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Hillsdale College Hillsdale, Michigan 49242 Vol. 2 No. 3
March 1973

THE CRISIS IN INTERNATIONAL ECONOMIC RELATIONS

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During the dark days of the Great Depression the world was learning an important lesson. When economic nationalism runs rampant and international trade and commerce disintegrate, a world-wide depression is unavoidable. In fact, every time an important country launches restrictive policies, a depression raises its ugly head. For one act of economic nationalism may generate an international movement to raise tariffs and erect many other trade barriers.

When America had learned this painful lesson it moved substantially toward a low-tariff policy. The Reciprocal Trade Agreements Act of 1934 authorized the administration to reduce import duties up to a limit of 50%. The 1945 renewal gave power to cut duties another 50%. And the Trade Expansion Act of 1962 authorized the President for a five-year period to reduce existing United States tariffs by as much as 50% in exchange for tariff reductions by other countries and to eliminate some tariffs altogether. Unfortunately, many a restrictive tariff remained effective on competing imports. And other protective methods, such as import prohibitions and quotas, export subsidies and excise taxes on imported raw materials were used to nullify the tariff reductions. And yet, in spite of such exceptions world trade and commerce enjoyed tremendous expansion since the 1930's. Between 1938 and 1970 the value of world exports, estimated in United States dollars, increased thirteenfold, from \$23.5 billion to \$311.5 billion.[1]

The new world trade of the post World War II era was marked by new circuits of trade that developed to replace the 19th-century system. The heart of the older system was the British Empire whose open-door policy had generated world-wide economic development along national lines of comparative advantage. Western Europe exported capital and manufactured goods to the less developed areas of the world in exchange for food and raw materials. The United Kingdom was the world's largest trading nation and London the world center of clearing and payments.

Since World War II world trade has undergone a number of significant changes: (1) The United Kingdom lost its former share of trade to the United States which became by far the world's largest exporting and importing country, with its main markets in Canada, Western Europe, and Japan. (2) Great improvements were achieved by the European Economic Community, particularly by West Germany, largely because of the reduction or abolition of trade barriers between its members. (3) Trade also increased with the Middle East and Venezuela mainly as a result of the discovery and production of crude petroleum. (4) Japan redirected her trade from China and Southeast Asia to the United States and other developed countries. (5) Most of the newly independent and less developed countries of Africa and Asia, the Latin American countries as well as the communist world lagged significantly behind the United States, Western Europe and Japan.

And yet, it is becoming apparent that the remarkable progress of the last 30 years may soon come to an end because the old foes of world trade and international division of labor are gnawing at their very foundation. In fact, the world is fast moving toward

im•pri•mis (ĭm-prī´ mĭs) adv. In the first place. Middle English, from Latin in primis, among the first (things). . .

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a new crisis in international economic relations. Suspicions and tensions are being created, generating a new isolationism that is fragmenting the economic world into feuding blocs. The United States is poised to confront both the European Economic Community and Japan, which effectively compete with American trade and influence throughout the world. A declaration of economic war between these blocs is a distinct possibility.

What are the causes of this universal urge toward self-destruction? What are the popular ideas that are guiding us on this ominous course? It seems that three particular sets of political and economic thought are mainly responsible for this new development.

First, the continuous growth of socialist and, in particular, Marxian economic thought has led to a renewed attack on private property and the profit motive in the United States no less than elsewhere in the "free world." The growth of socialism in turn is favoring militant policies of protectionism that promote national economic development rather than unhampered international intercourse.

Second, economic nationalism is a natural ally of socialism. Rooted in resentment, fear or envy of foreigners, it promotes the cause of protectionism as it aims to keep foreign goods out of the country and bar foreign investments, or at least subjects foreigners to severe limitations and controls.

And finally, the rise of governmental planning and control has given birth to an age of world-wide inflation that threatens to disrupt the international monetary system. Rampant inflation here and abroad continually disturb trade relations and threaten to engender a global currency panic. It is endangering the peaceful cooperation of the free world, thereby weakening its intellectual and economic strength and position toward the communist world.

Attacks on the Profit Motive

The challenge to the profit motive and the private property order is very old indeed. In the underdeveloped countries it is deeply rooted in ancient customs and mores. In the industrial countries of Europe and America it is the inevitable outcome of the sway of radical ideas. Young people challenging the existing value system and the private property order are lending new vigor to public attacks on the profit system. And government seizes upon this hostility to expand its own authority over economic activity and to use business as a principle source of ever greater tax revenue.[2]

In the United States as well as Western European countries the market order is under severe attack. Many prices are set by decree, and government operation and license are gradually replacing the law of demand and supply. Under the influence of such planning and directing by scores of central governments, the national economies are developing along diverging lines and therefore tend to differ materially from each other. In fact, to differ is the very objective of central planning. But this planned difference in structure and prices can exist only as long as it is protected by countless border restrictions that isolate the national characteristics of planning from the levelling influences of the world market. How, for instance, could the U.S. Government conduct

its agricultural policies of price support and stabilization, all designed to aid American farmers, without high import duties or even prohibitions that sever the United States market from the world market? Trade restrictions in the form of tariffs, licenses, quotas, embargoes, exchange controls, etc. are essential tools in the paraphenalia of government intervention. It is obvious that these very tools are designed to hamper world trade and commerce.

The growing role of government in our economic lives also makes every change in foreign trade the immediate concern of government. When foreign industries effectively compete with domestic industries because foreign production costs are declining or domestic costs are rising, government feels called upon to intervene. Prodded by industries that face keen foreign competition, government may endeavor to restore the previous conditions or, at least, retard the change through more restrictions on the foreign competitors. That government itself may have handicapped the domestic industries through crippling taxes, regulation or inflation is conveniently overlooked. Foreign imports are the easiest target for industries seeking protection from competition and politicians seeking their votes.

At the present these observations on the nature of protectionism seem to be especially relevant for the United States. In the face of growing European and Japanese competition the United States government appears to be posed to launch an offensive toward the containment of Europe and Japan. Since the United States has extricated itself from the war in Vietnam, it may be tempted to embark upon a new foreign adventure, an economic war against the two other economic powers. Surely the result of such a foreign policy offensive would be a highly dangerous trade war that would generate a world-wide depression and global currency panic.

After World War II the United States had become by far the world's largest exporting and importing country, with its main markets in Europe, Japan and Africa as important source of raw materials. But it seems that the era of global United States economic hegemony is now drawing to a close. Both the European Economic Community and Japan are successfully challenging the American position in all corners of the world. The European economic integration has spread from the original six to nine member countries. In addition, Switzerland, Austria, Greece and Turkey have entered into agreements of association with the EEC and Israel is pressing to do so. France's former colonies in Africa have signed preferential trade agreements, and it is likely that also Britain's former colonies will follow suit. Even some Eastern European countries, such as Yugoslavia, Rumania and Hungary are seeking special accords with the growing supermarket. And many others are talking about forging new relations with the Common Market, which in turn took the lead with a new form of foreign aid through trade for 91 less developed countries. Tariff rates were reduced, that is, the external tariff wall around the Common Market was lifted, to boost imports from those countries.

The enlarged European Economic Community now comprises some 250 million Europeans with a gross national product of more than $600 billion. The nine member countries export and import some $110 billion worth of goods, which represents nearly triple the United States trade and ten times that of the Soviet Union.[3] With Britain's membership in the Western Union, Europe may in fact become the most powerful trading area in the civilized world.

Washington is viewing this development with great alarm, which raises the crucial question of this decade: Will the United States learn to coexist with the European-African Supermarket and the Asian economic bloc led by Japan, or will it develop a case of paranoiac fear and launch a foreign policy offensive against these markets? Is Washington befriending Peking and Moscow in order to brand the European Common Market as the new enemy?

The Nixon statements and policies of August 15, 1971, clearly point up the dangerous international situation. When the United States encountered payment difficulties which were of its own making, it suddenly suspended gold payments and in violation of numerous agreements imposed a 10% import surcharge on all foreign goods. The Smithsonian Agreement, four months later, barely averted an economic war between the United States and the two other blocs through a compromise that raised the exchange value of some European currencies, lowered that of the United States dollar, and repealed the United States surcharge.

In the face of new economic difficulties, such as an international dollar crisis or a new recession at home, the United States government may be tempted again to point at Europe and Japan. It may repeat its popular claims that the world is treating the United States in a grossly unfair manner and that foreign intransigence is responsible for our difficulties. And in retaliation against all the foreign wrongs, real and imaginary, it may reintroduce the 10% import surcharge for an indefinite period, impose a sweeping range of quotas on Japanese goods, suspend all talks on world monetary reform until all American trade demands are met, and finally withdraw all United States troops from wicked Europe. In short, it may declare economic war on Europe and Japan, and thereby precipitate global disorder.

The prelude to such a disaster may come in the form of some militant United States demands for one-sided tariff concessions by Europe and Japan. Or, it may be a firm request that the Japanese Yen be revalued considerably and immediately, that the EEC halt or reverse the extension of its market to other countries, that both Europe and Japan introduce voluntary quotas on exports of highly competitive lines to the United States, or that they greatly increase their purchases of American military equipment. When such requests are rejected, as they undoubtedly would be, we must expect the new economic offensive to be launched.

Economic Nationalism Hampers World Trade and Retards Economic Development

Resentment, fear and envy of foreigners are probably as old as man himself. They have stood in the way of peaceful economic exchange and cooperation from the beginning of time.[4] But since the emergence

of an international economy with world-wide division of labor, economic nationalism has been most keenly felt as a destructive force that not only jeopardizes further progress but also would reverse and demolish the achievements of the past. Europe has paid an incalculable price for economic nationalism and is now struggling to overcome its deleterious effects through a common market.

But while Europe is gradually returning from this suicidal road many other countries, especially the colonial countries who only recently emerged from political hegemony, are badly affected by the nationalist bacillus. In Africa, Asia and Latin America economic nationalism, frequently in conjunction with racism, continue to ravish peace and prosperity. In fact, we know of no single year since World War II in which European or American property was not seized, confiscated, expropriated, or taxed discriminately just because it was foreign. It seems that most countries, especially in the undeveloped parts of the world, shy away from instant and total expropriation only because they are hopeful of trapping more foreign property through temporary restraint.

It is most unfortunate that in the name of national sovereignty and anticolonialism, the United States government has fostered economic nationalism in all corners of the world. It has exerted its great influence toward a reduction of European influence and possessions in Asia, Africa and Latin America. The United States urged the Dutch to leave Indonesia, the French to retreat from Indochina, demanded British and French withdrawal from Egypt, urged the Belgians to leave the Congo, the French to surrender North Africa, censured Portugal for her African possessions, and imposed sanctions on Rhodesia. But instead of political freedom and economic progress the change in most cases brought political dictatorships and economic stagnation. Together with European property many billions of American investments were seized by nationalistic regimes devoid of rudimentary economic knowledge.

Americans hold by far the largest share of international investments and therefore have most to lose from nationalization and expropriation. United States multinational corporations own countless numbers of offshore subsidiaries with foreign sales running into the hundreds of billions of United States dollars. GM is the largest auto maker in Germany, IBM the largest computer manufacturer in every Western European country, Continental Can virtually a monopolist in its field, Standard Oil a senior partner in the North Sea oil fields, etc., etc. All these multi-billion dollar corporations would be in grave danger of national takeover if the United States government should start an economic war aimed at increasing United States exports and limiting imports.

Even in the United States powerful political interests are attacking the multinational companies on comparative advantage through "exports of capital and technology." The government, therefore, is to erect an economic wall around this country to shut in United States capital and technology and to shut out imports of goods and services. With the ardent support by the AFL-CIO, these proposals, in fact, have been written into the Burke-Hartke Bill that would prevent United States companies from operating successfully abroad. The bill would tax United States multinational companies to pay total taxes here and abroad of 70 to 80 percent on their overseas earnings. It would authorize the President to prohibit overseas investments and the use of United States patents abroad if in his judgment such restrictions would increase employment at home. And finally, the bill would establish a comprehensive system of quotas on United States imports. [5]

We need not elaborate here how such policies do not create jobs in this country. On the contrary, they would destroy jobs both in the United States and abroad, would reduce labor productivity and incomes everywhere, and above all, would lead the world toward protectionism and nationalism that would engulf it in depression and chaos.

Inflation Threatens to Disrupt the International Monetary Order

World-wide inflation may have the same dire consequences as economic nationalism. The rise of the redistributive state, commonly called the "Welfare State," during this century ushered in an age of inflation and monetary destruction. Redistributive policy both breeds and in turn feeds on inflation. It breeds inflation because monetary expansion, which is believed to provide income and wealth, forms an integral part of popular doctrine and policy. In addition, every one of its chief features encourages inflation. A large number of spending programs lays a heavy financial burden on the public treasury which is tempted to provide the necessary funds through monetary expansion. At first, the Welfare State may merely endeavor to "redistribute" the wealth and income of its rich citizens, that is, of those who own and earn more than the average. But this very convenient and popular method of "redistribution" is soon exhausted while the demands on the state go unabated or even increase. As the raising of taxes on the majority of people is rather unpopular, and therefore politically inexpedient, the Welfare State is tempted to provide the promised benefits through deficit financing. It resorts to deficit and currency expansion as the least painful and most deceitful method of fund-raising.

The disastrous nature of inflation is clearly apparent in numerous economic, social and political symptoms. But the most spectacular effect of monetary depreciation that concerns us here is the gold and foreign exchange dilemma. When inflation raises the prices of goods and services, more foreign goods are imported while fewer goods are exported. Balance of payment deficits develop. In settlement of the debt, gold and other foreign exchange leave the country. In short, a government that depreciates its currency faster than other governments depreciate their currencies, and thus makes goods prices rise faster than they rise abroad, generates international payments deficits and drives gold out of the country.

Federal administrations from Truman to Nixon resorted to inflation at ever accelerating rates and thereby reduced American gold reserves until the United States faced international payment embarrassment on August 25, 1971. With only $10 billion of gold left in Fort Knox and owing more than $63 billion of short-term foreign liabilities the United States was forced to suspend international gold payments.[6] The Smithsonian Agreement, four months later, restored temporary stability in international rates and payments although it did not provide for a return to gold payments. It reduced the United States dollar by some 8 per cent and thereby American foreign debts. It inflicted huge losses on our foreign creditors through the dollar devaluation together with the upward revaluations of their own currencies.

The great danger to the international monetary order flows from the refusal of the United States to put its own monetary house in order, from its chronic trade and payment deficits that reflect an excess of United States consumption of foreign goods and services over its ability to pay. It is true, we offer to make payment in depreciating United States money and claims to money, and thereby export our inflation to any country willing to accept United States dollars. But how many more billions of dollars can our creditors be expected to accept and hold in exchange for their goods and services? How much longer can the richest and most powerful country on earth hope to live on some of its trade partners?

Refusal to make gold payments by the United States casts serious doubt on future monetary cooperation. The immediate prospect for world-wide monetary stability is not too bright. The United States as the huge debtor is taking the position that it is up to the countries with huge surpluses in their international payments to adjust their currencies upward against the dollar. It is Washington's basic premise that the United States is unfairly treated in international commerce and that it is time for others to change. Convinced of the indispensability of the United States dollar as a world reserve currency the United States is defiantly waiting for the others to act.

Bad debtors when called upon to make payment often make charges against their creditors. It is shocking, however, that the United States government should prove to be such a poor debtor. The foreign position generally rejects the Washington charge of unfair treatment. If the United States had adopted appropriate domestic policies, foreign officials argue, it would not have accrued its huge international payments deficits. Therefore, they want the United States to bring its financial house in order and cease to lean on its weaker partners. If the United States should ignore their pleas and continue its excessive inflation that is flooding the world money markets the creditor countries may want to protect themselves from massive dollar flows. They may resort to stringent foreign exchange controls, multiple exchange rates, and other controls over the United States dollar, all of which are designed to hamper international trade and finance.

The grave danger of a breakdown of the international monetary order raises the spector of an international catastrophe similar to the money panic of 1931 and the subsequent disintegration of the world economy. The Eurodollar market with more than $70 billion of short-term United States dollar funds is extremely vulnerable to sudden breaks and runs that may turn into a world-wide dollar panic. After all, how big a United States deficit can foreign creditors be expected to absorb? And what measure of financial loss from dollar depreciation and devaluation can foreign individuals and institutions be expected to withstand? Huge debts and growing losses provide the material of which panics are made. When debtors are forced to draw on all their resources, including their dollars, vis-a-vis the exchange markets, the United States dollar could fall to unbearable levels which would greatly disrupt foreign trade relations. In defense from such disruptions trade barriers may be erected the world over, which would trigger the dreaded economic war between the economic war between the economic blocs and precipitate a global currency panic.

It is apparent that world economic policy is adritt on the stormy sea of socialism, nationalism and inflation, and that we are in grave danger of soon undoing much of the progress that was made since the dark days of the Great Depression.

[1] United Nations, *Statistical Yearbook*, 1971, p. 383.

[2] Cf. this writer's "Are We Marxians Now?", *The Freeman*, August, 1972.

[3] United Nations, p. 384.

[4] Cf. Carlton J. H. Hayes, *Nationalism: A Religion*, The Macmillan Co., N.Y. 1960, p. 20 et seq; also Helmut Schoeck, *Envy*, Harcourt, Brace & World, N.Y., 1969,

[5] *Congressional Quarterly Service, Weekly Report*, 1972, pp. 1183, 1287, 2920, 3055-3057.

[6] *Federal Reserve Bulletin*, July 1972, pp. A77-78.

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