CHAPTER II

EUROPEAN ECONOMY IN CRISIS: AN OVERVIEW

Background: The Economic environment in the International Context

Europe has stepped into the eighties in a sombre mood. This is in marked contrast with the optimism displayed in the early seventies when there was comparative prosperity and the EEC had a substantial favourable trade balance. At the end of the 1960s, inflation had afflicted majority of the OECD countries, thereby affecting adversely their rate

1 In 1970 the main European issues centred around the prospect of British entry into the European community, and strangely the problem of pollution, with the recession has receded into the background. For details see, Cosmo Russell, "Europe in the New Decade", Contemporary Review (London), vol. 236, no. 1369, February 1980, pp. 57-63, and Bertrand de Jouvenel, "Back to Basics", The Futurist (Washington), vol. 14, no. 3, p. 11. Also see, Stefan Riesenfeld, "Building the Common Market and Beyond", Virginia Journal of International Law (Charlottesville), vol. 19, Fall 1978, pp. 1-45, and Tadao Kawakami, "The Crisis of the Capitalist World", Cambridge Journal of Economics, (London), vol. 3, no. 2, June 1979, pp. 189-202. To be more precise world trade had shown remarkable buoyancy throughout the early 1960s growing annually at an average rate of 7.8 per cent in terms of export volume. By the end of 70s the rate of expansion had slowed down to 6.1 per cent (annual average growth in 1970-78). Also see, Sukhamoy Chakravarty, "Reflections on the Present World Economic Conjuncture", Social... Scientist (Trivandrum), vol. 10, no. 8, August 1982, pp. 3-13.
of economic growth in 1970-71. In both USA and Western Europe, a policy of greater demand stimulation was resorted to in 1971-72 which coincided with the world economy's entry into a very expansive phase. Simultaneously, there was a substantial increase in money supply. As a consequence all the OECD countries experienced boom in 1972-73. On an annual basis, there was an increase in output in seven leading industrial countries by 8 per cent during the first six months of 1973. But inflation started forcing governments to pursue tighter economic policies. This was coupled with the quadrupling of oil prices of the OPEC States which exacerbated the recession.

'Harmonization' during the boom was followed by a total lack of co-ordination among the OECD countries during the crisis, which had its manifestation in an uneven distribution of deficits in the balances of current account. In 1975, while the United States and West Germany had a combined surplus of $22.5 billion, Japan and France were in balance, and the OECD countries showed a total deficit of $40 billion. Overall, the volume of industrial output in the OECD countries diminished by 10 per cent from July 1974 to April 1975, and the volume of intra-OECD trade fell by 13 per cent. The most crippling aspect of this economy has been high inflation and extensive unemployment. The slump of 1974-75 was instrumental in raising unemployment in OECD from 8-9 million to over
15 million. According to IMF estimates, unemployment stood at 16.3 million at the beginning, which constituted 5.5 per cent of the labour force. In 1980, the unemployment rate was estimated at 6 per cent. The legacy of past crisis continues even today as a marked slow-down in business is already underway on both sides of the Atlantic. Recession has

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2 See Lars Anell, *Recession, the Western Economies and the Changing World Order* (London, 1981), pp. 50-51. In USA, the Reagan administration is reluctantly bracing for a recession, as evident from the anti-inflation package of budget cuts and tighter credit which could help reduce inflation. However, economists have warned that the indications on recession are far from conclusive and are in part counter-balanced by other factors such as the continuing low level of business inventories and the significant growth in the GNP in the first quarter. See for background Steven Rattner, "Fear of Recession haunts US", *The New York Times New Services*, quoted in *Times of India*, 3 March 1980. The two facets of Reagan's economic policy are: (i) supply side economics, which involves a commitment to a robust economic output and income that will bring about a hike in public revenues that will effectively offset the reductions in taxes that stimulate the same economic expansion. According to Professor J.K. Galbraith, "Expansion will also be encouraged by relief from regulation and by reducing social expenditure... The companion piece is control of inflation". See, J.K. Galbraith, "Free Market Mystics", *New Statesman* (London), 9 October 1981, pp. 14-16. Also see, Alan Wolfe, "Sociology Liberalism, and the Radical Right", *New Left Review* (London), no. 128, July-August 1981, pp. 3-27, and *White Paper on International Trade, Japan External Trade Organisation* (Tokyo), 1980, p. 14. Also see, Francis X Clines, "Reagan stands firm on economic policies", *International Herald Tribune*, 18 November 1982. President Reagan still remains unruffled against mounting Congressional criticism against increased military spending of about $1.6 billion over a five year period which they feel would compound the recession. President Reagan on the other hand insists on making further cuts in non-military spending growth reducing federal budget deficits which might touch $200 billion a year. However, the
affected world trade to such an extent that in 1980 its growth rate has plummeted to 3 per cent from 6.7 per cent in 1979.

As an Economic Survey ominously points out:

In output, this could be virtually a no growth year for the 24 industrial economies - including the US, Canada and Japan... consumer purchasing power will be affected... Europe's latest prices are alarming, with increase at an annual rate of 21.5 per cent in January and February 1980 for Common Market and as much as 26.5 per cent in Britain and 31 per cent in Italy alone. 3

In order to understand the factors contributing to such a deteriorating economic performance in the industrialized economies, OECD had commissioned a report back in 1975 (called the 'McCracken report') which had classified them immediate fall-out from such budget deficits would be U.S. trade deficits, which in turn would contribute to protectionism. Large budget deficits would force the Treasury to borrow money thus raising interest rates which in turn would attract investment money from abroad, thus strengthening the dollar. This would make US exports less competitive, whereas imports would have an edge. This in turn would contribute to continuing depression in US Auto and Steel industry. For details see, Hobart Rowen, "US Economist Warns of Swelling Trade Gap", International Herald Tribune, 18 November 1982. Also see, Philip A. Klein, "Reagan's Economic Policies : An Institutionalist Assessment", Journal of Economic Issues (Lincoln), vol. 17, no. 2, June 1983.

3 Asiaweek (Hong Kong), vol. 16, no. 17, 2 May 1980, p. 36.
under three headings: shocks, errors of policy and changes in basic relationships which are 'endogamous' to the economic system. The shocks include hike in food and oil prices and the failure of the fixed exchange rate system that had held sway over the world's financial relations during 1980s. This was compounded by the almost reckless expansionary monetary policies which led to the boom of 1972-73 with consequent rise in inflation.4

Because of close financial ties among industrial economies, domestic inflation in one country infected its neighbour, setting off a chain reaction. According to the McCracken report:

4 However, one of the most important factors which helped in spreading inflation among the industrial economies was the collapse of the pegged rate system which led to rapid increase in international official liquidity: from $ 78.4 billion in 1969 to $ 183.7 billion in 1973 and $ 227.4 billion in 1975. Between 1970 and 1973, eighty five per cent of the increase owed to increases in foreign exchange resources. According to the McCracken report, creation of reserves on this scale contributed to the synchronised boom of 1972-73 and was therefore inflationary. James S. Earley, "What Caused Worldwide Inflation: Excess Liquidity, Excessive Credit or Both?", Review of World Economics (Tubingen) Band 117, Heft 2, 1981, pp. 213-43.

When a large number of countries are simultaneously pursuing expansionary policies, the combined multiplier effect for the system as a whole is stronger than an individual country would expect to be applicable to its own economy if it had acted alone; the OECD area is much less of an open economy than each of its components. 5

However, more than the internal and international factors contributing to inflation, the national governments had by their failure to exercise domestic discipline over their money supplies in 1971-72, led to the inflation of 1973-74. Close examination of the factors contributing to inflation however shows that none of them were essentially endogenous to the economic system. Increases in food prices during 1972-73 were for example partly due to inclement weather and poor harvests around the globe. Policy decisions were largely influenced by political factors, and were influenced by drastic changes in US and Canadian policies concerning food reserves, and Soviet decisions to import foodgrains rather than to cut down on livestock herds. 6 The hike in price of oil in 1973-74 owed more to government decisions

5 Keohane, ibid., p. 111. The Western governments resorted to easy monetary policies tempted by huge foreign exchange reserves in 1970-73.

influenced by economic and political factors, than to product of market forces. Similarly the dissolution of the 'Bretton Woods Regime' in 1971 may have been influenced by conditions reflecting political and even military action (e.g. the Vietnam war).

So we find that the 'avoidable policy errors' of 1970–72 owed more to political decisions which had induced an inflationary bias in policy. 7

Recession and Stagnation

The McCracken report had viewed the recession of 1974–75 as the tardiness in government decisions to control inflation. It observed:

There seems little doubt that a substantial recession was intended and most of us would argue, necessary to limit the risks of wage explosions and an accelerating price level - but also little doubt that it turned out to be steeper and deeper than initially expected. There was underestimation of the simultaneous lagged effects of restrictive policies and the external shock of the oil price increase, both acting concurrently in nearly all countries, interacting with - and reinforcing - progressive loss of confidence on the part of both business and consumers. 8

However the report did not sound optimistic about recovery, for it felt expectations of high rates of inflation and

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8 Keohane, n. 4, p. 114.
bleak prospects of future growth had stunted the normal, self-correcting forces present in market economies. It felt that the industrialized countries were in a dilemma: if they increased the pace of economic activity it would fuel inflationary expectations in commodity and product markets. If it failed to do so, it would dampen the spirit of the business circles thus perpetuating stagnation. So the report was 'prudent' enough to suggest a "narrow path to growth" that would do away with both inflation and stagnation:

It would involve a rate of expansion sufficient to encourage a recovery in investment both through spreading overhead costs and improving profit margins and through creating expectations of the need for additional capacity in the reasonably near future. The upper limit is set by the point at which a rapid increase in aggregate demand would reverse the trend towards a gradual winding down of inflationary expectations. 9

The idea of a 'narrow path to growth' could only be translated into action if there was a range of activity that could boost up confidence more than it would have reinforced inflationary expectations. 10 According to Robert O. Keohane, a critic of the McCracken report:

In economic terms, the "activity-elasticity" of confidence must be greater, across some

9 Keohane, n. 4, p. 114.
10 Ibid., p. 115.
range of activity, than the "activity elasticity" of inflationary expectations. Otherwise, moderate stimulative policies will worsen inflation more than they will increase investment. Yet despite the vital role of confidence and inflationary expectations in its recommendations, the report makes no attempt to present data on these factors, much less to estimate how they would react to different rates of economic growth. 11

Although the McCracken report failed to provide a coherent explanation to macro-level political-economic events such as inflation, it was unique for two reasons: (i) it raised some crucial questions about economics and politics in the capitalist democracies of the OECD. Its recommendations for economic policy suggested the need for political change although it remained silent on the questions of feasibility and consequences of such change. 12 (ii) The report went so far as to imply that for the sake of economic prosperity, modern democratic states need to exercise more discipline on their economies, while resisting the urge to confer short-term benefits on their citizens by resorting to large-scale public funding.

11 Ibid.

12 Also see, Edward S. Malecki, "The Capitalist State: Structural Variation and its Implications for Radical Change", The Western Political Quarterly (Salt Lake City), vol. 34, no. 2, June 1981, pp. 246-69.
More credible explanations have however come from critics like John Eatwell, who feel that the inflation and recession are clearly related to changes in institutional structure of capitalism, on both national and international scales which have taken place since the Second World War. These changes have resulted in a variety of shifts in the balance of power between labour and capital and the balance between nations' capitals (notably the relative economic decline of US economic hegemony), with consequent changes in the role of the state. These shifts exacerbate the contradictions of capitalism and the contradictions manifest themselves in economic and political conflict. 13

If we accept this argument then we would also have to infer that the decline of US hegemony has (i) generated a degree of confusion in international money markets since the 1930s; (ii) engineered conflict over the distribution of real income between the primary producer and the metropolitan countries resulting in a cycle of rising prices. Thus it would logically follow that these contradictions, lying at the roots of domestic and international depression are resolved and recreated in the process of inflation. 14


An Assessment of the Present Economic Crisis

Although the initial symptoms of depression had become pronounced by 1979, it was not unexpected for there had been a gradual decline in world gross domestic product from an average of 4 per cent in the 1970s to 3.8 per cent in 1979, to just over 2 per cent in 1980, which again dropped to 1.2 per cent in 1981. This decline was best reflected in world trade, whose average annual growth rate fell from about 7 per cent in 1976-78 to 6 per cent in 1979, 1.5 per cent in 1980 and 0 per cent in 1981. According to latest data released by GATT (General Agreement on Trade and Tariffs) global trade has not registered any expansion despite the economic recovery now under way in the industrial countries in the first seven months of 1983.

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16 GATT's report on International Trade 1982-83, quoted in The Statesman, 6 September 1983. This assessment comes after the decline in world trade by 2 per cent in 1982. Taking into account the limited gains up to mid-year, world trade would have to increase by a future 2 per cent in second half of 1983 to register a modest growth. This however is subject to continuing recovery and an absence of any major disruption in international trade on financial systems.
Monetary and Financial Crisis

Monetary and financial events have aggravated the crisis. The US dollar's strong appreciation at the end of 1980, brought about a depreciation of all currencies of the leading market economy countries. This owed to renewed pressure on US interest rates, and an increase in US money supply to the tune of $2.3 billion (1982 figure). US interest rates in turn were greatly influenced by US budget deficits which have been rising steadily. For example, earlier it was expected that the US deficit for fiscal year 1983 would be about $43 billion, but new projections are now pegged at $91.5 billion.


Federal Budget Deficits

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<tr>
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<td>66.4</td>
<td>4.0</td>
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US Interest Rates and its Impact on Europe

The US administration's policy on interest rates and the dollar might have undermined Europe's recovery from recession and could place new strains on the already fraught relationship between the US and its EEC allies. The three immediate causes of concern over US financial policy were high interest rates, the US budget deficit and 'benign neglect of the dollar'. However, the Reagan administration had earlier indicated that it would not succumb to European pressure to change its international policy on the foreign exchange markets. The 1982 Economic Report of the US President was even brazen enough to declare that the Federal Reserve will only be asked to intervene when it is "necessary to counter conditions of severe disorder on the financial markets". The report rejected charges that current US monetary and intervention policy was a case of 'benign neglect' and argued that the best contribution the US could make for preventing foreign exchange rate relativity was through price stability.19

19 John Palmer and Alex Brummer, "High US rates damage Europe", The Guardian, 21 February 1982. J.K. Galbraith, commenting on Reagan's economics has observed: "most would urge a firm fiscal policy as opposed to a tight monetary policy; better high taxes than murderous interest rates. There is also generally emerging support for an income and price policy, a recognition that there is not a modern highly organized economy that can combine high unemployment and reasonably stable prices without one". For details see, John Kenneth Galbraith, "An Essay somewhat in Defense of Economists", International Herald Tribune, 2 April 1982.
The irony of the situation is that the overpriced dollar has also adversely affected the US economy: in USA it implies an increasing pressure for trade protection for the weak industries and export subsidies for the strong. What is however ominous is the fact that the international value of the dollar would continue to be swung by huge flows of speculative money chasing the interest rates, rather than being set by USA's basic strength as an industrial producer and leader.

The United States by pursuing a high interest rate policy has not only undermined the concept of 'interdependence' it is so fond of harping (by exporting slow growth and unemployment to the industrialized world) but has also virtually blocked the access of many developing countries to commercial markets for finance. The interest rate burden for middle income developing countries has been rather heavy. As the International Monetary Fund noted in its 1981 report: "Interest payments on debt almost doubled between 1978 and 1980... and that was before the rise of rates.

20 The overpriced dollar by reducing the price of US imports e.g. oil, has however made a major contribution to the drop in the American inflation rate. This is however negated by high unemployment rate which surged to a post-war high of 9 per cent of the workforce (March 1982). For details see, Alex Brummer, "Slump in US brings record post-war Unemployed", The Guardian, 3 April 1982.
to historically high levels this year (i.e. 1981). In 1981, IMF's lending was at a record level setting fears within the Fund about a serious depletion in the level of usable currencies. But this would not soften the attitude of United States which refused to accept proposals for a fresh allocation of Special Drawing Rights (SDRs) or a new round of quota increases. The United States tried to nationalize its stoicism by saying if it had agreed to such proposals it could increase world liquidity at a time when there was so much inflation. The United States also pressurized IMF to tighten its conditionality at a time when recessionary pressures generated by the industrial economies have sharply reduced the growth rates within the developing world.


22 See, Joseph Gold, "Development of the SDR as reserve Asset, Unit of account and Denominator: A Survey", The George Washington Journal of International Law and Economics (Washington), vol. 16, no. 1, 1981, pp. 1-64. The developing countries would like to see: (i) a wholesale reform of the International Monetary Institutions; (ii) greater financial resources; (iii) more sensible decision-making, and (iv) an increase in the amount of soft-lending through the International Development Association. However, it is unlikely that these demands would be concerned, for we find the attitude of the United States (which had its reflection on IMF's lending policy) hardening. But this has also sparked off revolt among such leading borrowers like Brazil which is spearheading growing opposition to tough IMF loans in Latin America. For details, see, David Lipsey, "Brazil Rouses Fund Rebels", Sunday Times, 4 September 1983.
United States in contrast to its European allies has displayed a far more cavalier attitude towards the economic aspirations of developing countries which if realized could have contributed to a faster world economic recovery. This became evident the way it had cold shouldered the proposal for an IMF Energy Affiliate which had not only drawn support from most of the developing countries but also such staunchly pro-US industrial nations like Britain. Ironically energy happens to be one area where the industrial and developing countries have managed to find common ground. United States has been an exception among industrial nations in not reacting favourably to the Third World's (especially non-OPEC countries) efforts to gain self-sufficiency in energy which is crucial for strengthening the infrastructure and balance of payments position. Although 27 per cent of World Bank lending is for energy, it is possible that the

23 An important feature of India's borrowings from the World Bank was that a very high proportion of them was for energy development. Four large IBRD loans, about 75 per cent of the total funds were approved for two power projects (one a hydro-electric plant in the eastern region and the other a transmission network in Southern India), two Oil and Natural Gas Commission (ONGC) programmes (for producing gas from the South Basin field, west of Bombay) and exploring the commercial potential of hydroelectric power plant project, which has also received an IDA credit of $170 million. For details see, *The Hindustan Times*, 16 September 1983.
US Government might exert pressure to curtail its operations in the Third World's energy sector. A report prepared by John E. Swearingen, Chairman, Standard Oil Company, for National Petroleum Council of USA has urged the US Government to see that the World Bank and other official aid institutions do not displace private investment by providing funds at subsidized interest rates for speculative petroleum exploration in the Third World. The report has urged that the World Bank "confine the bulk of its energy sector activities to financing infrastructure improvements that will aid petroleum exploration and development in the Third World, and to aid downstream investments needed to utilize some or all of any oil found within local economies". Pipelines, distribution networks and marketing facilities were specifically cited. The report also suggested that the Bank "could assist in organizing existing exploration data prior to private company bidding and in some cases act as a catalyst to subsequent private exploration". The report is also significant, for while urging the US Government to substitute the World Bank with private US oil companies in the Third World's energy sector it has also asked for elimination of certain 'ambiguities' and inconsistencies in the Foreign Corrupt Practices Act and in anti-boycott legislation to
remove unnecessary hindrances on US companies operating abroad.\textsuperscript{24}

**TRANS ATLANTIC DIFFERENCES ON ROLE OF IMF/WORLD BANK**

While USA's espousal of the cause of its private oil companies in the Third World is understandable,\textsuperscript{24a} its


\textsuperscript{24a} Brian Levy "World Oil Marketing in Transition", *International Organization* (Ithaca), vol. 36, no. 1, Winter 1982, pp. 113-35. US oil companies have almost completed their withdrawal from the chemicals sector in Europe and are vigorously exploring for oil in third world markets like China.
attempt to dilute the role of soft-loan multilateral institutions like the World Bank is deliberate. However, this has not met with approval from Europeans. For example, Britain's Lloyds Bank feels that there should be a bigger role for official international agencies such as the International Monetary Fund and World Bank in channelling international capital flows, with commercial banks playing a secondary role and private investment stepped up. According to the Lloyds Bank the following measures should be taken to ease the world monetary crises:

(i) IMF should borrow on the Euromarkets and the World Bank should provide cover in the form of guarantees and political risk insurance for poorer countries to allow them to raise bond issues;

(ii) There should be a gradual move towards fixed exchange rates either by merging currencies into blocks such as the European monetary system or by general adoption of target zones. A return to a system of par values would have to be taken slowly because of the huge flows of hot money. It would be helped by closer co-ordination


of interest rate and economic policies and the United States would have to take a lead.\(^{27}\)

(iii) Special Drawing Rights (SDRs) should be extended to gradually replace the currency reserves and other reserve assets in order to impose greater control and management on international liquidity and help recurrence of inflation;

(iv) The IMF, Organization for Economic Co-operation and Development (OECD), Bank for International Settlements (BIS), the World Bank and development banks should co-operate more closely, without losing their incentives. This would be easier than forming a new institution to act as a world monetary authority, which would be needed to lend authority and discipline at the core of the system;

(v) There should be changes in the rigid division of countries, into developed and developing in order to recognise more varied interests and wealth creating ability.\(^{28}\)

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27 Paul Volcker, Chairman of the United States Federal Reserve Board, probably realises this, for in a break with Reagan philosophy, he has recommended a policy of modest intervention in currency markets to control the erratic dollar. However, like most conservatives he also is ambivalent, for he is also reportedly opposed to the idea of a new Bretton Woods conference to revise the monetary system but is reasonable enough to ask for a return to a system of fixed exchange rates. For details see, Bailey Morris, "Fed Chairman Recommends Modest Intervention to Control Dollar", The Times, 19 April 1983.

28 Peter Wilson-Smith, "Lloyds Chairman seeks a Greater Role for IMF and World Bank", The Times, 13 April 1983.
Till now United States has shown little interest in taking the suggestions of Lloyds Bank seriously. Probably its future strategy would be contingent on the outcome of the struggle between London, traditional centre of Europe's money market, and New York to corner the Euro-currency market. The major objective of US bankers to establish IBF (International Banking Facilities) was to radically increase US share of the $1.5 trillion Euro-currency markets. The US Federal Reserve Board has eased its regulations governing domestic banking enabling transfer of sizeable Euro-currency deposits to New York and other US money centres, thus enhancing the earning power of American banks and allowing business customers to deposit and borrow funds at competitive international interest rates. Similar to foreign branches of US banks, the IBFs can accept deposits free of the Fed's reserve requirements and interest rate limitations. This

29 Dun's Business Month (New York), vol. 119, no. 3, March 1982, pp. 101-2. The Euro-currency market was formed thirty years ago, when China and Soviet Union began depositing their dollar earnings in Europe rather than in the United States, which they feared might block their funds. As European and Japanese trade grew, the Euro-market expanded to include all major international currency, and today provides, up to 68% of all international trade financing and the bulk of banks' international deposits.
allows them to compete for funds of foreign businesses in US and foreign subsidiaries of US companies. However, in order to prevent leakage of deposits from the US market and insure the Fed's control of the domestic money supply, the IBFs cannot deal with residents in US or finance domestic activities. The fact that the incentives offered by the US government are paying rich dividends is proved by the success of the IBFs in attracting an estimated $80 billion of funds. 30

The European bankers have, however, remained sceptical of New York's growth as an international banking centre -- which they think would be slow and limited. In the tussle between Europe and US the big losers happened to be the 'artificial' off-shore centres of the Bahamas and Caymans, which have been accused by the Reagan Administration and the US Congress of engaging in illegal currency activities and a two-year study by the Senate Sub-committee, on investigations estimated that as much as $50,000 or (£ 34,000 or) a year is "laundered" or hidden in off-shore tax havens by US Corporations seeking to avoid the tax laws.

30 By the end of April 1982, the 175 IBFs within the US with assets over $50 million reported total assets of $110.8 billion of which $87.5 billion was in New York, which had 101 of the facilities. The US in total had a total of 328 IBFs. The earlier domestic regulations had forced many US banks to do their international lending and deposit taking at overseas subsidiaries, whether in London, the Bahamas or Bahrain. For details see, Robert A. Bennett, "New Banking Zones Boom in US", International Herald Tribune, 11 May 1982.
According to Bailey Morris, a noted financial analyst "US corporations and individuals seeking to launder their money off-shore are turning increasingly to British Commonwealth countries in the Caribbean and South Atlantic which court their business with tax breaks and stringent secrecy codes." The Senate has suggested a series of recommendations to correct these abuses. These include (i) Creation of an International Intelligence gathering operation for banking transactions, (ii) negotiation of country-to-country agreements to soften secrecy laws and strengthen prosecution laws, (iii) tighter control on the US offices of foreign banks, and (iv) expanded regulatory powers for US customs and banking authorities. Although all these measures are aimed at strengthening the IBFs, the US Government would like to have a say in the Euro-currency market which has been a

31 Bailey Morris, "Call for tighter controls on Currency Laundering", The Times, 23 March 1983. These tax havens lie within an arc extending from Bermuda to the Cayman islands, and include Arquilla, Antigua, the Bahamas, Barbados, Monsterrat, St. Vincent, the Turks and Calicos.

traditional preserve of the Europeans. This explains why the Senate report has recommended that the US administration launch a study of the $2,000,000 cr. eurocurrency market to arrive at a better system of control. This might include the creation of an international agency, supported by a network of treaties and administrative agreements to regulate Eurobanking by the central banks of the main trading nations.

The lack of regulation in the rapidly expanding Euromarket had led to widespread abuse culminating in the collapse of the Italian Banco Ambrosiano, in 1982, when it was discovered that $1,400 m. had mysteriously disappeared as a result of shady offshore transactions.

While easier regulations would make New York a tough competitor, but in the long run it would be difficult to dislodge London from its formidable position. While United States money centres might have innate, time-gone advantages in wooing US clients, it would not enjoy the same advantages as London, when it comes to doing business with the oil producers.

of the Middle East, who provide the Euro-market's liquidity. Moreover, US bankers admit that the OPEC countries are reluctant to have transactions with American banks having observed US freezing Iranian assets in 1980 with impunity. London also has another distinct advantage: English Law predominates in Euromarkets contracts, since it is 'demonstrably' more flexible and well adapted to Euromarket conditions.33

SLOWDOWN IN INTERNATIONAL BANKING ACTIVITY

While the tussle between Europe and United States goes on for the lion's share of the Eurocurrency market, international banking activity has slowed down. According to Bank of International Settlements,

the Euromarket's rate of expansion slowed markedly in the first three months of 1982. There was an overall 14 per cent decline in new Eurocurrency bank credits and a 25 per cent drop in new loans to non-OPEC developing countries. By the end of the first half, activity had recovered with the volume of overall bank credits up 20 per cent from the same period a year earlier and lending to non-OPEC countries ahead 8% per cent. Since then, however, in the wake of Argentina's

33 The other reason for London's pre-eminence is the network of communications, specialist bankers and contacts built up since the international loan market boomed in the early 1960s. For details see, Peter Rodgers, "US Challenges London's Deal", The Guardian, 17 May 1982.
financial difficulties and a widening concern about imprudent lending by banks, particularly in the US, Euromarket has slowed considerably. 34

The widest measure of overall international activity in terms of gross external assets grew at a markedly slower rate, presaging a similar trend for international lending. It is significant that banks in the US accounted for all of the small $3.5 billion growth of the inter-bank market for 80 per cent of the total $30 billion increase in net new lending to non-OPEC developing countries. 35 The success of the US banks owed particularly to their new tax-exempt international facilities in New York, accounting for a large part of the total first-quarter growth of international banking business. Part of the increase in external assets of US bankers

34 Carl Gewirtz, "Euromarket expansion slowed in first quarter, BIS says", International Herald Tribune, 30 July 1982, it is significant that over the past decade, the Euromarket has expanded by an average of about 20 per cent every year.

35 According to Bank of International Settlements, outstanding feature of the second quarter's (1982) developments was the $37.5 billion expansion of international activity by banks in the United States, $10 billion greater than the market's overall expansion. In contrast, banks in Europe, cut their overall activity by $4.7 billion, a big switch from the $8.7 billion increase in their activity registered in the first quarter (1982). For details see, Carl Gewirtz, "International Banking Activity Slows, Shifts towards US", International Herald Tribune, 2 November 1982.
totalled $27.6 billion, well down from the $40.7 billion expansion registered in the fourth quarter.  

However, there has been a slump even in the US money market. The volume of loan syndications excluding forced reschedulings was down from a year ago and interest rates remained high. Explanations offered range from a tightening of policy by a Federal Reserve Board worried about an excessive growth of the domestic US money supply to 'seasonal' aberrations related to end-quarter book keeping operations by the companies and end-fiscal operations of the Japanese. According to Arnold Simkin of Merrill Lynch, a consultancy firm, the focus of concern is the non-dollar based banks that have been active participants in the syndicated loan market. Many of these institutions neither had nor have a natural base of dollar deposits that could be used to

36 Jonathan Power, "Among the World's bankers, a loss of Nerve", International Herald Tribune, 30 July 1982. Banks in Japan were the only ones to show a sharp acceleration in the growth of their external assets and deposits in comparison with the fourth quarter (1982). Banks outside the US were not so fortunate for they offered further withdrawal of deposits by official monetary institutions - a decline of $4.5 billion in the first quarter (1982), bringing the cumulative drop since the autumn of 1980 to $29 billion.

37 Dollar interest rates remained high, particularly 'real rates' - the residue of the nominal rate of interest less the rate of inflation. Real dollar interest rates currently are estimated at 7 per cent, up from 6.6 per cent at mid-1982, 5.5 per cent at end 1981, and 0.4 per cent at end 1980. For details see, Carl Gewirtz, "Continued high Rates, drop in Lending worry Analysts", International Herald Tribune, 23 March 1983.
finance their loans. The dollars that they lent were dollars that they borrowed in the inter-bank market. But in many cases, the dollars lent are not earning the interest income needed to pay for the cost of the dollars borrowed.

Countries that have rescheduled their debts insist that they are current on paying interest and are only postponing the repayment of principal. But in reality, banks are forced to lend the borrowers the money that they need to meet their interest payments, troubled loans on which interest is being kept current do not run afoul of auditors, but it does nothing for the cash flow position of banks that suddenly do not have the anticipated income needed to pay their own expenses. These banks either have to bid for more dollars in the Euromarket's inter-bank market, putting upward pressure on interest-rates, or borrow money in their home market and sell those funds to buy dollars, putting upward pressure on the exchange rate.

United States bankers are also worried about the liquidity of the inter-bank market, since early 1982, the Swiss have sharply reduced the flow of funds, that they channel into the market. OPEC countries, once major suppliers of dollar deposits, are, with the exception of Saudi Arabia and Kuwait, themselves now running a deficit and making increasing demands for loans. Some analysts feel that even

Saudi Arabia, which has been a major purchaser of US government securities, may be feeling the pinch, ... while Saudi Arabia continues to roll over maturing US investments, it may no longer be pumping, new money into the US
market. If true that also could affect the level of interest rates as Washington needs to finance a record budget deficit in 1983. All of this spells continued upward pressure on dollar interest rates and continued reluctance of banks, especially non-dollar based banks, to undertake new commitments in the loan market. 38

US BANKING POLICY, MULTINATIONAL AID INSTITUTIONS AND EUROPEAN RESPONSE

International banking crisis provides us with an interesting case study where there is sharp divergence in policy between Europe and United States on the question of maintaining a viable world financial system. The Reagan Administration apart from following a contractionary banking policy is brazen enough to reiterate its determination to use multilateral aid institutions like the World Bank to follow its policy more directly rather than allowing it to contribute to world financial stability.39 In the case of World Bank this could be done for example by implementing a plan for the "maturation" of borrowers (such as India and China) out


of the "soft loan window" and for graduating higher income borrowers out of the IBRD into the private markets. 40 A US Treasury study, multilateral development banks prepared by Treasury Under Secretary Dr Beryl Sprinkel, recommends that future U.S. support for the multilateral development banks should be designed to encourage the bank's promotion of adherence to free and open markets; emphasis on the private sector as a vehicle for growth; minimal government involvement; and assistance to the needy countries who demonstrate an ability to make good use of available resources by adopting appropriate domestic economic policies. 41

The political motivation of US aid becomes evident from the fact that in the last 10 years, the United States has nearly doubled to 41 per cent the share of its aid programme that is politically motivated, as opposed to development oriented. This is also reflected in the fact that the Near East, primarily because of aid to Egypt and Israel, now accounts for nearly half US aid worldwide. 42


While increasing the quantum of aid which is politically motivated, it has spared no efforts to curb those activities of the World Bank which could have benefited the developing countries. It must be remembered that under Robert McNamara, the World Bank in the late 1960s and 1970s, had concentrated its activities on the very poorest in Africa, Asia and Latin America. According to Michael Prest, a commentator on World Bank's operations, "His strategy was in some measure a reaction against the 'trickle-down' theory and against the concentration on industry and infrastructure at the expense of the rural poor". What the United States wanted was a virtual abandonment of this "missionary" policy and has indicated that it is at a loss to understand why the Bank should deal only peripherally with the macro-economic policies of borrowing governments.

43 Michael Prest, "How Reagan threatens the Aid Givers", The Times, 28 September 1983. The key agency in this strategy was the IDA set up in 1960. The IDA makes interest free loans over 50 years to the most indigent people charging only a 0.75 per cent service fee. Over the last four years of IDA 6, for instance, the association has disbursed almost $12,000 million. Although it is a much smaller lender than the bank itself, the IDA is especially effective because the absence of interest rates mean that net disbursements (borrowings less repayments) are far lower. For a different view see, Ernest Feder, "The New Colonial Office", Economic and Political Weekly, vol. 18, no. 8, 19 February 1983, pp. 262-6. Also see, Richard Krooth, "The New Financial hecure", Economic and Political Weekly, vol. 18, no. 14, 2 April 1983, p. 523.
The World Bank on the other hand has sought to clarify that US government's misgivings about the World Bank are misplaced. A.W. Clausen, the World Bank Chief has emphasized the World Bank's role as a "catalyst for investment flows to the developing nations". He has rightly called attention to the fact that the institution's project resources financed the import of material, equipment and technical skills in a big way. US companies won "scores of contracts each year for equipment used in our third world ventures", and the scale of these contracts alone constituted "a sound self-interest argument for US support of the World Bank if ever there was one". However, in an apparent concession to US sentiments, the World Bank has conceded without any explanation one of the significant demands of the Reagan Administration - that a doubling of the "gearing ratio" to expand the Bank's resources for lending should not be allowed.

But such concessions apparently did not have the desired effect on the US Administration. So we find the US administration talking about reducing its share of the cost of IDA, from 27 per cent to 25 per cent, with a $750 million

44 N. Ram, "A World Bank case for Private Investment", The Hindu, 19 February 1982. The World Bank has declared that it is not going to recommend a change in the Bank's capital gearing ratio from the one-to-one ratio it presently enjoys. This refers to the fact that under its articles, the World Bank may not lend more than the equivalent of its capital and resources, a very conservative operating formula.
annual US contribution, that would give the UDA a $9 billion, programme for the three year period. But the IDA says that it would need $15 billion just to keep up with inflation and has been making a demand for $16 billion.45

In an interesting development, we find the World Bank pressing on the British government the urgent need for extra funds for the International Development Association, the Bank's concessionary lending over IDA faces collapse in 1984, largely because of US's failure to pay its agreed contribution. The World Bank's chief even went to the extent of asking Britain (and possibly Canada) to use the opportunity of the Williamsburg Economic Summit in May 1983 to impress upon US the gravity of the situation.46

Although it is not known whether Britain could prevail on United States to loosen its purse strings, but probably it realises along with other West European industrial powers that because United States already sells about one-third of its manufactured products to developing countries, encouraging Third World prosperity is in its own interest.47

46 Michael Prest, "World Bank seeks Britain's help to make Americans pay up", The Times, 5 April 1983.
47 Forcing developing countries to deflate their economies would not only weaken demand for imports, but also create political and social upheavals further hampering economic growth. Also see, Volkmar Kohler, "Global Order - The West and the Third World", Aussenpolitik (Hamburg), vol. 33, no. 3, 1982, pp. 282-4.
A brief written by a team of financial experts for the meeting of the British sponsored Commonwealth Ministers of Finance in Trinidad in September 1983 also did not approve of USA's dilution of the role of IMF which essentially deals with countries' short term troubles with foreign payments. It has pleaded for more funds for the IMF after raising considerable doubts as to the adequacy of the Fund's resources, even after the quota increase. It has advocated "more frequent quota reviews and has urged the IMF" to go into the market and use its standing to borrow money at cheaper rates than the developing countries can; then it can lend to desperate would-be borrowers at a lower than market rate". Another suggestion, which though unpalatable to the Reagan Administration, was made to reactivate the SDR by allowing the IMF to increase its distribution. This would have conformed to Brandt Commission's suggestion of a major new allocation of Special Drawing Rights which could provide

a major impulse to recovery. 49

**Policy Implications**

The international banking crisis provides us with a test case where Europe has refused to succumb to US pressure and has displayed considerable maturity in approaching a problem which if mishandled, could disrupt the world's trade and financial systems. For example, European central banks are refusing to consider providing part of a $6 billion package in emergency funds the IMF is seeking, unless the Reagan Administration succeeds in securing congressional approval for an increase in the US contribution to the International Monetary Fund.

According to Carl Gewirtz, a leading financial analyst "The Europeans are withholding approval of the emergency loan thinking this will pressurise Congress to approve the US quota increase and the IMF is halting new loans thinking this will pressure all its leading

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49 SDRs are credits entered in the ledgers of the IMF on which countries can draw to obtain the foreign currencies they need to settle their payment deficits. The major advantage of a new SDR issue compared with quota increases or borrowing by the fund is that it is not only fast but it does not create repayment obligations thus cutting down on the debt burden. Also see, Douglas C. Smith, "The Global Economy and the Third World: Coalition or Cleavage", *World Politics* (Princeton), vol. 29, no. 4, July 1977, pp. 584-609.
contributors to cough up the necessary funds." Also at issue is whether the quota increase would alter the amount of money borrowers can obtain from IMF. While the Reagan administration remains unmoved by the plight of developing nations and makes it clear that it would like to keep the level of access unchanged, many of its European partners would like to see an effective 15 to 25 per cent increase in the amount of money countries can borrow. The latest compromise that would limit borrowings by member nations to 102 per cent of their quotas or deposits in the IMF over the next three years was brought about under combined European, Japanese and Canadian pressure who insisted that a more

50 Carl Gewirtz, "Brinkmanship on eve of IMF Gathering", International Herald Tribune, 26 September 1983. According to Carl Gewirtz, "The level of commercial lending so far in 1983 is well short of the informal 7 per cent, the growth target the IMF had set, and some impetus is needed if the banks are to become more active."

generous allotment be given to countries with serious balance-of-payments problems.\textsuperscript{52} Probably it was the pressure exerted by its European allies that had induced President Reagan to warn the conservative members of his Republican Party not to block a $8.4 billion appropriations bill for the International Monetary Fund. He also had to clarify that failure by Congress to participate in a proposed 48\% expansion of the IMF's capital would result in a withdrawal by other major nations.\textsuperscript{53} What he deliberately concealed was the fact that US had a vested interest in seeing this loan granted for

\textsuperscript{52} For details see, Hobart Rowen, "IMF finds agreement on access", \textit{International Herald Tribune}, 27 September 1983. The compromise would allow member nations in such circumstances to draw 125\% of their annual quotas for a three-year term or a maximum of 375\% per cent. The 'compromise' was crucial for a continued deadlock would have shaken the confidence of the world in IMF's ability to manage the debt crisis and would have induced commercial banks to reduce their lending in third world countries. The European Commission has decided on a possible compromise that would limit the reduction in access to around 125\% per cent of the quotas, once they are agreed upon.

\textsuperscript{53} In pressurising Congress to pass the $8.4 billion loan for the IMF, President Reagan stressed that the money does not come out of the budget, but would be a loan. For details see, Hobart Rowen, "Reagan warns Conservatives against blocking IMF Funding", \textit{International Herald Tribune}, 28 September 1983. Another factor which might have induced President Reagan to prop up IMF is the reported emergence of a powerful, though new coalition of Latin debtors and developing countries of the Commonwealth, for details see, William Keegan and Hugh O'Shaughnessy, "IMF Meetings Sabotaged", \textit{Observer Business}, 25 September 1983.
although apparently it was expected to contribute to a sound financial system, its basic aim was to support trade and more than two million American jobs.54

However United States wants Europe to bear the major share of its burden of salvaging the IMF. But Europe has refused to oblige and so we find the Group of Ten representing the world's richest nations refusing to approve a request by the International Monetary Fund for emergency loans to fill a $ 6 billion to $ 8 billion "commercial gap" that IMF is likely to face by the end of 1983.55 The Europeans in the Group of Ten have especially expressed their resentment at the US Congress's delay of approval for the $ 8.4 billion US contribution to enlarge resources for the IMF. France, which has been the most vocal critic of the US has complained that IMF in seeking the $ 3 billion bridging loan did not

54 It is significant that one out of eight jobs in manufacturing depended directly on US exports. For details see, International Herald Tribune, 30 September 1983.

55 For details see, Hobart Rowen, "Group of Ten turns down IMF request", International Herald Tribune, 16 September 1983. IMF had sought $ 3 billion in emergency funding from the central banks of the major industrial nations to be matched by $ 3 billion from Saudi Arabia.
ask the United States to participate. The major industrial countries are also opposed to allowing the IMF to borrow in the commercial market for this might be construed as a direct bail out for commercial banks, which are refusing to lend directly to Third World countries, but which would be eager to lend to IMF.

It is significant that of the 30 per cent commercial credit extended by banks to developing countries, more than two-thirds went to Latin America. Of the latter, two-thirds were accounted for by Mexico, Brazil and Argentina. So if

56 IMF however believes that asking the US to share in the $3 billion would make it more difficult to get the $8.4 billion appropriation through Congress. It was partly correct for infighting over money for housing, loans to communist countries, and responsibility for the world's debt problems has complicated the Reagan Administration's task of winning approval in Congress to the IMF Bill. For details see, Clyde H. Farnsworth, "Reagan has new troubles in getting Congressional Passage of IMF Bill", International Herald Tribune, 13 September 1983.

57 It is significant that commercial banks have formed an association of their own called Institute of International Finance which is Washington based. The membership includes 180 of a possible 'universe' of 300. Seventeen out of the 20 banks with international exposure exceeding $10 billion are members. Although the IMF has been supportive of the Institute, it would prove difficult "to sort out an appropriate working relationship that will not sacrifice the principle of confidentiality. IMF interests overlap with the banks, but they are on opposite sides of the bargaining table." For details see, Alena Wels, "Banking on each Other", Observer Business, 9 October 1983.
the IMF is allowed to tap the commercial market, it would bail out the US banks.

As the US has not succeeded in persuading Europe either to bail our IMF, or allowing the latter to tap the commercial market for funds it would have no option but to induce the Congress to undergo a change of heart. It is unlikely that the Congress will withhold permission to the IMF bill for the Congress knows too well that its action would bail out none other than US commercial banks. From the foregoing analysis it is obvious that although USA's tough stand on the question of revitalising the World Bank and the IMF is apparently aimed at punishing the 'irresponsible' private commercial banks for their lending to Latin America in 1980 and 1981, it is motivated by the following factors: resentment against the third world, strong suspicion of multilateralism, and constraints upon the use of American

58 Out of $300 billion owed by the non-OPEC countries, 2/3rd are owed by the countries in the US backyard. For details see, ISG, "IMF's Liquidity Gap", Economic and Political Weekly, vol. 18, no. 29, 24 September 1983, pp. 1647-8. The latest stratagem employed by the IMF to cajole Europe to come to its rescue was to talk about its 'liquidity crisis'. However, European countries rightly suspect that its liquidity crisis is exaggerated. Going by the data provided by the Fund for the first six months of 1983, it is most unlikely that the purchases during the whole year would total more than SDR 13-14 billion (as against 1982's SDR 11 billion) as against the immediately realizable resources at hand which was to the tune of over SDR 25 billion.
power, because of refusal by Europe to toe its line. Commentators like David Watt however feel that it is necessary for both Europe and United States to take a unified approach in solving the international banking crisis:

the enlightened self-interest of the West and the northern hemisphere may require a more flexible and co-operative approach. President Reagan's address to the Bank/IMF meeting in October 1983 for instance combined support for the Fund in principle with a tenacious resolve to prevent its being able to expand in practice. The rescue of Mexico in 1982 and the rescue of Brazil now being negotiated are evidence that in a crisis, the instinct of self-preservation overrides dogma and suspicion. These countries cannot be allowed to default, for if, they did, a major financial crisis would follow. 59

However, the United States hardly seems to appreciate such sentiments of co-operation, for in order to have a better say in the running of such multilateral institutions it plans to set up an international emergency fund, outside the framework of the IMF. United States has however discreetly avoided the question of liberalizing the IMF framework. According to a financial analyst "Failure so far to allow the IMF framework to accommodate the expanding requirements of world trade and finance is responsible for a virtually complete surrender of the payments financing role to the private commercial

US has manipulated the mechanisms of IMF in such a way that the latter has been reduced to extension of its cover to only non-oil developing countries. However, the IMF cover is only a small fraction of what is lent by the commercial banks. Thus between 1980 and 1981, net commercial bank credit for these countries was $85 billion which was 15 times the Fund credit for the same period. So we find the US strategy has been to promote the interests of private commercial banks and float an institution where it can exclude the developing countries altogether from its decision-making body. In the process, it can also coerce other industrialized countries to abide by its decisions which would be skewed in favour of the commercial banks. As most of the largest banks are US based, the banks based in Europe would not be receiving a fair deal. In the overall analysis, we find although the United States has tried to turn the international banking crisis to its own advantage, the crisis has led to a collapse in short-term export financing, main motive force in international trade, thus affecting for example its business in Latin America. Even as the IMF and commercial banks are busy arranging financial bailouts to head off

60 See, ISG, "Why a non-IMF rescue Arrangement?" EPW, vol. 18, no. 3, 15 January 1983, p. 50. The US is reported to have bullied the other members of the Group of Ten to agree to consider the scheme on pain of vetoing IMF quota expansion.
defaults on foreign loans. The shortage of trade credits is crippling productive capacity of Third World debtors and thus their ability to repay debts. 61

The problem is most acute in Latin American countries which have been forced to slash imports from the US by $16 billion in 1983 from the 1981 level of $39 billion. According to a survey carried out by International Business Week:

Factories and farms that depend on critical imports, ranging from aircraft parts to insecticides have been unable to get hard currency from their central banks or trade credits from their traditional suppliers in the US, Europe and Japan. In the past 50% to 70% of US exports to Latin America went to longtime customers on open account, with exporters providing 90% credit. Such sales have practically dried up except for some US multinationals that are still supplying their Latin American subsidiaries on intra-company credits. The problem has been compounded by a toughening of terms for trade-credit insurance provided to US exporters by the Foreign Credit Insurance Association (FCIA), a syndicate of 41 major insurance companies backed by the US Export-Import Bank. 62

61 Robert J. Samuelson, "The World's bankers fiddle while the debts keep Growing", International Herald Tribune, 8-9 October 1983. Driven by the need to service their debts, many developing countries Brazil, Mexico and Argentina have embraced austerity. Similarly in Europe, France and Italy are resorting to anti-inflationary measures. However, one country's austerity dries up another's export market, for example, US shipments to Mexico dropped $6 billion in 1982. If too many countries contract, slumps would reinforce each other.

In an effort to smoothen the flow of trade, Ex-Im has planned to start re-insuring the commercial risk or FCIA export policies after 1 October 1983 in addition to political risk it was already re-insuring. Although US commercial banks have agreed to maintain existing lines of short-term credits to big debtors such as Brazil as part of their IMF led financial rescue packages but the banks' resources are under considerable strain and their risks have been enhanced by new medium-term loans that they are obliged to supply under terms of the bailouts. Thus banks are keeping aloof from new trade-financing business, and they would like official guarantees to cover their credits.

Ex-Im will have at its disposal $10 billion in export guarantee starting from 1 October, but this must be spread over US trade with the entire world, not just confined to debtor countries. The bank has earmarked $1.5 billion for Brazil and $500 million for Mexico, but US has been cautious enough to see that it is available only if the 23 other industrial countries that make up the OECD agree to provide "comparable support" for exports to those countries. The Bonn government under intense pressure from German Companies recently agreed to sustain exports by delaying a proposed increase in insurance premiums by Hermes, the government backed export credit agency, which is losing at
the rate of $370 million annually because of rising credit losses. France has also agreed to maintain its heavy export subsidies. Britain has also fallen suit by dipping into its reserves to support its Export Guarantee Department which insures 34 per cent of that country's non-oil imports, despite mounting losses.

Britain to its dismay has however discovered that its competitors are using aid money to create job generating exports. For example, France has been using a subtle mixture of aid and export credits to capture markets, mostly former British colonies that have been dominated by suppliers from United Kingdom. Anglophone Africa is now regarded as a priority area for French aid, with emphasis on tied Treasury loans in the form of mixed credit. It has also signed lines of credit since 1980 with Malawi, Uganda, Tanzania, Kenya, Sudan and Zimbabwe. This partly explains why France has been eager to announce its intention to reach the 0.7 per cent of GNP as recommended by the United Nations target for aid by 1988 in respect of its aid to independent countries. According to John Lawless, "This will require an annual increase in real terms of about 11 per cent a year. If this target is to be adhered to a very considerable increase in French aid may be expected over the next few years, with
obvious implications for her competitors. 63

While fierce debate ranges within the European Community on the use of export credits in capturing markets, US, Japan and European Community are trying to arrive at a consensus in announcing a new plan for establishing interest rates for export credits. If approved by OECD nations participating in the negotiations, the new system for government backed credits would be adjusted automatically, in line with a weighted average of key currencies. This system would set the level in relation to commercial interest rates. The plan would also imply reductions in subsidies which have been the main target of US negotiators who have insisted that export credit rates may be more aligned with market borrowing costs. 64

The Reagan Administration has in a compromise move dropped its demand that the phasing in of cutbacks begin in 1984. This was a part of the concession demanded by France which had sought sharper cuts to reflect a 2 percentage

63 John Lawless "Call to revamp aid strategy", The Times, 6 September 1983. This is the summary of a report prepared by Peter Godwin, a director of the merchant bank Lazard Brothers and Chairman of the Tropical a body of businessmen that advises government on export policy and promotion in the region.

64 Axel Krause, "Pact resorted on Rates for Export Credits", International Herald Tribune, 14 October 1983.
profit fall in commercial borrowing charges. It is significant that France and Italy, fearing that the proposed system would work against countries with relatively high interest and inflation rates had previously opposed the agreement, urging lower rates for the package. The plan involves a small cut 0.65 percentage point in rates charged to all but the richest borrowers. The cut was temporary and would be offset by adjustments made in 1985 and 1986. The negotiators agreed on a drop to 10.7 per cent under the proposed agreement. Interest rates under the proposed plan would range from 9.5 per cent to 12.4 per cent. All currencies whose market interest rates were below the maximum 12.4 per cent provided for in the agreement would be classified as low interest rate currencies. The maximum rate for developed nations would remain at 12.4 per cent. Interest rates under the plan would be calculated at the market rate, plus a margin reduced to 0.2 percentage point from the current 0.3 percentage point.

Export credit is therefore an area where there is reasonable consensus between allies of the Western alliance which might succeed in giving a semblance of outward cohesion to the alliance. There are also indications to show that under strong pressure from its staunchest ally Britain, the Reagan administration might also compromise on the question of budget deficit. Although earlier the Reagan
Administration was refusing to compromise on either its supply side economic programme or its arms build-up it is now giving second thoughts to its economic policy and might consider tax increases if the Congress is unable to reduce public spending.

What is worrying the Reagan Administration is its increasing budget deficit which is expected to reach $196 billion in 1984 fiscal year, $205 billion in 1985 and $214 billion in 1986. This greatly contributed to the high level of American public borrowing as a share of gross national product, which stood at 6 per cent in 1983. This has raised the spectre of a debilitating interest rate when private demand for credit grows with the recovery picking up. 65

While United States has given enough hints that it wants to accommodate European interests on the question of export credit and budget deficit, it has remained ambiguous on the question of interest rate, although if budget deficit could be brought down by taxation, that

65 Under the present system, only currencies with interest rates falling below the bottom of the range were included. Britain could pay subsidies only for financing credits for poor, developing nations and not to those classified as "intermediate" borrowers such as Brazil.
problem could also be solved amicably. 66

EUROPEAN ECONOMIC CRISIS AND ITS IMPACT
ON TRANSATLANTIC ECONOMIC RELATIONS

Economic crisis has attenuated the friction between Europe and United States. Commenting on the need for a re-appraisal of the relationship, Henry Kissinger, the former US Secretary of State wrote:

The special frankness and trust that may have been originally resorted to as compensation for a disparity of power may now be even more essential in the partnership of equals that must characterise the future relations between Europe and America. After the war, American leaders applied a heavy dose of our missionary zeal and the full vigour of our "problem solving" energy to the task of promoting Europe in integration. Despite the idealism of our commitment, tensions between America and a unified Europe were inherent in the logic of what we were so enthusiastically endorsing. We had grown accustomed to the devastated, temporarily impotent Europe for the post-war Europe; we forget the Europe that had launched the industrial revolution that had invented the concept

66 In a similar situation, Mrs Margaret Thatcher, Prime Minister of Britain took the politically unpopular step of raising indirect tax rate by pushing through sharp increases in value added tax to 15 per cent. As a result public borrowing as a share of gross domestic product dropped sharply from an estimated 5 per cent in 1980 to 3 per cent in 1981-82 and 2.75 per cent in 1982-83. For details see, Bailey Morris, "Reagan's Lesson on Public Spending from a Strong Ally", The Times, 12 October 1983. Also see Rudolf Bahro, "Capitalism's Global Crisis", New Statesman (London), vol. 104, nos. 2700-1, 17-24 December 1982, pp. 26-29. John Palmer, "US Budget Developments put Fear into Europe", The Guardian, 3 May 1983.
of national sovereignty and that had operated a complex balance of power for three centuries. A Europe reasserting its personality was bound to seek to redress the balance of influence with the United States. 67

However from the available evidence, we find that Henry Kissinger's expectation has not been belied. Europe has not remained passive to US economic policy which has been orchestrated in such a way as to undermine the resilience of its economy.

In case of monetary policy for example, we find that monetary tightness in the United States has become a major source of policy conflict between US and Europe:

High US interest rates have prevented European countries from lowering their interest rates to stimulate output in Europe, as such a lowering of interest rates would result in currency depreciation and inflation. Worse, the tightening of US monetary policy, while it reduces inflation there, increases inflation in Europe without much of an increase in European growth because Europe suffers a terms of trade deterioration that offsets in part the benefits to output from increased competitiveness. Europe is in the awkward position of having to tighten its monetary policy to fight the imposed inflation (due to US

deflation) thus losing the benefit from the added growth. 68

In order to counter the American move, EEC Central Banks often had to announce a series of sweeping interest rates to head off a new bout of currency devaluations which could pose a threat to the future of the European Monetary system. Strains also emerged between the stronger and weaker EEC currencies to such an extent that some countries had to contemplate withdrawing their currencies temporarily from the EMS given the obligation to defend a fixed exchange rate. It was a crisis of this kind which led the break-up of the old EEC currency 'snake' in the early 1970s, but it was expected that the EMS could be developed into a fully blown EEC monetary system with greater use of the European currency units instead of national currencies.

The EEC felt that a stronger EMS accompanied by a greater pooling of financial sovereignty by the different EEC economies is a dire necessity if the European Community as a whole is to become more independent of US monetary policy. But as John Palmer, rightly observes:

Although all the ten share a desire to free themselves from the influence of Washington's high interest rate policies, they are divided about how far and how fast they can move to make the EMS a genuinely multinational multinational monetary system in Europe. 69

But there has been a marked change in the way the global markets now have started looking at the US currency. Volatility of the interest rate which had powered the dollar's four year rise to a record 2.73 Deutsche Marks in August 1983 are receding. Market attention is now fixed on huge and growing deficits in US trade and in the current account and federal budgets. According to a recent report in International Business Week -

Although a lower dollar would make European and Japanese exports less price competitive, government officials and central bankers are breathing a sigh of relief. For them, it means improved chances of nurturing a feeble European recovery into a sturdier upswing. They can do more to stimulate growth without risking an increase in their

inflation rates and a domestic currency plunge, two factors that killed French reflationary efforts. 70

It is significant that interest rates are being displaced by economic fundamentals such as the expected $70-80 billion US trade deficit and $30 billion current account deficit. Even if there is the accompanying risk that continuing US budget deficits of $180 billion a year will hike up interest rates when there is a collision between government borrowing needs with that of corporate, it would not be enough to halt a dollar slide. Even if there is a rise in US interest rates in 1984, it would be against the background of a dollar depreciation and not an appreciation. This is because the switch to focusing on fundamentals would make it harder for the US to attract the huge capital inflows that have helped to support the dollar. Some analysts feel that these funds would begin to flow out of US investments and be reinvested in the yen and strong European currencies. This switch implies that US interest rates could be moving higher even as the dollar falls. But in the early stages of dollar weakness, European governments are likely to cushion its fall by pushing their interest rates down in

order to help their own recoveries.71

Export credit is another area which could become an issue of conflict in a period of economic slowdown and could have created a serious rift in the Atlantic Alliance. The issue of export credit had also created a rift among members of the EEC, with some EEC members openly coming out in favour of United States. The Italians and the French, for example wanted to keep something closely resembling the present arrangements and the Germans and the Dutch had supported the Americans in a drive to make export credit terms more related to market terms and perhaps eliminate subsidies altogether.

Table 1

MINIMUM RATES ON HIGH INTEREST RATE CURRENCIES

<table>
<thead>
<tr>
<th>Credit Term</th>
<th>2 to 5 years</th>
<th>5 to 8½ years</th>
<th>8½ to 10 years</th>
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</thead>
<tbody>
<tr>
<td>Rich countries</td>
<td>12.5</td>
<td>12.4</td>
<td>not allowed</td>
</tr>
<tr>
<td>Intermediate</td>
<td>10.85</td>
<td>11.35</td>
<td>not allowed</td>
</tr>
<tr>
<td>countries</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Poor countries</td>
<td>10</td>
<td>10</td>
<td>10</td>
</tr>
</tbody>
</table>

Source: The Times, 11 April 1983.

The UK department of Trade, which is the ECGD's sponsor Department had favoured the proposal given by the European Commission which would retain the present state of minimum fixed interest rates but reduce it slightly (perhaps half a per cent) to reflect some of the recent fall in market rates. This proposal in effect, would broadly maintain the present level of export credit subsidy on new loans. These subsidies have been as high as 7 per cent for the Italians, who even with a budget of about £1,000 million a year, cannot subsidize lira rates down to the range of 10 per cent to 12.4 per cent permitted by the consensus for high interest rate currencies. The French subsidise fairly heavily, about 2 per cent to 5 per cent since their market rates are about 14 per cent to 15 per cent. Britain subsidizes lightly on new loans, as its interest rates closely correlate to the consensus minima. On the question of export credit we find the EEC being subjected to sustained US pressure. US had been insisting for a long time that interest rates on export credits, which are basically government subsidised loans used to promote overseas sales should be brought more into line with commercial realities. But France and Greece

72 According to Malcolm Crawford, an economic analyst, "The British Treasury wants to cut subsidies for export credit which cost £ 587 million in 1981-82 but less in the years just ended, partly because market interest rates have come down, and partly because consensus rates have been increased from their low levels of the 1970s'. For details see, Malcolm Crawford, "Export Credit split Governments", The Times, 11 April 1983.
had blocked EEC acceptance of the higher rates sought by Washington.73

France was initially reluctant to pay any heed to US pressure for it felt if it cuts back subsidies, it might risk export contracts. However, ultimately even France had to succumb to US pressure although before giving its assent, it insisted that US should introduce its shorter duration credits on 15 October 1982 rather than January 1983 as

73 In 1982 itself, United States had succeeded in forcing the EEC states to agree to a new set of export credit rules, which pushed up interest rates on government backed loans western nations give to poorer nations. The 10 EEC states had also bowed to US pressure for additional increases in the charges on trade credits financing exports to the Soviet Union, East Germany and Czechoslovakia. The only proviso sought by the EEC was that Greece and Ireland should be exempted from the increased charges for one year. The minimum interest rates offered to 'relatively rich' countries was hiked to 12.15 and 12.4 per cent from 11.5 per centage point. Nations classified by the OECD as intermediate were asked to pay an extra 0.35 point, bringing the new charges to between 10.85 and 11.35 per cent. Although for the poorest, the rates remained at 10 per cent, under US pressure, several developing countries like Brazil, South Korea and Taiwan had been reclassified as intermediate rather than poor nations. For details see, Philip Stephens, "EEC bowing to the US, agrees to raise rates on export Loans", International Herald Tribune, 1 July 1982.
earlier planned.74

With France succumbing to US pressure, decks were cleared for a compromise solution enabling the industrially advanced countries to pull themselves back from the brink of a trade war on export credit subsidies.

However ultimately the OECD consensus seems to have been approved even by the most-hard lined EEC state. It has

74 A French request for a 0.5 per cent reduction in interest rates for Third World borrowers had been rejected and France had no other alternative but to oblige. For details see, Leonard Doyle, "EEC backs Compromise on Credits", The Guardian, 1 July 1982.

The EEC position on export credit does not always reflect the OECD position. For example, in 1982 both the Americans and the Community wanted to see Japan take more than the 0.3 drop in its present official rate of 9 per cent, 0.6 per cent above its protagonists market rates. They had also agreed that the USSR and other COMECON countries should be moved up from the middle-income to the relatively rich category of borrowers. The OECD has been observed to be much more flexible in arriving at a consensus on the question of export credit, and probably subjects it to periodical review. For example, the existing OECD consensus on export credits lasting from November 1981 to May 1982 provided for interest rates of between 10 and 11.25 per cent. The 22 nations subscribing to the consensus have since been debating a compromise aimed at reconciling their differing attitudes on interest rates. But the new Common Market counter proposal argued for a lower increase in the minimum, government backed credit rate for relatively rich borrowing nations and a cut in that for countries in the poorest category. The package gave a top rate of 12.25 per cent for long term credits, and a bottom rate of 9.5 per cent, 0.25 and 0.5 per cent lower respectively than those suggested in the compromise proposal and backed by the USA. The EEC also wanted a phasing up period for the new rates. For details see, Rod Chapman, "Export Credits war Booms", The Guardian, 16 June 1982.
succeeded in setting minimum interest rates at which capital
good sales can be made to developing countries.

The new deal will not only boost export sales, but
will also mean a large saving in public expenditure. The
interest rate subsidy, which the Treasury pays banks to
compensate between market and consensus rates will be greatly
reduced over the next three years. The most attractive
feature in the new agreement is a fully automatic adjust­
ment of interest rates every six months, starting in
January 1984: 75

Table 2
ECGD REVISED MINIMUM INTEREST RATES
(old rates in brackets)

<table>
<thead>
<tr>
<th></th>
<th>Category (relatively rich)</th>
<th>Category II (intermediate)</th>
<th>Category III (relatively poor)</th>
</tr>
</thead>
<tbody>
<tr>
<td>For credits</td>
<td>%</td>
<td>%</td>
<td>%</td>
</tr>
<tr>
<td>between 2-5 years</td>
<td>12.5 (12.15)</td>
<td>10.35 (10.85)</td>
<td>9.5 (10)</td>
</tr>
<tr>
<td>inclusive</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>For credits</td>
<td>12.4 (12.4)</td>
<td>10.7 (11.35)</td>
<td>9.5 (10)</td>
</tr>
<tr>
<td>over 5 years</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: The Times, 14 October 1983.

75 John Lawless, "Subsidies deal averts World Trade War",
The Times, 14 October 1983; also see, Robert L.
Rothstein, The Weak in the World of the Strong: The
Developing Countries in the International System
(New York, 1977), pp. 3-72; and Andre Gunder Frank,
"Global Crisis and Transformation", Development and
Europe and United States has arrived at a consensus not only in the areas of monetary policy and export credit, but it is poised to encompass banking too. But in this case, the adverse effect on developing countries is more pronounced.

US banks are quietly but aggressively marketing to foreign banks a scheme enabling both to profit extra profits out of loans to developing countries. The aim is to entice foreign lenders to price their loans over the prime rate of US banks rather than over the traditionally used London interbank offered rate. Prime is more profitable for US banks, which are offering to split these gains with their foreign colleagues. 76

Till now non-US banks were reluctant to price their loan participations over the prime rate. 77 This is because these institutions fear that in the event of a financial crisis, they could never be certain whether they would have a ready access to the New York money market to fund at profit commitments based on the prime rate. But the US banks are

76 Carl Gewirtz, "US banks push prime based Loans", International Herald Tribune, 20 October 1983. This American strategy is going to cost the developing countries heavily, for the prime rate currently 11 per cent is always more expensive for borrowers than is Libor, whose offered rate is 9.5 per cent.

77 Prime is a purely managed rate created by banks. Currently it stands 195 basis points what New York banks would have to pay for issuing 90 day certificates of deposit (100 basis points equal one per cent). According to Carl Gewirtz, a banking expert "that rate is as good a proxy as any for measuring what big US banks pay to buy deposits, but the real cost-including customer deposits on which banks may pay no interest is lower."
trying to convince their European counterparts that the prime rate is much more attractive than the LIBOR, a pure market rate set in relation to other short term interest rates.

Banks theoretically fund their participations at the London interest bid rate, an eighth of a point below the offered rate. But major banks can expect to attract deposits at 1/8 to 1/2 below the bid rate-'miniscule' compared to the spread of 195 basis points that US banks have between their cost of funds and prime. This higher inherent profit for banks using prime as the base rate in syndicated loans is reflected in the margin that borrowers pay. Hard pressed developing countries are indirectly helping United States to translate its strategy into action. Brazil, to use a current example is offering lenders 1½ points over the prime rate or 2 points over LIBOR to reschedule $ 5 billion of overdue debt and provide $ 6.5 billion in new money. 78

Till now developing countries were resisting tying their loan rates to prime. But to attract a wider group of banks especially regional US banks, borrowers acquiesced in offering lenders that option from 1980. But even then they are allowing no more than 50 to 60 per cent of a loan to be tied to prime. But with the eruption of the

78 Also see, Peter T. Kilborn, "Brazil seen unlikely to meet Terms for Aid", International Herald Tribune, 21 October 1983.
international banking crisis in August 1982, the focus of borrowers has shifted from the cost of money to availability at whatever price. The US banks since then have been trying to induce the European banks to opt for the prime pricing by offering prime-Libor swaps that effectively transform a foreign bank's LIBOR funding into prime-based funding. As a result both the lenders could earn bigger profits - at the expense of a higher interest rate charged to the borrower. Although it remains to be seen whether the US strategy would work but as we have been observing Europe to give in to US

79 The present global recovery while easing the problem of financing Third World debt, will by itself not resolve the problem. With commercial banks (mostly European) likely to desire a much smaller role in financing developing countries, the US banks are likely to play a much bigger role, although it is unlikely to affect the role of the present emergency lending regime. For details see, the summary of a study by Richard S. Dale and Richard P. Mattione entitled 'Managing Global Debt' in Hobart Rowen, "Study sees long-term Debt Crisis", International Herald Tribune, 24-25 September 1983. The US official policy seems to centre around the following: to edge out the European banks or at least make them subservient to US banking policy and to increase control over domestic American banks so as to make them important tools of US foreign policy. This is being done by deliberately aggravating uncertainty over whether US Congress will pass an $8.4 billion appropriations for the IMF and discouraging US commercial banks from extending long term credits. But given the existing level of commitment of US banks in Latin America US government banking regulations seems to be inadequate. For details see, Leonard Silk, "Banks face Public-relations Problem in seeking Support for their Rescue", International Herald Tribune, 22-23 October 1983.
pressure the outcome is not difficult to conceive, although interestingly all the compromises agreed upon have been at the expense of the developing countries. Analysts like Richard S. Dale and Richard P. Mattione feel that the current emergency lending system, more or less supervised by the International Monetary Fund needs to be strengthened, but they also concede that eventually new restraints must be placed on the banks that lend money and the poor nations that borrow.

The US banking authorities are not only encouraging US banks to woo its European counterparts so that a concerted move can be mounted against developing countries, but they are also at the same time being encouraged to cultivate them. The double-faced nature of this strategy became evident when Chase Manhattan, one of the leading US banks was forced to deny an allegation that it has not only been playing a dual role as adviser to the Government of Venezuela and Chairman of the group of Banks seeking to negotiate a rescheduling of its debt, but has also betrayed the trust reposed on it by its sister banks.80

80 A group of 13 international banks of which Chase is the Chairman, has been seeking to develop with the Venezuelans a plan of action to refinance the $26 billion owed by the Government and its agencies to the banks. More than half of this is short-term debt, due to be repaid in one year.
Lack of sound understanding between Europe and United States on monetary and banking policy has not only affected embryonic attempts at European Monetary Union but also the growth of an EEC inspired unified financial market in Europe. This is despite attempts by the EEC to facilitate the development of a common capital market. In the process EEC had produced a series of draft directives which were of especial interest to UK, which had complacently believed that once it joins the EEC, London could become the financial centre of the EEC.

Whatever little unification has been achieved in European or world capital markets has taken place independently of, and often in spite of the EEC. But that owes to market forces which has succeeded in bringing about a semblance of 'interdependence' in the economies of the western world. For example, the growth of the Euro-dollar market has not been to the liking of either the EEC or the

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82 Ibid., p. 19.

The Bank of England and the UK Treasury had claimed that a major reason for their volte face on banking supervision involved in the 1976 White Paper and 1979 Banking Act was motivated by the need to satisfy the EEC's Fourth Draft Directive on banking regulation and supervision.
US Government. This stateless financial system's growth was aided by Rule No 8 of the Financial Accounting Standards Board (FASB-8) which requires US companies 'to translate gains or losses in foreign currencies right onto the income statement in the quarter in which they occur - thus creating a whole new reason for multinational business to jump quickly from one currency to another'. 83 The MNCs which played a significant role in the growth of this market have been wary of interference by either the US Government or the EEC, for they wanted to have an uninterrupted access to the free, alternative capital market. So this market has remained relatively free from the fluctuations in transatlantic relations.

The MNCs are determined to keep the Euro-dollar market as its exclusive preserve for the considerable benefits it can reap from it, 84 but even states in the EEC itself,

83 Business Week (New York), no. 2548, 21 August 1978, p.76. This also owed partly to uncertainty in foreign exchange markets partly because of exchange controls.

84 The MNCs also used the Euro-markets for financing their subsidiaries operations in the lowest-cost currency at hand, e.g. OLIN Corporation got its French subsidiary to bill its Italian subsidiary for goods in Belgian francs. Italian short-term interest rates were 18% while Euro-Belgian franc rates were only 7%. Olin financed its operations by going into a third currency and by borrowing it in Euro-markets. Olin had assets in Belgium and was exposed at the time under Rule No. 8 of the Financial Accounting Standards Board. By borrowing in Belgian francs, it not only saved financing costs, but also balanced out its exposure by matching new liabilities with assets. By using the Euro-markets, Olin was able to combine liability management with currency exposure management.
like France had been found to encourage this market. When
the French Franc is weak, the government tightens domestic
credit, forcing French companies to borrow outside the
country.

But the Euro-dollar market's attempt to forge
transatlantic relations by trying to integrate the economies
of United States and Western Europe (especially in the
banking sector) has been most unwelcome to the EEC. Reasons
why the EEC has not responded favourably to the integration
of banking markets are: (1) integration has taken place
across a wider area than that comes under the ambit of the
EEC. This has been associated with an expansion of American
Banks in European centres. Both developments are inimical
to the 'little Europe' or 'Charlemagne mentality' and to the
latest anti-Americanism often implicit in EEC policies. (2)
The growth of Eurocurrency markets has made it much harder to
maintain fixed exchange rates. This has been very unwelcome
to the EEC which has insisted on fixed exchange rates as a
prerequisite for monetary union. 85 (3) 'State solution' to

85 The term 'Charlemagne mentality' was originally coined
by Schumacher in the early 1950s and used later by De-
Gaulle to describe the inward looking nature of the
EEC. However, what the EEC strictures could not do to
impede the growth of the Euro-dollar market has been
brought about by recession. The reluctance of banks
to lend to heavily indebted countries has caused a
dramatic slump in the issue of syndicated loans.
Completions of medium-term Euro-credits or loans
monetary integration - fixed exchange rates has been in conflict with the market solution - the Euro-currency markets. Thus banking is a classic example of state intervention which hampers market forces working to integrate economies.

Recession and the Interaction of United States and European Economic Policies: An Assessment

Some of the common tendencies that have influenced the evolution of most industrial countries during the 1960s and 1970s are increase in the size of social transfers, the policy of monetary accommodation of wage and price increases, the growth of rigidities in labour markets and the decrease in the share of income going to capital mainly in Europe. It is largely because of these two tendencies, and because of the two waves of oil price increases that industrial countries have all jointly moved into a period of stagflation stifled by capital shortages brought on by high government debt. To make matters worse, private savings are being mopped up by government borrowing, leaving insufficient funds for investment in industry. For example, in the seven leading industrial countries in 1982, government borrowed for their

organized by groups of International Banks from funds outside the borrowers' domestic market totalled $1.3 billion in November 1983 well down from $4.1 billion in September 1983. For details see, International Herald Tribune, 1 November 1983.
own use an average of 20 per cent of private savings double the average figure for 1976-81. Arthur Dunkel, Director-General of the General Agreement on Tariffs and Trade (GATT) has criticized the Reagan Administration's argument that US economic recovery could pull the rest of the world out of recession. He has insisted that economic recovery cannot by itself solve the problems of capital shortage, international indebtedness and protectionism. According to GATT -

...economic recovery does bring an opportunity that if bolstered through appropriate policies to cut protectionism and government budget deficits could lead to a new prolonged period of prosperity after 10 years of economic stagnation...solution lies in increasing exports which in turn requires a return to free trade principles rather than notions of 'fair' or 'organized' trade. 86

However economic slowdown has forced both Western Europe and US to flout GATT inspired free trade principles although even here they have made compromises even if at times it has been tinged with bitterness. However, while

conflict over issues like export credits or imports of American textiles has been temporarily resolved, sensitive issues like EEC agricultural subsidies or pipeline deal had threatened to strain the Western Alliance. What has complicated matters is President Reagan's single-minded pursuit of a "grand coalition" to rein in the Soviets, which has remained insensitive to European commercial interests at a time when Europe is starving for export orders. Here we would be attempting a few test cases to examine US's insensitivity to the economic interests of its allies.

**Soviet Pipeline Deal**

Relations between the European Community and the US had worsened after the refusal of the Reagan Administration to re-consider its ban on the sale of equipment for the Soviet natural gas pipeline to Western Europe, although the EEC was convinced that the US had no legal power over companies in Europe contracted to provide pipeline equipment. President Reagan's anti-Soviet rhetoric does

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not however explain the US ban on the pipeline. Behind it lay hard commercial interests. Before the ban went into effect, the US coal industry had warned the Reagan Administration that the construction of the multi-billion dollar Soviet natural gas pipeline could threaten the growth of American coal exports to Western Europe and hurt the United States mining industry. 89

IN US, the Interstate Commerce Commission was told by the State and Commerce Departments that they were opposed to deregulation of rail rates for shipment of coal. The agencies reportedly felt that such a deregulation might raise coal prices at a time when the US is trying to persuade its western allies to switch over to US coal rather than Soviet natural gas. In a brief filed on 21 December 1982, the State and Commerce Department in connection with the ICC deregulation case said:

The United States has attempted to convince its friends and allies that US coal represents an energy source that is preferable to oil from unstable Middle Eastern States, gas from the

89 According to Dan Morgan, "the pipeline issue had showed up sharp divisions between the US Government which opposed the project and the European allies which looked to the project to stimulate the equipment exports business and create jobs in the short-run and to provide new sources of energy by the middle of the decade. For details see, Dan Morgan, "US Coal Industry worried by Soviet Pipeline", International Herald Tribune, 15 February 1982."
USSR, or coal from South Africa or Poland....
The question of future energy sources is crucial to the economic strength of the West. 90

What is however less known is the fact that US has always sold substantial amounts of coal in Europe, primarily metallurgical coal, used in the steel industry. However coal exports to Western Europe rose dramatically after 1978 as a result of rising oil prices and erratic coal production in Poland, which was the main competitor to US coal exports. The Polish crisis engineered by the Polish Trade Union Solidarity not only provided President Reagan with an opportunity to promote the interests of a powerful coal lobby, but also artificially forging Atlantic unity by raising the Russian bogey. Although the Europeans had finally refused to succumb to US pressures initially they were ambivalent: France for example, held up a major sale of computerized equipment to the Soviet Union which was the first test of a drive by President Francois Mitterrand’s government to tighten up controls on strategically sensitive exports. Involved was the proposed sale by Thomson-CSF of computerized pipeline surveillance equipment, and the deal could be worth $600 million spread over a ten year period. According to Joseph Fitchett, who had been examining

French role in the pipeline controversy:

Plans for a better policed export policy, which is still being debated in the Government coincides with a campaign by the Reagan Administration to align NATO allies, Japan and neutral industrial countries behind a more rigorous approach to high-technology exports to the Soviet Union or to certain third-world countries that might use them against the West. The tougher French scrutiny of East Bloc exports in contrast to past liberalism in export sales—under-scores the Mitterrand and Reagan Administration's similar outlook on Western security. 91

The French Banks were however the first to break the impasse: they announced a plan to lend the Soviet Union $140 million to help finance purchases of French equipment. As a result of the loan, USSR was able to finance the entire hard currency cost of the French made equipment it planned to buy for the pipeline, roughly estimated at $1 billion. It thus saved itself from having to put up any of its cash at a time when it was believed desperately short of foreign exchange. The French banks that agreed to the loan which will cover 15 per cent of the cost of the equipment, are the state-owned Credit Lyonnais and two privately owned banks on the verge of nationalization, Banque de Paris, et des Pays, Bas and Banque de l'Union Européenne. However,

the only snag lay in the fact that the credit was on market terms and had no government guarantee. Secondly, it was more expensive for the Soviet Union than an earlier loan arranged by the same banks to cover the other 85 per cent of the cost of the equipment. This loan was guaranteed by the Government and had carried a subsidized interest rate of 7.8 per cent. Interestingly, in December 1981, a consortium of German banks led by Deutsche Bank refused a Soviet request for credit to cover the entire hard currency costs of pipeline equipment produced in West Germany. Instead they decided to stick to their original offer of lending only 85 per cent of the cost. According to financial sources, West German banks did not take kindly to the French decision to lend the entire foreign currency cost of French made pipeline equipment. According to Paul Lewis, a commentator:

They claimed it broke a gentleman's agreement between them not to go over 85 per cent. US officials also reacted angrily to the French move, saying that it had embarrassed the West German banks and appeared to violate the spirit of a NATO agreement in January '82 to suspend economic co-operation until Martial law was lifted in Poland. 92

92 Paul Lewis, "French banks approve Soviet Pipeline Loan", International Herald Tribune, 12 February 1982. The pipeline would enable the Soviet Union to sell Europe 40 billion cubic metres of Siberian natural gas per year by the end of this decade, eventually earning $5-6 billion annually in foreign exchange. As a result W. Germany, Italy and France would be getting between 25 and 32 per cent of their natural gas supplies from the Soviet Union.
Although Britain has been a staunch ally of US, from the very beginning it took a firm stand on the pipeline issue. The British Trade Secretary Cockfield tabled an order under the 1980 Protection of Trading Interests Act which provides for safeguard of British commercial interests against attempts by another state to apply its laws outside its own borders. The British Minister in the Trade Department, Peter Rees, was provoked enough to comment that extension of the Reagan Administration's ban to US subsidiaries abroad was contrary to the principles of international law. He had also demanded to know why the US sanctions do not include an embargo on American grain exports to the USSR.  

One can gauge Britain's irritation if one looks at the volume of business which were to be transacted by British companies. For example, John Brown, a leading British engineering firm itself had a contract worth £ 104 million. This had prompted Lord Cockfield, under the terms of the Protection of Trading Interests Act, to order two other firms Baker Oil Tools (United Kingdom), Smith International (North Sea) and American Air Filters to comply with the contracts and ignore the US embargo. The other


two British companies affected were engaged in supplying critical parts for the pipeline; they were Walter Kidde company and Andrew Antennas. Walter Kidde had a £9.5 million ($16.3 million) contract to provide firefighting equipment for the pipeline, and Andrew Antennas had a £1 million contract for communications equipment. Like British companies Italian firms were also affected, but to a lesser extent; for example Italian turbines were part of a $520 million order from Nuovo Pignone for


Among the British companies John Brown would have been the most affected if it had lost the £104 million Siberian contract, for in 1982 it had been suffering difficult trading conditions in respect of its manufacturing operations. In 1981-82, it made a profit of only £14 million although substantial profits on a series of design projects (petro-chemical plant, oil, rigs etc.) looks set to flow in 1984. To counter the US embargo, John Brown felt that it should attempt to switch the battleground out of the US administration's court where the Department of Commerce might be expected to hold more sway into the statutory courts, where there would be greater scope to raise general points of law. For details see, *The Observer*, 12 September 1982.

About 940 jobs were provided by the two new companies covered by the UK Government's protection order. Walter Kidde, employing 700 at Northolt, Middlesex has a £9.5 million order to supply all the firefighting equipment for the project's 41 gas pumping stations strung along the 5,500 kilometre pipeline, which represents half the firm's annual turnover. It is also significant that an estimated £146 million of about £200 million of UK orders for the pipeline were covered by the Government's protection of Trading interests Act. For details see, Rod Chapman Maggie Brown and Patrick Keatley, "Pipeline sanctions threat Widens", *The Guardian*, 11 September 1982.
57 turbines and 19 compressor stations. Compliance with the ban would have jeopardized the jobs of more than 6,000 employees, because the order represented nearly 70 per cent of the company's current contracts.

In case of West Germany, the US embargo would have affected the financially troubled AEG-Telefunken AG, its second largest electrical group which would have lost an order worth DM 650 million, for it would have failed to utilize a US license for rotary blades needed to build 47 gas turbines for the pipeline's compressor stations. It is significant that AEG was the only West German firm with a pipeline contract directly dependent on a US manufacturing licence. West Germany had however refused to follow the example of France which had ordered French companies to honour contracts with Soviet Union. This however did not prevent the West German Government to offer the troubled AEG-Telefunken guarantees totalling 600 million Deutsche Marks (£ 142 million) that would allow it to borrow funds to carry through initially important orders. According to the Times:

It is not proposed that the state should replace the private sector in aiding AEG. Money due to be supplied by the banks would be essential if the company is to meet its liquidity needs ... the Bonn Government has no intention of taking either a direct, or indirect stake in the company ... decision to come to the aid of West Germany's most

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notorious lame duck has been prompted primarily by concern for the country's image as an exporter of goods on world markets. 96

The German banks however played a crucial role in providing Soviet Union with badly needed hard currency. The German consortium which arranged loans was headed by Deutsche Bank and the Dresdner Bank, and the agreement was signed with Soviet Bank for Foreign Trade. It is significant that USSR and FRG had succeeded in developing middle and long-term financing, not only in connexion with the gas pipeline but also Russian imports of West German machinery and chemicals. 97

The West Europeans got an unexpected ally in Japan, when the latter too expressed its displeasure over the US ban. President Reagan's ban apparently also affected a Japanese-Soviet project to develop oil and natural gas off the far eastern Soviet island of Sakhalin. Japan was so perturbed over the ban that it asked for an exemption, for it would have provided Japan with 3 million metric tonnes

96 The Times, 15 July 1982.

of gas over 20 years beginning in 1988. Japan's sensitivity is explained by the fact that Japan needed electrical logging equipment made by the Schlumberger of the United States for the project. 98

After Japan had joined the fray there were signs that the Reagan Administration might take a more flexible stand, for US hinted that the ban could be reversed if allied governments raised the price of their credits to the Soviet Union. West Germany and France acknowledged that their credit terms were subsidized at the penalty of their taxpayers, but they resented US pressure to modify their policy. France asserted that it had little latitude over credit arrangements because of a secret protocol with the Soviet Union. 99


99 Joseph Fitchett, "US Pipeline Flexibility Hinted", International Herald Tribune, 29 June 1982. Also see, Joyce Lasky Shub, "Behind the Pipeline spat a growing wariness", International Herald Tribune, 29 June 1983. France and Germany has countered the Reagan Administration's charge that they have been unusually indulgent towards Soviet Union by claiming that the US could inflict greater damage on the Soviet economy than even a unified Europe could, simply by denying itself the Soviet grain market. It is significant that of the 4 per cent of Soviet GNP that is allocated to foreign trade, 2.5 per cent is with the United States. Taking a cue from United States, West Germany has staunchly defended trade with East European bloc, although in the pre-summit Versailles talks (1983) of the Atlantic Alliance, it indicated that it was ready to raise its down payments on Soviet purchases. At Versailles, the Reagan Administration tried to accommodate its allies on three issues: technological innovation, intervention in
A recent OECD study however points out that the Soviet Union had already taken necessary precautionary measures even before President Reagan's ban had come into operation, and more significantly it had remained nonchalant about the outcome of negotiations between United States and Europe on the pipeline issue. In order to manage the debt crisis and counter a drop in foreign exchange earnings, caused by falling oil prices, the Soviet Union and its allies had imposed austere policies at home and almost cut off trade ties with the West where banks and industries were reluctant to extend more credits.100

The Soviet Union's interest in building the second stage of the Siberian gas pipeline is explained by its need for hard currency which it was finding it difficult to get because of the oil glut and tougher credit terms. However, the OECD study had to concede that the Soviet Union and its allies had done a remarkable job of severe debt crisis but

at great economic and social cost which will for years affect their industries. This however did not deter the conservatives in the Reagan Administration to bolster its thesis that trade with Soviet bloc countries is dangerous for strategic and economic reasons and should be sharply curtailed.\textsuperscript{101} The hardline stance taken by President Reagan on the pipeline issue was however done at the expense of US firms: for example, the pipelaying sold by Komatsu of Japan was to have been supplied by Caterpillar tractor. Similarly, Alsthom-Atlantique of France, one of the compressor makers had built turbines using technology it had acquired from General Electric much earlier.\textsuperscript{102} The pipeline issue should be examined however in the broader Western policies on East-West Trade. A report prepared by the non-partisan Congressional Office of Technology Assessment, reviewing US export control laws, has observed that the anti-Soviet sanctions -

\textsuperscript{101} Most trade experts however feel that Reagan's policy extended US control beyond what is allowed by international law. They felt that US might have over-reached its lawful jurisdiction and in the process undermined the ability of US Corporations to export their technological skills. The US Commerce Department's new policy, if implemented would have barred both foreign subsidiaries and licensees of US companies from any future exports from US if they had taken part in the Soviet pipeline project. For details see, Tamar Lewin, "Legal basis of US sanctions over Pipeline is Questioned", \textit{International Herald Tribune}, 28 June 1982.

\textsuperscript{102} Clyde H. Farnsworth, "US says it can block Pipeline know-how", \textit{International Herald Tribune}, 11 February 1982.
had damaged the US economy by denying farmers a big export market for grain and by closing the lucrative machinery and equipment markets to American companies. If an important Soviet political goal is to generate as much divisiveness as possible among the NATO partners and to encourage the West Europeans and Japanese to depart from US policies on East-West relations, the gas pipeline embargo was a welcome political windfall for the USSR. 103

The report has warned the Congress and the Administration to keep this in mind during deliberations on new US export controls which have been strongly contested by the EEC. The same extra-territorial controls which had provoked European anger during the pipeline dispute are embedded in legislative proposals extending the US export Administration Act, and this, the report felt, should be amended. According to Bailey Morris, a commentator on the pipeline issue:

Neither Europe nor Japan is likely to endorse the United States position to the extent that retrenchment takes place, particularly in granting credits to or buying energy from the Soviet Union - it will be in large part due


John P. Hardt and Kate Tomlinson, "Potential Role of Western Policy towards Eastern Europe in East-West Trade", paper presented to a conference on Economic Interchange with the USSR in the 1980s, at Elkridge, Maryland in April 1982.
to the state of the world's economy and to domestic concerns. 104

Policy Implications

The Siberian pipeline issue105 is a blatant example of US's attempt to extend the principle of extraterritoriality, a term applied to legislation in one country which affects the sovereign rights of other countries. Although the United States eventually lifted the sanctions, it took the precaution of introducing a bill in April 1983 to renew the Export Administration's Act, which contained more stricter measures:

In particular, the bill proposed that the United States Administration be allowed to impose unilateral controls on imports from countries, whose sales to other markets may have compromised national security. The United States would give its definition of


105 See for details, Alex Brummer, "Reagan's attempt to Clobber the Russians has only made Europe see Red", The Guardian, 5 July 1982.


national security and in practice would be mainly concerned with exports in COMECON. 106

US's allies however have refused to toe its line. Britain for example took the unprecedented step of examining whether such legislation would break GATT rules. The European view is that not only does this legislation offend the sovereignty principle, and in any case difficult to enforce, but that it contradicts American efforts to liberalize other kinds of trade, and would in no way help easing the tension arising from conflicts in agricultural trade.

The Siberian pipeline deal on closer inspection reveals some interesting details: not only it was the largest Soviet-Western trade deal ever but it also had been concluded at a time when East-West relations had touched an all time low, with the US Government pressing western governments to support its 'Afghanistan sanctions' against Moscow. In 1981, the US Government had made several attempts to


The Europeans have however not been averse to exploiting loopholes in US embargo on the pipeline. For example, Allen West of Brighton (General Electric owned company) had won clarification from the US Commerce Department, that backup equipment for the pipeline was not covered by the ban. For details see, Maggie Brown, "Loophole opened in US Embargo on Pipeline", The Guardian, 28 August 1982.
dissuade the West German Government from sponsoring the project. Interestingly, the US embargoing of deliveries for the project by US companies and their subsidiaries and licensees in Europe, came only after the contracts were signed. The US in a bid to discourage the Europeans advanced the following arguments:

(1) The large steel and engineering contracts were increasing West European export dependence on the USSR.

(2) The usage of Soviet natural gas would entail a significant energy (import) dependence on the USSR: 30 per cent of FRG gas consumption in 1990, and about 26 per cent for France. As a result these countries might become vulnerable to Soviet blackmail. 107

107 It is doubtful whether US itself was convinced of its own arguments, for a CIA memorandum has pointed out that the ban on the pipeline gear was unlikely to succeed. However, it was quick to point out that the ban could force Moscow to cut back its domestic pipeline construction programme, forcing a reduction of domestic gas deliveries by as much as 30 billion cubic metres a year. It also pointed out that using some combination of Soviet and West European equipment deliveries through the new export pipeline could probably begin in late 1985 and reach nearly full volume in 1987, about one year later than if the sanctions had not been imposed. For details see, Dan Morgan, "Ban on Pipeline gear is unlikely to Succeed, CIA memorandum says", International Herald Tribune, 2 September 1982.

Philip Hanson, "Western Policies on East-West Trade with particular reference to the Pipeline Issue", paper presented to Annual Conference of British
(3) The pipeline is one of six being built from Urengoi, the others being meant for domestic Soviet usage. According to Philip Hanson, who had examined the pipeline issue:

Western technology inputs into this pipeline (chiefly in the form of efficient 25 megawatt (MW) turbines for compressor stations) are potentially a major help to the Soviet domestic economy in the event of serious energy bottlenecks. The extra domestic capacity which the line represents could be used for deliveries to the Western USSR in such a case, and the deal builds extra security into Soviet domestic energy arrangements at a time when this could be critical (the mid-1980s).

Against these arguments it has been contended that the European Community will only rely on Soviet natural gas supplies for a maximum of 4 per cent of its total energy needs by the 1990s (Table 3). The European Commission has showed that the Community could survive for up to six months with a 25 per cent reduction in its natural gas supplies. By 1990, EEC will be producing 56 per cent of all its needs.


108 Philip Hanson, "Western Policies on East-West Trade with particular reference to the Pipeline Issue" (Mimeo), Centre for Russian and East European Studies, Birmingham University, 1983.
of gas, besides diversifying supplies. Apart from USSR, the other main suppliers of gas will be Norway (12 per cent) and Algeria (10 per cent). Britain, which finds most of its gas requirements in the North Sea, will obtain the extra gas it needs from Norway. The Community has also begun negotiations with the suppliers in Canada, Camerons, and Nigeria as well as a number of Middle Eastern countries.

Table 3

NATURAL GAS SUPPLIES IN 1990

<table>
<thead>
<tr>
<th></th>
<th>Total natural gas consumption</th>
<th>Gas imports from Algeria</th>
<th>Libya</th>
<th>Norway</th>
<th>USSR</th>
</tr>
</thead>
<tbody>
<tr>
<td>West Germany</td>
<td>68</td>
<td>-</td>
<td>-</td>
<td>8</td>
<td>20</td>
</tr>
<tr>
<td>France</td>
<td>42.9</td>
<td>9.2</td>
<td>-</td>
<td>2.9</td>
<td>12</td>
</tr>
<tr>
<td>Italy</td>
<td>44.5</td>
<td>13.2</td>
<td>2.6</td>
<td>-</td>
<td>7(8)</td>
</tr>
<tr>
<td>Holland</td>
<td>38</td>
<td>-</td>
<td>-</td>
<td>2</td>
<td>-</td>
</tr>
<tr>
<td>Belgium</td>
<td>12.7</td>
<td>5</td>
<td>-</td>
<td>2.9</td>
<td>(.5)</td>
</tr>
<tr>
<td>Britain</td>
<td>61.5</td>
<td>-</td>
<td>-</td>
<td>16.5</td>
<td>-</td>
</tr>
</tbody>
</table>

Amounts shown are in 1000 million cubic metres. Amounts shown in brackets are still subject to negotiation. Luxembourg, Ireland, Denmark and Greece do not import any natural gas from outside the EEC.


The other arguments proffered are the following:

The Soviets would probably be replacing dwindling hard currency earnings from oil rather than making an
appreciable contribution to their present rates of hard-
currency exportation; secondly they have remained unenthusias-
tic about purchasing technology ahead of grain (see Table 4).

Table 4

USSR, REPORTED HARD CURRENCY MERCHANDISE IMPORTS
($ million Current Prices)

<table>
<thead>
<tr>
<th>Year</th>
<th>Total Imports</th>
<th>Food</th>
<th>Machinery and pipe</th>
<th>Food as % total</th>
<th>Machinery and pipe as % total</th>
</tr>
</thead>
<tbody>
<tr>
<td>1970</td>
<td>2701</td>
<td>230</td>
<td>1095</td>
<td>10.4</td>
<td>40.4</td>
</tr>
<tr>
<td>1971</td>
<td>2943</td>
<td>405</td>
<td>1179</td>
<td>13.8</td>
<td>40.1</td>
</tr>
<tr>
<td>1972</td>
<td>4157</td>
<td>981</td>
<td>1533</td>
<td>23.6</td>
<td>36.9</td>
</tr>
<tr>
<td>1973</td>
<td>6547</td>
<td>1841</td>
<td>2167</td>
<td>28.1</td>
<td>33.1</td>
</tr>
<tr>
<td>1974</td>
<td>8448</td>
<td>1001</td>
<td>2989</td>
<td>11.8</td>
<td>35.4</td>
</tr>
<tr>
<td>1975</td>
<td>14257</td>
<td>3319</td>
<td>6102</td>
<td>23.3</td>
<td>42.8</td>
</tr>
<tr>
<td>1976</td>
<td>15316</td>
<td>3401</td>
<td>6239</td>
<td>22.2</td>
<td>40.7</td>
</tr>
<tr>
<td>1977</td>
<td>14664</td>
<td>2412</td>
<td>5915</td>
<td>16.5</td>
<td>40.4</td>
</tr>
<tr>
<td>1978</td>
<td>16951</td>
<td>3175</td>
<td>7238</td>
<td>18.7</td>
<td>42.7</td>
</tr>
<tr>
<td>1979</td>
<td>21593</td>
<td>6568</td>
<td>7656</td>
<td>30.4</td>
<td>35.5</td>
</tr>
<tr>
<td>1980</td>
<td>25428</td>
<td>9792</td>
<td>7507</td>
<td>38.5</td>
<td>29.5</td>
</tr>
<tr>
<td>1981</td>
<td>27945</td>
<td>10525</td>
<td>6290</td>
<td>37.7</td>
<td>22.5</td>
</tr>
</tbody>
</table>

These arguments seem to have had little impact on United States for it was reported to have sought ways to delay the second Soviet pipeline project. The second pipeline was scheduled to tap the Yamburg gas deposits roughly about 150 miles (240 kilometres) north of the Urengoy fields that would feed the pipeline under construction. However, the USSR sensing US opposition has already pushed full development of the Yamburg field out of the 1980-85 Five Year Plan. The opposition was linked to Western restrictions on easy credit terms, interest rates and technology transfer.  


The second pipeline would parallel the first along the 3000 mile transmission system connecting the arctic region of Western Siberia to the Western borders of the Soviet Union, from where the system eventually could serve 10 European countries. The first pipeline would probably begin operating in the mid-1980s barring further complications.

The US pressure on its Western allies to restrict export credits did not always succeed. France, for example, has always delayed plans for a harder West European line on credit to the Soviet Union. According to the International Herald Tribune: "the proposal for more expensive credit was designed to emphasize western anger at Moscow's alleged involvement in the Polish crisis. Greece was the sole exception to have objected to the proposal." It was emphatic in observing "the delay was the latest example of the difficulties that Western Europe faces in striving to maintain a firm front of disapproval at Soviet pressures on Poland, while at the same time safeguarding domestic commercial
The pipeline issue clearly shows that the US opposition to the pipeline had been ineptly expressed and that its glib lexicon of carrot and stick has not really helped Poland. According to Jonathan Steele of the Guardian "the more that the West tries to use its economic, technological and allied military superiority to gain concessions from the Soviet Union the more it will contribute to the feelings of insecurity of the men who run the Communist system in the Soviet Union". After withdrawing the sanctions, Washington is now seeking closer western co-ordination of trade policies generally towards the USSR and has been interests." For details see, International Herald Tribune, 27 January 1982.

EEC has always found it difficult to take concrete measures for the proposal to tighten export credit to Moscow would require the approval of all western industrial states, in the framework of the Paris-based Organisation for Economic Co-operation and Development. It would have involved upgrading the Soviet Union to the category of advanced industrial state, instead of intermediate state as at present. This would mean a rise in interest rates to 11 per cent from 10.5 for loans from two to five years, and to 11.25 per cent from 11 for loans from five to eight and a half years. France has remained lukewarm to the proposal for it knows that the move could have important consequences for a 25 year gas supply contract that France had signed with the Soviet Union.

emphasizing credit and technology issue. 

Despite US withdrawal of sanctions, long-term commercial interests of West Germany in the Soviet pipeline deal has


United States has become oversensitive about export of critical technologies to Soviet Union. This became evident from two of its actions: (1) closure of Silicon valley to Soviet citizens to allay fears that Russians might spy on computer technology. Significantly, these kinds of restrictions were first introduced by the Soviet Union in 1951, with the United States responding with curbs of its own. The new restrictions promulgated by United States actually reduces the areas off limits to Russians from 24 per cent to 20 per cent of the US land mass, matching the Soviet Union's percentage. (2) joint investigations being carried out by South African and American investigators into allegations that South Africa is a key link in the smuggling of advanced European technology to the Soviet Union. It is significant that US computers seized by West German officials on board a cargo ship in Hamburg are believed to have been shipped in October 1983 from South Africa with the Soviet Union as the ultimate destination. The computers are said to be capable of controlling nuclear missiles and to be of the same type as used by Pentagon. For details see, Michael Hornsby, "South African Link in Computer Smuggling", The Times, 21 January 1983.

Under US law, all applicants for export licences for computers going to South Africa have to be vetted by the US Department of Commerce, to ensure that the user is not Armscor, the State armaments producer, or the South African military or police.

been adversely affected. This became evident from Soviet Union's decision to produce their own large compressor stations for five domestic pipelines due to be built this decade. As a result Soviet contracts, for the construction of 130 compressor stations for five trunk pipelines would not materialize. It is significant that companies in West Germany, France, and Italy would lose more than $10 billion worth of business, if indeed the Soviet Union has the capacity to build the stations.

112 Dusko Doder, "Kremlin may build Pipe Units", International Herald Tribune, 30 June 1982. The Soviet Government would build the large 25 megawatt turbines for such stations at the LMZ plant in Leningrad. The reported Soviet decision to produce new large turbines does not affect the contracts signed by Western European firms particularly in the construction of the 3,500 mile pipeline scheduled to carry Siberian natural gas. The only snag with the largest Soviet turbines is that they operate at half the capacity of the General Electric 25 megawatt model.

113 According to Philip Hanson, the Soviet pipeline project in two important respects is a special case: "first, it is a 'self-financing' product-payback project which will also (over and above repayment) be capable of making up for at least part of the generally expected fall in hard-currency export earnings from 1981 in the mid—late 1980s. Second, it is a project in which the scope for economic leverage by the West is at least matched by the capability for leverage against the West with which it endows the Soviet Union; and such leverage as it provides for Moscow is in the especially useful form of leverage tending to widen cracks in the Atlantic alliance." For details see, Philip Hanson, "The Role of Trade and Technology Transfer in the Soviet Economy", Paper prepared for the conference on East-West Economic Interchange in the 1980s, organized by the California Seminar on International Security and Foreign Policy, Elkridge, Maryland, 15—17 April 1982.
Farm Exports: US farm exports to traditional EEC agricultural markets have been a bone of contention for the last several years. The aggressiveness of US farm lobby is explained by the fall in income of US farmers: for example, their net income has fallen from $25,000 million (£16,400 m) in 1980 to $20,000 million (£13,000 m) in 1982 and this could drop as low as $16,000 million (£10,500 m) in 1983. Measured in terms of purchasing power their income is one-third of what it was in 1972. However, US farmers still lead the world food exporters, selling $41.7 billion in produce overseas in 1982, an increase of 70 per cent since 1976. But because of its subsidies, Europe is in the second place and moving up fast with export sales of $27 billion - a 156 per cent increase since 1976. While American farm exports rose 13.1 per cent a year, on average in the decade to 1980, Common Market exports rose at a 16.9 per cent annual rate.

114 For background see, Nicholas Butler, "The Ploughshares war between Europe and America", Foreign Affairs, vol. 62, no. 1, Fall 1983, pp. 105-22.

115 The Times, 14 March 1983.

116 Paul Lewis, "EC by subsidies gains on US in food Exports", International Herald Tribune, 1 March 1983. In 1983, the EC countries are proposing to increase farm prices by another 5.5 per cent on the average, although world prices outside the community are falling.
this imbalance, the US has taken certain measures like: introduction of a new programme of 'blended' credit ($50 million) for Egypt to finance sales of farm products ($20 million for corn and $30 million for tobacco). This provoked France to complain strenuously about the sale for it rightly felt that it was being squeezed out from a traditional market, but US made it clear that this deal was essentially a warning against excessive European subsidies. 117 The US Senate has played a crucial role in stepping up farm exports. For example, the Senate Agricultural Committee approved legislation authorizing gifts of surplus grain to US exporters who compete with farmers in the European Community. But the European Community has also not remained silent; it has granted export subsidies on 55,000 tonnes of wheat to Central and South America in retaliation to retaliate for the flour sale to Egypt. 118

117 The new deal did not affect a programme under which the United States provides Egypt with grain and food worth $250 annually. As Egypt has been a traditional European grain consumer, the US sale reflected one of the toughest problems in European-US relations. For details see, International Herald Tribune, 29 March 1983. Also see Bailey Morris, "EEC in farm talks with US", The Times, 8 April 1983. The US deal with Egypt has generated intense pressure in the Community to protect its agricultural markets from US competition. The Community as a retaliatory measure increased its subsidy for wheat sales to China, a traditional US market and it also increased subsidies on floor. For details see, International Herald Tribune, 9 March 1983.

118 Seth S. King, "Senate Panel back Grain Plan", International Herald Tribune, 4 March 1983. Similarly
However, it would be wrong to assume that only now for the first time, agricultural trade has become a live and contentious issue in transatlantic relations.

According to Nicholas Butler, a research analyst at the Royal Institute of International Affairs, Chatham House:

Questions of access and protection have been subjects of constant concern to American farmers and traders since the establishment of Europe's Common Agricultural Policy 25 years ago. Now, though under the pressures of surplus stocks of grain and falling farm incomes, there is a new area of contention - competitive subsidies designed to win or ensure shares in an erratic world market. 119

He has also emphasized the influence exercised by US-EEC bilateral relations on international agricultural trade relations for the last 30 years. According to him:

European and American attitudes to proposals for the liberalization, regulation or management of key agricultural product markets have determined the role and success of international institutions, and the fate of attempts to reach international agreements on agricultural matters. Domestic policy decisions taken in Brussels and Washington, have determined not only the state of the world market but have also become important and divisive items.

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Iraq received $230 million in credits to finance purchases of US farm products. For details see, James Vicini, "US backs talks with EC on Trade", International Herald Tribune, 11 March 1983.

119 Nicholas Butler, n. 114, p. 105.
on the agenda of trade talks, ministerial meetings and summits. 120

But there is little likelihood of an amicable settlement in transatlantic agricultural trade and there may be more conflicts erupting in one form or another which are inevitable given the nature of agriculture policy-making and the callousness shown to international or external effects of internal national policies. But this is bound to affect US-EEC relations, and as Nicholas Butler rightly warns: At risk in a continued conflict are not just the resources misallocated, but also the co-operative Atlantic trade relations built up gradually over decades. Those good relations, reflecting common interests and not just a balance of advantage, underpin the wider political alliance - which will itself be weakened if the consensus on trade is unravelled product by product.121 Ironically, agriculture was not a crucial issue in the early phase of GATT negotiations in the late 1940s and early 1950s. According to data available for 1950, only 15 per cent of grain production was allocated for trade. Individual countries which later became member-states of the European Community, pursued protectionist policies but with limited technological support they had no other alternative but to depend on

120 Ibid.

121 Ibid., pp. 105-6.
imports, which became dovetailed to production of North American corn and wheat. In the United States, less than 20 per cent of grain production was reserved for exports. And it is interesting to note that in the early 1950s, the US agricultural community was obsessed with the idea of preserving and protecting agricultural development. Initially United States was opposed to attempts made by GATT and leading farm product exporters such as Australia to liberalise agricultural trade. As a study by T. Warley has wryly observed:

The US found itself having to depend its disruptive actions on agricultural import restrictions, disposal of surplus stocks and use of export subsidies. 122

All of these constituted elements of an agricultural policy which was basically geared to domestic farm prices and farm income support but not to trade expansion.

Only in 1955, the Eisenhower administration took necessary steps to stop United States from violating its GATT obligations because of its domestic policies. Direct support of the US farm sector, under legislation enacted back in the 1930s was made legal, but US was still reluctant to include agriculture with other industries, covered by the

various GATT agreements, confirming the widespread view that US agricultural policy was greatly influenced by domestic decision and not by international agreements. But already the problem of excess grain had started troubling US agricultural policy makers but the balance of interests within the US farm sector was still tilted in favour of those seeking protection.

This picture however suffered a sea-change with the newly formed European Economic Community enacting its Common Agricultural Policy, the contours of which started emerging after 1957. In the words of Nicholas Butler:

American negotiators entered the Kennedy Round trade talks of the 1960s with a nominal commitment to inclusion of agriculture alongside trade in manufactured goods in the GATT agreements but there remained a degree of ambivalence at the heart of the American position. On the one hand, American producers saw the Europeans institutionalising measures to protect national markets which their own exports would have difficulty in penetrating. The need for secure and growing commercial exports was increasing, especially for US grain, the output of which grew by 25 per cent between 1950 and 1960. From 1954, onwards the Eisenhower Administration initiated and steadily expanded the PL 480 program which distributed surplus grain on concessional terms to less developed countries. Though productivity spurred on by technical advance was expanding at unprecedented rates, US farmers were still suffering declining real incomes and were falling further behind their counterparts in industry. 123

However, this fails to provide us with a composite picture for other US farmers were not favourably disposed towards liberalization of trade. So the CAP as set out in the 1958 Stresa Conference did not pose any immediate threat. According to S. Tangermann, "compared with the widespread use of quantitative trade restrictions in national policies the basic instruments of the CAP looked rather liberal."

As the price levels were not fixed, there was a prospect that status quo about traditional US markets would continue to be maintained. Emphasis was also laid on structural policy, which was expected to reduce the number of farmers and potential output provided care was taken for the right set of support prices. It was also expected that there could be a compromise between German interests and French, who were clamouring for a strong, protectionist agricultural system.

It was only over the years that the real import of CAP, which was highly protectionist in nature, became evident. Two of its features especially were of great importance: (I) its system of variable import levies designed to insulate domestic producers from any fluctuations affecting world markets, (ii) very high basic support prices designed to help the most marginal producers retain their business. The other factor was political in nature,
which served US foreign policy objectives. This involved a support for the establishment of the EEC and the wider ideal of European co-operation. No wonder such considerations helped US to overlook its parochial agricultural interests.

Within the Community, no one thought about accommodating US agricultural interests, for the Community members were still large-scale importers of US grain, and were suffering a substantial deficit with the United States on agriculture, and more significantly they were not convinced of the possibility that the CAP could bring about a transformation in the European farm sector. This explains why Europe had remained unperturbed by the 'chicken-war' in 1962-63, when the substitution of high CAP levies for the lower German tariffs which had existed previously on poultry imports had edged the United States out of the market. But once the mechanisms of the CAP had been agreed upon, the EEC was hamstrung in responding to international challenges. The CAP had not only become a major achievement of common action but also an essential part of "an internal bargain, compensating agricultural exporters among member countries for the improved access to their non-agricultural markets which more industrialized countries had gained." 124

It was against this background that the Community offered its major concession on the CAP in the initial phase of Kennedy Round negotiations but it maintained its reservations on the US demand for exposure of agricultural trade practices to the full scrutiny of GATT. To add insult to injury, they also did not approve of American attempts to have import levies converted to fixed tariffs. Similarly, they did not approve of subtle attempts made by US to shift the basis of farm support to income supplements: a far cry from guaranteed prices which acted as a catalyst to production. Instead, the Community proposed a freezing of all forms of supports to producers of particular products including grains. According to Nicholas Butler:

...it was a genuine concession - in that it placed a restriction on measures considered to be essentially matters of internal policy - and at the same time a negotiating device, in that it established the CAP as an accepted and legitimized part of the international trading structure. The proposal was that the agricultural part of the Kennedy Round negotiations should aim at consolidating all measures of support for agriculture, whatever their forms, with an agreement that a ceiling of the total level of support would not be breached. The objective was neither harmonization nor the removal of subsidies, but the limitation of their growth. 125

To the United States the proposal became palatable only in retrospect; as the impact of CAP on production and trade became obvious. It became obvious that instead of promoting liberalization or open access, it was leading towards an entrenchment of protectionist domestic policies. The United States had no other alternative but to ask for guarantees of access for particular products, like soybeans, which was in line with an agreement reached during the earlier Dillon Round of GATT talks.

In order to avoid the breakdown of the overall trade talks, the EEC offered a sop to United States in the form of bilateral agreements which granted a number of specific tariff and access concessions on priority products. For example, the grain negotiations were transferred from the Kennedy Round negotiations to the International Wheat Council's discussions on an international grain agreement. By the early 1970s, it seemed that the US had got resigned to the CAP, although it continued to pay lip service to open access or liberalization. The US had in the meantime discovered new and lucrative markets in the Community: for example, exports to the EEC of soybeans, free of duty had expanded by 50 per cent in the decade up to 1970s. US agricultural exports for example, had begun to expand rapidly. Exports of wheat as a proportion of US production
had reached 76.8 per cent in 1972 which owed greatly to Soviet purchases, growth of trade with Japan and the developing countries of South-East Asia. The development of the CAP and growth of European self-sufficiency undermined previously secure markets for US exporters. Although the Tokyo declaration of 1973 emphasized the special status enjoyed by Agriculture, the US was hoping a transformation in the CAP owing to internal and external pressures.

US negotiators in the Tokyo Round argued for widespread use of export subsidies and other non-tariff barriers. The twin aims were not only to secure existing agreements on access (particularly with reference to soybeans) but also to ensure that the output trends of the farm sector under the CAP did not affect US markets elsewhere. In contrast, the European approach to the problems of agricultural trade was to favour international management in the interests of supply security and price stability within a given range for markets which were proving to be insecure and volatile. In the words of Nicholas Butler:

The Community emphasized the disruptive effect of the US soybean embargo in 1973 as an example of the instability which agreement on security of supply could mitigate. EEC representatives argued for some form of stock holding as a means of underpinning the market, and for the isolation of agriculture as a separate subject of negotiation, clearly distinct from the wider discussions of trade policy in the Tokyo Round.

126 Nicholas Butler, n. 114, p. 111.
In contrast to the US strategy of relying on the market mechanism for meeting the problem of instability and world food shortage, the Community laid more importance on international trade management, which reflected its own internal approach to agricultural policy. But any attempts to bring about any convergence in US and European policies was bound to fail for the Community had stuck to the words of the mandate which had declared quite explicitly that the "CAP's principles and mechanisms should not be called into question and do not constitute a matter for negotiation". While US had no other alternative but to accept these words for the internal workings of the CAP, it remained sceptical of its applicability to its external effects. Thus it is seen that the divergent approaches of the Community and America owed more to immediate interests than to any ideological conflict.

The issue remained unresolved for the next six years, and in 1979 both sides signed a vague agreement, but a clause in this agreement has still kept the dispute alive. That clause enjoins upon the signatories:

Not to grant directly or indirectly any export subsidy on certain primary products in a manner which results in the signatory granting such subsidy having more than an equitable share of world export trade in such product, account being taken of the shares of the signatories in trade in the product concerned during a previous representative period, and any
special factors which may have affected or may be affecting trade in such product. 127

The clause might appear clear and concise but it hardly helped in resolving the disagreement. The Community has always regarded export restitutions as an integral part of its agricultural policy. 127 The Community has found it difficult to soften its stance because of the pressure exerted by member states with strong agricultural sectors, especially France, and from the agricultural lobby in general to have an explicit export policy. With problems of surplus disposal increasing, the demand for a sustained export strategy has gained ground. This demand was most succinctly expressed by Henry Nouyrit, Deputy Director of the French Confederation of Agricultural Cooperatives:

For exports there is no real policy. So called "surpluses" are disposed of as the opportunity arises. There is no plan for exports, no medium term policy. Exports have become a sort of undesirable adjunct to intervention. Financial preoccupations over export restitutions have inhibited a proper commercial policy involving an effort to establish permanent trade flows, to seek out new markets and to develop commercial instruments such as credits and long term contracts. 128

To a great extent, the Commission has shifted towards the

127 Ibid., p. 112.

French position and the Commission toyed with the notion of long-term contracts and special credit facilities. In 1981, the Commission in its Reflections on the CAP published in 1981 proudly talked about success of its exports in coming years "by providing the CAP with instruments similar to those enjoyed by major agricultural exporting countries (the United States, Canada, Australia and New Zealand) in particular the ability to include long-term agreements". Although Britain and France have remained less than fully convinced, the Commission has "coalesced around the position that the Community should at least have the instrument available". 129

So if there is no marked change in policy one could expect sales agreements of three to five years duration to be signed between the Community and a number of importing countries. From the European point of view, such a policy is unlikely to face any problem in terms of the Tokyo Round agreement. 130 The US however believed that

129 Ibid.

130 In 1980-81, the EEC became a net-exporter of wheat and feed grains for the first time since the creation of the CAP. Its sugar exports more than doubled to 4.5 million tonnes in 1980-81, from 2.1 million tonnes in 1976-77. Similarly, the Community has in the life of the CAP moved from being the largest importer of poultry in the world to its largest exporter, while in beef and veal the EEC has shifted from being a net importer to being the second largest exporter. For details see, Peter Norman, "US and Europe head for
the Tokyo Round settlement in 1979 marked a firm agreement, with the internal arrangements of the CAP accepted, but the role of subsidized European output on world markets firmly restricted. Their disillusionment explains some of the anger which has permeated the current dispute. World market conditions have only heightened the dispute. Since 1980, despite exceptionally large-scale Soviet imports and discovery of a regular Chinese market, there has been a fall in world prices for grain and stocks have continued to accumulate. This is bound to affect United States, Trade Conflict". The Times, 27 April 1982.

According to Peter Norman, "The EEC is held to be fully insulated from the world market. Production, rewarded as it is guaranteed prices, is subject to no demand restraint. Although the Americans believe that the resulting high food prices in Europe hold down demand for farm products, the EEC's Common Agricultural Policy gets around the problem by using subsidies to sell the surpluses."

131 Nicholas Butler, n. 114, p. 113.

132 It is interesting to note that in 1982, the Reagan Administration was considering a plan not to renew the United States 6 year-old grain agreement with the Soviet Union. This was because the State Department had recommended that the controversial agreement be allowed to lapse, when it expired on September 1982, though Department of Agriculture wanted it to be extended. It is significant, that US's grain sales to the Soviet Union had become a sensitive international issue: the US was accused of demanding 'unequal sacrifice' of its allies by opposing Soviet natural gas pipeline deal and sales of sophisticated industrial equipment to Moscow, which largely benefits Europe and Japan, while continuing grain sales primarily benefit US farmers. It should be noted that the
and harden its stance vis-a-vis EEC, for in 1983, for the first time since 1972, the US had a deficit in trade with the European Community, after having surpluses of $3.5 billion in 1982 and $8.7 billion in 1981. It is significant that agricultural trade, which accounts for nearly a quarter of US exports to Western Europe fell to $7.6 million in the year ending 30 September 1983 from $8.9 billion a year earlier. US has become so sensitive on agricultural trade questions, that even on the frivolous question of trade in corn glutten, used as a substitute for cereals in animal feed, it maintained a tough posture. The trade at issue amounted to about 2.7 million tonnes and was worth around $500 million (£280 m) to USA in 1981. This made the European Commission so exasperated that it proposed to negotiate in the context of the General Agreement on Tariffs and Trade (GATT) for a limit to the amount of corn glutten

\[\text{current agreement has a proviso that the Soviet Union must buy at least 6 million tonnes of US grain, roughly half corn and the other half wheat, a maximum of 8 million tonnes on US private grain markets. For details see, Robert C. Toth, "US may end Grain Sales to Soviet Union", International Herald Tribune, 30 June 1982.}\]

133 International Herald Tribune, 14 December 1983. Main cause of the deficit owes greatly to the gap between the fast growth rate in the United States and the slow rate in Western Europe. The other crucial factors were a stronger dollar and a reduction in US farm exports.
that the US can sell to Europe. 134

However events have shown that the European Community has equally remained insensitive to US interests. This became evident when the European Parliament under pressure from farm lobbies voted in 1982 to increase prices for farm commodities by 7 per cent instead of 4.4 per cent as recommended by the European Commission. Although decision by the Parliament is not binding, its vote could increase tensions in the escalating disagreement between the United States and Europe over the Community's farm export subsidies. 135

Policy implications: As an outgrowth of prolonged recession, the competition to export farm products, which on a worldwide scale accounted for nearly 15 per cent of the $2 billion annual volume world trade in 1981 and 1982 has become more bitter. According to Clyde H Farnsworth, who has analysed EC-US agricultural trade relations:

134 Like agricultural products, dairy products have also become thorns issue in EEC-US relations. For example, the European Community, worried that the United States may be preparing to dump its vast dairy surplus on world markets, has taken steps to increase its sales of low-priced butter to the Soviet Union. For details, see International Herald Tribune, 9 March 1983.

faced with a depressed market for their industrial goods, nations have sought to take up the slack with agricultural exports: at the same time, they are trying to check the flow of such imports into their domestic markets. 136

What is often not emphasized is the immense influence that farm populations and farming interests continue to wield in industrial democracies. In recent years, multi-billion clusters of interests have grown up around agriculture: huge agribusiness enterprises, medium-sized equipment manufacturers, small town farm supplies operations and the banks that supply credit. In US, agriculture contributed 20 to 25 per cent of the US Gross National Product, and the farm lobby commands extensive funds and wide political contacts.

The biggest customers: largest markets for US agricultural products ranked by 1982 exports as may be seen from the following Table (Table VI):

Table VI

US AGRICULTURAL EXPORTS FOR FISCAL YEAR (1982)  
(In Billions of Dollars)

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<th>1982 Exports ($ billion)</th>
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<td>Japan</td>
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<td>Netherlands</td>
<td>3.0</td>
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<tr>
<td>Soviet Union</td>
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<tr>
<td>Canada</td>
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<td>1.4</td>
</tr>
<tr>
<td>Mexico</td>
<td>1.2</td>
</tr>
<tr>
<td>Taiwan</td>
<td>1.2</td>
</tr>
</tbody>
</table>

Source: US Department of Agriculture, quoted in International Herald Tribune, 28 February 1983.
In Europe and Japan, the farm lobbies exercise such clout that they have succeeded in forcing consumers to subsidize farmers through artificial food prices imposed by the governments. These lobbies place greater emphasis on protecting markets, while American farmers with the exception of sugar growers favour free trade and wider exports. The US on the other hand has been exerting pressure on Europe and Japan to liberalize farm trade practices. The US wants specifically the Japanese to accept more beef and citrus products, and has asked Europe to agree to phase out their export subsidies. Behind the toughening US position is the steadily deteriorating economic picture for American farmers which is reflected in the declining purchasing power: the US Agriculture Department figure shows that farm income is one-third of what it was in 1972. An indication of the increasing pressure on American farmers is the decline in price of a bushel of wheat which has fallen from $4.10 two years ago, to $3.40 now. In contrast, support policies insulate farmers in Europe and Japan from most market fluctuations faced by American farmers. Secondly, in Europe, agriculture enjoys a special significance of bringing European nations closer together, and it is also significant that the EC's Common Agricultural Policy with its variable import levies, high guaranteed prices and export subsidies, counts among major post-war achievements in that regard.
To shelter European farmers, the European Community like Japan, keeps domestic prices well above world market levels. Proceeds from food import levies, supplemented by other Government funds, are then channelled into the agricultural sector as subsidies for export which ultimately affects the US. Japan which could be another potential market for US agricultural exports, has farmers who exercise a disproportionately large influence over the ruling Liberal Democratic Party. US has found to its chagrin that beef and citrus markets in Japan has been shielded from American competition. Secondly, unusually high support prices encourage excess production of rice which is exported to other Far East markets, again competing with US exports.

In the agricultural trade war with Europe and Japan, United States has failed to receive any support from GATT, which has rejected US allegations that European nations were unfairly subsidizing agricultural sales. The EC, even though is a competitor to US in third-country projects, is itself the largest customer of the American farmer. Thus in any trade with Europe, the American farmer would be highly vulnerable.

Europe however can draw solace from the fact that in the US, unlike in Japan and Europe, consumer groups are beginning to serve as a counterweight to the farm lobby. A coalition put together by consumer groups in early 1981,
fought the dairy lobby to a draw by curbing the steady rise in the support price of milk. But at the same time, the farm lobby in United States has become more aggressive: among the most politically active lobbies is the Wheat Growers' Association which has a $1 million annual budget for lobbying at Washington. Working hard behind the scenes, the farmers' groups have persuaded the Congress to appropriate $750 million since October 1982 to support export with 'blended' or subsidized credits to such countries as Brazil, Egypt, Morocco, the Philippines, Pakistan, Portugal and Yugoslavia. This might bring forth European retaliation not through subsidies but directly, by curbing their imports of American soybeans, corn gluten etc. In the final analysis, CAP would be difficult to change even if it continues to hurt US agricultural interests, for it was a crucial part of the bargain that created the Common Market. It was a compromise in which France insisted on help for its farmers as compensation for the economic and social risks it suffered in giving West Germany's powerful industry tariff free entry to its markets.

While Europe remains the world's biggest agricultural importer, it is gradually undergoing transformation into a net exporter of many farm products. From 1973 to 1980, Europe's self-sufficiency in grains rose from 91 per cent to 101 per cent, in wine from 99 per cent to 105
per cent, in milk powder from 231 to 341 per cent, in butter from 98 to 119 per cent and in sugar from 91 to 125 per cent.

But the US has allies within the EC in its battle to reduce export subsidies. It must be noted that subsidizing farm exports, storing surpluses and other costs takes three quarters of the $21 billion annual budget that member nations have allocated to finance a wide range of programmes.

Although it is unlikely that the EC will dismantle its agricultural export-subsidy system to make more room for American farmers, it is offering to join the US in setting up an informal world food cartel that would push prices higher by stocking more surpluses and preventing a dumping war that could bring down the prices.

Export Credits: US companies operating in the EEC under the Domestic International Sales Corporation (DISC) system\(^\text{137}\) has also contributed its share to deteriorating EC-US trade relations. The EEC considers DISC a clear export subsidy

and feels that the system could be considered illegal under the trade rules of General Agreement on Tariffs and Trade. Under sustained pressure from the European Community, the US Administration has devised a substitute for controversial tax incentives for US companies that sell US made goods overseas. Overseas promotion of US goods are achieved now through special tax code provisions that allow the formation of a domestic International Sales Corporation.

**Multinational Corporations:** The MNCs have also indirectly contributed to the worsening of transatlantic relations. European multinational companies like ICI, Unilever, Cadbury Schweppes, Reckitt and Coleman have campaigned against tax laws enforced by several US States including Oregon, Illinois and California alleging that they infringe the US Constitution. At the centre of the legal wrangle is the issue of unitary taxation, a system under which a Company's tax liability is calculated on a proportion of the world wide profits of the entire group. The campaign has been carried out by UNICE, the Confederation of European Employer Organizations supported by UK Government and European Community.¹³⁸

Although it remains to be seen what comes out of the legal wrangle, the EEC is encouragingly drafting of

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¹³⁸ *The Times*, 22 March 1982.
sweeping measures to regulate the management and operations of MNCs in the Community. The regulations which are in various stages of EEC's complex legislative process is part of a long-term effort to harmonize the business laws of the EEC's 10 member states. It would require the MNCs to consolidate the financial reports of all their European operations and disclose expansive data on their plans and strategies. They would increase corporate liability for defective products and give workers a major say in management decision-making. Among the most controversial proposals is the Vredeling proposal, which was proposed by the Dutch Socialist member Henk Vredeling in 1980. It would have required parent corporations to give workers a semiannual 'clear picture' of the corporation's financial situation, development and annual plans, marketing strategies, new products and technologies. 139

Under strong US pressure, the present draft is being heavily amended. The main requirement of the revised directive is that companies should, once a year, supply workers' representatives with information about the company comparable to that provided to shareholders. Changes involving closures or new working practices should be

revealed at least 30 days in advance and an opportunity for consultation provided before they are implemented. 140

Against a background of increasing trade conflicts as a fall-out of continuing recession in Europe, it would be interesting to examine how the European Community wishes to respond to the economic crisis. One aspect which might be gratifying for the developed countries is the continued import demand in developing countries which has led trade in manufacturing goods to outpace output, a trend remarkable taking into consideration the sluggish world demand and increasing protectionism in industrialized countries. 141

According to a survey by GATT, world trade declined in 1981, for the first time since 1958, contracting by 1 per cent on annual basis. The decline after growth of 21 per cent in 1980, was the result partly of a fall in export values expressed in dollars, and partly of a stagnation in the volume of goods traded. Economic recovery requires large


141 France is blocking a move by the industrialized nations to maintain the Williamsburg summit commitment to roll back protectionism. It is refusing to allow tariff cuts agreed by the United States, Japan, Britain and other European nations to take place immediately. France is insisting that there must be 2 per cent growth in the EEC economy as a whole before it will sanction any move towards trade liberalization. For details see, John Lawless, "France blocks cut in Tariffs", The Times, 12 December 1983
volume of investment and restoration of business confidence, whose absence has helped keep long-term interest rates high. Interest rate reduction could be implemented by lowering taxes on savings to free more capital for investment and cutting public budget deficits to compensate for the loss in tax revenue. The one per cent decline in world trade value to just under $2 trillion in 1981 was paralleled by zero growth in the volume of goods traded. Secondly, inflation had slowed to 10\% per cent from 13 per cent in 1980 although half the developed states had higher inflation rates in 1981 than in 1980. 142

The world economic recovery is now taking hold and apparently it seems to be benefitting both the IDCs and the industrialized west, by easing the adjustment problems of debtor countries. Developing countries other than oil producers are expected to narrow their payments deficits to $68 billion in 1983 from $108 billion in 1981. If this adjustment has to continue with more momentum, it would need a combination of export growth, structural change and

Policy implications: From the foregoing analysis we find that the present economic crisis has brought about a chill in

This is largely the view of the IMF but its critics especially the Group of 24 are arguing for more expansionary policies to increase demand for their exports and cure the debt problem. It is significant that even within the Reagan Administration, there has been a conflict over how expansionist or austere budget policy should be. Treasury Secretary Donald T Regan takes a more expansionist line, tolerant of higher deficit, while Martin S. Feldstein, Chairman of the Council of Economic Advisers has pressed for smaller deficits. It is interesting that the IMF remains critical of the US policy calling for a credible plan for reducing fiscal deficits in countries including USA where structural budget deficits are high in relation to available savings, while recognizing that austere programmes will hamper the growth of both exports and imports in the world economy. The IMF has dismissed the argument that the debt problem can be solved just by taking actions to expand trade. For details see, Leonard Silk, "IMF expected to retain tough policy on Debt"; International Herald Tribune, 17 October 1983.

United States not only has shown remarkable stoicim towards world economic recovery, but has also remained indifferent to appeals by multilateral aid institutions for increased aid or increase in its contribution. Although the World Bank has launched an aggressive campaign to force the United States to raise its contribution to trigger donations from 33 other large donor nations, US has remained unmoved. The World Bank had hoped to go into negotiations on the seventh replenishment of funds for the IDA with a strong commitment from the US to boost the total level of contributions to an estimated $12.6 billion over three years. Without this commitment, it would be difficult to persuade other donor nations to give much more than the restrictive level of $9 billion over three years. According to Bailey Morris "this would not be enough to see the poorest countries through the second stage of debt crisis at a time when new food shortages threaten Sub-Saharan Africa." For details see, Bailey Morris, "US rejects Clausen's cash Appeal"; The Times, 6 December 1983. For details on the pressure exerted by the EEC on US on the aid question, see K.N. Malik, "EEC presses US for more IDA Aid"; Times of India, 14 December 1983.
transatlantic economic relations, notwithstanding efforts at making compromises, which has however been made mostly at the expense of the Third world. To cite a recent example: the US is pressing for an agreement among industrialized countries to eliminate subsidies in export credits for steel mills built in the Third World. The 24 industrial countries in a display of rare unity has agreed to a project of cataloguing all known steel mill projects in the world and the financial term offered by export-import agencies.¹⁴⁴ Most of

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¹⁴⁴ The decision was made at a session of the export-import group of the Organization for Economic Co-operation and Development (OECD). For details see, Clyde H. Farnsworth, "US seeks to cut foreign Steel aid", International Herald Tribune, 27 December 1983.

The issue of financing steel mills is assuming significance because of global overcapacity and threats in the United States, the European Community and even Japan to bar steel from developing countries to protect the domestic industries. Until earlier in 1983 competition for exports had led to increasing subsidies on credits for equipment sales, but only now the industrialized countries seem to have woken up to the fact that about 10 per cent of world steel capacity is in the developing countries. In response, they would like to prevent more advanced Third World countries from implementing major plans for steel mill expansion to improve their trading position.

In the wake of the world debt crisis some of the projects have been cut back drastically. Mexico, for example, has stalled plans to add 7 million metric tonnes of capacity. Indonesia, the Philippines, Brazil, Taiwan and South Korea are among other countries planning expansions that have been delayed. For details see, International Herald Tribune, 27 December 1983. It is interesting to note that in the United States, the Commer Under-Secretary wrote the President, Export-Import Bank urging him to turn down financing for equipment for a mill to be built by Pohang Iron and Steel Company of South
these governments operate credit agencies similar in nature to the Export-Import Bank of the United States. Its function is to provide direct loans or credit guarantees to foreign buyers of equipment made in their country. Many of the loans offered are at subsidised rates, which signifies that the borrower pays much less than if it had borrowed from a commercial bank.

While it remains to be seen whether US succeeds in forcing the other OECD countries to toe its line on the question of subsidising export credits, it seems to have succeeded in getting its policy vis-a-vis multilateral aid institutions\(^{145}\) like the IMF approved by West Germany, an important member of the EEC. This latest development is significant for this would bring about a semblance of convergence in American and European policies towards multilateral aid institutions. It is significant that with the strong backing of West Germany, US is leading the fight to end the interest rate subsidy, and the IMF is expected to

yield to pressure to pay higher interest on the money it borrows from rich, industrialized nations and charge more for the loans it gives to poor countries. The US objective is to reduce the budgetary cost to zero of support to IMF. 146 At present when IMF borrows from the USA and West Germany, it pays 85 per cent of the market rate. As a result, at current levels, lenders receive 7.4 per cent from IMF against the market rate of 8.7 per cent. 147 Because it pays lower interest for the money, IMF has succeeded in passing on the savings to the poor, less developed countries. But the US Congress has objected to the interest rate subsidy and this view has been echoed by West Germany. US Congress's objection is apparently based on the estimates provided by US Treasury which states that the interest rate subsidy has cost US tax

146 The initiative to end the subsidy comes as the Reagan Administration draws up its budget for fiscal 1985, which begins in October 1984. For details see, Clyde H. Farnsworth, "IMF may raise interest on lending, borrowing", International Herald Tribune, 31 December 1983, 1 January 1984.

147 The market rate is computed on the basis of average yield of three-month Treasury Bills in the USA, West Germany, France, Britain and Japan. For details see, The Statesman, 1 January 1984. IMF now charges only 6.75 per cent on the money it lends to the poorer nations from the quotas of members. It can charge less than the 7.4 per cent that it pay the creditor countries because it meets some of the cost from the earnings of a trust fund established after the sale of some of its gold in 1972 and 1978. Also see, Thomas E. Weisskopf, "Reaganomics: Is it finally Working?" Banner (New York), 1 October 1983, p. 32:11.
payers up to $100 million a year over the past decade. But US’s tough stand would cost the IMF dear for in 1984 IMF is expected to lend about $14 billion to a number of cash short third world countries. Under the new proposal, higher interest would be levied in phases and linked to concessions for the developing countries in their access to enlarged IMF resources. The developing countries can do very little under prevailing circumstances because under terms of post-war settlement between America and the Europeans the voting strength is linked to contributions. US has also gained a significant victory on the agricultural front. Its pressure tactics vis-a-vis the European Community's Common Agricultural Policy seem to have started paying dividends: sustained US pressure seems to have played a significant role in forcing the EEC in adopting measures to cut the cost of the Common Agricultural Policy, although apparently it is meant to save about £100 million from 1984’s £1000 million agricultural budget. The Commission in its latest move is using its management powers to delay payment for produce which it buys at the EEC's fixed intervention prices. In the case of milk for instance, dairies will be paid a minimum of four months after delivery, rather than the present two months gap. 148

148 According to Ian Murray, "this delay, it is hoped, will force the dairies to try to unload their milk to buyers prepared to pay quickly. In turn this will put more milk on the market and force down the price, making it less profitable for farmers to produce. Delaying
However it remains to be seen whether the Commission can make substantial savings for part of the savings from the 1984 budget will be nominal because money will have to be paid eventually from the 1985 budget. In the same way, about £ 210 million frozen in payments from 1983's budget will have to be paid in 1984.

Only on the question of steel trade, the European Community seems to have resisted succumbing to US pressure, besides this the European Community governments have agreed to place extra tariffs (7.2 per cent import duty) on imports of US chemicals and plastics, if deadlock persists on steel trade.

Europe's Response to the Economic Crisis

While most of the OECD countries had succeeded in overcoming the major problems arising out of the 1974-75 recession, the basic structural, economic problems had
tactics are also being used on other products, notably cereals, where payments will take three months instead of two. The Commission expects similar results, though they are difficult to quantify at this stage." For details see, Ian Murray, "EEC plays a waiting Game to trim its Farm Budget by £ 100 m", The Times, 23 December 1983.

149 Loss of trade to the Community as a result of President Regan's steel measures amounted to $ 200 million over the four year period. For details see, International Herald Tribune, 25 November 1983.
remained unresolved. But some European countries, in particular West Germany, Sweden and to lesser extent France and the Netherlands had succeeded partially in tackling most of the endogenous and exogenous problems. The relative success of these countries in tackling the problem of growth, unemployment, balance of payments, capital investment and inflation are outlined in Tables VII to XI. These tables also reflect the failure of the British, Italians and Spanish to resolve the underlying economic problems of the 1970s. One curious aspect of the problem is that only those nations like West Germany and Sweden in particular, that have been able to resolve or mitigate the political difficulties of the recession have succeeded in tackling the basic structural and cyclical economic problems. According to Andrew Cox:

States which have failed to arrive at political and social consensus over the sharing of economic burdens and which have pursued polarised/ideological policies have tended to experience economic and political failure. Britain and Italy and to a lesser extent Spain, with its peculiar political problems of transition from despotic authoritarianism to liberal democracy in the 1970s, fell into this latter category. 151

150 Andrew Cox, "The World Recession and European Political and Economic Responses", in Andrew Cox, ed., Politics, Policy and the European Recession (London, 1982), p. 16. These include lack of social consensus, ungratified social and economic expectations, demands for greater political involvement, and participation of labour and the need to incorporate conflicting outmoded group and sectional interests.

151 Ibid., p. 16.
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* Estimate

Source: OECD, Economic Outlook (various).
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a Goods, services and all transfer payments
b Estimate

Source: OECD, Economic Outlook (various)
### TABLE X

CONSUMER PRICES: OECD AND SEVEN MAJOR EUROPEAN COUNTRIES

(% changes from previous year)

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* Estimate

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* Estimate

Although it is difficult to have a single blueprint for economic recovery and prosperity for Europe as a whole, there seems to be a correlation between countries that have tried out neo-corporatist/incorporatist solutions and relative economic prosperity and success.

By corporatist we mean that an essentially privately owned economy is subject to state intervention with its dual function of control and regulation. In such an economy, private profit receives inducement but business and financial interests tolerate the state's role in providing for social welfarism and modernization. These two interests are integrated into the decision-making structures of the state alongside trade unions/labour representatives who are allowed to play a crucial role in decision making in return for co-operation behaviour on wages and labour relations.

But in France, President Mitterrand's shift from a policy of economic growth and reduction of social inequalities to one of retrenchment and a freeze on planned social progress has affected such corporate ethics. But according to Diana Geddes, a journalist, "that dissatisfaction is not being expressed collectively; there is not the same tradition of
committed mass union militancy as in Britain. The reasons are obvious: only about 20 per cent of French workers are unionized, and these unions are poorly organized and divided among themselves. As these membership cuts across industrial sectors and trades, the strikes weapon is not nearly as effective as in Britain. More significantly, there has been a tradition in France of government consultation of the 'social partners' unions and employers since the last world war. The advent of the socialist government has provided the trade unions with greater access, both formal and informal, to ministers and even to the President himself.

Corporate ethics in France has suffered another deep blow recently with the firm stand taken by the famous automaker Peugeot that it would neither re-open its strike-bound Talbot assembly plant nor pay the 17,000 workers' there. This announcement has brought about a test of political


It is not surprising to learn from the latest comparative figures (for 1979) that the number of days lost in Britain through strikes per worker is seven times higher than in France.

Also see, R.J. Harrison, Pluralism and Corporatism: The Political Evolution of Modern Democracies (London, 1980), quoted in Cox, n. 150, p. 31.
strength between France's leading trade unions and the government. The outcome of the prolonged dispute could have a lasting impact on the government's industrial policy and its future relations with unions, which have become increasingly hostile to Prime Minister Pierre Mauroy's apparent reluctance to safeguard jobs in ailing sectors of the French economy. 153

This decline of corporate ethics confirms our hypothesis that these forms of intervention and incorporation, by themselves do not ensure a steady economic growth. This is confirmed by the more successful track record of less corporatist West German economy when compared with the more corporatist Swedish, Dutch and French economies. What however seems more obvious is that given the need in the late 1970s and early 1980s to resolve economic problems by curbing social and economic expectations and asking all sectors of the society to share the burden, those states which refuse to shed their welfare ethics would face insurmountable political problems in addition to economic constraints. So it is seen that -


countries like Britain which have to face the adversarial political forces of capital and labour as well as party policies which limit the possibility of consensus; countries like Italy with a fundamental division between left and right and a state structure which is basically corrupt and discredited...this is not to say that the more corporatist countries have not experienced political problems; this they surely have and will continue to do. The point here is however such countries are less hamstrung by the need to find consensus and political harmony over economic goals, which allows for concerted and consistent actions to deal with economic problems. 154

In West Germany (as is evident from Tables VII to XI) we find that the highest growth rate per annum has been registered since the 1974-75 recession. This record is an accomplishment if one takes into consideration the fact that West Germany's growth rate before 1973-74 was below the OECD average, which is a reflection of the resilience and strength of the economy. Figures available for unemployment (which is consistently below the OECD average with only Sweden having a better performance over the decade), balance of payments (having a strong surplus until 1979), inflation (the lowest over the decade), and fixed investment (consistently higher average growth rate) show that West German economy has been the most capable and resilient in facing the two oil price

rises. This however does not discount the fact that West Germany has been facing difficulties: for example, a strong Mark had affected its competitiveness in exports. The average growth rate is lower than in the 1960s, structural and regional unemployment and de-industrialisation have set in and unit labour costs have been rising with marked fall in productivity.

The remarkable resilience of the West German economy is explained by the fact that post-war political and institutional arrangements have played a crucial role in generating consensus on economic goals and the role of the state. The other factor is equally important: a relatively new industrial infrastructure created by post-war construction and close relationship between the banking and industrial sectors. Another factor which is often not taken seriously is the crucial role played by the SPD/FDP coalition government in the 1970s in coalescing labour and business interests in government, assisted up to 1977 by a Concerted Action Programme (incorporating business, labour, financial institutions and the government and bureaucracy). This had ensured that the state succeeds in orchestrating a series of measures aimed at economic recovery without generating ideological conflicts of interest. According to Andrew Cox:

Interestingly, institutional arrangements have assisted the SPD/FDP government because the Bundesbank has been constitutionally responsible for imposing relatively restrictive monetary policies
after 1972. This has meant that much of the opprobrium for financial stringency and public expenditure cuts has fallen on the Bundesbank rather than on the Government, which has ensured a greater degree of co-operation with the Government. 155

All sectional economic interests have also rallied behind the government for they are convinced that the government should intervene positively in three important areas of the German economy: in energy, where the state intervenes to remove bottlenecks in the market, in high-technology industries where the state's role is confined to support and development of high-technology (like microprocessors) and to resolve intractable problems through the use of regional policies and active manpower policies) to solve regional and structural problems. 156 Emphasizing on the increasing role of the state, Andrew Cox has rightly observed:

Thus, there is no conflict in Germany over the need for the state to intervene to purchase equity in declining staple industries or to encourage mergers and underwrite expensive

155 Cox, n. 150, p. 18.

research and development costs because both business and labour recognize the need for state action to generate economic growth. 157

The state's careful handling of the economy has paid rich dividends: by January 1980, Gross National Product (GNP) was projected to exceed 1.2 trillion marks with an increase of 2.5 per cent for the year. Unemployment was expected to remain between 3 and 3.5 per cent and consumer prices were projected to rise by only 4.5 per cent. What was more evident was the fact that the Government was highly responsive to the needs of the private sector, and that in the state's industrialization programme the Federal Ministry of Research and Technology was playing an increasingly crucial role. Analysts like Guido Goldman have drawn our attention to West Germany's emphasis on research and development to increase the technological component of its industry:

West German thrift, concentrated banking deposits, retained earnings and subsidies have permitted the allocation of substantial resources of R and D. West German Companies have increased their R & D outlays from 0.5 per cent of domestic output in 1964 to 1.5 per cent in 1977. Today that figure probably exceeds 2 per cent whereas in the US it is less than 1 per cent. Well supplied with capital, West German firms

157 Cox, n. 150, p. 18.
are less concerned with rate of return than with the quality of the product. 158

But the German economy has its share of difficulties so well. Since 1975, the effect of the oil crisis has been the reduced growth rate in the economy and exacerbated the problem of unemployment and diluted the concept of welfare. According to Andrew Cox:

Since 1975, the SPD/FDP coalition, despite pursuing mildly reflationary measure to ease Germany out of the recession, has had to reduce expectations about public expenditure and consumption and emphasise the need for public expenditure on capital infrastructure investment. This has meant of course a desire also to reduce wage demands and maintain the competitive position of German exports in an increasingly competitive world market. The consequence of this has been the demise of Concerted Action in 1977 as the trade unions became disillusioned by the rejection of social reforms in favour of increased aid for business and profits at the expense of wages and social expenditure. 159

As a consequence there has been an increase in worker militancy and wildcat strikes especially in areas affected by de-industrialization and structural or regional decline


159 Cox, n. 150, p. 19.

Also see, Robert W. Cox, "Labor and Hegemony", International Organization (Wisconsin), vol. 31, no. 3, Summer 1977, pp. 386-424.
like the Ruhr. Despite this, wage bargaining has remained moderate although a need is felt for a positive even if limited state role in the economy. As both sides of the industry are willing to negotiate and compromise if the need arise, West Germany is poised to face the 1980s with more optimism than many other OECD countries.

Among European States which have experienced difficulties in facing structural problems of the pre-recession period as well as bracing for the impact of recession, Britain fares the worst among its closest competitors in Europe. With the exception of 1973, Britain's growth rates over the decade have always been below the OECD average. According to Andrew Cox who has drawn a dismal economic picture of Britain:

Prior to the oil crisis Britain's growth rates are comparable with Italy.... Unemployment has also gone from bad to worse

160 This is in marked contrast to what existed earlier. According to Somnath Ghosh who did a study on participative management in West Germany 'strikes during the term of an agreement were banned irrespective of whether specific provisions in this regard were included in the agreement or not.' What was more shocking is the fact that 'unions were forbidden to exercise economic measures against an employer in relation to renewal or improvement of agreement clauses before the expiry of the terms of that agreement'. For details see, Somnath Ghosh, "Participative Management: Applicability of the West German Model", Indian Journal of Industrial Relations, vol. 19, no. 3, 1984, p. 348.
and Britain's rates have been consistently worse than the OECD average; since the oil induced recession, only Italy and Spain have worse records. This weak position has been underlined in the current account balance of payments which has been in deficit and continually balanced by invisible earnings and, from 1977, oil exports have masked a deteriorating export performance which in the 1980s (given the oil and interest rate induced strength of the pound) will probably be worse. 161

All indicators of economic performance in Britain underlie the fact that Britain has failed to find a viable solution to the economic problems which have continued to warp its economy. No reform has touched the antiquated industrial base of the economy and there has been a lack of capital and high-technology investment. In the export front, Britain's performance leaves much to be desired as is reflected in the bankrupt state of its Exports Credits Guarantee Department. The crisis affecting Britain's Exports Credit Guarantee Department owes greatly to the dramatic increase in non-payment to British exporters by both individual companies and by the host of countries rescheduling their entire overseas debt. The political risk alone produced claims totalling £ 1.1 billion in 1983, up by £ 234 million from the previous year. According to the Business Observer:

161 Cox, n. 150, p. 24.
The Government faces the prospect of heavy and ongoing handouts from the taxpayer to keep the Exports Guarantee Scheme in operation. Apart from the manifest political embarrassment, this would also put Britain foul of the GATT which stipulates that exports must not be indirectly subsidised by cheap insurance. 162

To strengthen its sagging economy, Britain is relying more on its oil revenue, for North Sea is now the biggest producer, outside OPEC of top quality 'sweet crude oil' and is competing directly in the market with oils from other hard-pressed OPEC producers such as Algeria, Libya and Nigeria. 163 This has alarmed OPEC so much that it is planning to invite Britain to formalise its production within the OPEC quota system. (See Table XII) The move is an attempt to head off a potential trade war between Britain and the still oil rich Middle Eastern countries. 164

164 OPEC has declined to make any official comment, but unofficial suggestions have been preferred that those countries with which Britain has a substantial trade surplus might start placing valuable orders elsewhere. On the other hand, although UK Government has always refused to limit North Sea output to a fixed level agreed with OPEC, it is aware of the fact that to refuse to acknowledge OPEC's case could upset present oil price stability. It is significant that North Sea output is running at 2.4 million barrels a day, 12.5 per cent above the figure notified to OPEC in March 1983. OPEC has argued that by limiting output, it has kept oil prices nearer $29 a barrel rather than $25 which could have resulted if output were increased. For details see, The Times, 7 November 1983.
### TABLE XII

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</table>


Britain has remained unmoved by the OPEC threat and to make its oil industry more competitive has decided to

165 UK has been under considerable pressure from US to give no or little assistance to OPEC and to allow the full play of free market forces to determine OPEC prices. For details see, Steve Vines, "OPEC: Lawson Pact", *The Observer*, 13 March 1983.
privatise it. This is being done through British Gas, whose on-shore oil field at Wytch farm was sold to private bidding and efforts were made to sell all its North Sea oil assets valued at £750 million to £1000 million. For this reason British Gas's extensive holdings in North Sea oil fields (including Beryl Hutton, Montrose and Fulmar) have been formed into six different companies at different stages of development. British Gas has however expressed its disapproval of the Government's plan to privatise it, and has been reluctant to proceed with the Wytch Farm field sale. 166

The British Government under Mrs Thatcher has however overruled British Gas's objection for it feels that

166 Proven reserves are put at 220 million barrels, making it the largest on-shore oil field in Europe. Additional unproven reserves could take this to 350 million barrels. For details see, The Observer, 3 April 1983. The British Government however did not react kindly to British Gas's delaying tactics, and so it has urged Britain Gas to push forward with its negotiations to sell the Corporation's half share in Britain's biggest on-shore oil field at Wytch farm in Dorset. The talks were supposed to be held with a Dorset consortium including Premier Consolidated, led by Tricentrol, Clyde Petroleum, Gas Oil, Acreage and Carless Carpel. The Corporation has put the value of its share in Wytch farm at £500 million. The other half is owned by BP. For details see, The Times, 31 March 1983.

While Britain has succeeded in building up a viable oil business, the reverse is true for OPEC. OPEC's latest output figures show that its crude oil exports fell by 22.7 per cent in 1982 to 14.28 million barrels a day. The value of exports dropped by 21.5 per cent from $255.61 billion to $200.79 billion. It is significant that OPEC's share of world crude oil trade dropped from 71.6% in 1981 to 63.9% in 1982. Its share of world production fell from 40.3% to 35.3%. For details see, The Times, 7 November 1983.
BGC's monopoly is a 'serious disincentive' to gas exploration which had led to British Industry not getting all the gas it wanted. According to Nigel Lawson, the British energy Secretary, the new measures including private access to BGC's pipeline system "will for the first time introduce real competition into the market for gas". However according to John Andrews of the Guardian:

It remains to be seen whether gas consumers like the steel and paper and board industries will get lower prices by dealing direct with the North Sea oil companies. Since in the past BGC has kept the price it pays to the companies well below world rates. 167

Feeling in British National Oil Corporation (BNOC) is more favourable to 'privatisation' (which would encompass the Corporation's development and production activities) for it feels that it would be given an opportunity to free itself from the control of the Treasury. 168 However, 'privatization'

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168 Significantly in 1980, BNOC made a pre-tax profit of $309 million. Among the most important proposals drafted by Nigel Lawson, the most significant are the following: (1) the transfer in 1982 of the entire oil producing business of BNOC to the private sector with the state retaining only a minority stake. BNOC's business interests would include the producing fields of Thistle, Dunlin, Ninian, Statfjord and Murchison, the Viking Gas field and potential production from Beatrice, Brae and Hutton. (2) the privatization of BGC's monopoly right to purchase natural gas from the North Sea and sell the gas to industry. However BGC's gas fields were not affected and BGC's monopoly on sales to domestic consumers remain intact and there were no plans to allow British Gas to be sold overseas.
in UK did not have a smooth sailing. According to Jonathan Davis, a noted commentator:

Experience in the last four years with their attempts to privatize BNOC and the British Gas Corporation's oil assets has underlined that shifting from the public to the private sector is a long, complex and tortuous business; it is littered with technical, legal and political obstacles - as well as false leads and the occasional decisive intervention of external circumstances. 169

Nor does privatizing a company always relieve the Government of financial demands from it. According to another noted commentator, Barnaby J. Feder:

Britain reduced its holding in British Aerospace from 100 per cent to 43.4 per cent in three years. Nevertheless, a company request for about $612 million in Government aid may be crucial to its future as a participant in the A-320 to be built by Airbus Industrie, the German, French and British Consortium and perhaps to the future of the plane itself. 170

169 For details see, Jonathan Davis, "Why rolling back the state Frontiers is so tortuous", The Times, 25 August 1983. In the case of BNOC for example, it was the rise in price of oil and supply uncertainties of 1979, promoted by the Iranian revolution, that played a decisive role in persuading the British Cabinet that it should keep the rump of BNOC intact as a State Oil Trading Company. Also see, Fariborz Ghadar, "Political Risk and the Erosion of Control: The Case of the Oil Industry", The Columbia Journal of World Business (New York), vol. 17, no. 3, Fall 1982, pp. 47-51.

But this has not deterred Britain from proceeding with 'privatization'. It has sold all or much of its stake in 12 ventures and many more sales are in the offing. However, privatization does not imply that the Government ceases to exercise influence in a Company. For example, when Britain collected most of its North Sea oil exploration and production interests in a new company called Britoil and sold 51 per cent of it to private investors for $767 million (at current exchange rates) it retained special voting rights to block a takeover by foreign investors.

'Privatization' however has not generated much public indignation in Britain. The mood of the British public is sought to be captured in the following observation made by Barnaby J. Feder:

the recession and the industrial restructuring generated by it have led to state take-overs of many companies to prevent the job losses that would come with bankruptcy. At the same time, the economic troubles have persuaded millions of European voters that there are limits to the social services they can support. 171

Probably what is more significant is the fact that the mechanics of privatization has forced Britain to devote a great deal of attention to the actual structure of its basic industries. For example, British Telecom’s management

and accounting systems were negligible by commercial standards until planning began for its sale. Another argument put forward by the British Government is that privatization encourages competition which in turn reduces costs and improves services to consumers. In its bid to popularise 'privatization' it has started propagating that the 10 per cent of British Industry that is nationalized is bloated and complacent. But 'privatization' would not signify an end to Government role in industry. Its continuing role is clearer still in the case of British Telecom, which is expected to bring in almost $6 billion when a 51 per cent stake is sold. Telecom, according to the latest plan, will be regulated by a newly created office of Telecommunications and the Government will allow only one competitor in the field of basic services.

While it remains to be seen whether 'privatization' lends competitiveness to British public sector undertakings, the labour front provides us with a very disquieting picture; between 1975 and 1981, Britain lost through strikes an average of 571 working days per 1000 employees, compared with 411 days in the EEC as a whole. The unhealthy atmosphere

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172 In 1981, 197 working days per 1000 were lost through strikes in Britain. The highest strike rates were experienced in Canada (899), Australia (814), Italy (588), and the United States (370). Countries least troubled by disputes were Germany (3), the Netherlands (6), Japan (14) and Norway (17). For details see, The Times, 31 March 1983.
in the British labour front has not only embittered relations between the Government and labour \(^{172}\) but has also hardened labour's attitude towards introduction of new technology, especially in old, maturing industries. \(^{173}\)

But what is more ominous is the fact that there is evidence to suggest that Britain's technology policy still has remained largely geared towards its defence sector and there has been no substantial spin-offs: 53 per cent of Britain's publicly funded research is devoted to defence, compared with 35 per cent in France, 12 per cent in West Germany and only 4 per cent in Japan, and some labour groups rightly feel that efforts should be made by Britain so that Defence scientists and technologists are re-

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\(^{173}\) This was most evident in 1980, when the Conservatives passed the Coal Industry Act, requiring the National Coal Board to break even by April 1984. The central plank of NCB strategy was the automation programme begun in the 1970s, with mine operating system (MINOS) a standardised computer system for the surface control of all colliery operations. Interestingly, NCB superpits automatically defined others as 'uneconomic'.

deployed in socially useful and exportable technologies. 174

While UK's Defence sector is busy exploiting the most promising scientists and technologists, the British Industry is threatened by University Grants cuts. 175 But it must be conceded that sincere efforts have been made by Science Research Council to bring about a shift in emphasis towards industrial relevance (budget $70 million a year) and dirigiste projects have been given priority for their industrial importance, one of the latest fields

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Also see, Richard S. Rosenbloom and William J. Abernathy, "The Climate for innovation in Industry", Research Policy (Amsterdam), vol. 11, no. 4, August 1982, pp. 209-25; and


175 In engineering and technology, it is down by 5 per cent since 1979. It is significant that admissions to University Science and Engineering courses in Autumn 1982 were 4 per cent below that for 1979. For details see, Peter Wilby, "Industry threatened by University Grant Cuts", The Times, 19 December 1982.
singed out for priority being 'industrial robots'.

It remains to be seen whether SSRC's belated efforts pay dividends, for Britain's industrial profile has changed for the worse over the years. An ILO study entitled "Structural adjustment in the United Kingdom Manufacturing

The SRC already spends over $100,000 a year on robots. Now it will make another $1.1 million available. The SRC is also engaged in exploring ways of helping graduates to adapt to work in industry. One idea which is bandied around is to sandwich work is a company with continued training at University. According to the Economist, 'the greatest value is the feedback they should provide in making University teaching of engineering and science more relevant to industry'. For details see, The Economist, 8-14 March 1980, p. 94. Also see, Gavin Scott, "Is British Science on the Wrong Track?", The Listener, 3 March 1983, pp. 7-8. Paul Feyeraband, Science in a Free Society (London, 1982), p. 210; Keith Pavitt, ed., Technical Innovation and British Economic Performance (London, 1980), p. 350; and I.G. Csizmadia, "The Dialectical Interaction of Science, Technology, Economy and Politics: A Quest for Rational Research Policies", Science and Public Policy (Guildford, Surrey), vol. 9, no. 5, October 1982, pp. 255-61; and Sol Encel, "The post-Industrial Society and the Corporate State", The Australian and New Zealand Journal of Sociology (Kensington), vol. 15, no. 2, July 1979, pp. 37-44.

Industry" has observed that its industry has borne the brunt of economic recession and shrinking job market. Looking at shifts in industrial activity over the past ten years, the study suggests:

UK may have become a specialist in low-value products within industries;...and its competitive gains have been principally over the Third World:

The UK has come to occupy a weak position in the division of labour among industrialized countries, importing goods that need highly-skilled, technically trained labour and exporting products that need only semi-skilled workmanship. Yet it is also logical to suppose that the UK's specialisation in less sophisticated products will increasingly put it into competition with these low-wage but increasingly productive countries. 177

177 UK case study is the ninth in an ILO research project on Employment, Trade and North-South Co-operation, quoted in The Telegraph, 16 February 1984. This ILO study has considered the history and prospects for British manufacturing in the cotton, consumer electronics and motor car industries, and feels that there is 'need for a fairly radical break with past patterns of behaviour'. This study has pointed out that many of Britain's industrial problems derive from 'deeply ingrained cultural and historical factors, which for so long have been ducked with the excuse that attitudes cannot be changed by legislation'. Historical records however point out to the lack of consistency in British industrial culture. According to Leslie Hannah, 'between the 1880s and mid 1920s, Britain was experiencing slower rates of growth of output per head than in any other decades of the last hundred years. At a time when Germany and America were shifting resources into new industries and new markets, Britain was falling behind because her entrepreneurs were for whatever reasons failing to do so.' For details see,
It is unlikely that in the near future, British economy would take a turn for the better, if one has to draw conclusions and projections from the present state of British economy. The economic malaise is much deeper than that to meet the eye. According to Andrew Cox:

there is a divorce between the interests of the City and the productive base of the economy; there has been a continual rise in expectations of increased living standards and wages without increased productivity and profitability; and an ever increasing burden of rising public expenditure on a declining private economic base.... in large measure the failure to resolve these problems (which were apparent before the oil crisis and not caused by it) has been due to political stalemate and inertia than through economic myopia. British Governments throughout the 1970s and particularly since 1972 have pursued ever increasing neo-corporatist solutions which have mirrored the state interventionist policies in other European countries. Unfortunately, due to the adversarial nature of political life in Britain and the defensive strength of both labour, business and financial interests to resist state modernisation and rationalisation of the financial and industrial base, it has been impossible for any Government to make centrist neo-corporatist policies work in office.

Britain has therefore oscillated between neo-


Also see, Christopher Saunders, Engineering in Britain, West Germany and France (Brighton, 1981), p. 6; and Vincent Cable, "VIII : Britain, the 'new protectionism' and Trade with the newly Industrialising Countries", International Affairs (London), vol. 55, no. 1, January 1979, pp. 1-22.
liberal, monetarist solutions and failed corporatist prescriptions, forcing the British economy into a permanent downward spiral. 178

Europe's Industrial and Technological Response to the Economic Crisis: Problems of Industrial Adjustments

Until 1973, the six original members of the European Community had sustained rapid economic growth. This enabled them to discard certain traditional industries in favour of new technologies. The high growth industries which spurred their booming economy were chemicals, oil


Also see, David Coates, "Britain in the 1970s: Economic Crisis and the Resurgence of Radicalism", in Andrew Cox, Politics, Policy and the European Recession (London, 1982), pp. 141-66.

One general indicator can be found in the United Nations Statistical Yearbook for 1978. According to UN data, taking 1975 output levels as 100, the total product of the United Kingdom economy between 1960 and 1977 moved only from 72 to 105 (grew in total by 45 per cent over the period). Over the same period, the Japanese economy moved from 28 to 106 (grew by 378 per cent), the West German economy moved from 57 to 109, the French from 47 to 108 and the US economy from 61 to 111.
and energy products other than coal, electrical and electronic equipment. Italy and the Netherlands made rapid strides in steel industry, whereas Italy alone consolidated its position in textiles. Similarly, France carved out a niche for itself in agricultural and industrial machinery, while West Germany made its presence felt in transport, construction and along with Britain) in food processing industry.

Since 1973, steel, textiles, clothing and paper, together with industrial construction, building materials and ship building have suffered severe setbacks in all countries owing to factors like competition from newly industrialising countries and twin challenges posed by US and Japan. 179

179 Emil Kirchner, "The European Community and the Economic Recession: 1973-9", in Andrew Cox, ed., Politics, Policy and the European Recession (London, 1982), p. 219. Lately, the economic outlook in terms of investment, seems to have changed for the better. An EC Commission Survey has found out that investment in the EC will increase in 1984 by an inflation - adjusted 4.7 per cent after a 2.5 per cent drop in 1983. From the survey it appears that investment in the engineering and metal sectors will be favoured with a special emphasis put on restructuring plans for the steel and car industries. For details see, International Herald Tribune, 9 February 1984. The investment plans for 1984 appear to reflect a better outlook for total demand and improving profitability of companies. Also see, Ernst-Otto Czempiel, "Germany and the Third World : The Politics of Free Trade and the Free Hand", in Wolfram F. Hanrieder, ed., West German Foreign Policy, 1949-1975 (Boulder: Colorado, 1980), pp. 181-96.
The problem has been exacerbated because of the half-hearted attempts made by older, industrial countries to adjust themselves to a new industrial and technological environment. Countries like UK still have not lost faith in their old industries like ship-building, coal and steel. The latest Annual Expenditure White Paper brought out by its Department of Trade and Industry provides numerous insights into Departmental inconsistency and confusion by not only putting emphasis on the application of new technologies but also supporting ship-building, steel and (with the Department of Energy) coal! According to Tim Congdon, a critic of the White Report:

The Government therefore is simultaneously subsidizing high technology and low technology. If by some lucky chance run-of-well, it could set about subsidizing them and the department's operations would acquire a new lucidity of purpose, one is reminded of the idea, attributed to the European Commission, that there might be 'a dynamic role for traditional sectors'. The thinking, if it may be called such, seems to be that the department is to help the reallocation of resources from decaying industries to those with an exciting high-tech future. The aid to steel, ship-building and coal is, in other words, an unhappy but inevitable mistake which arises from the reluctance of the Department of Health and Social Security to take on new responsibilities.

Ironically, spending on 'scientific and technological assistance' is due to rise from £324 million in 1983-84 to

180 Tim Congdon, "White Paper that could be a Script for 'Yes Minister'", The Times, 22 February 1984.
£ 410 million in 1986-87 while support for previous 'flops' such as steel, ship-building and Concorde is to be phased out. But what is amazing is that, as the accompanying table shows, the number of civil servants superintending this process is to fall by a grand total of five between 1 April 1984 and April 1985 and to be constant thereafter.

TABLE XIII

DEPARTMENT OF TRADE AND INDUSTRY MANPOWER TARGETS TO 1987

<table>
<thead>
<tr>
<th>Date</th>
<th>Numbers employed</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.4.1984</td>
<td>12,738</td>
</tr>
<tr>
<td>1.4.1985</td>
<td>12,733</td>
</tr>
<tr>
<td>1.4.1986</td>
<td>12,733</td>
</tr>
<tr>
<td>1.4.1987</td>
<td>12,733</td>
</tr>
</tbody>
</table>

Source: Table 2.4.2, Government's Expenditure Plans, 1984-85 to 1986-87, Cmd. 9143-II.

The fact that Britain needs to revamp its outdated industrial and technology policy has been pointed out by noted British technology policy experts as Roger Williams, who has observed:

The country's share of world trade in manufactured goods fell precipitately in the 1960s (15 to 9 per cent), but worse still there is evidence that imports have on balance become steadily more technologically advanced than
exports. Inevitably, manufactures have contributed a falling proportion of overseas earnings (52 per cent 1971, 43 per cent 1981), leading to a historically advanced deficit on advanced goods. Inevitably too, and worsened by the international recession, employment in manufacturing industry has fallen sharply (8.1 million 1971, 5.7 million 1982). This economic slide relative to other advanced industrial countries which has resulted has been disguised only by the strength of the service sector and the fortuitous arrival of North Sea oil. 181


The European Community however continues to be a lucrative market for British manufactured goods. Manufactured exports to the Community increased by 480 per cent between 1972 and 1980, compared with 237 per cent to Japan and 234 per cent to the US. The Community now takes 43 per cent of British exports compared with 29 per cent a decade ago. While exports to the Community rose by an average of 28 per cent a year between 1972 and 1980, imports from it grew by only 24 per cent a year. West Germany has now displaced the United States as Britain's biggest trading partner; and all the other members of the Community except for Greece and Luxembourg are among UK's top 12 export markets. For details see, The Times, 5 January 1983.

This is in marked contrast to what existed a decade back, when Britain's trade with the EEC had moved into deeper deficit, with imports outstripping exports at an annual rate of around £1.6 billion in the first four months of 1974. At that time, British capital investment was nearly stagnant, with a 5 per cent increase in real terms in 1974, provoking the Economist to comment 'there is little possibility of the Community agreeing to a really generous industrial free-trade zone with Britain, although such arrangements have been agreed on for the European Free Trade Association countries'. For details see, The Economist, vol. 251, no. 6827, 29 June 1974, pp. 61-62.
Among the factors contributing to the performance of any country's manufacturing industry, the capacity for goal-oriented and sustained technological innovation is important, hence the need for a "national technology policy". British technology policy has remained dispersed rather than concentrated, for British Technology Policy planners had tacitly assumed that there was a necessary correlation between R and D expenditure and growth. Although in 1964, UK had provided itself with a Ministry of Technology, its bureaucracy continued to treat technology as a tool rather than a policy, focussing instead on industry. 182

Lack of co-ordination between the Treasury and the Department of Industry has also contributed to the state of anarchy which pervades the official technological and industrial establishments in UK which is concerned with policy-making. The Treasury has always reacted unfavourably to British support for such projects as Airbus, Jaguar, and the British Telecom Computer. According to Howard Davies, a former British Treasury official:

This Treasury impotence should be a source of concern and never more so than now, when the focus of economic decision-making has again passed to the industrial sector. The inner core of the Treasury may pore over drafts and

redrafts of the Budget speech, whose outline seems clear already from the November statement and the Public expenditure White Paper, yet the Prime Minister's time in recent months has been more taken up with Airbus, Jaguar and the new British Telecom Computer (ICL or IBM) than with interest rates, sterling M3 or even the public sector borrowing requirements...the forces of darkness always seem too strong. Led by an indigent company with the Ministry of Defence in tow, marshalled by the Department of Industry - a lobby in search of a cause - an unholy coalition evolves around each spendthrift proposal. Adding insult to injury, the Foreign Office can usually be found parroting the profligates' case, squawking "Anglo French relations", its own equivalent of "pieces of eight" in the Prime Minister's ear. 183

Ignoring the tight-fisted Treasury's advice, the British Government has continued to increase its R and D expenditure: UK's latest Department of Trade analysis of Industry's R and D spending shows that it rose by 63.5 per cent to £3.8 billion between 1978 and 1981. But a new EEC survey shows two disturbing trends: one is that over the period from 1963-1981, British high-technology exports grew less rapidly than those of any other EEC member. Britain actually achieved an eight-fold growth rate almost half that of France. Half the Government spending on R and D which

183 For details see, Howard Davies, "Clipping the big Spenders' Wings", The Times, 3 March 1984. According to Howard Davis, "The Treasury has lost another industrial policy battle. British Aerospace has been given funds to manufacture the wings of Airbus Industries' next loss-making venture and £250 million of tax payer's 'launch-aid will be invested in a plan with little chance of commercial success."
is a quarter of the total, went for defence: this appears to have produced little spin-offs into civil products and relative to the amount spent; only limited exports. 184

But the British Government seems to be determined to imbibe new technology. The Government is planning to spend more than £100,000 million supporting a series of academic research projects to find ways of encouraging the acceptance of new technology. This is one of the 17 international programmes following the 1982 economic summit held at Versailles. But some academics fear that the projects to be paid for by the Department of Trade and Industry could amount to an exercise in opinion management. Their fears are not entirely unfounded, for the principal objectives of the programme, as laid by the Department, is to formulate lessons for industry and Government on how to secure greater acceptance of new technologies by developing their positive aspect, and minimizing their negative aspects, from an enhanced understanding of the cultural and organizational determinants of public attitudes. Acceptance of new technologies

at the workplace would be main, but not the sole focus of the work. 185

This exercise in opinion management probably is one of the attempts aimed at softening public opinion regarding £350 million research programme on the most advanced computer technologies. Provisions have also been made for a £3.5 billion investment in cabling half of the UK. The key to cable TV would be the non-entertainment two-way services: home banking, home shopping, which, Information Technology Minister Kenneth Baker, feels will give new impetus to British industry in general. Cable will also be a rival to the telecommunications network of British Telecom and Mercury, and it is felt that the extra competition should result in more services to the public apart from being price competitive.

Britain has drawn up an ambitious scheme called the the Alvey programme in this area which will concentrate on


This comes after publication in March of a Working Group Report on technology, growth and employment, which suggested that the roots of opposition to new technologies sometimes go beyond technical considerations. Applications have already been invited from selected research groups in the fields of four projects: information technology and the organization; new communications technology and the consumer; comparative national assessments and historical studies of the problem.
four areas:

(1) software engineering: This involves the development of more efficient and improved ways of instructing computers.

(2) very large scale integration (VLSI): highly advanced and tiny chips, which are extremely fast and powerful.

(3) Man machine interface: This means finding new ways for people, often non-specialists to communicate with computers by voice, touch or sight.

(4) Intelligent knowledge-based systems (IKBS): Sometimes also called expert systems, which give computers a specialist knowledge, making them function more like a human brain.

186 Richard Brooks, "Britain's £ 4,000,000,000 technology Gamble", The Times, 1 May 1983.

The British Cabinet Office Information Technology Advisory panel in its report, October 1983, prepared by the Institute of Information Scientists observed; "we wish to underline the need for a strong and effective British Information Industry based on our existing resources which include high grade professional skills. Success in promoting and developing this industry will improve the numbers (and the quality of) employment; it will generate economic wealth, both directly and indirectly; and it will help Britain to increase its overseas earnings." It is significant that 1982 was designated as the Information Technology Year and the same year had embarked it on a programme to increase the awareness of British Industry to the presence of computers, telecommunications, automation, control and video.

For details see, Bill Johnstone, "Technology Transfer", The Times, 20 February 1984.
Britain's successful thrust in information technology has already generated considerable interest in US, which is keen to co-operate. It is significant that IBM is keen to abandon its traditional independence and is prepared to co-operate with European information technology industry. Telecommunications is one sphere in which the US-owned Computer Group is seeking a joint-venture with a European company. This explains why IBM is lobbying hard to be included in the £350 million British Government programme to stimulate research in advanced information technology and fifth-generation computers following the Alvey Report. But the Alvey Committee had recommended that foreign owned companies like IBM should be excluded from the co-operative Government-induces back to parent organizations abroad. 187

It is ironical that while IBM is trying its best to find a place for itself in the European Community's ESPRIT programme (European Strategic Programme for Research and Development in Information Technology), 188 Britain along

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188 Similar argument has been offered about whether the programme should be restricted to European-owned companies or be open to American multinationals with European research and development activities. It is significant that IBM hopes to take part in three Esprit projects. ESPRIT is concentrating on three key technologies: advanced microelectronics, information processing and software technology, and will be directed to two specific applications: office automation and
with West Germany showed considerable tardiness in approving the plan, which could be done only after they had accepted Commission re-assurances about the need for Community budget stringency.

While Britain has remained lukewarm towards the Community's ESPRIT programme, it has been enjoying a boom in new high-technology ventures that shares several characteristics with the phenomena of Silicon valley in Northern California and Route 128 round Boston and Cambridge, Massachusetts. British companies like Xionics, have done such advanced work that they are reckoned by some experts to have a two-year lead in one of the most fastest-growing areas of computer-technology: so-called local networks, that make different brands of computer compatible with one another.

Recession may also have contributed its share: both the threat of unemployment and the shortage of finance for university research might have spurred the creation of many new companies. Another stimulus is the advent of cheap micro-electronics. Now that a basic micro-computer can be assembled for as little as $ 50 or so, the amount of start-up

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computer integrated manufacturing. A four-year 'technology pull' phase would be followed by five-years spent in the late 1980s on 'market push'. For details see, Victor Smart, "Europe's great industrial gamble", Observer Business, 4 March 1984.
capital needed by a new company has been substantially reduced. A high proportion of new companies was started by employees of existing venture capital firms - but finance is still not as plentiful, as in the United States. 189

It remains to be seen whether Britain's new found dynamism in high technology is reflected in its export of manufactures, for the latest data indicates that Britain's deficit on overseas trade in goods other than oil widened by a massive £ 5.3 billion a year to £ 7.5 billion. The deterioration was concentrated in trade in manufactures which recorded a deficit of £ 2.1 billion, the first since the industrial revolution, after a surplus of £ 2.5 billion in 1982. 189a

189 The Economist, vol. 280, no. 7195, 25-31 July 1981, p. 83. The British banks and National Research Development Corporation was initially not very enthusiastic about these high-technology ventures and had refused to put up money.

189a According to Frances Williams: "The worsening trade balance, only partly reduced by a growing oil surplus, was the chief factor behind the drop in overall current account surplus from £ 5.6 billion in 1982 to £ 2 billion in 1983. A £ 500 million deficit on visible trade - the first since 1979 was countered by a £ 2.5 billion surplus on the invisible account, which includes services such as insurance and shipping. For details see, Frances Williams, "UK trade surplus falls to £ 2 bn", The Times, 9 March 1984.

British Press reports give the feeling that Britain has been trying for scapegoats to explain its decline in trade in manufactures: one recent example being the veiled insinuation that bureaucratic incompetence by the European Commission is partly to blame for the failure of British firms to win any big orders for Japan's huge telecommunications market. On closer examination, it is observed that eighteen out of the 23 major foreign orders placed were from the United States, which has been lobbying hard and relatively successfully for NTT to open up its market. What British sources have carefully omitted is the fact that Britain had yet to liberalize its own telecommunications market.

What is often forgotten is the fact that British oil revenue would inevitably drive up the value of the pound, making British products more expensive and foreign imports cheaper. Eventually this would force a structural change in the British economy away from traditional manufactures like steel and cars to more sophisticated goods and services. But in the short-run, industry would shrink and

190 Peter McGill "EEC Lose Out", Observer Business, 4 March 1984. Nippon Telegraph and Telephone (NTT), Japan's monopoly telecommunications supplier for the domestic market, bought 11 billion yen (about £32 million) worth of foreign equipment and materials in 1982, and expects to place another 30 billion yen worth in the current financial year. It is small compared with its total procurements: 648 billion yen in the past financial year. NTT's latest bulletin reveals that the only 'major' order from Britain was for some 'dry-process paper' from the UK subsidiary of Rank Xerox.
unemployment would rise dramatically.\textsuperscript{191}

Terry Barker, co-director of the Cambridge Growth Project at the University of Cambridge has pointed out that other energy-rich industrial countries, like Norway and the Netherlands have absorbed their oil and gas fortunes without destroying their industrial structure or provoking large-scale unemployment. And in a paper that has gained currency in anti-Thatcher political circles, Professor Barker suggested that a North-Sea oil investment fund be created to offer low-interest loans for new, high-technology industries that would generate competitive exports when oil outflow begins to dwindle.

North-Sea oil's contribution to the balance of payments now running at over £ 13 billion is expected to fall to zero by the end of the decade. That gap would be too big to be bridged with proceeds from overseas investments on which the British government has reposed faith, or by higher earnings from services. Only a return to a surplus on trade in manufactures could help in balancing Britain's overseas payments. But creating capacity in the new expanding, high value-added sectors of manufacturing will

require much more than a competitive value for sterling. Britain's National Economic Development Office has therefore argued for greater investment in the equally crucial areas of product innovation, design, improved management techniques and marketing. 192

Although the latest British budget has called for slashing corporate tax rates over the next three years, at the same time, the Government has reduced tax breaks on investments in plant and machinery. By this act, the Government expects to speed up investment as companies would move forward spending plans to beat the planned withdrawal of tax reliefs. But on closer examination, one can discern that the budget would tend to help service industries at the expense of capital-hungry manufacturers. 193

192 The Times, 10 March 1984.

193 The latest budget seems to be a follow-up of a radical plan submitted by a group of conservative businessmen and MPs way back in 1981. The main point of the plan was to ease the burden of interest payments on industry by allowing firms to deduct corporation tax at the time of repayment to the banks. The banks would be repaid by the Government and business would avoid the normal 18 months delay before relief comes through. The report observed that at a short-term cost in tax-relief of £300 million, some £3 billion of investment funds could be generated. For details see, William Darling, "March by state control takes one step backwards", The Guardian, vol. 125, no. 18, 1 November 1981, p. 3. Also see, Terry Barker, "The Economic Consequences of Monetarism: A Keynesian View of the British Economy, 1980-90", Cambridge Journal of Economics (London), vol. 4, no. 4, December 1980, pp. 319-36.
The French Response

France had seen its industrial expansion gathering momentum in the 1960s which had contributed to its high rate of growth for most of the 1950s and 1960s. It was unprepared for the increase in inflation fuelled by the escalation in oil prices. Although it was less prone to stagflation, it had suffered overcapacity in basic steel, chemicals and shipbuilding which had also affected all other major competitors.

By 1978, it was more than clear that France would have to make a choice between general impoverishment and enhancing the competitive capacity of French firms. To quote the 1978 Report on the Adaptation of the Seventh Plan: "Thus employment is linked to growth. Growth is linked to the balance of payments, which in turn is linked to the adaptation of our industry." The French Government kept harping on this argument, in order to dispel the illusions of those who thought that it was the prime duty of the state to ensure conditions favourable to full employment. Instead it stressed on the importance of the combating inflation and promoting industrial redeployment. By 1980, France had taken unemployment for granted, so the Employment Commission of the Eighth Plan regretted that the concentration upon
competitiveness had relegated unemployment to a secondary position:

There seems to be a sort of general acceptance of unemployment within French society. Consequently, when the main economic, social and political forces attach greater importance (sometimes unconsciously) to other objectives, the growth of unemployment becomes, after inflation, a way of regulating an economy confronted by serious problems of structural adaptation. 194

But the French insistence on competitiveness has not been able to prevent the downturn in productivity: there has been a marked decline in its average annual increase: from 5.1 per cent in 1969-74 to 3.6 per cent in 1974-79 (and even 3.3 per cent in 1977-79). This has also been followed by the reduction in work week. Prior to the 1974 recession, reduction of the work week was most manifest in large firms nursing the most dynamic industries, but since the recession the reduction has affected mostly small firms in the declining industries, with low productivity and pay, as a way of adjusting to full in demand.

Another interesting development which is taking place is the re-structuring of production under the impact

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of technical change and the challenge posed by foreign competition. According to Jack Hayward:

Agriculture, which had been characterised by a rapid reduction in its workforce in the decade 1963-73 (annual fall of 128,000 mainly among farmers rather than farm labourers) has since experienced a slowdown to 72,000 per annum (even lower since 1975 at 60,000 to under half the pre-1974 rate) playing its traditional role as a rural refuge from the full impact of industrial slump. Whereas industrial employment had been increasing annually by 64,000 in the period 1968-73, from 1973-79 it was falling by an average of 68,000 each year, the fall first being registered in the last quarter of 1976. Over half of the jobs lost in the period from 1975-8 were in industries - notably textiles, iron and steel - that had been deciding even before the recession. However, the mainstay of industrial employment, the expanding motor-car industry, itself went into recession in 1980.

Decline in agriculture has been more than compensated by the increase in the service sector, where the number of jobs has increased by 170,000 in 1962-3, 240,000 in 1968-73 and 223,000 in 1975-79. But according to Jack Hayward:

this overall growth conceals a change in the type of tertiary employment, from an emphasis on trade prior to 1963, to public-service employment since then, especially health services in the most recent period...finally, there has been steady growth in the number of white-collar employees, managers and

195 Jack Hayward, ibid., p. 115.
members of the liberal professions, which is consistent with the expansion in the service sector despite the dire predictions for the future arising from foreseeable technological advance, notably in electronics. 196

The French Government's insistence on competitiveness in French firms has indirectly contributed to increase in bargaining position of the employers, who have tried their best to reverse the 1960s' trend towards unified and stable conditions of employment. They have sought to do it by increasing the number of special types of fixed term and temporary contracts to enhance managerial capacity, to reduce manpower costs and giving wide powers to the management.

Attempts at making the workers a docile lot has not been entirely successful as is evident from the current spate of industrial unrest that is sweeping France. 197 The carrot and stick policy adopted by the French Government towards its working class populace is reflected in the

196 Ibid., p. 116. While the end of fixed term contracts accounted for 25 per cent of those registering as seeking employment in 1976, the number had risen to over 35 per cent in 1980.

197 Diana Geddes, "France braced for mass demonstrations as industrial unrest spreads", The Times, 2 March 1984. This is the biggest single display of union discontent since the socialists came to power in May 1980. For details see, Diana Geddes, "Strike halts French Services", The Times, 9 March 1984.
parallel increase in public and social security expenditure from 1974-78, which has grown 1 per cent faster than revenues and 3 per cent faster than the Gross Domestic Product. Table XIV also shows that because social transfer payments have been increasing annually at 7.9 per cent on average, compared with other public expenditure, by 1978 they constituted for over half of the total.

**TABLE XIV**

**FRENCH PUBLIC EXPENDITURE, 1971-78**

<table>
<thead>
<tr>
<th></th>
<th>1971</th>
<th>1978</th>
<th>%</th>
<th>Rate of average annual growth(%)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>(current)</td>
<td></td>
<td></td>
<td>(constant francs)</td>
</tr>
<tr>
<td>Wages</td>
<td>61.6</td>
<td>169.8</td>
<td>13.8</td>
<td>5.8</td>
</tr>
<tr>
<td>Consumption</td>
<td>41.1</td>
<td>95.3</td>
<td>10.5</td>
<td>3.2</td>
</tr>
<tr>
<td>Investment</td>
<td>29.2</td>
<td>65.8</td>
<td>7.3</td>
<td>2.8</td>
</tr>
<tr>
<td>Social transfers</td>
<td>145.6</td>
<td>460.5</td>
<td>50.8</td>
<td>7.9</td>
</tr>
<tr>
<td>Economic transfers</td>
<td>21.6</td>
<td>67.2</td>
<td>7.4</td>
<td>7.6</td>
</tr>
<tr>
<td>Other public expenditure</td>
<td>19.7</td>
<td>47.4</td>
<td>5.2</td>
<td>3.7</td>
</tr>
<tr>
<td>Total public expenditure</td>
<td>518.8</td>
<td>906.0</td>
<td>100.0</td>
<td>6.2</td>
</tr>
</tbody>
</table>

The economic slump had the greatest impact upon competitive private-sector investment, which failed to stage a recovery to the 1972 figure until 1978, while the rate of self-financing also staged a comeback in 1978 and 1979. There was also a sharp decline in investment by firms, which fell as a percentage of sales from 4.9 in 1972 to 3.5 in 1976 (Table XV).

**TABLE XV**

INVESTMENT AND SELF-FINANCING BY NON-NATIONALIZED FIRMS, 1972-78

<table>
<thead>
<tr>
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<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Investment (1970=100)</td>
<td>118.7</td>
<td>124.1</td>
<td>120.8</td>
<td>108.3</td>
<td>117.9</td>
<td>115.4</td>
<td>118.6</td>
</tr>
<tr>
<td>Rate of self-financing</td>
<td>74.5</td>
<td>69.0</td>
<td>57.7</td>
<td>62.3</td>
<td>64.0</td>
<td>61.6</td>
<td>73.4</td>
</tr>
</tbody>
</table>


Between 1972-76, the long-term debt of firms increased by 79 per cent and short-term bank loans by 96 per cent, while there was a sharp decline in profits owing to growth
of wages and consumption. The nationalized industries fared better by increasing their investments by 75 per cent in volume between 1973-78 and by an annual rate of 10.4 per cent in volume over the entire span of the Seventh Plan (1976-80) though by 1979 investment had been curtailed by 9 per cent. This commendable performance owed to two major public-investment programmes: (1) modernisation and doubling in capacity of the telephone system, (ii) electro-nuclear programme of Electricite de France, which was an attempt to substitute nuclear power with other forms of energy.

The Government's wish to promote investment in the competitive sector had failed to yield any result on the cost side because of the increase in real wages in the early 1970s and by the increasing share of the wage bill represented by employers' social-security contributions: 22.7 per cent in 1972 and 25.6 per cent in 1978, which encouraged the substitution of capital for labour.

In September 1976, Prime Minister Raymond Barre introduced his much vaunted 'Stabilisation Plan' which laid emphasis on curbing inflation, reducing consumption of energy and boosting exports. These involved adoption of anti-inflation measures combining tight monetary policy,
increased interest rates and balanced budgets, especially from October 1974. However according to Jack Hayward:

the initial concentration on controlling industrial prices was not consistent with the Seventh Plan's priority for industrial development. Following a period of hesitancy over the future of planning, the preparation of the Seventh Plan in 1975-6 was characterised by an ephemeral revival of optimism in the possibilities of returning to the pre-crisis expansion and a growth rate of 5.5 per cent (7.2 per cent for industry) was envisaged, based notably on a high rate of investment. This return to 'go' after 'stop' quickly caused France to run into balance-of-payments deficit and Raymond Barre to run into balance-of-payments deficit and Raymond Barre was called upon to carry out a more consistently deflationary policy in August 1976, following a conflict between President Giscard and Prime Minister Chirac that was broader and more political than their differences over how to tackle the economic recession.

The Barre Plan not only aimed at improvising a set of short-term inflationary measures, but was also intended to usher in a less dirigiste policy. The other changes brought about had equally far-reaching consequences:

The Seventh Plan's commitment to full employment was tacitly abandoned and the stability of the currency was presented as a precondition of containing the growth in unemployment. Membership of the European Monetary System had the virtue of making the parity of the

While the Barre Plan was taking shape, important changes were taking place in the Ministries dealing with Industrial Policy. In 1974, the Chirac Government had created the Comité Interministériel pour l'Amenagement des Structures Industrielles (CIASI), which made a transition from its role as a fund-raiser to that of a preserver of small business and jobs in general. CIASI came under the control of Direction General de l'Industrie, so that the Ministry of Industrial Development could undergo a transformation from a clientele-dominated, sectoralised ministry to one solely concerned with restructuring of French firms into large multi-sectoral groups. DGI had a crucial role to play: especially in carrying out the selective approach of deciding which industries - such as machine tools and micro-processors should receive help on a priority basis, and which firms should be singled out for favour, especially those dealing with large public contracts in the electro-nuclear field. The intra-bureaucratic implications of the recession became evident through (i) the Ministries of Industrial Development and (especially) Foreign Trade which became commercial conduits of French goods, (ii) Foreign

199 Ibid., p. 125.
Relations Division of the Finance Ministry which insisted that financial assistance to firms should be tied to their export potential. This division has played a crucial role in industrial decision-making since 1974, including decisions on French overseas investment.

Policy confusion continues to haunt the sensitive issue of the flow of foreign investment. According to estimates made by the Industry Ministry in 1971, one-fifth of French industrial jobs and one-quarter of sales were due to foreign firms, which were concentrated in large firms, especially in the oil, electrical and electrical engineering, chemicals and motor car industries. But the Ministry of Finance through the Treasury Division has made it known that although its prerogative is confined to short-term balance of payments advantages of Foreign investment in France, it is not greatly in favour of overseas investment by French firms because this involves a drain on the balance of payments, involving expensive guarantees. The Regional Planning Agency (DATAR) on the other hand, is always in favour of investment inflows because of its interest in creating jobs in areas which are under-industrialized or which have been affected by recession. On the other hand the stand taken by the Ministries of Industrial Development or Defence has always been nationalistic, which confuses the foreign firms,
who are often invited by DATAR to invest. The Treasury Division ultimately is responsible for clinching the issue, and so Jack Hayward is probably right in observing "So national policy can become the plaything of intra-bureaucratic battles between various parts of the state apparatus, subject to the superimposition of a decision at the highest levels in the light of political considerations." 200

The right wing electoral triumph of March 1978 saw the ushering in of liberal-conservatism, giving top priority to the performance of internationally competitive French firms, which were supposed to modulate national economic activity. The key reports, commissioned by the Committee on the Financial Situation in December 1958, and the 1960 report on 'Obstacles to Economic Expansion' provided the necessary blueprints, which had laid stress on competitiveness, restraint upon public expenditure and curbing of protectionism. For the coming decade they became the gospel of both the administrative and business elites. It

200 Ibid., pp. 127-8.

consisted in making of the industrial firm the economy's essential decision-making centre and of profit the driving force of growth. It did not signify 'disengagement' by the State but the introduction of new forms of state intervention based upon supporting private business rather than defining objectives and direct intervention. 201

They however drew succour from the recommendations contained in the earlier two reports, namely the Montjoie Report on Industrial Development in 1968, and Nora Committee Report on Public Enterprise, which had laid emphasis on competitiveness in the public sector. 202

While the French Government was busy taking follow-up measures based on these reports, it was at the same time busy rescuing basic steel industry resulting in nationalisation. What was more amazing was that in the same month it vowed to help the lame ducks:

the old ghost of dirigisme is once again haunting France; many want the state prodigally to assist firms in distress, providing them with a sort of social security that would guarantee them against foreign competitors, helping them financially to preserve jobs. Such a policy of public aid

201 Ibid., pp. 131-2.

202 The Montjoie Report had observed that French industrial backwardness, was due to a miniscule industrial base, owing to transfer of resources away from sectors exposed to foreign competition to those that were sheltered, resulting in low profitability and investment.
to firms would anaesthetise their natural antibodies and atrophy their vitality. It is the way to decadence. 203

By 1978-79, the Government had abandoned price control, first in manufacturing industry, and more prudently in the service sector which was an indication that the Government had made a switch from dirigisme to reliance upon macro-economic monetary and fiscal instruments for curbing inflation.

The socialist electoral victories of May-June 1981, have brought about a major shift in the Government industrial policy, quite apart from sweeping nationalisations. In 1981, the French Ministere de l'Industrie announced two main facets of its new policy: (i) Government aid to industry would no longer be directed towards the newer science-based industries to the often deliberate neglect of the older, more traditional industries, (ii) In future, government assistance will be more selective and will provide assistance, in various forms, to those cases, firms or products, in whatever industry, which it feels merit support, either for economic or for social reasons. 204

203 Hayward, n. 194, p. 133.

The nationalisations extended state control to about 40 per cent of industrial output. Eleven key industrial groups - which had more than $40 billion in sales in 1980 were caught in the socialist's net - the 'immediate' take-overs included the arms-making branch of Matra, a fast growing high-tech firm and the 80 per cent of aerospace giant Avions Marcel Dassault-Breguet Aviation. The others brought under state-control included the two major steel-makers Sacilor and Usinor. The others which were slated for eventual take-over included: Compagnie Generale d'Electricite (electrical engineering), Pechiney-Ugine-Kuhlman (aluminium-copper-chemicals), Rhond-Poulenc (synthetic fibres, drugs), Saint-Gobain-Pont a Mousson (glass, building materials) and Thomson-Brandt home appliances electronics). Besides these domestic companies, three largely foreign owned companies were also on the socialists' take-over list: computer-maker CII Honeywell Bull (47 per cent US owned), ITT France, a subsidiary of the New York based International Telephone and Telegraph Company, a pharmaceutical maker Roussel-Uclaf, 57 per cent-owned by West Germany's Hoechst AG. Even after nationalisations, the Government insisted on maintaining 'existing technological, industrial and trade ties' and 'showing flexibility in both the form and the timing of
Along with nationalisation, the French Government has undertaken an austerity programme, which involves an attempt to reduce public and private demand by 65 billion francs (about $890 million) or the equivalent of 2 per cent of the gross national product. It is based on higher social security contributions, higher public service tariffs, a mandatory loan of 10 per cent of income-tax paid and currency controls that include unpopular restrictions on travel.

The Socialists are however partly responsible for the economic malaise that has prompted this austerity programme. When they assumed power in the spring of 1981, they took some populist measures like increasing the minimum wage by 10 per cent, old-age pensions by 20 per cent, automatic benefits for large families by 25 per cent and housing allowances by 25 per cent. Programmes were also announced creating up to 200,000 public sector jobs. This resulted in an unemployment growth rate slower than that of countries


like USA or West Germany, but at the same time it generated a double-digit inflation that produced a large foreign trade deficit. Because of the weakness of French Industry in many sectors, much of the new money in circulation was utilised to pay for imported goods. The inflation and deficits weakened the franc that required heavy foreign borrowing, as a result of which the official foreign indebtedness at the end of 1982 stood at 235 billion francs. This was compounded by the fall in corporate profit, and the volume of corporate investment dropped by 7 per cent in 1982.

But latest developments clearly show that the Socialist Government in France is having second thoughts on nationalisation. A bill that would have made it possible for nationalised companies to sell majority owned subsidiaries to private companies is on the agenda of the Parliament for more than a year. The Government's bill, known literally as a 'breather' for the public sector - 'la respiration du secteur' - would, if passed, make legal the transfer of majority owned subsidiaries of nationalized companies to the private sector, though they would still be subject to Government control. But latest developments clearly show that the Socialist Government in France is having second thoughts on nationalisation. A bill that would have made it possible for nationalised companies to sell majority owned subsidiaries to private companies is on the agenda of the Parliament for more than a year. The Government's bill, known literally as a 'breather' for the public sector - 'la respiration du secteur' - would, if passed, make legal the transfer of majority owned subsidiaries of nationalized companies to the private sector, though they would still be subject to Government control.207 A nationalised company

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is currently allowed to acquire majority ownership in a private enterprise, but the same concession is not given to a private company to acquire majority ownership in the subsidiary of a nationalized company. For example, CROUZET SA, a private French maker of aeronautical navigation gear, ran into rough weather in 1983 when it tried to acquire SFENA, a company in the same sphere, which is 99 per cent owned by government controlled institutions. SFENA's Comite d' entreprise, a panel, whose job under French law is to represent the interests of employees, opposed the acquisition. To add insult to injury, France's highest tribunal ruled that the privatization of SFENA was against the constitution and ordered CROUZET to divest itself of its holding in SFENA.

Yet with the proliferation in the number of subsidiaries in the public sector after the 1982 nationalisations and stagnation of investments in private firms, the more pragmatic members in the socialist Government have recognized that it would be to the advantage of the nationalized company, the subsidiary and the private company - if the sale of certain subsidiaries are allowed in which the Government retains a majority interest. This more flexible

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208 For details see, H.S. Chopra, "India and Western Europe: Development Co-operation", in Satish Kumar, ed., Year Book on India's Foreign Policy: 1982-83 (New Delhi: Sage, 1984).
attitude towards the public sector also fits into the earlier popular industrial strategy of 'filière' advocated by Jean-Pierre Chevenement, the former Industry Minister. Under the filière concept, the pragmatists in the Government argued that a nationalised company might try to get rid of subsidiaries that did not form part of its core business. But Jean-Pierre Chevenement, who is also the leader of the far-left CERES faction of the Socialist party, remained ideologically opposed to the idea and against the legislation designed to allow the sale of nationalized assets.

Now, with the nationalized companies approaching the market the French Government has found a more convenient way to raise money. According to Sherry Buchanan, an observer of the French corporate scene 'it is clearly less embarrassing ideologically to go to the capital markets than is to denationalize - which is what the bill would have, in effect, allowed. Second, with the boom on the bourse, it may be a more efficient way to raise funds. And raising funds on the foreign exchange is easier than trying to get a bill through parliament that was opposed from the beginning by hard-line societies and by the Communists.' The Ministry of Industry, under Laurent Fabius, successor to Chevenement, no longer believes that the filière concept is suitable for French industry and so at present the selling off of nationalised
assets is a less pressing issue: today the Government has reverted back to CRENEAU, a policy of identifying specific markets. Taking a cue from the French Ministry of Industry, Compagnie Generale d' Electricite (CGE) has put up for sale 19.6 per cent of a subsidiary, Compagnie Electro Financiere, for FFr 74.4 million ($9.3 million). The sale leaves CGE with 59.4 per cent of Electro Financiere, a holding company which has a 10 per cent stake in CGE's two biggest subsidiaries: Alsthom Atlantique and CI'T Alcatel. In 1983, four state-owned firms had already set the tune by issuing 'participatory certificates' a form of non-voting loan stock, thought up by the Finance Ministry and first used by Saint Gobain, which is expected to put one-third of Saint-Gobain Emballage, its packaging subsidiary, up for sale in the not too distant future. 209

It remains to be seen whether this volte face indicates a sea-change in the Mitterrand/Mauroy Government's ambitious 'state capitalist' approach but probably we would tend to agree with Philip G. Cerny, who had observed:

the structural and conjunctural pressures and constraints which led to the first formulations of Socialist economic strategy, highlighted the tensions within that strategy in practice and forced a refining and reconsideration of that strategy-leading to a shaking out of priorities,

which stands in contrast with certain of the original conditions and objectives of the overall strategy itself.

The German Response

West Germany among all the EEC countries had the most constructive government policy for long-term improvement of conditions for growth: especially in identifying bottlenecks (like energy and easing structural adjustment by stimulating innovation (as in micro-electronics). In adopting this policy, the SPD (Social Democrats) had played a pivotal role. State support in the development and introduction of new technologies was recognized with the creation of the Research and Technology Ministry in 1972. What was


Competitiveness in French industry has been adversely affected by the hourly wage increases in manufacturing, which through August 1983 were rising at an annual rate of around 10 per cent, although by the end of 1983 it petered down to about 9 per cent. But the rate also remained substantially higher than the 5 per cent rate in Japan and Britain and the 4 per cent rate in West Germany and the United States. Salaries and social charges paid by employers to the Government represent about 70 per cent of French industry's operating costs and these charges were considerably higher than those in most neighbouring European countries. For details see, Axel Krause, "French firms warming up to Austerity", International Herald Tribune, 24 October 1983.
more important was the crucial role played by bankers in industry and the emergence of an industrial-banking oligarchy. According to Kenneth Dyson -

The Government was insulated to a greater degree than in Britain from the complex and detailed problem of monitoring and in responding to the problems of major companies. The banks served as an 'early-warning' system which identified weaknesses in industry and on occasion mounted rescue operations. 211

Growth rates fluctuated between 5.1 per cent in 1976 to 2.6 per cent in 1977, 3.5 per cent in 1978 and 4.4 per cent in 1979. Investment rates of 25 per cent of GDP in the 1950s were stabilised during the next decade, but their decline in the 1970s reflected a rising average age of plant and machinery. But in comparative terms investment figures were impressive enough to make Germany the most powerful industrial power of Western Europe. Fixed capital formation as a percentage of GDP had increased steadily from 20.8 per cent in 1977 to 22.9 per cent in 1979. In 1975, Germany's gross fixed capital investment accounted for 31 per cent of the EC total and represented 29 per cent more investment than in France. But at the same time, West Germany had been experiencing de-industrialisation. Industry's share of GDP

dropped from 54 per cent in 1970 to 48 per cent in 1978. Even then, by international standards it was remarkably high. Whereas industry's share of GNP was 41 per cent in Britain and France in 1975, the figure for Germany was 51 per cent. West Germany had laid great stress on exports, which accounted for 27 per cent of GNP in 1978, with half of its total volume catering to EC's market. Recession's impact was partly offset by its successful export drive on OPEC markets, as a result of which it enjoyed a trade surplus with the oil-producing countries till 1978. But after 1970, its exports had become less competitive in terms of unit wage costs than those of the USA and Britain (but became more competitive than those of France and Italy). But Germany remained unrivalled in the capital goods sector, and plant construction with a market share of 50 per cent. According to Kenneth Dyson, an observer of the German industrial scenario:

The machinery and industrial plant exports which make up more than half the total were relatively price-inelastic, and in this area German industry proved notably adaptive. If exports were hit by the appreciation of the mark, the steady decline of domestic inflation provided support. To the aggravation of other countries the payments surplus rose to 41 billion DM in 1978 (although in price-adjusted terms it actually declined), but the rising costs of imported materials and import penetration sent it into deficit in 1979. One major change was the rapid expansion of
foreign direct investment, notably by the chemical and electro-mechanical industries. Nevertheless, in 1977 foreign industrial investment amounted to only 4.6 per cent of total capital spending at home. 212

Recession however had a visible impact on the employment pattern: 1.6 million jobs were lost between 1970 and 1976 (428,000 in construction alone). However, an increase of jobs in services and public administration could do little to offset losses in industry. The problem of structural unemployment has however remained intractable since 1975, and it was discovered in 1977, that every second unemployed person has not completed occupational training. So, it was unlikely that the situation could be reversed by global reflationary measures or by investment in rationalisation.

212 Dyson, n. 211, p. 42.

West Germany's emphasis on exports to offset the impact of recession has suffered a blow with the failure of its government sponsored export programme called Hermes, which for the first time has paid out more in claims than it received in premiums. The insurance claims began to be registered as companies stopped receiving payments from their customers in debt-ridden developing countries. According to Sherry Buchanan, a critic of the European export plans, 'high interest rates have driven up the export agencies' cost of raising funds... to end the subsidies would mean that their industries would lose their share of export markets, with the consequent loss of jobs at home.' But as Hermes has refused to give export cover to large, West German companies, the latter have been forced to use their French subsidiaries to get better export credit terms. For details see, Sherry Buchanan, "European Export Plans Running deeply in the Red", International World Tribune, 22 February 1984.
One of the major anxieties about German industry since recession has been the falling rate of investment (beginning in the 1950s) on the age of machinery and plant. From the early 1970s investment was geared towards rationalisation and labour substitution. This prompted firms like Daimler-Benz (motor vehicles) and Deutsche Babcock (industrial plants) which were expanding in 1975-76 to do so with the same or reduced labour force. Recession had even sharper effects on employment and investment in other sectors. In 1974 as a result of price explosion, chemical giants like Hoechst had record profits. But by 1977-78, when the mark was appreciating and prices were depressed, they experienced poor turnovers and profits. Between 1970 and 1978, the chemical industry had shed over 40,000 jobs.

The German steel industry had remained unperturbed by the recession, and in 1974 it had established its reputation as the largest, most efficient European producer by accounting for 34.2 per cent of EC capacity and being the biggest EC exporter. With worldwide recession and the crisis in construction and motor vehicle industry, the steel industry entered a four-year crisis period from 1975 to 1978. According to Kenneth Dyson;

Profits were halved in 1974-5 and 1975-6, and the industry went heavily into the red
in 1976-7. Firms like Klockner and Thyssen were badly affected. By 1978 there were fears that the industry was losing ground to other European states whose steel firms benefitted from huge government subsidies. The turnabout occurred on the Rhine and in the Ruhr in 1979 when there was the best post-war production of steel (with the exception of the two record years of 1973-4). The major problem was that the firms were unable to make full and speedy use of spare capacity because of heavy shedding of manpower in past years.

The strain of contraction had its impact on politically powerful industrial lobbies like the Association of the Iron and Steel Industry. It manifested itself in the new competition for state aid, for example for share of the federal Government's steel research programme. But the EC's steel cartel of 1977 united the steel managers, who forced the German producers to withdraw from the arrangement in 1980. By 1983, Brazil and South Korea had replaced West Germany, Europe's biggest steel producer, as the second biggest steel supplier to the United States. Germany has suffered the most from the effects of the European Community's steel quota system, the EC's effort to reduce European steel capacity and restructure the industry to help it survive the worldwide slump in sales. As a result, West

213 Dyson, n. 111, pp. 46-47.
Germany has committed to pay $1.1 billion to reshape its steel industry.

Recession had its greatest long-term impact on high technology. This has resulted in West Germany being behind its US and Japanese competitors in certain key areas of micro-electronics, data systems (both computer and software), robotics and bio-technology. A recent report released by the Ministry of Technology has highlighted some of the sectors where German firms are lagging behind:

**Data Systems:** In total world turn-over for computer sales in 1982, US companies garnered $24.1 billion, Japanese $6.2 billion and West Germany $3.7 billion, with French and Britain trailing. In West Germany, IBM holds more than 50 per cent of the domestic market in general purpose computers compared to Siemens' 20 per cent.

**Components:** West Germany continues to import more than 50 per cent of the microchips it uses in its industries. Japanese sources cited in the report show that in 1982, Japan's microchip exports to West Germany increased by 57 per cent, while German exports of integrated circuits to Japan fell by 25 per cent.

**Robotics:** West Germany imported 40 per cent of its robots in 1982, mostly from Japan whose 250 robotic companies produced nearly four times as many robots as Germany's 20 firms - 12,000 compared to about 3000 machines.
However this drawback has been partly compensated by the strength of various German firms in power engineering, industrial automation, electro-medicine, measurement and control systems and laser technology. This combined with a wide range of capital goods had contributed to West Germany's favourable 41.9 billion mark surplus in its 1983 balance of trade. This stands out in sharp contrast to US merchandise trade balance which was in deficit in 1983 by $60.5 billion.\(^\text{214}\) The West German Government has however refused to remain complacent. This became evident with the West German Parliament's approval of a 3 billion mark research development scheme to be applied to 'backward' technological sectors over the next four years.\(^\text{215}\)

At the same time the CDU-CSU/FDP coalition government has pledged to reduce state participation and subsidies in industry and public services. Earlier the call to 'privatize state enterprise' and renew the social market economy were a central policy target of his coalition. But both have met with mixed success. The Government had first used Veba energy conglomerate as a trial balloon, by placing

\(^{214}\) *International Herald Tribune*, 3 April 1984.

\(^{215}\) Half the funds were earmarked for research on advanced microchips and tomorrow's computers. The rest is spread over the entire high-technology field. For details see, Uli Schmetzer, "Industry applauds an ambitious plan to Invest in Future", *International Herald Tribune*, 3 April 1984.
on the market a 'cautious' 13.75 per cent of its 43.75 per cent holdings. Rather than effecting a sale of its interests, the Government appears to be concentrating on greater efficiency and opening up traditionally state-controlled areas to private enterprise.

The West German Government's policy response to the threat of economic recession was greatly modulated by the liberal and institutional structure of its domestic economy. Much emphasis was placed on two institutions: the central bank to usher in economic stability, and the big commercial banks to assist the adaptation of industry to market changes. According to Kenneth Dyson:

State and bank power was matched to privately formulated and competitive market strategy oriented to the requirements of industrial efficiency and product development. Domestically, the commercial banks, as market-oriented institutions themselves, ensured that the strategies and structures of industry were sensitive to the working of the market in which they developed their own particular expertise. Internationally, the German government and banks sought to breathe new life into transnational institutions and arrangements in order to ensure stabilisation of the international economy and to open or maintain access to foreign markets. 216

In other words, German economic policy did not consciously seek to put constraints on market so as to insulate the firms. Secondly, the Government's economic policy drew

216 Dyson, n. 211, p. 57.
succour from the premise that the problems of stability and growth had its roots in economic causes and could not be effectively tackled by dealing solely with their political symptoms. This was reflected in the government's aloofness from the political pressures of industry exercised by commercial banks in the sphere of industrial policy and in the central banks insulation from reflationary political pressures in the sphere of currency management. So the entrepreneurial role of the state was muted, except when the structural problems of industry were found to be too grave for the banks to handle alone (i.e. in the case of Ruhr coal industry in the 1960s and the Saar steel industry and the ship-building industry in the 1970s).

The recent militancy by the German trade unions however has threatened the stoicism of the State. Faced with recession, the German trade unions have demanded an immediate reduction in the work-week from 40 to 35 hours with no cut in pay. The unions argue that cutting the work-week is the only way to create jobs for West Germany's 2.2 million unemployed (8.8 per cent of the workforce). The German employers, on the other hand contend that a work-week shortened by five hours would lead to a 12.5 per cent jump in the costs of production, just as the strengthening Deutschemark is making competition tougher for German
products in the world market. A worried centre-right coalition led by Helmut Kohl, the Chancellor has tried to diffuse the situation by offering early retirement for 58 years or older. But the militant leadership of IG Metall, which with 2.5 million members has traditionally been Germany's wage pace-setter, has dismissed the offer as woefully inadequate. Against this background it would be interesting to see how the Kohl Government could expect an economic growth of at least 2.5 per cent in 1984 after a gain of 1.5 per cent in 1983. 217

The European Community's response to Economic Recession

The Community's response to the economic crisis of 1974-75 could be summed up as follows:

(1) Co-ordination of national economic and monetary policies of EC countries.

(2) The selective intervention in the EC economy as a whole through the EC financial instruments.

(3) Development of a co-ordinated energy policy.

(4) Emphasis on a Community industrial policy.

Co-ordination of national, economic and monetary policies of EC countries was manifested in the form of the European

Monetary System (EMS). It was aimed at ushering in steady growth and stable prices, a gradual return to full employment and a reduction in regional disparities. Later a European Monetary Fund (EMF) was also set up in 1981, implying the optimal use of the European currency unit (ECU) at a reserve asset, besides serving as a means of settlement.

EMS has been accepted by all the member states, with the exception of Britain, which for the time being has kept itself detached from its intervention mechanism. Although France has accepted it, Jean Pierre Chevenement, former research and industry minister and leader of the left-wing of France's ruling socialist party has called for withdrawal of the French franc from the European Monetary system. He feels that the withdrawal would bring about a 15 per cent devaluation of the franc against the Deutsche Mark. Such a drop might also improve export competitiveness and boost economic growth in France. 218

The European Council of December 1978 had gone out of its way to promote the cause of EMS, although apparently it voted for measures aimed at assisting the least prosperous Community countries. It is significant that

218 International Herald Tribune, 15 March 1984. Small devaluations which the French Government had accepted since 1981 were useless since inflation eliminated any exchange rate gains.
it wanted the Community institutions and the European Investment Bank to make special loans available for a period of five years to such countries effectively participating in the exchange and intervention mechanism. Although the Commission felt that the EMS was working smoothly, the EMS was suffering from two shortcomings: first the ECU was hardly used as a settlement instrument; secondly, the interventions on the markets were not adequately carried out with Community currencies (rather the dependence was mostly on US dollars). What was more important was the fact that countries with deficits in the system could fall back upon sources of capital outside the Community rather than credit mechanisms of the EMS. More ominously, the rates of inflation all diverged excessively, reflecting lack of coordination.

Lately, it appears that the ECU has achieved semblance of success. In 1983 for example, companies, banks and international organizations borrowed 2.34 bi European currency units, making the units the third most popular 'currency' on the international bond market after the dollar and the Deutsche mark. It is significant that since 1981, a total of 4.35 billion of ECU-denominated have been sold internationally, according to data prov
by Luxembourg-Kredietbank. But it remains to be seen whether the ECU could act as a reserve currency to challenge the power of the dollar for countries like Britain had at the outset made its reservations clear on the ground that the EMS should be regarded as a first step towards the restoration of international monetary stability rather than a move towards economic and monetary union within the Community.

Another Community response to the economic crisis of 1974-5 has been to provide more Community resources to stimulate economic growth, to promote vocational training and retraining of workers, to provide assistance to ailing industries, to alleviate problems of economic divergence, and to stimulate research and development of new energy sources and technology. Action by the European Community through its financial instruments is effected through the European Social Fund, the European Regional Fund, and the ECSC Fund, which come under the broad category of Community grants. (See Table XVI)

TABLE XVI

AID BY THE EUROPEAN SOCIAL FUND AND THE EUROPEAN REGIONAL DEVELOPMENT FUND

(1) ESF: Distribution of Grants by Sector, 1972-9 (in million u.a.)

<table>
<thead>
<tr>
<th>Types of intervention</th>
<th>1972-5 Community</th>
<th>1976-9 Community</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>million u.a.</td>
<td>%</td>
</tr>
<tr>
<td>Agriculture</td>
<td>81.9</td>
<td>9.8</td>
</tr>
<tr>
<td>Textiles</td>
<td>15.4</td>
<td>1.85</td>
</tr>
<tr>
<td>Agriculture &amp; Textiles</td>
<td>16.9</td>
<td>2.02</td>
</tr>
<tr>
<td>Young people</td>
<td>35.1</td>
<td>4.19</td>
</tr>
<tr>
<td>Women</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Handicapped Migrants</td>
<td>52.9</td>
<td>6.33</td>
</tr>
<tr>
<td>Article 4</td>
<td>202.2</td>
<td>24.18</td>
</tr>
<tr>
<td>Regions</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Technol. Advance Enterprises</td>
<td>528.4</td>
<td>63.19</td>
</tr>
<tr>
<td>Handicapped</td>
<td>105.6</td>
<td>12.62</td>
</tr>
<tr>
<td>Article 5</td>
<td>634.0</td>
<td>75.82</td>
</tr>
<tr>
<td>Total</td>
<td>836.2</td>
<td>100.00</td>
</tr>
</tbody>
</table>

TABLE XVI (contd.)

(ii) ERDF: Distribution of Grants by Sector and Country 1975-9 (in million u.a.)

<table>
<thead>
<tr>
<th>Types of intervention</th>
<th>Industry Crafts Services</th>
<th>Infrastructure</th>
<th>Hill forming area infrastructure</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>million u.a.</td>
<td>%</td>
<td>million u.a.</td>
<td>%</td>
</tr>
<tr>
<td>Belgium</td>
<td>10.59</td>
<td>1.17</td>
<td>20.91</td>
<td>1.21</td>
</tr>
<tr>
<td>Denmark</td>
<td>4.33</td>
<td>0.47</td>
<td>29.87</td>
<td>1.71</td>
</tr>
<tr>
<td>Germany</td>
<td>101.29</td>
<td>11.2</td>
<td>78.25</td>
<td>4.53</td>
</tr>
<tr>
<td>France</td>
<td>165.96</td>
<td>18.33</td>
<td>255.74</td>
<td>14.65</td>
</tr>
<tr>
<td>Ireland</td>
<td>83.71</td>
<td>9.25</td>
<td>81.83</td>
<td>4.7</td>
</tr>
<tr>
<td>Italy</td>
<td>246.76</td>
<td>27.27</td>
<td>829.6</td>
<td>47.5</td>
</tr>
<tr>
<td>Luxembourg</td>
<td>-</td>
<td>-</td>
<td>2.62</td>
<td>0.15</td>
</tr>
<tr>
<td>Netherlands</td>
<td>5.52</td>
<td>0.61</td>
<td>35.87</td>
<td>2.05</td>
</tr>
<tr>
<td>United Kingdom</td>
<td>286.89</td>
<td>31.7</td>
<td>410.06</td>
<td>23.50</td>
</tr>
<tr>
<td>Total</td>
<td>905.05</td>
<td>100.00</td>
<td>1744.72</td>
<td>100.00</td>
</tr>
</tbody>
</table>

From Table XVI it is evident that the ESF grants are largely geared towards regions and young people, comprising nearly 90 per cent of the total in 1979. However, the former, whilst increasing in absolute terms by 66 per cent between 1978 and 1979, has been decreasing as a percentage of the total ESF outlay since 1976. Another significant development has been increase in funds for projects assisting the young unemployed which recorded an increase by almost 70 per cent between 1978 and 1979.

From the same table it is evident that nearly two-thirds of the total grant of 2,826 million EUA (by the end of 1979), went into infrastructure investments. The overall allocation of the ERDF increased by 72 per cent between 1978 and 1979. However, while infrastructure investment were augmented by 90 per cent in the same period, industry and service-sector investments only obtained a 42 per cent increase.

The ECSC Fund for the readaptation of workers has provided aid totalling nearly 200 million EUA between 1975 and 1979, distributed nearly equally between coal and steel sectors. Germany and France were the main beneficiaries, but if we combine the two sectors the lion's share would go to United Kingdom. Data provided by the Community indicates that 140,000 workers (58,000 in coal and 82,000 in steel) benefitted from the Fund between 1975 and 1979.
Similarly, the Guidance Section of the European Agricultural Fund (EAGGF) provides individual grants to help modernise the structure of agricultural production and distribution. Resources made available to EAGGF have increased substantially and now run at around 500 million EUA per year, with a much higher proportion earmarked for underprivileged areas.

The other financial instruments available with the Community are administered through the European Investment Bank (EIB) which was set up ostensibly for making a balanced contribution to the development of the Common Market. This is done through development of investments benefitting small and medium-sized undertakings and support for investments in the energy sector. Lately, the EIB has shed its insularity and its ambit has encompassed 13 Mediterranean countries and 58 APC countries, which are signatories to the Lome Convention. From Table XVII, it is evident that EIB loaned have doubled between 1976 and 1979, and that the fastest growing sector has been that of energy. Over the same period, this sector was augmented by 165 per cent and was by far the largest single item in the EIB budget in 1979, amounting to 44 per cent of the total. The two major beneficiaries were Italy and UK, accounting for 76 per cent of total loans, followed by Ireland and France, drawing 20 per cent.
### TABLE XVIII

**LOANS BY THE EUROPEAN INVESTMENT BANK, NEW COMMUNITY INSTRUMENT AND THE ECSC**

(i) EIB Loans by Sector and Country

<table>
<thead>
<tr>
<th>Financing of Projects</th>
<th>Total 1975-9 (in million u.a.)</th>
<th>NCI Loans by Sector and Country (loans allocated by mid-1980) (in million u.a.)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Prod. Sector</td>
<td>Infra-structure</td>
</tr>
<tr>
<td>Belgium</td>
<td>26.6</td>
<td>-</td>
</tr>
<tr>
<td>Denmark</td>
<td>51.3</td>
<td>62.4</td>
</tr>
<tr>
<td>Germany</td>
<td>15.5</td>
<td>-</td>
</tr>
<tr>
<td>France</td>
<td>53.1</td>
<td>668.2</td>
</tr>
<tr>
<td>Ireland</td>
<td>119.9</td>
<td>312.6</td>
</tr>
<tr>
<td>Italy</td>
<td>774.3</td>
<td>1322.9</td>
</tr>
<tr>
<td>Luxembourg</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Netherlands</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>United Kingdom</td>
<td>461.6</td>
<td>981.9</td>
</tr>
<tr>
<td>Non-Member countries²</td>
<td>1502.3</td>
<td>3346.0</td>
</tr>
</tbody>
</table>

a Industry, agriculture and services
b Austria and Norway

*Source:* EIB and NCI figures were taken from "Tendances et Perspectives économiques à court terme: Les instruments d'emprunts prêts dans le cadre des instruments financiers"
TABLE XVII (contd.)

(ii) ECSC Loans and Types of Interventions, 1954-78 (Community)

<table>
<thead>
<tr>
<th>Types of Interventions</th>
<th>1954-75 million u.a.</th>
<th>%</th>
<th>1976-8 million u.a.</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Iron ore mines</td>
<td>25.75</td>
<td>0.98</td>
<td>75.1</td>
<td>2.5</td>
</tr>
<tr>
<td>Conversion</td>
<td>327.33</td>
<td>12.49</td>
<td>245.2</td>
<td>8.5</td>
</tr>
<tr>
<td>Iron and steel industry</td>
<td>1550.50</td>
<td>59.16</td>
<td>1736.9</td>
<td>59.7</td>
</tr>
<tr>
<td>Coal industry</td>
<td>421.58</td>
<td>16.09</td>
<td>710.7</td>
<td>24.5</td>
</tr>
<tr>
<td>Thermal power stations</td>
<td>111.52</td>
<td>4.25</td>
<td>44.7</td>
<td>1.54</td>
</tr>
<tr>
<td>Workers' housing</td>
<td>173.27</td>
<td>6.61</td>
<td>81.3</td>
<td>2.8</td>
</tr>
<tr>
<td>Retraining-resettlement</td>
<td>7.11</td>
<td>0.27</td>
<td>0.5</td>
<td>-</td>
</tr>
<tr>
<td>Technical research</td>
<td>3.12</td>
<td>0.12</td>
<td>0.7</td>
<td>-</td>
</tr>
<tr>
<td>Miscellaneous</td>
<td>0.74</td>
<td>0.03</td>
<td>12.5</td>
<td>0.4</td>
</tr>
<tr>
<td>Total</td>
<td>2620.92</td>
<td>100.00</td>
<td>2907.6</td>
<td>100.00</td>
</tr>
</tbody>
</table>

Source: General Reports of the European Communities (1975-8), pp. 46, 62, 59, 62 respectively.
The other financial instrument is New Community Instrument (NCI), which was created in October 1978 to raise loans on the capital market in conjunction with the EIB. The objective was to promote investment projects which could accelerate the convergence of the economic policies of the member-States and to make the Community almost self-sufficient in energy supplies. This instrument was also to be used in conjunction with the European Monetary system for making loans available at subsidised interest rates to less affluent members of the Community fully participating in the EMS scheme. The total volume of loans made available at subsidised rate was pegged at 1,000 million EUA a year for five years, with an interest rate subsidy of 3 per cent. The subsidy was however fixed at 200 million EUA a year for five years.

Besides NCI there is also provision for ECSC loans, which are disbursed according to articles 54 and 56 of the ECSC treaty. The loans are generally provided for projects which include those for modernisation and conversion of steel plants, and the provision of loans often at low interest-rates, for generating new employment in areas of coal and steel production.

As is evident from Table XVII ECSC loans have doubled between 1976 and 1978, i.e. slightly more in
quantum than the amount provided between 1954 and 1975. The largest item (60 per cent of the total) are loans for modernisation in the iron and steel industries, followed by loans for coal industry (25 per cent).

Besides, the European Commission was authorized by the European Council in March 1977 to raise capital for financing the construction of nuclear power stations and industrial installations for recycling fuel. The European Commission was authorized by the Council to negotiate loans up to an initial sum of 500 million ECU, followed by a second instalment of the same amount, authorized in December 1979. By mid-1980, 385 million ECU had been lent to promote power station projects in the Community. Community financial instruments, exercise a lot of clout, but lack co-ordination. According to Emil Kirchner "A more effective co-ordination should, for example, ensure that the training schemes supported by the ESF can provide the appropriate skills for the new jobs created with the aid of the ERDF, which might also, along with the EIB, help to pay for infrastructural facilities which the new factories will need."

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Although the ESF and ERDF can be used as partial repayment of national aids, the Commission has reiterated that the real aim of these Funds is to supplement rather than replace Government payment but if the given data is analysed one finds that Community aid seems to be used as replacement rather than as supplement. This gap has increased from 52 per cent in 1977 to 93 per cent in 1978, and it has remained constant since then. It is ironical that there is a disparity between the amount of Community aid requested and that called up by member governments. For example, at the beginning of 1979, the total proportion of ESP aid granted but not called up had touched 300 million EUA. For the ERDF, the figure was 180 million EUA and for the Guidance Section of the EAGGF, the amount was 220 million EUA. Similarly, in 1978 1,350 million EUA of ESF aid was granted, but only 569.5 million were called up. In the Guidance section of the EAGGF, the respective figures were 1,100 million EUA to 356 million EUA.

While the European Community’s role in promoting a common energy policy and a common industry policy would be discussed in the other chapters, the EEC has taken the first positive step in the formulation of a common science and technology policy by approving a second four-year term for the FAST programme - Forecasting and Assessment in Science and
Technology by doubling its budget to 8.5 million ECU (European Currency Units), or more than £ 5 million a year. This would enable FAST to contribute to the Community's technological competence, by helping in the exploration of bolstering Europe's old economies - against American and Japanese competition and new technological advance, while looking 'warily' at the social implications of the latest developments. 221

221 Auriol Stevens, "Boost for EEC 'think tank'", The Observer, 23 October 1983. The EEC has given FAST permission to develop new research programmes around the following major themes: new alternatives for possible economic growth; new strategic industrial systems, transformation of service activities with technological change; and natural, renewable resources and their management.