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BEFORE THE SUBCOMMITTEE FOR FOREIGN ECONOMIC POLICY OF

THE JOINT ECONOMIC COMMITTEE -- U.S. CONGRESS

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I am grateful to you, Mr. Chairman and to this Subcommittee for the honor of being invited as a European to participate in your hearings on future United States foreign economic policy.

Before dealing with the main subject that is under consideration by your Committee at the present hearings, I would like to make some general remarks on what seem to be fundamental trends in trade and investment during the seventies.

This is a world of sweeping changes affecting all aspects of human life and reaching increasingly even the remotest places on the globe. It is therefore of vital importance for businessmen, administrators, and legislators to constantly keep under review past developments and to correctly assess future trends. If we look ahead at international economic relations in the seventies, there is at least one basic fact of which all of us can be certain: the life of the average American or European citizen will be influenced more than ever before by events outside the specific region or country he is living in. He will purchase more products that have been produced, partly or wholly, in other countries or continents. More people will work with companies having their main operations in other parts of the world, and all of us will increasingly depend on business conditions prevailing elsewhere. We shall thus, no doubt, come closer to the "one-world economy" which will prevail at some later stage of human history.

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International trade will continue to expand faster than world gross national product, even if one excludes the substantial amount of trade that will be carried on within regional groupings like EEC, EFTA, Central American Common Market, LAFTA, etc.

Trade expansion will continue to be fastest among the highly industrialized countries, essentially North America, Europe, and Japan. Manufactured goods will further increase their share in total world trade.

But trade will be only one aspect of the evolving pattern of foreign economic relations. The network of the international economy will be even more fundamentally determined by a greatly increased mobility of capital, technical and managerial know-how, and even of labor. The world-wide reductions of trade barriers and of restrictions to capital movements have created a new situation in the world economy: industrial corporations are more free than ever before in their choice as to how and where to manufacture and market their products, by setting up subsidiaries in overseas markets or granting licences to foreign companies. In the past decade United States direct foreign investment has grown substantially faster than its exports. There is no reason to believe that this trend will be suddenly reversed in the seventies.

This development is not very surprising. Indeed, there are limits to the cost advantages to be obtained by concentrating production at one point from which to supply the whole world. Economies of scale that might perhaps be derived from such a concentration may be more than offset by higher transportation and handling costs and by insufficient ability to adjust to specific market conditions in distant countries.

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If one realizes that exports and foreign investment are only two different methods of penetration into foreign markets, it becomes clear that a fair amount of American exports of manufactured goods may increasingly be replaced by production through American sussidiaries in the overseas markets. It is therefore quite natural that the "traditional" United States' trade surplus is diminishing or even disappearing and that investment income is more and more financing imports, tourism, and other services which the United States requires from other countries: in 1969 income on foreign private investment amounted to nearly $8 billion per year or 22 per cent of United States merchandise exports. This compares to $1.7 billion per year or only 13 per cent of exports during the years 1950 to 1954. It can be safely expected that by the end of the next decade income from foreign investment will be an even more important item in the U.S. balance of payments than it is today. The United States, principal "rentier" of the world, will have to accept an increasing flow of imports from the outside if it wants to enable the host countries of American investment to earn the foreign exchange necessary to finance the remittances of investment income.

Let me add a few remarks on what I conceive to be major trends and problems in the field of international trade and trade policy during the decade ahead.

It seems to me that the seventies will be a period of intensified international competition. When the Kennedy Round negotiations will have been fully implemented by 1972, tariffs will be lower than at any moment of modern history. According to plans which are being worked out at present, the less developed countries will enjoy duty free access to large segments of the developed countries' consumer markets. The lowering of tariff barriers

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will go parallel with further reductions in transportation costs which can be expected as a result of a more generalized application of advanced handling techniques (container ships, air cargo, etc.). There is no guarantee for industries in particular countries to preserve any "traditional" advance. Both the United States and Europe must learn no longer to consider their advance in certain industrial sectors as a given fact of life. It may well be that they will both be evicted from relatively safe market positions which they hold in certain sectors. Such changes are painful. The problems both the United States and Western Europe are facing in established industries like textiles and shoes are a case in point. Whatever the difficulties, the solution cannot be found in resisting the inevitable and mutually profitable changes but only in a smoother process of adjustment. Economic policy must increasingly encompass measures providing for long-term structural adjustment. If we do not succeed in making substantial progress along these lines, it will be very difficult to embark upon further trade liberalization. The United States, when it adopted the Trade Expansion Act of 1962, clearly recognized the close relationship between trade policy and adjustment measures; but it will, no doubt, be necessary to go beyond the provisions of the Trade Expansion Act.

Some students of trade policy wonder what measures towards further trade liberalization might be taken after the Kennedy Round reductions will have been fully implemented. They already envisage a situation where the exchange of manufactured goods will no longer be hampered by the existence of tariff barriers. However, if we look dispassionately at the world trade situation most likely to evolve in the seventies, it appears that we must

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set more modest benchmarks. As long as fundamental economic conditions and policies continue to remain as different as at present, we can hope at best to get only a few steps closer to the ultimate goal of free trade. In other words, we should concentrate our efforts on certain sectors where tariffs remain excessively high compared either to those protecting other industries or in relation to value added.

There has been increasing awareness recently of the restrictive influence which might be exercised on world trade by the existence of numerous non-tariff barriers. In a way, this is a perfectly normal consequence of the successful reduction of tariffs and the quasi-disappearance of quantitative restrictions which makes other barriers loom larger.

We have had this experience within the EEC. After internal tariffs had been eliminated, businessmen suddenly discovered all sorts of other hindrances to their exports, such as administrative rules, fees, sanitary prescriptions, technical norms, public procurement procedures, or simply different habits. We found it both challenging and extremely difficult to attack these less tangible impediments to an unrestricted flow of goods. Progress is therefore bound to be slow, in some areas even very slow.

When trying to eliminate non-tariff barriers at a world level, difficulties will be infinitely greater than within a homogeneous group of countries, such as the EEC members, which are contractually bound to create one large domestic market for their agricultural and industrial products.

I understand that the GATT industrial committee has identified some 800 categories of non-tariff barriers, including such diverse things as customs valuation methods, tariff classifications, prohibitions on advertising certain alcoholic beverages, and certain forms of discriminating taxation, for example on automobiles and spirits.

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It is my impression that all of the major trading nations have their fair share on this list and that, therefore, the "burden" is much more equally distributed than quite a few people, especially in the United States, seem to think. Whatever the problems and difficulties, it seems of vital importance that we tackle them and that the international trading community makes some progress, in the years to come, towards eliminating a fair portion of those non-tariff barriers which prove particularly harmful to trade.

Considering the difficulties involved, and particularly the problems of defining concessions on a basis of reciprocity, negotiations will inevitably be long and cumbersome. It is, therefore, of vital interest to all participants that any agreement which may be reached at the negotiating table will also be "honored" by the respective national legislatures. We simply cannot afford to go into such lengthy negotiations without being fully convinced of the "credibility" of our negotiating partners. Let me add in this connection that the delay of action by Congress concerning the abolition of ASP which is part of the Kennedy Round agreements has caused some scepticism as to the United States' credibility in the field of non-tariff barrier negotiations. I do therefore hope that Congress will quickly adopt the trade bill which President Nixon submitted to Congress on November 18.

Let me now turn to that part of international economic relations that concerns more directly the United States, on the one hand, and the EEC, or rather Western Europe, on the other.

Since the end of World War II, the United States has consistently given its support to the idea of European political and economic unity. The United States did so because it was convinced that a prosperous and united Europe would be the best guarantee for peace on the European continent. At the

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same time, the United States had undoubtedly hoped for a united Europe assuming increased responsibility in world affairs and thus relieving the United States from the strenuous burden of being the sole safeguard of freedom in the western world.

Recently, however, there have been signs, at least in American public opinion, of some changes in the traditional United States' support of European unity. There seems to be a growing disillusionment with that policy. Some think that it was one of the "grand and sad dreams of American foreign policy in the past 20 years."

It is therefore not surprising that some highly esteemed personalities in American political life have recently expressed fears that British entry into the EEC, once considered a primary objective of U.S.-European policy, might have deleterious effects on the United States which should therefore reconsider its support for British entry.

What then is the past record of European integration and what is its outlook for the seventies? How does this process affect American economic and political interests? How will U.S.-European relations be influenced by further progress towards economic and political cohesion in Western Europe?

As far as our past record is concerned, we need not be ashamed of ourselves. Within only 12 years we achieved more in terms of economic unification than many of us dared to hope in 1956-57 when we drafted the Rome Treaties setting up the EEC and Euratom. The six EEC economies have become closely interdependent. Goods and labor move nearly without any restrictions. We have thus made substantial progress on our way towards achieving our principal, economic goal, that is, to create one big domestic market on the European continent. Recent events have made people realize that we have to push this process further, full economic and monetary union being necessary to ensure lasting success. Plans are actually being drawn up to achieve all this by 1978-1980.

Economic integration in Europe has been a major factor responsible for spurring economic development. The spreading of prosperity among all layers of the population has undoubtedly helped to contain movements of social unrest which might otherwise have arisen.

Politically our achievements have been much less conspicuous. We have not created any new institutions in the field of political cooperation, particularly for foreign and defense policies. For a variety of reasons and historical circumstances, our efforts to achieve more institutionalized political cooperation among European countries have failed so far. However, this apparent absence of specific political action should not lead one to believe that Europe has not gotten closer to unity. There can be no melting of six or ten national economies into one economic union without a substantial amount of political cohesion among the countries concerned. The creation of the EEC has been an essential factor in eliminating the century-old distrust and enmity between the Western European powers, especially France and Germany.

But our task is far from being accomplished. At The Hague conference in December, 1969, the EEC Governments reiterated their resolution to go ahead with the task of unifying Europe. We shall progressively tackle highly sensitive issues that touch the basis of national sovereignty, like monetary union.

It appears that the EEC will have to accomplish essentially four tasks in the seventies:

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- define its outer boundaries, i.e. settle the long pending problem of enlargement

- create a modern agriculture able to compete in the world market with a minimum of government interference and avoid surplus problems, thus contributing to an orderly world market in agricultural products.

- shape the instruments and institutions for coordinating or unifying basic economic policies within the EEC, particularly in the monetary and industrial fields

- apply trade policies which take into account the important responsibilities of the Community in world trade

- set up coordinating machinery in political areas not presently covered by the EEC Treaty.

If, as I am confident it will, the EEC succeeds in achieving substantial progress in each of these areas, this will have an important bearing on U.S.-European relations. To the extent that the European countries will harmonize or unify their policies in a growing number of fields, the United States will progressively be confronted with a single position only, instead of six or ten. Technically this will undoubtedly simplify our dealings. But it does not necessarily imply identity of views. As long as six or ten European countries acted more or less independently of each other, they were likely simply to adapt their policies to whatever measures were taken by the United States.

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This adjustment mechanism worked satisfactorily because of the imbalance of "power" between the United States and each European country individually. However, when the European countries get together to decide certain things in common, such decisions may have repercussions on United States policy formulation. Indeed, the mere fact that European countries decide in common on certain questions will give such decisions a substantially greater weight even outside Europe. Suppose, we already had some kind of monetary union within the Community, as is presently envisaged for the late seventies, and all Central Banks within the Community decided to raise their re-discount rates to the same level. It is quite evident that the impact of such a decision on United States monetary policy would be subsntially greater than if only Belgium or Italy raised its rates. This example indicates the new type of reciprocity, or the interdependence, which will evolve in U.S.-European relations as a consequence of a higher degree of economic and political integration within Europe. Some may regret the days when there was essentially only one decision center in the Western world and when the United States was free to give not too much weight to the policies followed by other nations. But it should not be overlooked that the new relationship which is gradually developing between the United States and Europe will, at least in certain fields, bring about that sort of power sharing that the United States hoped for when it supported European unification.

The United States will less frequently have to take "lonely" decisions, for, in addition to American public opinion, Europe may have its word to say, as happened recently on the question of a general tariff preference system in favor of the less developed countries. As long as there continues to be

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basic agreement between the United States and Europe on fundamental policy issues that determine our common way of life, there can be advantages to a certain degree of emulation and rivalry between the two Atlantic regions.

We simply have to realize that our views are bound to differ in certain fields and that in a growing number of economic policy issues neither side can dictate its solution to the other. To the extent that common solutions may be required or desirable, they will have to be agreed upon in a dialectical process of challenge and response. This appears to me to be the deeper meaning of any "Atlantic partnership" concept.

Turning to more immediate and concrete United States' concerns with respect to European unification, I should like to make a few remarks on two vital Community issues: its enlargement and its agricultural policy (CAP). Indeed, it appears that the United States judges the Community primarily on the basis of its policies in these two fields.

As far as the enlargement of the Community is concerned, it is a political imperative. The six-member Community is to be considered as only a preliminary stage of European unification. Indeed, Western Europe is too small in size to be able to afford to stay permanently divided in different groups amongst its 20 odd countries. For well known reasons, the enlargement has not been achieved earlier. But the Community has now arrived at a point in its history where this issue must be settled. Without a solution of this question progress in other fields might well be blocked forever. It is, therefore, a key issue for the Community, for Europe, and also for the United States.

That is why I regret Senator Javits' recent statement evoking the possibility of the U.S. Administration withdrawing its support of British

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membership. As former Italian Permanent Representative to the EEC I had many occasions to gratefully acknowledge the moral and political support which previous administrations have given to European unification. But as a European citizen I should also make quite clear my conviction that the Europeans have a right to organize their economy and society as they consider it to be in their best interest, provided they respect their international obligations.

What then will most probably happen when the Community is enlarged by four new members -- the United Kingdom, Denmark, Norway, and Ireland?

They will join an existing customs union. GATT provides for such an enlargement, and sets the rules to be followed in such a case.

It should be recalled that in the field of manufactured products, which cover the major part of U.S. exports, EEC tariffs are on the average significantly lower than those of both Britain and Ireland. Under the hypothesis that Britain (and the other candidates) would adopt the common external tariff, subject to some minor adjustments, the United States would get a more favorable access to the British market for some 60 per cent of its exports.

The situation might be different for certain agricultural commodities. But it is my impression that the impact of British entry on U.S. farm exports has been greatly exaggerated. In fact, there is only one major U.S. agricultural product, feed grains, which benefits from a higher protection in the EEC than it does presently in Britain. On such important U.S. export items as soybeans, oil cakes, vegetable oils, dried fruits, and vegetables, the level of EEC protection is either lower or about the same as that of Britain. In the case of tobacco, which is the most important single agricultural product exported to Britain, accounting for about two fifths of total

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U.S. farm exports, total tariff and excise charges are higher in Britain than in the Community. Considering these factors, it is by no means excluded that U.S. farm exports to Britain which have been stagnating at about $400 million during the last six years may be stimulated as a consequence of Britain's joining the EEC.

Whatever may be the result of these different, conflicting forces that are likely to affect U.S. exports of industrial and agricultural goods to Britain, overall U.S. imports into Britain should be favorably influenced by the positive effects which British entry in the Common Market will most probably have on its rate of economic growth.

While the case of Britain, Ireland, Denmark, and Norway is relatively simple, the links with other European countries raise a different set of problems. Roughly these countries fall into two categories, those unable or unwilling to subscribe to the political objectives and implications of the Rome Treaty, and those not yet in a position to become full members of the Community. Sweden, Austria, Switzerland, and Finland, pursuing for different reasons a policy of neutrality, belong to the first category. Spain, Portugal, Greece, and Turkey to the second. All of these countries do between 50 per cent and 70 per cent of their trade with other European countries. Because of their small size they would no doubt suffer injury if they stayed completely outside of the economic integration movement which is going on in Europe. It is therefore of vital importance to them that mutually acceptable solutions be found to settle their special problems.

Canada and the United States finding themselves in a somewhat comparable position have tried to solve their special trade difficulties on a basis

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limited to one major industry, automobiles. By virtue of the U.S.-Canadian Automotive Agreement of 1965, for which the GATT partners have granted a "waiver", the United States and Canada are able to do about one third of their trade free of duties and other restrictions. In the case of Europe, it will no doubt be necessary to find solutions on a more general basis. There is no question of concluding "preferential agreements" designed to produce minor trade advantages for the Community. It is a question of progressively bringing these countries into the vast European market which will gradually come into existence.

Of course, this will mean that sometime by the end of the seventies U.S. commodities exported to most West European countries may be hit by tariffs -- however moderate -- while those from West European countries integrated in the Common Market will not. However, from the European point of view the situation is entirely the same as regards goods imported into the state of California from New York on the one hand and from Europe on the other hand. The analogy may appear farfetched. But, after all, Europe is simply realizing, after decades of international strife, that it is imperative to create a single economic area if it is not to fall hopelessly behind the natural "continental powers" like the United States, China, or the Soviet Union.

We shall therefore have to revise our traditional concepts of what is foreign trade. Today nobody would consider commercial transactions carried on between two German cities such as Hamburg and Nuremberg as part of foreign trade. But as recently as 1880 they were still "foreign trade" in the same sense that trade between Germany or France and Denmark is today.

Twenty years from now foreign trade will be done essentially on an inter-continental basis, the intra-continental flow of goods being more and more assimilated to domestic trade. It is in this perspective that one should look at European integration as well as at similar integration drives that have developed in Latin America, Africa, and, to a certain extent, in Asia.

There can be little doubt in my mind that the shaping of economic unity in Europe has not caused injury to the United States in the past. On the contrary, I am inclined to think that American businessmen, more than anybody else, knew how to fully benefit from the changing economic conditions of one single market and the increase in prosperity that went along with European integration.

Indeed, American exports to the EEC increased more over the last decade than to any other part of the world. On the other hand, American direct investment within the EEC more than quadrupled in the ten years following the beginning of the Common Market. This record is unique in the history of economic relations between nations. American investments are heavily concentrated in the manufacturing industries where affiliates of U.S.-based companies account for up to 80 per cent of total output and investment. The replacement value of U.S. direct investment and participation within EEC is estimated at some $30 billion. Assuming an annual turn-over of two dollars for every dollar invested, sales should be in the order of $60 billion per annum, i.e. roughly fifteen times U.S. exports of manufactured goods towards the Community. These figures clearly show that in order to correctly appraise the closeness of U.S.-European economic relations one must not just look at the trade statistics, because they tell only part of the story.

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It has become "en vogue" in the United States to accuse the common agricultural policy of being one of the major factors accounting for, what is considered by the United States, an unsatisfactory development of its agricultural exports towards the EEC: while U.S. agricultural exports to the Community increased by 17 per cent between 1963 and 1968, exports of manufactured goods went up by 44 per cent. I think it would be unfair not to admit that in some cases the common agricultural policy may have negatively affected U.S. agricultural exports to the Community.

But one should not overlook a certain number of basic tendencies in world agricultural trade and attribute their consequences to EEC agricultural policy. Indeed, total U.S. agricultural exports have been stagnating since 1964. As the share of the EEC market accounting for roughly one fifth of total U.S. farm exports has not diminished during that period, one has to find a more fundamental explanation for this trend. In my mind, the explanation lies essentially in the unprecedented increase of agricultural productivity in all countries, whatever their system of agricultural protection, and their level of agricultural prices.

When agricultural productivity increases at some 6 per cent to 7 per cent per annum while consumption rises by only 1 per cent to 3 per cent, the degree of self-sufficiency of traditional deficit countries, like Western Europe or Japan, is bound to increase. It is to this basic change in the pattern of agricultural production and trade that the United States and other exporting countries have to adapt themselves.

Of course, it is contrary to economic reason that Europe should try to produce agricultural commodities which it could import from the United States or other countries at substantially lower cost. However, one should not forget that in all developed countries, including the United States, agricultural problems cannot simply be solved by applying economic criteria. It is not possible to expel some 5 or 10 million farmers within a few years from the countryside without provoking a social and political uproar. Nor can one undo within 10 or 15 years the shortcomings of a hundred years' agricultural policy striving for more food production and trying to preserve the so-called "family farming". It is good to remember in this connection that the United States had its first experience with agricultural surpluses as far back as the early twenties and that 30 years later it still had to resort to a most impressive food aid program under PL 480 in order to get rid of tremendous agricultural surpluses.

The European agricultural problems can be solved only by a progressive integration of agriculture into the market economy. This requires fundamental changes in habits, in farm size, in production, and marketing methods. In democratic countries such changes cannot be brought about overnight.

Indeed, Europe can only reduce its farm population if the excessive farm labor can be transferred to other sectors, in particular to manufacturing industry. Already, the proportion of the active population engaged in farming in the Community has come down within ten years from over 20 per cent to 14 per cent. But it is still far away from the 5 per cent figure of the U.S.

We are well aware in Europe of the seriousness of these agricultural problems, and they figure high on the priority list of the Community. Action will be taken, but nobody could solve these problems overnight.

Some may have had doubts in past years as to the capacity and political will of Europe to pursue a dynamic policy of unification. I do not blame them. We have indeed gone through a period of stagnation and hesitation.

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But since the European Community summit meeting last December, it is clear that these political obstacles have now been overcome. I did draw your attention already to the important decisions about a program for full economic and monetary union. Negotiations for accession of Great Britain and other European countries are now being actively prepared.

In all fields, European integration seems to have refound its dynamism, and this corresponds, I think, to a desire that has characterized American foreign policy ever since World War II. Indeed, the existence of a strong and stable European partner seems to be a prerequisite for lasting and coherent Atlantic co-operation, based on a better equilibrium in possibilities and efforts than we have today. To work together effectively, Europe must be organized. We shall not always agree on everything, but our fundamental approaches to world problems are the same. We must set up, I think, appropriate mechanisms of permanent consultation to be able to work together in the most effective way.

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