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US-European Community Trade Relations.

Confrontation or Cooperation?

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To the Foreign Trade Association

of Southern California

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Mr Chairman, Ladies and Gentlemen,

I would like to thank you and the Foreign Trade Association of Southern California for the chance of sharing some thoughts with you today on the relationship across the Atlantic. And for the invitation to come again to the West Coast. For a European it is always a delight to be here. But it is also a challenge. For to be on the Pacific seaboard of this great continent provokes for us a question. Where is Europe in the international economic and trading scene which is your world and does it matter very much when you get there?

Any European living in the United States quickly understands this paradox. Some of the old links with Europe have been weakened. The generation of post-war American statesmen who were mixed up in the reconstruction of Europe after the war is now largely gone. There has been a shift in wealth and power from the North-East to the South and the West. In 1918, California had 2 million people, now it has 24. The demographic centre of the United States is now west of the Mississippi. The demographic centre is in fact moving West at the rate of some 55 feet per year. The distribution of seats in the House has been altered in favour of the South and the West. So this has led naturally enough to a greater interest in the Pacific rim, to a lesser interest in Europe.

But at the same time there has been a dramatic change in the involvement of the United States in the outside world. For something like one hundred years after the Civil War, foreign trade was never more than 4 to 5 percent of American GNP. Then in the 1970s there was an explosion. Now the figure is 12 percent and rising.

One fifth of American industrial production is exported, 40 percent of American farm land is devoted to exports. Thus foreign trade has played a dramatic part in the fivefold increase in real terms in American GNP between 1939 and 1986. Foreign trade is now an indispensable part of American prosperity. And central to American foreign trade and the standard of living of the United States is the relationship across the Atlantic.

In 1986 the twelve member European Community emerged as the largest export market of the United States - and as a customs union with a single external tariff and no tariffs between our Member States we are entitled to regard ourselves as one market. That year US exports to the Community totalled $53 billion compared with $45 billion to Canada and $27 billion to Japan. Total US trade (exports and imports) with the Community was $133 billion. And all this over low tariffs and with very few import restrictions.

As George Shultz said in Brussels a couple of years back - we must be doing something right.

The second reason goes wider. The Community accounts for something like one-fifth of world trade, the United States for about 15 percent. So together we account for more than one-third of world trade. And this places on us both very heavy responsibilities. For if any mutual escalation of trade restrictions were to break out, if the shutters were to come clanging down on both sides of the Atlantic, then the one world trading system which has underpinned over the last forty years the biggest rise in prosperity in the recorded history of the world would be bust. And we would be back sooner than many of you could believe not only to the poverty and the misery of the 1930s but to some of the terrible political ghosts which haunt every journey through an economic wasteland.

The third reason goes even wider. Europe and the United States, whatever arguments we may have from time to time, share common democratic values. No European should forget the Marshall Plan, the Berlin airlift, the founding of the North Atlantic Treaty Organization in the common defence of freedom and the generous and statesmanlike support which the United States gave to the beginning of European unification in the 1950s. These common values are not put at risk by trade disputes. But the solidarity of the Western Alliance would inevitably be shaken by an all out trade war.

All this is not to say that the international economic environment depends only on the transatlantic relationship. Quite apart from the problems you have with Japan and some industrialising countries in East Asia there are some formidible general questions. Can the debt crisis of the developing countries be maintained by prudence and wisdom from both borrowers and lenders? Can exchange rate instability be contained before it puts an intolerable strain on the one world trading system?

These are reasonable, indeed essential, questions. But there is another question I would like to concentrate on today. That is the question of protectionism. Protectionist pressures have reached such a dangerous point that they pose a threat to the entire world trading system. I am conscious so that I run the risk of seeming to single out pressure in Washington for protectionist measures as the centre of the world's ills. This would be a one-sided presentation. Americans have every right to expect not lecturing by foreigners but a fair and balanced discussion of mutual problems. So a fair question at this stage is what is Europe doing about protectionism? Is it protectionist in industry or in agriculture? What is its policy on world trade? What is it doing about its growth and unemployment? These are fair questions. So let me try to deal with them.

First is the European Community protectionist? Our industrial tariff averages something like 4½%. This is about the same average as the US tariff. But over 10% of US industrial imports come in with a tariff of over 15%, some more than 40%. Only one percent of EC industrial imports come in with tariffs of 10% or more. Our tariff on all imports if we take into account our measures to help developing countries averages only 1%.

What about the loss of jobs caused by imports? Senator Dole once pointed out that in the last ten years the United States has lost over 600,000 jobs in just three industries alone, textiles and apparel, steel and footwear. This is certainly a tough problem. But the corresponding figure for the Community is one and a half million. Textile imports have doubled over ten years leaving us with an import penetration level more than twice that in the United States. But we are not contemplating any new restrictions on imports. Steel imports have been cut, this we had to do because we have forced through between 1980 and 1985 reductions of 32 million tons of capacity - with another 20 million scheduled to go over the following three years. But the reductions in imports have been moderate compared with US import cuts.

I do not think anyone could fairly claim this shows the Community to be protectionist.

"Ah" folks will then say, "what about agriculture?" The CAP has become the Great Scapegoat of the Western World. But this is an affair more of myths than of reality. Let me quickly dispose of some of the myths. It has been alleged that we subsidize our agriculture far more than anyone else. In fact, last year the Community subsidized 11 million farmers to the tune of $22 billion, compared with $26 billion of farm price support expenditure on 2.5 million farmers in the United States. A very senior US official recently said in testimony before a Committee of Congress that the EC comes only third in the agricultural subsidies league after Japan and the US. Moreover, incomes of EC farmers have fallen by 30 percent over the past 10 years, compared with a rise of 19 percent in general Community incomes.

Secondly, does the Community with this policy shut out US farm exports? For fiscal 1986 the Community retained its position as the biggest US farm export market, $6.4 billion compared to $5.1 billion of exports to Japan. Moreover, while US farm exports to non-EEC countries in 1986 nosedived by 19 percent, exports to the EC hardly dropped at all - by just 3 percent. We now take a quarter of all US overseas sales of farm products. We are not only the American farmer's best customer, but the biggest importer of farm products in the world.

Third, are we engaged in massive undercutting of American farm products on world markets with our subsidized exports? The fact is that the Community and the United States compete only over about a quarter of US farm exports, mainly wheat and, to a lesser extent, dairy products. The international trading rules provide that agricultural export subsidies are permitted but should not be used to get more than an equitable share of the world market. What then has happened to the EC share of the world market in wheat and dairy products? The high point of American wheat exports was 1981-82, when the US accounted for 49 percent of the world market. In 1984-85 this had dropped to 36 percent. Was this the Community's responsibility? Hardly, since our share remained stable between 14 and 16 percent. That of other exporters rose much more sharply. What about dairy products? For years the American share of the world market was nil. In 1985 it was 10 percent, an increase achieved mainly at the EC's expense.

These are the facts. They describe, like an oil painting, a picture. But what is the future? Are we going in a protectionist sense or not? Let me give you three reasons why we are on the side of the angels - slowly and painfully maybe, but pointed in the right direction. The first is agriculture. We have made it clear that we are willing to negotiate about agriculture in the new trade round launched last September at Punta del Este. Our motive here is the best possible one - one of self-interest. We are the biggest player on the world trading stage, with 20 percent of world trade. We realise that the one world trading system enshrined in the General Agreement on Trade and Tariffs cannot be kept going without successive major trade negotiations. And given the importance of agriculture in world trade today, a negotiation cannot take place without agriculture. So we need to negotiate about agriculture. What we are not willing to do is single out simply our export subsidies as the negotiating agenda. We want everything on the deck. And we are not much attracted by the idea of putting agriculture on a special "fast tract".

A settlement in an area as important and huge as agriculture cannot realistically be reached in advance of the other main components of the negotiation. But the key to a solution in this area seems to me not in the framing of the GATT wording - helpful and supportive though this will finally be - but in tackling government subsidies to farmers on both sides of the Atlantic which, with the inexorable march of productivity, are pushing up production surplus on a saturated world market.

And here the Community has made a start. In 1984 the Community decided to cut dairy output and by 1985 it had already fallen by between 4 and 5 percent. Support prices for grain were frozen last spring for the third consecutive year. Production has been made less attractive and returns to farmers have been reduced by at least 15 percent. Furthermore, in December last year the Council of Ministers agreed that dairy production be cut over a two-year period by just under 10 percent and that the price of beef should be reduced by some 13 percent. The EC butter mountain - now some 1.5 million metric tons or more than 80 percent of world stocks will be brought down to 350,000 tonnes and the beef mountain should be cut by some 50 percent by the end of 1987.

These agreements are the biggest changes in the Common Agricultural Policy since it was established in 1962. They will result in savings from the 1989 budget of between $1 and 2 billion. I need hardly add that these cuts have been very unpopular with Community farmers. Bankruptcies and foreclosures are not an exclusively American problem. Many European farmers were forced out of business by earlier cutbacks. Many more will be now. So we watch with sympathetic interest the proposals now being formulated by the United States administration to trim its own farm support programme in the years ahead. In the meantime, we in Europe can already point to decisive and painful action on this path.

Then second the question of growth. I have the feeling living in Washington that we in the Community have come to be regarded as economic stumblebums. So let me set out some facts which I hope will correct this impression. From 1970 through 1980 EC annual growth averaged 3.1 percent, while US growth was 2.7 percent. In 1985, EC growth was 2.4 percent, while the US economy expanded by 2.7 percent. Growth in 1986 for both the EC and the US was the same, 2.5 percent. In 1987, our forcasting services in the Commission reckon that the Community will expand at about 2.3 percent and the US by some 2.4 percent.

So our track record is not so different. But this is not an excuse to refrain from doing better and here we can point to progress among the six major industrial countries to promote a more balanced global growth, reduce existing imbalances and stabilize exchange rates. I would pay tribute here to the initiatives of Treasury Secretary Baker. It was in no small measure due to him that at the Paris meeting of February 22 it was industrial countries with external surpluses who committed themselves to strengthening demand while those in deficit would reduce their domestic imbalances and external deficits. Europe played its part. Within this framework Germany pledged to propose an increase in the size of the tax reduction already enacted for 1988 and to consider a comprehensive tax reform to take place in 1990.

A third factor is the Community internal market. We have managed to abolish tariffs between Member States. This was no negligible achievement if you reflect that the tariff rates between Member States in the late 1950s were as high as 50-60 percent. But there still remain a range of internal barriers which impede trade between our Member States - frontier formalities, different technical standards and government purchasing requirements. So the Commission put to the Council in 1985 a precise programme with 300 proposals, name tag and timetable attached. If this programme is adopted as we hope by 1992, it will mean that by that date businessmen will be able to trade and invest in a single market of 320 million people as easily as they can between the States of the Union here. This could mean a near doubling of our standard of living. That would be quite some growth and it would not only mean a more prosperous Europe; it would mean an even better trading partner for the United States.

I hope that what I have set out is a fair and reasonable account of the contribution the Community has made in keeping open its market and resisting protectionism and contributing to growth. I do not say that we have all the answers or that angels' wings are sprouting on our side of the Atlantic. But like the pianist in the Western saloon we are doing our best.

What about the situation here? We all know about the protectionist pressures in Congress. This is not to criticise. This is simply to observe. With a trade deficit of $170 billion Americans are worried understandably about their jobs.

But in all this there is one dangerous folly which applies not simply to the United States but to any country in a similar situation. To think that you can deal with a trade deficit by legislation is a mistake. Trade legislation can do some very useful things. It can give the administration authority for a new trade round. It can help in such areas as training, readjustment and education. But some ideas do not help. If a boondoggle is defined as "any project on which government funds are wasted" (I quote from William Safire's Political Dictionary), then a project which would result in a loss of jobs can good be called jobsdoggling. There is a good deal around. Let us look at some of the examples.

A bill has been introduced which would limit textile imports to their 1986 level and restrict growth to 1 percent a year. This could only be achieved either by reneging on the agreements with developing countries recently negotiated under the Multifiber Arrangement (MFA) or by cutting exports of textiles to the US from the EC or both. Either course would mean the end of the MFA and would be likely to provoke retaliation. Certainly, if restrictions were imposed on European exports of textiles to the US, the Community would be likely to retaliate with restrictions on US textile exports to Europe, which are up 42 percent from last year and still rising. Result: Loss of American jobs.

A second jobsdoggle is requiring countries with a large current account surplus with the US to cut the surplus dramatically or face a special tariff. This would conflict with international obligations, throw a large wrench into the current round of trade negotiations and could easily boomerang. Other countries could pass similar legislation. In 1980, the US ran a surplus with the Community of $18 billion. Would the US appreciate it if, when it gets into a surplus position again with a number of its important trading partners, tariff increases were to be imposed on American exports? In the meantime, the result would be retaliation and the loss of American jobs.

A third jobsdoggle is reciprocity sector by sector. It has been argued that unless foreigners give the US equal treatment in certain specific sectors such as telecommunications, barriers should be erected against their exports of the same products to the United States. First, deregulation in the US telecommunications area, to take this as an example, did not happen overnight. The process started in 1968 and is still going on. Second, the US has a surplus, not a deficit, of $500 million with the EC in telecommunications equipment and of several billion dollars if one considers telecommunications and computers together. Finally, everyone can find sectors in which one country gives better treatment than others. In the case of wool textiles, for instance, tariffs in the Community are less than half those in the United States. To some, this would be a case where the Community could insist on reciprocity.

To try and get reciprocity in every specific sector would mean massive new restrictions sprouting up everywhere on world trade. Reciprocity is essential in trade negotiations. But it can only be achieved by overall reciprocity: trading off the disadvantages in one sector for advantages in another. Forcing reciprocity in one sector by imposing barriers would simply lead to retaliation from the other party. Result: Loss of American jobs.

A fourth jobsdoggle is action, possibly of an automatic kind, under Section 301 of the US Trade Act of 1974 (unfair trading practices). It is all very well to ask for tough and aggressive action under domestic legislation, but unfair trade practices generally turn out to be what the other fellow does - never what one does oneself. What really matters is whether actions by a contracting party of the GATT are in conflict with the international trading rules. Otherwise "tough" action by the US will be followed by equally tough action by others against US exports. And it should always be remembered that while the international trading rules on, say, subsidies and dumping may not be perfect, they are the only rules we have. Amending them should be done by multilateral agreement, not unilateral action which could simply result in retaliation by others against American exports. Result: Loss of American jobs.

Of course, we do not know as yet quite in what form legislation will emerge from Congress. The Administration have - very rightly - opposed protectionist provisions. But the fundamental point for us all to bear in mind is that there is no quick fix to a trade deficit. To try and do so by legislation which bashes foreigners invites retaliation and is simply self-defeating. The real solution lies in reducing the budget deficit in an appropriate exchange rate and increasing competitiveness. Five million American jobs now depend on exports, both in the farm sector and in industry. Some of the proposals I have mentioned may sound superficially attractive as a means of reducing the trade deficit, but in practice they would simply result in the loss of hundreds of thousands of American jobs.

I do not make these points in a quarrelsome or hostile way. The world owes an enormous amount to American support over the years, for the one world trading system and for the leadership the United States supplied in supporting and heading some major trade negotiations. But the privilege of friendship is frankness.

You have a major macro-economic question in terms of the budget deficit. We have problems with unemployment and growth. Let us both take our macroeconomic responsibilities. Let us keep our cool in the trade arguments which we have inevitably from time to time. Let us work together in the areas where we can - the new trade round and the problems of indebtedness of developing countries. And let us hope that on this path we can together keep the one world trading system which, with all its imperfections, has made possible over the last 40 years the biggest increase in prosperity in the recorded history of the West.

If I have spoken at length about the European perspective, let me try and adjust the balance by a quotation from a great American. As long ago as 1844 Emerson wrote some lines about trade and America which are worth recalling today. He wrote, I quote, "The philosopher and lover of man have much harm to say of trade but historians will see that trade was the principle of liberty. That trade planted America and destroyed feudalism. That it makes peace, and keeps peace, and it will abolish slavery". Let us on both sides of the Atlantic try and comport ourselves in our economic relationship that we can remain faithful to the memory of these words.