansion and Escape* (Marshfield, Mass.: Pitman Publishing, 1985).

2. The analysis in this chapter concentrates on trade relations among developed market economies. For issues involving the underdeveloped countries, see Chapter 6 of this text; for East-West trade issues, see Chapter 10.