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Dür: *Theorizing the Contagious Effects of Regionalism*

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**Theorizing the Contagious Effects of Regionalism:
European Integration and Transatlantic Trade Relations,
1957-1963**

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**Theorizing the Contagious Effects of Regionalism:
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Abstract

Regionalism leads to defensive reactions by excluded states. In this paper, I suggest a specific mechanism through which preferential trading arrangements (PTAs) have such external influences. When facing potential trade-diversionary losses from the creation of a PTA, exporters in excluded countries can overcome collective action problems and influence the trade policies of their governments. These governments have several options of how to react to exclusion: retaliation, setting-up of an alternative arrangement, negotiating nondiscriminatory reductions of the trade barriers restricting access to the PTA, or accession to the PTA. The choice of strategy depends on the issue-specific bargaining power of excluded countries. Member countries, however, only agree to alleviate the negative consequences for exporters in excluded countries if they receive substantial concessions in trade negotiations. I assess the resulting theory in an explanation of the United States' reaction to the creation of the European Economic Community (1957), and the ensuing transatlantic trade relations in the early 1960s.

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1. Introduction

In this paper, I argue that in many cases the trade policy chosen by a country is a reaction to the trade policies chosen by other countries. In particular, I show how preferential trading arrangements (PTAs) influence the foreign trade policies of excluded states, and, how, in turn, member states of the PTA react to the trade policies chosen by excluded states.¹ I undertake to outline a mechanism through which PTAs can have such external influences by developing a theory that stresses the mobilization of exporters, the choice of an appropriate response strategy by the governments of excluded countries, and higher expectations of concessions by PTA members.

A short examination of the history of trade policy gives initial support to the contention that the trade policies (free trade versus protectionism) and strategies (discriminatory versus non-discriminatory) chosen by different countries are interdependent. The founding of two customs unions in the North and the South of the German Confederation in the 1820s stimulated a series of negotiations that finally led to the creation of the *Zollverein* (1834), which, once established, itself had important external effects.² In the 1860s, the conclusion of the Cobden-Chevalier Treaty between Great Britain and France encouraged the

¹ The term “preferential trading arrangement” refers to all trade agreements that reduce barriers between two or more countries without including the most-favored-nation rule. This comprises partial and full free trade areas, customs unions, and single markets. In the following, I use the term PTA rather than “regionalism”, as the effects that I concentrate upon do not depend on whether a PTA is between geographically adjacent states or not. Nevertheless, the term regionalism could be used since most PTAs are regional.

negotiation of a whole set of further agreements.³ Imperial trade policies had external effects, as well. When Great Britain embraced preferential arrangements with its colonies in 1932, for example, this had major repercussions for excluded countries, and in the longer run motivated the creation of the General Agreement on Tariffs and Trade (GATT) in 1947. After the Second World War, the external effects of European integration stimulated several rounds of enlargement, and countries that were either not able or not eligible to accede to the EEC tried to find other ways to react to it. Most recently, one reason brought up in the United States (U.S.) Congress in favor of the passage of the Trade Act of 2002 was the necessity to negotiate bilateral agreements to recuperate the loss of market shares incurred because of the PTAs that other countries had concluded in the preceding years.⁴

Despite the importance of these phenomena, few explanations have been provided so far. For the most part, the literature on trade policy has neglected the influence of external factors upon a country's trade policies. In their explanations of trade policies, many authors focus on internal factors such as the economic characteristics of a country, namely the degree of factor specificity and comparative advantage, the nature of domestic political institutions, or the ideas

² For the creation of the *Zollverein*, see for example Mattli (1999), 115-21. For its consequences for excluded states, see Pahre (forthcoming), Chapter 11 ('The Spread of the Trade Treaty Network').

³ This argument is also made by Lazer (1999).

⁴ For example, Congressional Record (2002), 107th Congress, 2nd Session, S7836. See also Senator Chuck Grassley who mentioned the fact that over the last 10 years the US's "ability to penetrate foreign markets [had] eroded, as other nations [had] engaged in

and beliefs of domestic decision makers. Others stress the influence of security alliances or of the distribution of power in the international system.⁵ As Robert Pahre has pointed out, theories of trade-policy making often “assume that each state chooses its tariff in a political vacuum, unaffected by the choices of others.”⁶

The explanation provided in this paper is based on the basic insight that actors hurt by discriminatory trade policies will react to them.⁷ This basic idea is not new: Both Kenneth A. Oye and Richard Baldwin, for example, contend that by imposing costs on outsiders an initial step towards regional market opening can trigger further market openings.⁸ Walter Mattli maintains that outsiders will respond to regional integration when their economic growth lags behind the one experienced by members of the PTA.⁹ Finally, Robert Pahre argues that

preferential trade agreements to [the US’s] detriment” as main reason for his support of the Trade Act. Press Release, Lexis-Nexis.

⁵ A huge literature exists for each of these approaches; here, there is no space to appraise all these studies. For two recent review essays, see Milner (2002;1999).

⁶ Pahre (1998), 468.

⁷ Customs union theory shows that the creation of a PTA leads to changes in trade flows that can hurt exporters in excluded countries. See the seminal study by Viner (1950) and the recent review essay by Panagariya (2000). Due to dynamic gains, which can favor some exporters in excluded countries, the overall welfare effects for excluded countries can be positive.

⁸ Oye (1992) uses the cases of commerce and finance in the 1930s, the American Super 301 legislation, Canadian-American free trade, and the Single European Act (SEA, 1987) to elucidate his line of reasoning empirically. Baldwin (1993; 1995; 1997) provides a formalization of the argument and focuses on the effects of the SEA for the enlargement of the EU.

⁹ Mattli (1999) discusses the establishment and maintenance of the *Zollverein*, the EEC, and several integration schemes outside of Europe.

cooperation that discriminates against outsiders can spread, either by growing or by stimulating cooperation among third parties.¹⁰

These existing studies, however, have neglected at least three elements of the contagious effects of regionalism that seem to be essential for a comprehensive theory: First, thus far there exists no satisfying explanation of the domestic processes that drive the change of trade-policy preferences of an excluded country. The puzzle is that before facing commercial discrimination, excluded countries are not willing to liberalize, but once they feel the negative effects of a PTA, their trade preferences change. Second, an important question is which strategy an excluded government will choose in response to discrimination, i.e. whether it will retaliate or rather try to engage in negotiations with the members of a PTA. Finally, the reactions of member countries of a PTA to the demands of excluded countries for relief require theorizing.

I will first elaborate a theory addressing these three issues and then show how the resulting theory can be applied in an explanation of the case of transatlantic trade relations following the creation of the European Economic Community (EEC, 1957). In this empirical part, the argument is that the major change that occurred in post-World War II trade policies, namely the end of a period of stagnation in trade liberalization, which lasted from 1947 to 1960, was a

¹⁰ Pahre (forthcoming), Chapter 11 ('The Spread of the Trade Treaty Network'), studies nineteenth century trade treaties, and especially the external effects of the *Zollverein*.

consequence of the creation of the EEC and the defensive reaction of the U.S.¹¹ The case derives its importance from the fact that at that time the U.S. was a hegemonic power. Showing that such a power changed its trade policy due to the creation of a PTA abroad will make it plausible that many lesser powers have experienced similar influences. Based on primary and secondary sources, I will demonstrate how exporters in the US mobilized, how they influenced American trade policies, and how Europe reacted to the American initiative to reduce trade barriers.

Some alternative explanations of the puzzle at hand can be thought off: Parallel trade-policy decisions, for example, can be due to geopolitical considerations; once some powers have established preferential agreements, others might wish to balance this move by creating alternative agreements. The diffusion of ideas can have similar consequences; most obviously, the political or economic success of a PTA can motivate political actors in other countries to engage in discriminatory trade policies as well. Furthermore, several countries facing the same technological or economic challenges can react to them by choosing similar functional responses.¹² In the case study included in this paper, I will control for these alternative explanations.

¹¹ While – to my knowledge – there exists no empirical test of this claim, several authors have suggested such a linkage. See for example Preeg (1970), 29-30 and 220; Baldwin (1997), 866. World Bank (2000), 102, however, criticizes these accounts. Winters (1999), 37, especially points to the lack of a theoretically established link between the creation of the EEC and the Kennedy Round.

¹² Schirm (2002), for example, argues that the recent wave of regionalism has been caused by a convergence of state preferences attributable to the common exposition to the challenges posed by increasingly global markets.

2. A Theory of the External Political Effects of PTAs

As pointed out above, three issues are of central importance in establishing a theory of the external political effects of PTAs, namely the domestic processes in third countries, the choice of an adequate response strategy by third countries, and the reactions of member countries of a PTA to third-country initiatives. I will address each of these three issues in the following sections.

The Mobilization of Exporters in Excluded Countries

I argue that when lobbying against losses of foreign market access, exporters can overcome collective action problems more easily than when lobbying for gains of foreign market access. Consequently, they can better influence their government's decision-making.¹³ This explanation of the domestic processes determining excluded countries' reactions to discrimination differs substantially from existing ones. Oye, by concentrating on the influence of reciprocity on the empowerment of exporters, completely neglects the possibility that also in the absence of discrimination states can use reciprocal bargaining to reduce their tariffs.¹⁴ Baldwin assumes that exporters lobby against losses but not for gains because in a competitive industry additional gains would immediately be lost

¹³ The theory builds on a pluralist conception of trade-policy making, in which different domestic interests try to influence decision-makers. I assume that trade policies are determined by the relative strength of import-competing and exporting interests. This is consistent with a sector-specific (Ricardo-Viner) model of trade-policy preferences. An alternative approach (Stolper-Samuelson) sees a conflict between the abundant and the scarce factors of production. For a discussion of this point, see for example Brawley (1997). Other studies stressing the importance of exporter lobbying are for example Milner (1988); Gilligan (1997).

¹⁴ Oye (1992), 54-5. In his empirical analysis, Oye assumes unitary state actors and does not study interest-group behavior.

with the entrance of new competitors.¹⁵ This explanation, however, faces the problem that not only declining sectors lack competition. Successful industries can have high costs to entry and/or exit as well and thus principally favor voice over exit.¹⁶ Finally, Mattli contends that decision-makers value independence, and that therefore they resist demands for joining a PTA unless growth rates in the PTA exceed the growth rates of the excluded country.¹⁷ When arguing that an excluded country has to fulfill the same demand and supply conditions as the initially integrating countries to achieve regional integration, however, Mattli treats the demand for integration in an excluded country as completely independent from the fact that it is an *excluded* country.

In contrast, I argue that the puzzle of different degrees of exporter lobbying should better be addressed by looking at the collective-action problems that firms face in their decision to lobby or not. If discriminatory trade policies hurt exporters they have three possibilities to react to them: First, they can try to adapt, in general meaning mean that they can export a slightly different product that does not face the same level of trade diversion. Second, they can invest inside the borders of the PTA to avoid discrimination (capital diversion), but

¹⁵ Baldwin (1993). It is however not clear why this point should not also inhibit protectionist lobbying. Gains from rent seeking in one sector, which increase the returns to capital in this sector, can attract additional investments, until the returns to capital are equal to other sectors.

¹⁶ If entry costs are high, a firm will enjoy oligopolistic powers and thus prefer voice (i.e. lobbying) to exit. If exit costs are high, firms will have the same preference ranking. As the sectors characterized by economies of scale will show most trade diversion, this problem is aggravated even further.

some products cannot be produced abroad, and foreign countries can restrict foreign direct investments (FDI). Third, they can lobby the own government to engage in reciprocal trade negotiations to reduce the negative consequences of discrimination.¹⁸ The approach taken by a firm depends on the intensity of discrimination, the product it exports, and other factors such as its access to political decision makers.

In the case that a firm decides to lobby its government, it has to overcome collective-action problems. Collective-action theory shows that large groups pursuing a collective good will underprovide it due to free riding.¹⁹ Lobbying is a collective good because its benefits accrue to all members of the respective group, independent of whether they contributed to the provision of the good. Therefore, only small groups trying to get concentrated benefits will be able to lobby the government. One such concentrated group can be exporters, but when lobbying for gains of foreign market access, collective action problems can be prohibitive because trade agreements are incomplete contracts.²⁰ Exporters are not interested in the agreement itself, but in its economic effects, i.e. the effect on exports that it will have.

¹⁷ Mattli (1999). Mattli tests this argument for several rounds of enlargement of the EU and the *Zollverein* respectively, and finds support for his hypothesis (see the tables on pp. 82, 117).

¹⁸ The loss that an exporter faces can be a loss of market share, a loss in the value of exports, or a loss in profits.

¹⁹ For an overview of collective action theory, see the seminal work by Mancur Olson (1971).

²⁰ Ethier (2001), 220-21, stresses the fact that trade agreements are incomplete contracts for the signing governments. He mentions among others the requirements for dispute settlement and commensurate punishment arising from this problem.

These effects on exports, however, are difficult to predict for several reasons. First, the time lag between negotiations and implementation makes it difficult to foresee the overall economic situation at the time when the agreement is having practical consequences. Second, foreign governments can enact domestic industrial policies that undo the liberalizing effects of a trade agreement. Third, if trade agreements follow the MFN principle, liberalization gives exporters from several countries the same access to previously protected markets. These exporters will not be sure who among them can gain from the agreement. Fourth, in the case that an exporter does not yet have access to a foreign market, she also faces the problem of the absence of a distributional network. All these factors insert risk in the consequences of a trade agreement for exporters.²¹ A factor that measures the risk arising from imperfect foresight thus reduces the utility that exporters can derive from lobbying and makes collective action problems prohibitive.

While exporters when lobbying for gains of foreign market access face high risk, import-competing producers do not face the same risk in deciding whether or not to lobby, since reducing barriers to trade will hurt them with very high probability. This conclusion that import-competing and exporting interests face different risk levels when lobbying their respective governments depends on the presence of at least one of the following two conditions: First, if there is a large number of exporters of the same product (in one or several countries), and

²¹ Risk levels vary among different products: their values depend on factors such as the

all compete with each other, it will be difficult to predict the own benefits from a trade agreement. Second, if there is asymmetric information that favors import-competing interests only they will know to what extent reducing trade barriers will hurt them. In this case, however, costly lobbying by import-competing interests could be a signal that tells exporters abroad that a trade agreement would be beneficial for them.²² This assumption of different risk levels for exporters and import-competing producers is supported by Judith Goldstein and Lisa Martin: “Exporters only know that some market will open up, not whether they will be able to capitalize on this opportunity in the face of international competition. In contrast, protectionists know precisely what protection they will be losing as a result of liberalization, enhancing their incentives to mobilize relative to exporters.”²³

For exporters, however, the situation changes when they have to lobby in defense of their existing trade shares abroad. In this case, the effects of discrimination on exports are direct, thus reducing risk about the economic effects, and making mobilization far easier. Exporters that already supplied a share of the market in a specific country are sure that under the old competitive conditions they can keep this share or even increase it. In the new situation, however, they might lose a part of their market share to competitors producing

number of producers of the same or a similar good, and the price elasticity of demand.

²² In addition, assuming loss aversion rather than utility maximization would explain the different mobilization for losses or for gains. For loss aversion see for example Levy (1997).

²³ Goldstein/Martin (2000), 608.

inside the PTA. Due to reduced risk, they are now able to lobby and push their government to provide a solution that maintains their exports. The protectionists cannot increase their lobbying activity because they were already fully mobilized before the creation of the PTA. While opposition to trade liberalization was dominating in the situation without PTA, after creation of the PTA the balance of lobbying can shift and push the government of the excluded country to react to the discrimination. Raymond Vernon in his analysis of foreign direct investments writes in support of the argument that losers lobby more than beneficiaries: “Any threat to the established position of an enterprise is a powerful galvanizing force to action; in fact, if I interpret the empirical work correctly, threat in general is a more reliable stimulus to action than opportunity is likely to be.”²⁴

An Excluded Government’s Reactions to Discrimination

Following a pluralist model of trade-policy making, I assume that the balance of protectionist and free-trade interests is important in determining trade policies.²⁵ Consequently, if exporters mobilize and increase the pressure on their governments to seek a solution that maintains access to foreign markets, the government will feel compelled to react. The problem for all excluded governments is that discriminatory trading arrangements create externalities that

²⁴ Vernon (1966), 200.

²⁵ Rather than assuming that politicians maximize campaign contributions, it seems appropriate to assume that as the politicians’ time and resources are limited, they have to allocate time; lobbies can influence this allocation of time by providing information about salient issues.

belong to the kind that Oye defined as “divertable goods”.²⁶ Divertable externalities are distinct from other externalities because an actor can redirect them to other actors by pursuing a specific course of action. The special feature of negative divertable externalities is that they create a strong incentive for all actors to divert them immediately; the fewer actors that are left with the costs, the more concentrated they are, and the fewer other actors exist to which the externalities can be diverted. Pushed by domestic interests and recognizing that discriminatory trade policies create such divertable externalities, governments of excluded countries have various options to respond to a PTA, namely threatening retaliatory policies, setting-up an alternative one, negotiating nondiscriminatory access, and joining the agreement.²⁷ Non-discriminatory and discriminatory trade policies are therefore alternative strategies, and the choice between them depends on which one maximizes utility in a specific situation.

²⁶ See Oye (1992). The term “externalities” denotes the differences between private and social costs and benefits.

²⁷ Negotiating nondiscriminatory access can take the form of a bilateral commercial treaty including the MFN clause or of multilateral trade negotiations. Joining the agreement does not only include the option of accession, but the signing of a preferential trade agreement with the members of a PTA. Some studies have suggested that there are several possible modes to react to discrimination. An article in the *New York Times*, November 4, 1962, 24, points out that outside countries reacted in six different ways to the creation of the EEC: membership application (Great Britain), application for associate membership (Greece), trade negotiations on a limited list of items (Israel), larger tariff-cutting bargain (USA), condemnation (Communist countries), and occasional protest (Latin America). Baldwin (1993) mentions accession, multilateral liberalization, and the setting-up of an alternative PTA. A World Trade Organization (1995), 51-54, publication refers to accession, alternative agreement, and multilateral liberalization as possible courses of action. Mattli (1999) distinguishes “two integration strategies”, accession, or setting-up of an alternative agreement. Yarbrough/Yarbrough (1992) study different trade-policy strategies, such as bilateralism, minilateralism, or multilateralism. They, however, provide a completely different explanation not based on the external effects of PTAs, but on relation-specific investments.

I suggest that the appropriate response depends on the issue-specific bargaining power of the excluded state relative to the PTA. The four possible reactions to discrimination can be ordered from least costly for domestic interests to most costly, i.e. from retaliation over setting-up of an alternative agreement, MFN negotiations, to accession. Retaliation is the most desirable strategy, as it minimizes the costs imposed on domestic interests. In addition, the retaliatory strategy has the advantage that it can be picked unilaterally, while all other strategies depend either on the willingness of the member governments of a PTA to accommodate foreign exporters, or on the availability of other countries to create a preferential trading agreement. The drawback of the retaliatory strategy is that, if unsuccessful, the conflict can escalate into a trade war.

The setting-up of an alternative agreement is the second-best strategy, because it provides exporters with preferential access to alternative markets, without imposing particularly high costs on import-competing groups. Furthermore, it can increase the bargaining power of states participating in such an alternative PTA. Negotiating nondiscriminatory access is less desirable because it entails higher costs and smaller potential gains. Joining is the most costly action because it normally requires the payment of a particular entrance price. Since most PTAs include regional clauses, some excluded countries will try to establish a preferential link with the PTA, stopping short from joining the

agreement.²⁸ Establishing such a preferential agreement with a PTA, however, is not necessarily a less costly alternative, as the excluded country runs the risk of ending up in a hub and spoke relationship with the PTA.

An excluded government chooses the best obtainable strategy, dependent on its relative issue-specific bargaining power. Power, however, is an elusive notion, which is difficult to conceptualize. It therefore seems useful to distinguish two types of power, overall power and issue-specific power, both of which are relative measures, i.e. they measure power relative to the power of other actors. Overall power can derive from structural factors such as differences in size, military power, and wealth among countries. In trade negotiations, however, states usually cannot employ these overall power capabilities easily and thus their trade-specific bargaining power, which is determined by the best alternative to negotiated agreement (BATNA), gains in importance.²⁹

The BATNA in trade negotiations is the *status quo*, a unilateral increase of protection, or an agreement with a third country. For a country that seeks the reduction of specific foreign trade barriers to avoid trade diversion, however, all of these are bad alternatives, thus reducing its bargaining power. As long as a country does not need an international agreement, i.e. if the pressure from

²⁸ The *Zollverein*, for example, was restricted to German states and the Ottawa Agreements to the British Commonwealth, while the EU and the EFTA are limited to European countries.

²⁹ Baldwin (2002), 180/181, first draws attention to the “fungibility problem” (i.e. of how easily power resources from one issue-area can be used in another issue-area, and then argues that conceptualizing power “within specific scopes and domains” (i.e. for one specific issue and in relation with one specific actor) is preferable to trying to establish the

exporting interests on a government is low, it disposes over large trade-specific bargaining power. In trade negotiations, the BATNA is consequently defined by the balance of interests in the negotiating countries relative to each other, i.e. the political importance of exporting and import-competing groups inside a country.

Three economic and two political factors are important in determining the balance of domestic interests, and thus the issue-specific bargaining power. The economic factors are the regional concentration of a country's exports, the amount of imports relative to exports, and the amount of foreign trade relative to the country's economic size.³⁰ First, a regional concentration of exports increases bargaining power with countries outside of this region by making a regional option available, but reduces the bargaining power with the countries in this region by increasing dependence on their markets. Second, a large importer has more bargaining power since it can threaten to limit access to its market without fearing retaliation.³¹ Third, the amount of foreign trade relative to economic size is a factor because a country that is trade dependent will be under stronger pressure to find a compromise than a predominantly self-sufficient country.

Besides these three economic factors, two political ones affect the balance of interests inside a country. First, domestic institutions influence the importance of exporting vis-à-vis import-competing groups by providing access or by helping in the aggregation of some interests. Second, as shown above, sometimes

overall power of an actor. The conceptualization of power as determined by the BATNA is similar to Putnam (1988), 442, or Moravcsik (1998), 62.

³⁰ The position of a country as supplier of important goods can also be a source of power.

the two groups may not be equally mobilized. If protectionist interests are more mobilized than free trade interests, a country's bargaining power is higher than if exporters are mobilized. Once discrimination mobilizes exporters in excluded countries, consequently, these countries lose bargaining power. The creation of a PTA thus reduces an excluded country's trade-specific bargaining power, with the size of the reduction depending on the degree of trade diversion.

Three distributions of power can characterize the relationship between the members of a PTA and excluded countries. The issue-specific bargaining power can either be biased in favor of one side or be approximately equal. If the excluded country has far more issue-specific power than the member countries, it will choose retaliation. Accession is the strategy chosen when the balance of power is heavily biased in the other direction. When the two sides have more or less the same bargaining power, an excluded country chooses one of the intermediate options.

Some historical examples elucidate this linkage between choice of strategy and bargaining power. Retaliation is a possible action if the relative issue-specific power of the excluded country is overwhelming. In the late 1850s, Prussia as representative of the *Zollverein* protested against the Austrian customs union with Modena, which contributed to its lapse in 1859. In 1904, Bulgaria and Serbia agreed to introduce free trade between the two countries and to adopt similar customs practices. When the Austro-Hungarian Empire complained that this

³¹ Benham (1941), 120-23, discusses this question.

would violate its MFN treaty with Serbia, the latter country yielded, and a simple commercial treaty substituted the PTA. In 1932, Great Britain opposed the formation of a PTA between the Benelux countries, and its position was so powerful that it brought the project to fall. Threats of retaliation, however, are not credible if the issue-specific power of a country is not high enough. In the late nineteenth century, the German Empire threatened to retaliate against the Commonwealth countries when they started to introduce Empire preferences, but could not make its threat credible due to its dependence on access to the British market.

Setting-up of an alternative agreement is the ideal strategy if the issue-specific power of an excluded country is not high enough to threaten retaliation. Latin American countries in the 1960s legitimized their decision to pursue preferential trade agreements with their competitive disadvantage in the European market caused by trade diversion. In reaction to the creation of the EEC, also Great Britain first chose to set up the European Free Trade Association (EFTA) as an alternative agreement. In the end, however, this strategy did not prove satisfactory and the government became willing to pay the price linked with accession. In the 1980s and 1990s, also the U.S. government used alternative agreements as response to discrimination.

A country with slightly lower issue-specific power will try the nondiscriminatory path. Great Britain in the nineteenth century fits into this category, when its issue-specific power therefore was limited due to its

dependence on markets for its exports. The U.S. used this strategy as well to respond to discrimination in the twentieth century, because it had very spread-out trading interests. Especially in the first half of the century, the US was in a particular situation in which it had huge trade balance surpluses with some countries, but deficits with a few suppliers of resources.³² Accession is costly for entering countries, because members will demand compliance with all existing regulations. As can be seen in the recent negotiations for enlarging the EU, entering countries have to accept a high price for entrance.³³ Only a country with low issue-specific power will accept to pay this price.

The Response by Member Countries of a PTA

With regard to member countries, the question is under which circumstances they would agree to reduce discrimination against excluded countries in trade negotiations. This is a particularly interesting question as in many cases the liberalization of trade among members of a PTA imposes costs on import-competing industries, thus making them more likely to advocate protectionist policies and to oppose trade negotiations with outsiders. In the existing literature, however, it has received little attention.³⁴ I argue that discriminatory trade

³² In the 1950s, it chose the nondiscriminatory path because it did not find it very costly to pursue an MFN policy in its negotiations with Europe while external competition was low. This competitive advantage however did not hinder the predominance of protectionist interests in the 1950s.

³³ In the case of the EU, entering countries have to accept the *acquis communautaire*.

³⁴ Milner/Mansfield (1999), 604, maintain that “we know little about whether, once in place, regional arrangements foster domestic support for broader, multilateral trade liberalization or whether they undermine such support.” Mattli (1999), 63, suggests that under certain circumstances the members of a PTA might not be willing to accept new members, though

policies shift the *status quo* of excluded countries away from their ideal point, thus increasing the win-set of negotiations.³⁵ This is a result of the necessity felt by third states to achieve a deal that reduces discrimination hurting its exporting industries: Member governments in contrast are satisfied with the *status quo*. Having an ideal point close to the *status quo* means having a good alternative to negotiated agreement and thus being able to extract substantial concessions in negotiations.

Therefore, in negotiations with outside countries, member countries can expect concessions that they could not have got before creating the PTA.³⁶ In this context, providing concessions signifies giving better market access to the exports of a foreign country.³⁷ Such expected asymmetric concessions ensure that the political gains derived from better access to foreign markets for exporters prevail over the costs imposed upon import-competing groups. In many cases there appears to be evidence that domestic actors pushing for a PTA understood this effect on their bargaining power in subsequent trade negotiations with

without providing theoretical reasoning to back up his statement. Bhagwati/Panagariya (1996), 50, criticize Baldwin's (1995) formal model for neglecting this issue.

³⁵ Mansfield/Reinhardt (forthcoming), 8-10, argue that PTAs increase the leverage of members by providing an insurance mechanism if multilateral attempts fail, by pooling resources, and by accumulating the market power of individual members. The argument made in this paper is distinct in that it stresses the increased leverage stemming from the fact that the PTA's negative externalities move the *status quo* of excluded countries away from their ideal point.

³⁶ While trade negotiations generally follow the principle of reciprocity, I contend that bargaining power is important in defining what the parties to an agreement define as reciprocal concessions. See Hody (1996), 146. For the importance of reciprocity, see for example Rhodes (1993).

³⁷ In some instances, especially if the trade concessions an excluded state can provide are not of great use for the member countries, issue-linkages might be used to get concessions in other fields.

excluded countries. I argue that exactly this awareness of increased bargaining strength makes member governments agree to enter into negotiations.

The trade relations of the German Empire with Russia in the late nineteenth century provide an interesting example for the contention that discrimination shifts bargaining power. As Germany had to cope with higher tariffs than France in exporting to Russia, it first engaged in a tariff war with Russia, but finally decided to find an agreement. In the negotiations, “Germany was the more inclined to make terms, because [...] Russia had made a commercial treaty with France (June 27, 1893) conceding most-favored-nation treatment and the reduction of some duties, which caused concern to the industrial interests in Germany.”³⁸ The increase in bargaining power depends on the degree of discrimination a PTA is imposing on excluded countries. PTAs with very low external tariffs or among countries with low levels of imports will not lead to a large shift in relative bargaining power.

A final question that is important to discuss in this context is whether PTAs increase the power of the individual members states, or only of all the members together as a group. The immediate answer is that a PTA enhances the power of the group, but not of the individual members, as the latter have an incentive to engage in concession diversion, thus reducing trade diversion for excluded countries. In practice, however, most PTAs include clauses that regulate negotiations with third countries. This is obvious for customs unions, which

³⁸ United States Tariff Commission (1919), 476.

follow a common commercial policy. Members of other PTAs, however, aware of the importance of preferential access to the partner countries' markets for the benefits derived from a PTA, have also often voluntarily agreed to restrict negotiations with third countries as some examples can illustrate.

The Middle German customs union, which was set up in 1828, included a provision that restricted the conclusion of commercial treaties with countries “where a customs system was in existence”. The intention of this clause was to increase the bargaining power of the member countries vis-à-vis the North and South German customs unions. In the end, however, the pressure on the member countries was so strong that some ended up defecting on this provision. Consequently, the group was not able to bargain collectively with Prussia or Bavaria.³⁹ In 1931, the proposal for an Austro-German customs union included a provision that proscribed independent commercial negotiations of one party with third countries.⁴⁰ The Ottawa Agreements stipulated that some preference margins had to be maintained for several years and thus limited the possibility of individual signatories to engage in negotiations with third countries. In 1958, the EEC presented the “Rapport Ockrent” to excluded European countries, which had demanded the creation of a free trade area. One of the demands in this plan was that the members of the free trade area should be compelled to cooperate on their external trade policies, as – in the French point of view – the advantages of the free trade area depended not only on free but also on preferential access to

³⁹ Price (1973), 227-29.

neighboring markets. If one country decided to establish free trade with third countries, the other members of the free trade area would no longer enjoy an advantage in this market.⁴¹ The most recent preferential agreements are exceptions to this rule that PTAs include rules on negotiations with third countries, which also is a reason for why there has been such a proliferation of agreements.

3. A Case Study: The Creation of the EEC and Transatlantic Trade Relations, 1957-1963

When in 1957 six European countries agreed to create the EEC, they not only set out the rules for abolishing internal tariffs, establishing a common external tariff, and a Common Commercial Policy, but also embarked on the creation of a Common Agricultural Policy (CAP), and the association of some former colonies. Initially, it was not clear whether the EEC would be trade diverting or rather trade creating, but fears about the economic effects of the EEC were very widespread among excluded countries.⁴² Already in 1957, some excluded governments voiced their objections to the discriminatory features of the plans for European integration. In Europe, the concerns encouraged talks concerning the establishment of a free trade agreement comprising several excluded countries. In the U.S., the discrimination facing American exporters became a

⁴⁰ Viner (1950), 11.

⁴¹ Frank (1961), 221.

⁴² Humphrey (1962), xiii; Patterson (1966); Hieronymi (1973). There is a large literature written around this time on the possible trade diversionary effects of the Common Market. See for example Kravis (1962); Lawrence (1962); Piquet (1964); Balassa (1967). Overall, it is quite likely that the creation of the EEC led to more trade creation than trade

major issue from 1958 onwards, and intensified when the first preferential tariff reductions were carried out.

I argue that these fears caused by the creation of the EEC stimulated the trade negotiations within the GATT in the 1960s, which moved the GATT from deadlock to trade liberalization. While in the late 1940s and 1950s several negotiations were unsuccessful in liberalizing trade, both the Dillon Round (1960-62) and the Kennedy Round (1964-67) led to a major liberalization of transatlantic trade relations. In the following, I will first assess whether the fears about the creation of the EEC set off a mobilization of exporters in the U.S. Second, I will analyze the debate within the U.S. with regard to an adequate response to the challenge posed by the creation of the EEC. Finally, I will deal with the question of the determinants of the European reaction to the American offer to engage in multilateral trade negotiations.

The Mobilization of Exporters in the U.S.

As soon as information about the plans for the creation of the EEC spread in the U.S., exporters started to express their concerns. Already in 1957, an article in the *Wall Street Journal* mentioned that there was fear of the common market among U.S. executives. This article also suggested a connection between these fears and increasing support for more liberal trade policies: “Groups backing more liberal trade see some favorable omens on their side. They believe the European

diversion. Nevertheless, the argument is valid as long as at least some excluded industries felt threatened by trade diversion.

Common Market and other developments have made businessmen feel the need of a liberal foreign trade policy.”⁴³

In the hearings for the 1958 renewal of the Reciprocal Trade Agreements Act (RTAA), the common market was a major topic. The Chamber of Commerce of the U.S. declared: “The threat of being shut out of traditional European markets by high tariffs is of acute concern to United States businessmen. The gradual elimination of trade barriers among the six common-market countries, coupled with the maintenance of a common tariff against the outside world, will place American exporters to the area at an increasing disadvantage vis-a-vis their competitors within these countries.”⁴⁴ The representative of the Caterpillar Tractor Co. added that the administration should try “to preserve for American industry a worthwhile place in the great new integrated market which will arise in Europe.”⁴⁵ Even more concerned than manufacturers were agricultural interests. The American Cotton Shippers Association, for example, argued that because of the common market, American cotton exporters could “be seriously hurt in cotton’s most important and most promising export market.”⁴⁶ Not surprisingly, the increasing concerns led to special hearings on the threat posed by the Common Market before the Senate Committee of Interstate and Foreign Commerce in 1960.⁴⁷

⁴³ *Wall Street Journal*, July 30, 1957, 1:1 and 12.

⁴⁴ United States. Congress. House of Representatives (1958), 639.

⁴⁵ *Ibid.*, 255.

⁴⁶ *Ibid.*, 434.

⁴⁷ United States. Congress. Senate (1960).

The Dillon Round reduced some tariffs, but the feeling was that discrimination required a further initiative to reduce the EEC's external trade barriers. Therefore, the U.S. Administration proposed the Trade Expansion Act (TEA), which gave the President more sweeping power to engage in trade negotiations. Substantial exporter lobbying accompanied this decision by the administration. The Committee for a National Trade Policy (CNTTP), including about 2000 capital-intensive members, was the major exporter lobby. Among its activities in favor of the TEA was a conference on trade policy with the President as main speaker. It also set up a Coordinating Council of Organizations on International Trade Policy with the former Secretaries of State Christian A. Herter and Dean Acheson as honorary members. The United States Council of the International Chamber of Commerce, which included members such as the Ford Motor Company, Pepsi Cola, several banks, tobacco companies, the Motion Picture Association of America, Standard Oil, and Gillette, stated:

We are confronted today with the swift fusion of other countries into major trading blocs. The six-country European Economic Community and the seven-nation European Free Trade Area are already in existence. The Sino-Soviet trading bloc is an accomplished reality. A customs union of four Central American countries is launched, and a Latin American Free Trade Association is beyond the talking stage. Similar projects are under consideration in southern Asia, North Africa, West Africa, and the Middle East. All of these arrangements have some bearing on our commercial policy.⁴⁸

The National Foreign Trade Council (NFTC) stated in the final declaration of its annual convention in 1961: "The grant of additional bargaining authority is particularly essential if American exporters are to hold their own in the European

⁴⁸ U.S. Council of the International Chamber of Commerce (1961), 2.

Common Market and other common markets and free trade areas.”⁴⁹ The U.S. Chamber of Commerce backed the TEA and issued a resolution in favor of the bill, but there were dissenting voices that mainly criticized the relief aid for workers included in the TEA.⁵⁰ Henry Ford, the chairman of the Ford Motor Company, stated that the “Administration must have from the Congress a mandate to go out to minimize Europe’s external trade barriers and must be empowered to bargain effectively.”⁵¹ The American Paper & Pulp Association was worried about the prospect of an eventually enlarged EEC including its foremost competitors from Scandinavia. Support came also from the aerospace, the machine-tool, and the electronics and electrical industries.⁵² Besides these exporters, the major labor unions supported the bill.

Business Week reported that a nationwide survey of industry executives had found “considerable business support for free trade with Europe and a widespread recognition that we need some kind of change in tariff policy if only to maintain our bargaining position.”⁵³ From the 150 executives interviewed, 25 per cent strongly favored freer trade with Europe and an equal percentage opposed it. The support came from auto manufacturers, business machine makers, machinery and appliance manufacturers, electronics firms, and

⁴⁹ Final Declaration of the Forty-Eighth National Foreign Trade Convention (New York), October 30 – November 1, 1961, p9. National Archives at College Park (hereafter cited as: NACP), State Department Records, Central Files, Record Group 59, Decimal File, 1960-63, File 411.0041.

⁵⁰ *New York Times*, May 3, 1962, 1, and *New York Times*, May 4, 1962, 32. See also *Wall Street Journal*, February 27, 1962, 9:2.

⁵¹ *New York Times*, January 18, 1962, 12.

⁵² See United States. Congress. Senate (1962); Barrie (1987), 200-13.

international oil companies. The chemical, the copper and brass, rubber, glass, cement, watch, and pottery industries voiced opposition. A poll of executives conducted by the Research Institute of America and published in June 1962 found that 57 per cent of the respondents were in favor of the TEA, and only 25.7 per cent were opposed to it.⁵⁴

Strong support for the TEA came also from the agricultural sector. Already in 1960, the U.S. Feed Grains Council expressed great urgency for action to maintain market access in Europe.⁵⁵ Among others, the American Farm Bureau Federation, the National Farmers' Union, the U.S. National Fruit Export Council, and the Florida Citrus Commission supported the TEA. All of them complained about the trade diversionary consequences of the CAP. Citrus interests were particularly worried about the prospect that various Mediterranean countries could be associated with the EEC. Even the traditionally rather protectionist National Grange took a liberal position and stated concern about the EEC's agricultural policy. In the hearings on the TEA, its representative affirmed that the National Grange was "gravely concerned over the proposals of the European Common Market countries to increase their import control measures against U.S. agricultural commodities."⁵⁶

⁵³ *Business Week*, December 9, 1961, 25-26.

⁵⁴ *New York Times*, June 27, 1962, 11.

⁵⁵ U.S. Feed Grains Council, Letter to Christian Herter SoS, November 15, 1960. NACP, State Department Records, Central Files, Record Group 59, Decimal File, 1960-63, File 411.0041.

⁵⁶ United States. Congress. House of Representatives (1962), 2656.

Agricultural interests backed the TEA because they hoped that the U.S. government would trade access for American agricultural goods to European markets with European access to American industrial markets. While they were concerned about the immediate impact of the CAP, they were also aware of the huge market with which the EEC could provide them in the case of a reduction of trade barriers. This appears to have increased their tendency to lobby the U.S. administration to improve access to the EEC. Some agricultural interests, however, were more skeptical about the prospects of negotiating with the EEC. The U.S. National Fruit Export Council (and to some extent also other agricultural interests), for example, demanded that the President should threaten with retaliation in the case that the EEC did not open its market voluntarily: “The legislation should provide that whenever the EEC or any other foreign country takes action to nullify or impair concessions granted on these products, equivalent withdrawals will be made by the United States.”⁵⁷

The chicken war, from January 1962 onwards, contributed to the burgeoning of these concerns in the American agricultural sector. The chicken war evolved because a variable levy on poultry imports that came into effect in July 1962 as part of the EEC’s agricultural policy led to a decline of U.S. poultry exports especially to the German market.⁵⁸ As the EEC was not willing to compensate the U.S. for this decline, the conflict escalated and could only be

⁵⁷ Ibid., 3160.

resolved after the ruling of a GATT panel. In this context, both the National Farmers' Union and the Institute of American Poultry Industries were active in making American politicians aware of what they conceived of as a big problem. Many in the agricultural industry shared this concern; not all of them were as radical as the manager of the export division of a food producer was who characterized the EEC as "uncommon common market" and "Frankenstein monster".⁵⁹

The major protectionist groups were the Trade Relations Council and the Nation-Wide Committee for Import-Export Policy.⁶⁰ The latter mainly represented woolens, bicycles, glassware, and some agricultural groups.⁶¹ Despite large exports to the EEC and despite the danger that trade diversion would hurt chemical exports, the U.S. chemical industry was largely opposed to the TEA.⁶² The major trade organizations in this sector were the Synthetic Organic Chemical Manufactures Association (SOCMA) and the Manufacturing Chemists Association (MCA).⁶³ On the firm level, among the declared opponents to the TEA were exporters like Dow Chemical, Du Pont, and Monsanto. One factor

⁵⁸ A variable levy is a duty that differs according to the import price with the purpose of keeping the domestic price constant. For the chicken war see for example: Talbot (1978); Zeiler (1992), 135-9.

⁵⁹ United States. Congress. Senate (1963), 14. See also Talbot (1978), 78.

⁶⁰ For their activities, see for example *New York Times*, January 18, 1962, 1 and 12.

⁶¹ Barrie (1987), 180.

⁶² See for example *New York Times*, February 26, 1962, 38; Preeg (1970), 52. The fact that the chemical industry was protectionist is troubling not only for my explanation but also for the major contenders. Intra-industry trade characterized the industry. As some authors contend, intra-industry trade should facilitate free-trade preferences. In addition, the firms dominating the sector were multinationals, but still protectionist, what also goes counter to Helen Milner's hypothesis that multinational companies support free trade. Milner (1988).

explaining this opposition of the chemical industry to the aims of the TEA is the high number of foreign subsidiaries that characterized the U.S. chemical industry. From 1958 to October 1959, 30 different U.S. chemical companies set up new plants in Europe.⁶⁴ By producing inside the EEC, the U.S. chemical industry had no longer an interest in negotiating lower trade barriers. Both SOCMA and MCA strongly opposed the repeal of the American Selling Price (ASP), a method of evaluating some chemical tariffs based on the price of the good in the U.S. market rather than the import price.⁶⁵ Only in the textile sector was there equally strong opposition to the Kennedy Round as in the chemical sector.

A systematic analysis of the testimony for the TEA in the Hearings of the Ways and Means Committee of the House of Representatives shows that in 1958, 35, and, in 1962, 30 exporters appeared as witnesses.⁶⁶ This was markedly more than the 15 exporters that testified in 1955, or the 14 that testified in 1953.⁶⁷ Among the 30 exporters lobbying in 1962, 18 mentioned the threat of exclusion from the Common Market as the main reason for the need of new trade legislation. Counting all private sector witnesses, among 37 representatives of

⁶³ Curtis/Vastine (1971), 100 and 122. See also Zeiler (1992), 150, Endnote 53.

⁶⁴ Economic Research Department (October 1, 1959): "A List of Companies with New Operations in Western Europe During 1958-1959 (Since the Start of the European Common Market)." Reprinted in United States. Congress. Senate (1960), 235-59.

⁶⁵ The ASP was also applied to some non-chemical tariffs.

⁶⁶ United States. Congress. House of Representatives (1958). United States. Congress. House of Representatives (1962).

⁶⁷ United States. Congress. House of Representatives (1955). United States. Congress. House of Representatives (1953). These numbers would have been even lower if there had not been a campaign controlled by the government of Venezuela, which asked American exporters of goods to Venezuela to testify against the imposition of oil quotas against Venezuelan oil.

specific companies that appeared before the Committee, 22 supported the legislation while 14 opposed it (one could not be classified). Even more unambiguous was the support among broad trade associations comprising several sectors, where, from 33 witnesses, only one opposed the legislation and 22 supported it (the rest either dealt with the question of adjustment assistance in the bill or could not be classified for other reasons). At the same time, however, of 83 sectoral coalitions, only 12 supported the bill. Finally, in the agricultural sector, support was dominant, but with some exceptions from the cattle and dairy sectors, which feared competition from Canadian farmers. Overall, roughly 45 per cent of the 182 witnesses whose position on the bill could be established supported it. In the Senate, the ratios were very similar, with a slightly stronger showing of protectionist interests.⁶⁸

While not conclusive, this evidence on interest group lobbying in the U.S. at least broadly supports the contention that in the wake of the creation of the EEC, exporters in the U.S. mobilized to lobby their government, aiming at a reduction of the potential trade losses caused by this step. In the following section, I will show how this lobbying effort influenced the reaction by the U.S. government.

The Reaction of the U.S. Government

In the late 1950s, although some U.S. exporters already voiced concerns about the implications of the EEC, the U.S. government, in accordance with its foreign

⁶⁸ United States. Congress. Senate (1962).

policy since the late 1940s, expressed its continued support for European integration. Nevertheless, to alleviate the consequences for American exporters, the American government requested from Congress the authority to cut American tariffs by 20 per cent in reciprocal trade agreements as central element of the Trade Agreements Extension Act (TAEA) of 1958. In support of the passage of this act, the American Under-Secretary of State, C. Douglas Dillon, argued that the existence of a common market in Europe required an adequate American response:

Whatever the level of the Common Market tariff is to be, its general nature will be settled within the next 4 to 5 years. Any reductions which the United States and other countries may seek, even on a reciprocal basis, will be much harder to obtain if the Common Market area has already become accustomed to the operation of a higher tariff. The best chance we will have to achieve the reductions that are important to our export trade will be to negotiate them before the new tariff has become solidly established.⁶⁹

Once passed, the TAEA became the basis for the negotiations with the EEC in the Dillon Round.⁷⁰ In this round, the U.S. tried to achieve unilateral concessions from the EEC; the latter, however, largely refused to make such unilateral concessions and instead proposed a linear reciprocal 20 percent cut of industrial tariffs. Inhibited by the lack of appropriate negotiating authority, the U.S. negotiators could not reciprocate. They were more interested in getting concessions on agriculture, but the EEC negotiators argued that as long as they had not agreed on a common agricultural policy internally, they could not negotiate on it externally.

⁶⁹ Dillon in United States. Congress. House of Representatives (1958), 2647.

⁷⁰ For the Dillon Round see Curzon/Curzon (1976), 168-75; Eckes (1995), 180-3.

When the Dillon Round failed to alleviate fears in the U.S., especially of agricultural interests, the U.S. administration soon contemplated the start of a new, more far-reaching round. Knowing that the TAEA of 1958 would expire in 1962, the administration began to think about new trade legislation in 1961.⁷¹ There were demands from various sides for a new approach including linear tariff cuts, which was a major break from the product-by-product negotiations used in earlier rounds.⁷² In requesting trade legislation for such a round, the threat posed by the EEC to American export interests was the major topic. In October 1961, Representative Hale Boggs told the press that new legislation was required to deal with the challenge emanating from economic integration in Europe. In a report solicited by the Joint Economic Committee of the Congress and submitted in November 1961, Christian A. Herter, prior secretary of state, and William L. Clayton, former undersecretary of state, suggested a liberal U.S. trade policy and even a formal link to the EEC, through a “trade partnership” of the U.S. with the EEC.⁷³

Within the administration, two proposals were made concerning new trade legislation: First, a proposal by the Special Assistant to the President for Trade Policy, Howard Petersen, suggested an authority to cut tariffs by 50 percent. Petersen stressed the importance of the EEC for U.S. trade policy, as “goods from

⁷¹ For these developments see for example Diebold (1999); Hawkins/Norwood (1963), 114-23; Kaplan (1996); Ilgen (1976), 174-79; Pastor (1980); Winand (1993), 173-90.

⁷² Frank (1961), 197.

⁷³ See for example Ilgen (1976), 175-76.

outside the Community will face a growing measure of discrimination.”⁷⁴ Petersen suggested that possibly the President would need more authority to reduce discrimination, but deemed a more sweeping request politically infeasible. Second, a report written under the guidance of the undersecretary of state for economic affairs, George Ball, suggested replacing the existing RTAA legislation with radically new trade legislation. This legislation should include entirely new powers for the President, but the President should allow for sufficient preparation by asking Congress for it only in 1963. Ball considered such a new approach vital because the creation of the EEC would “unlock new political pressures from various directions—from U.S. exporters, from Latin American countries, from the British Commonwealth, and from the European Economic Community itself.”⁷⁵ He continued: “If the differential between external and internal tariffs [of the EEC] is to be substantially lowered (and we must reduce this differential if we are to avoid having our exports placed at a major disadvantage) the common external tariff of the EEC must also be reduced on an across-the-board basis.”⁷⁶ By late October 1961, President Kennedy was still undecided between the two proposals.

⁷⁴ Letter by Howard C. Petersen to George W. Ball, October 4, 1961, enclosed: “Proposals for 1962 United States Foreign Trade and Tariff Legislation”, 3 (classified). NACP, State Department Records, Central Files, Record Group 59, Decimal File, 1960-63, File 411.0041.

⁷⁵ Memorandum for the President by Dean Rusk, October 24, 1961, attached are two memoranda prepared by Ball (confidential). NACP, State Department Records, Central Files, Record Group 59, Decimal File, 1960-63, File 411.0041. The quote is from the first memorandum, dated October 23, 1961.

⁷⁶ Ibid. The quote is from the second memorandum, dated October 23, 1961, 3.

On November 1, 1961, George Ball, in a speech before the National Foreign Trade Council, publicly outlined his proposal. As the reaction to this test was largely positive, Kennedy began to support the Ball approach.⁷⁷ From this date onwards, President Kennedy clearly stated his demand for a substantial new authority: “I think that, quite obviously, we have to realize how important the Common Market is going to be to the economy of the United States. One third of our trade generally is in Western Europe and if the United States should be denied that market we will either find a flight of capital from this country to construct factories within that wall, or we will find ourselves in serious economic trouble.”⁷⁸ Because of the urgency of the matter, Kennedy decided to ask Congress to pass the new trade legislation already in 1962. Speeches before the Committee for a National Trade Policy (November 20, 1961), the National Association of Manufacturers (December 6, 1961), and the labor union (December 7) gave Kennedy strong impressions of support for the new trade legislation.⁷⁹

On January 11, 1962, Kennedy, in an address to Congress, characterized the development of the EEC as “the greatest challenge of all.”⁸⁰ Two weeks later, he sent the bill requesting trade authority to Congress. In the message introducing the TEA to Congress, the President again alluded to the EEC:

⁷⁷ Taber (1969), 64-5.

⁷⁸ Quoted in the *New York Times*, November 9, 1961, 14.

⁷⁹ Preeg (1970), 46. The speeches to the National Association of Manufacturers and the labor union are reprinted in *Department of State Bulletin*, December 25, 1961, 1039-1052.

⁸⁰ *Department of State Bulletin*, January 29, 1962, 159-163.

But as the new external tariff surrounding the Common Market replaces the internal tariff structure, a German producer—who once competed in the markets of France on the same terms with our own producers—will achieve free access to French markets while our own producers face a tariff. In short, in the absence of authority to bargain down that external tariff, as the economy of the Common Market expands, our exports will not expand with it. They may even decline.⁸¹

In addition, Kennedy stressed the dangers arising for the American economy from the investment diversion that could be a consequence of the exclusion of American companies from the common market. He stated: “Unless our industry can maintain and increase its share of this attractive market, there will be further temptation to locate additional American-financed plants in Europe in order to get behind the external tariff wall of the EEC.”⁸²

In the TEA, the President requested authority to make 50 per cent linear cuts of the rates existing on July 1, 1962. A special rule allowed the complete abolishment of duties for industrial goods for which the U.S. and the EEC together accounted for at least 80 per cent of world exports. If the United Kingdom had joined the EEC, this provision would have covered 50 per cent of U.S.-EEC trade.⁸³ The list of products covered by this provision included aircraft, automobiles, machinery, and most chemical products, the industrial products for which most trade diversion was expected.⁸⁴ Of equal importance, the trade bill as

⁸¹ See reprint of the speech in Preeg (1970), Appendix B, 282-90, here: 287.

⁸² Ibid., 284.

⁸³ Curzon/Curzon (1976), 179. In these 80 per cent of world trade intra-EEC trade, and trade between Communist countries were not included. See also Diebold (1999), 241.

⁸⁴ Hawkins/Norwood (1963), 116-7.

proposed by Kennedy severely changed the peril point provision.⁸⁵ Peril points were no longer limits to reductions as in earlier trade legislation, but only suggestions to the President outlining the probable consequences of a reduction of a specific tariff. In order to help workers in endangered industries, the bill proposed adjustment assistance in the case that increasing imports hurt an industry.

Despite widespread support for the trade legislation, some economic sectors were opposed to an opening of the American economy to international competition. First among them was the textiles industry that had strong support from Southern Democrats in Congress. By negotiating an international agreement with the countries exporting textiles to the U.S. to restrict textile imports, the Kennedy Administration bought off this major opponent to trade liberalization. Further sectors that requested protection were the lumber, oil, carpet, and glass industries. All of these sectors received some concessions to conciliate them with the trade program.⁸⁶

After implementation of these measures, the TEA fared quite easily in Congress, with a clear majority supporting the bill in the House (298:125).⁸⁷ In the Senate, the most important issue was the rule concerning the special authority in the negotiations with an enlarged EEC. By that time, the probability of British

⁸⁵ The peril-point provision, which had been introduced to the RTAA in 1948, required the President to abide by the judgment of the Tariff Commission on whether the tariff for a product could be reduced or not.

⁸⁶ See for example the extensive treatment in Alkema (1999), 222-26, of Kennedy's decision to raise tariffs on glass and carpet imports.

entry had already dropped markedly. There was awareness of the fact that a failure of Great Britain to enter the EEC would make the part on free trade with the EEC redundant. The intention of the Douglas amendment was to give the President authority to negotiate under the 80 per cent authority even if Great Britain did not enter the EEC. The administration opposed this amendment on the ground that it could influence negotiations in Europe between the EEC and Great Britain. The amendment still passed the Senate, but was dropped in the conference between the House and the Senate. As in the House, the bill passed the Senate with a huge majority (78:8). In both chambers, the support for the bill was bipartisan, although a slight majority of Republicans in the House was opposed to the bill.

Alternative explanations of the TEA mainly stress the importance of geopolitical considerations. Thomas W. Zeiler, for example, sees a strong influence of security concerns in the decision in favor of passing the TEA. He states that “the liberal trade bloc in Congress understood the fundamental link of the TEA to national security.”⁸⁸ There is no doubt that political considerations determined American support for European integration, thus initially making economic considerations less important.⁸⁹ As the former U.S. President Dwight D. Eisenhower remarks in his memoirs: “Though some provisions of the Rome treaty might serve to restrain trade between Europe and the outside world, the

⁸⁷ For the debate in Congress, see Barrie (1987), 237-62.

⁸⁸ Zeiler (1992), 154.

⁸⁹ Melandri (1975), 143; Winand (1993), 263.

possible building of a powerful United States of Europe was a dream, that some day, I hoped to see realized.”⁹⁰ The undersecretary of state for economic affairs, George Ball, who was important for pushing through the TEA, strongly favored European integration.⁹¹ This was also realized by the press at the time:

There are well-founded suspicions, for example, that Under Secretary George Ball and his colleagues at the State Department see the bill more as an instrument of international politics than one of domestic economics. This is most troubling to export-minded industrialists who look to future U.S.-Common Market negotiations as a means of opening the burgeoning consumer market of Western Europe to American products and thus stimulating growth here.⁹²

Despite this importance of geopolitical interests, economic interests seem to have been essential in creating a basis of support for the TEA. The mobilization of exporters due to the fears of trade diversion coincided with executive preferences in shaping the TEA. There is also reason for suspicion that the geopolitical rhetoric was not least a means to garner additional support for a legislation intended to appease exporter interests. Officials in the State Department, for example, explicitly recognized that the TEA had to be “sold in foreign policy terms” to achieve maximum support.⁹³

Why did the U.S. choose to use MFN negotiations to respond to the discrimination threatened by the creation of the EEC? The U.S. administration

⁹⁰ Eisenhower (1965), 125.

⁹¹ See the oral history by W. Michael Blumenthal, printed in Eckes (2000), 49-51. In a later section, Blumenthal calls Ball “a Europeanist first and foremost” (55). This might have been important in determining the U.S. Administration’s support for British membership in the EEC. Winand (1993) stresses the importance of the Europeanists around Ball in determining the course of the American administration vis-à-vis the EEC.

⁹² *Wall Street Journal*, September 27, 1962, 12:4.

⁹³ W. Michael Blumenthal to Mr. Schaetzel, November 14, 1961. NACP, Decimal NACP, State Department Records, Central Files, Record Group 59, Decimal File, 1960-63, File 411.0041.

discussed various options of how to respond to European integration, such as retaliation, creation of an alternative PTA, and multilateral negotiations. In the Chicken War, the U.S. imposed retaliatory duties against EEC exports, but without success. Already very early, some commentators mentioned the possibility of creating a transatlantic free trade area that would have included not only the EFTA countries but also Canada and the U.S. in a preferential trading arrangement.⁹⁴ Such plans, however, were discarded by the State Department with the argument that concluding a deal without the EEC would not bring them any closer to the aim of lower EEC barriers to trade.⁹⁵ The choice of the multilateral approach is consistent with the hypothesis that the issue-specific power of an excluded country determines its strategy. A preferential agreement would have meant a very hard blow to the multilateral trading interests of the U.S.; at that time, regionalizing its trading interests was not a viable option. Neither was retaliation a possible strategy. As there was no viable alternative, engaging in multilateral negotiations was the best the U.S. government could do.

The EEC Reaction to the U.S. Initiative

When the U.S. Congress passed the TEA, there was no unified reaction among European governments. As the *Economist* wrote, at the beginning it was not even

⁹⁴ President Kennedy, in an address to the National Association of Manufacturers in December 1961, summarized these options when stating: “I am *not* proposing—nor is it either necessary or desirable—that we join the Common Market, alter our concepts of political sovereignty, establish a ‘rich-man’s’ trading community, abandon our traditional most-favored-nation policy, create an Atlantic free-trade area, or impair in any way our close economic ties with Canada, Japan, and the rest of the world.” Reprinted in *Department of State Bulletin*, December 25, 1961, 1039-1052, here: 1046 (emphasis in original).

clear whether the EEC would accept the U.S. initiative: “It is questioned whether the prospect of lower American tariffs is so enticing that the common market will promptly throw open western Europe to American products.”⁹⁶ In their statements, most European industrial sectors were not opposed to negotiations, but rejected the specific rules set out in the TEA. They argued that tariff reductions alone would not be able to resolve the problems that their exports faced in the American market. Why did the European governments nevertheless accept the American invitation to engage in trade negotiations? By concentrating on the cases of France and Germany, I will show that neither geopolitical nor domestic economic interests pushed them unambiguously towards trade negotiations with the U.S.⁹⁷ Instead, from the beginning there was an understanding that Europe’s increased bargaining power gave it the possibility to extract major American concessions in these negotiations.⁹⁸ In support of this argument, one observer stated:

In the initial phase of the bargaining the Americans were inclined to overplay their hand: they made it sound as if they were doing the rest of the world a favor in negotiating on industrial trade, and required a satisfactory agricultural agreement as a kind of sweetener. It was, however, clear that the United States had just as strong a motive as any other nation outside the EEC to arrive at an arrangement which would lessen the trade discrimination that would be introduced into the international system once the Community had established its customs union.⁹⁹

⁹⁵ *New York Times*, October 12, 1965, 67, 79.

⁹⁶ *Economist*, September 22, 1962, 1099.

⁹⁷ For the purpose of this paper, I use an “intergovernmentalist” approach in explaining policy-making in the EEC. For this approach see Moravcsik (1998).

⁹⁸ Many commentators agree that the EEC was in a strong bargaining position. See, for example, Kravis (1962), 97; Johnson (1963), 114; Zeiler (1992), 225.

⁹⁹ Shonfield (1976), 19.

In France, although the business response to the TEA was very cautious, there was acceptance of the negotiations in principle. In January 1963, the French industrial association, *Conseil national du patronat français* (CNPf), stated its acceptance of tariff negotiations but included certain conditions: the elimination of disparities in tariff schedules between the US and the EEC, the elimination of NTBs, and an equilibrium of offers between developed countries.¹⁰⁰ In addition, it asked for the consideration of special circumstances for some French industries. In May 1963, the Paris section of the French Chamber of Commerce pointed to disparities and NTBs as big problems in the upcoming negotiations. A resolution passed by the chamber distinguished various types of barriers that hindered European exports to the U.S.: customs legislation (American Selling Price, customs formalities, anti-dumping), escape clause, Buy American Act, and other legislation (antitrust legislation, Food and Drug Act, internal taxes, Agricultural Adjustment Act). The resolution demanded the exclusion of specific sectors from tariff reductions (industrial machinery, electric and electronic material, agricultural products) and the extension of the escape-clause regulation to all signatories of the GATT if the U.S. was not willing to renounce on its use.¹⁰¹

¹⁰⁰ This position by the CNPF is cited in: “Note. Préparation de la Conférence Kennedy. Opinions des producteurs français.” February 5, 1963. Archives Diplomatiques, Paris (hereafter cited as: AD), Service de Coopération Economique, No. 931. The demand for the elimination of tariff disparities was mainly aimed at the reduction of particular tariff peaks in the U.S. tariff schedule.

¹⁰¹ Chambre de Commerce & d’Industrie de Paris, May 9, 1963, ‘Futures négociations commerciales en application du Trade Expansion Act’. AD, Service de Coopération

In a letter to the foreign minister in August 1963, the French Federation of Mechanical Industries complained that the agreements sought in the Kennedy Round could not provide major advantages for the French mechanical industry in the American market.¹⁰² As was pointed out by the Federation, this was a consequence of the special features characterizing the American market, for which tariff barriers were not the principal obstacles. While not helping in the opening of new export markets, the negotiations could very well lead to problems for the industry in its home market. More specifically, the Federation expressed its support for finding a solution to the problem of disparities, but wanted to include American tariffs in the range between 25 and 30 per cent in the list of disparities. Furthermore, to increase the effectiveness of the harmonization measures, no tariffs on mechanical products should be reduced below 12 per cent. Finally, it demanded the removal or change of other barriers to exports to the American market like labeling regulations, the Buy-American Act, and the anti-dumping regulations.

The French automobile industry emphasized the need for “true reciprocity”. In the Kennedy Round, therefore, automobiles should be included in the European exceptions list as a provisional exception to be withdrawn from this

Economique, No. 930. The U.S. included escape clauses in its trade agreements that provided the possibility to withdraw specific concessions if they hurt domestic industries.

¹⁰² F.I.M.T.M. ‘Négociations tarifaires C.E.E./Etats-Unis au sein du G.A.T.T.: Note complémentaire de la Fédération des Industries Mécaniques’, August 1963. AD, Service de Coopération Economique, No. 949.

list after achieving true reciprocity.¹⁰³ This reciprocity should not only concern the U.S. and Great Britain, but also the other EFTA countries, Japan, and the developed Commonwealth countries.¹⁰⁴ On the firm level, Renault opposed the opening of the French market for tractors and Berliet, a French lorry maker, opposed the liberalization of the lorry market, because of fear of British competition.¹⁰⁵ The French Union of Chemical Industries pointed out that an inequality of possibilities between the American and the European chemical industry was brought about by the far higher capital investments in the American chemical industry. In order to establish a better balance, a “depeaking” of especially high U.S. tariffs would be necessary. It also predicted that the French chemical industry would demand exceptions for a large number of chemical products. As in all European countries, also in France the chemical industry mainly criticized the ASP. In the final stages of the Kennedy Round, the French chemical industry affirmed that in the case of American abolition of the ASP, it would be willing to accept a large reduction of the European tariff.¹⁰⁶ Finally, representatives of the agricultural sector in France took a very protectionist

¹⁰³ In the Kennedy Round, the EEC and the US agreed to follow a linear rule of 50 percent cuts of industrial tariffs, but with some exceptions for particular products that were included in exceptions lists.

¹⁰⁴ Chambre Syndicale des Constructeurs d’Automobiles à Monsieur le Ministre des Affaires Etrangères Paris, July 7, 1964. AD, Service de Coopération Economique, No. 932.

¹⁰⁵ Renault expressed this demand already in the negotiations concerning British enlargement. See: Renault, le Président Directeur Général P. Dreyfus, à Monsieur Wormser, Directeur Général des Affaires Economiques et Financières, Ministère des Affaires Etrangères, December 21, 1961. AD, Service de Coopération Economique, No. 2109.

¹⁰⁶ *Le Monde*, February 17, 1967, 22.

position.¹⁰⁷ The French agricultural sector was mainly interested in the development of a European common agricultural policy. By opening the German market for French agricultural products and at the same time keeping American competitors out of this market, French farmers hoped for considerable gains.

In brief, there was some disapproval among a number of French economic sectors when confronted with the prospect of new trade negotiations, but most were not opposed to the principle of negotiation.¹⁰⁸ Instead, they demanded specific conditions for their acceptance of negotiations. As *Le Monde* put it, “Already, the most entrepreneurial among our industries think that we absolutely have to seize this possibility to obtain from Washington the suppression of the most burdensome obstacles – this does not only concern the tariff peaks – that often interfere with the efforts undertaken to sell in the richest market of the world.”¹⁰⁹ Only the agricultural sector was wholeheartedly opposed to a reduction of the protection recently granted as part of the CAP.

The French government’s position was largely in accordance with this interest group opinion. In a speech on February 20, 1962, the French Foreign Minister Couve de Murville stated that the EEC would be reluctant to eliminate tariffs with the U.S. altogether. While not opposing negotiations, his main demand was “complete reciprocity”.¹¹⁰ When first confronted with the TEA, the

¹⁰⁷ Neunreither (1968), 373.

¹⁰⁸ *Le Monde*, May 2, 1964, 1. *Economist*, April 13, 1963, 169.

¹⁰⁹ *Le Monde*, April 30, 1964, 20. My translation. For a similar appraisal of the French industry’s position see also *Frankfurter Allgemeine Zeitung*, May 4, 1964, 14.

¹¹⁰ *New York Times*, February 21, 1962, 9.

French delegation in Brussels stressed that it was important to realize that the U.S. tariff schedule included various prohibitive duties that inhibited European exports.¹¹¹ For the negotiations to be interesting for European exporters, the U.S. would have to reduce these extremely high duties and also discuss its protectionist customs regulations of the U.S. Later studies of the subject by the French Foreign Ministry largely confirmed this initial position. The general conclusion was that France should accept a preliminary exploration of the American proposal in the GATT. Within the EEC, however, France should push for a position that made European participation conditional on the acceptance by the U.S. of specific European demands. For example, the Foreign Ministry deemed simultaneous negotiations concerning NTBs necessary, in particular concerning the ASP and the Buy American Act.¹¹²

In Germany, both the Federation of German Industries (BDI) and the German Chamber of Industry and Commerce (DIHT) supported the Kennedy Round and an opening up of the EEC to more international trade.¹¹³ Fritz Berg, influential President of the BDI, was also member of the executive of the German section of the *Comité européen pour le progrès économique et social* (CEPES) that spoke in favor of multilateral trade liberalization in the Kennedy Round.

¹¹¹ 'Aide - Mémoire à l'attention de M. le Secrétaire Général', Bruxelles, October 22, 1962. AD, Service de Coopération Economique, No. 930.

¹¹² 'Note', Ministère des Affaires Etrangères, Direction des Affaires Economiques et Financières, Service de Coopération Economique, November 19, 1962. AD, Service de Coopération Economique, No. 930.

¹¹³ Rhenisch (1999), 105, mentions that some parts of the BDI had opposed the creation of the EEC because it excluded important countries from the common market.

CEPES supported the EEC's quest for special rules to reduce disparities and criticized the ASP and other NTBs in the U.S. In a publication, CEPES argued: "The EEC has now as a result of its favorable position in the negotiations as largest importer in the world the chance to demand, as price for an easier access to the most interesting market, that the trade barriers to the United States should be reduced or modified. If they miss this chance, the U.S. will without pressure from outside probably never abolish these protectionist administrative practices."¹¹⁴ Another broad industry association, the German section of the International Chamber of Commerce was particularly active in contacting the German Administration and pushing for a liberal course.¹¹⁵

With regard to sectoral interests, two of the four largest German industries supported trade liberalization (the chemical and mechanical industries), while two supported protectionism (the steel and textile industries). The German chemical industry stressed the importance that the abolition of the ASP had for its exports to the U.S., pointing out that the ASP led to tariffs of up to 200 per cent.¹¹⁶ Aware of the importance of public relations work in the U.S., it produced a leaflet in which it stated: "In accordance with its outward looking attitude in

¹¹⁴ CEPES-CED (1964), 30, my translation.

¹¹⁵ See for example 'Stellungnahme der deutschen Landesgruppe der Internationalen Handelskammer zu den Dokumenten der IHK Nr. 102/20 betr. Zolldisparitäten und Nr. 102/21 betr. Nichttarifäre Handelshemmnisse' (January 1964). Politisches Archiv, Berlin (hereafter cited as: PA), B53-III-A2, No. 276.

¹¹⁶ Verband der chemischen Industrie E. V., August 29, 1963, to Ministerialdirigent D. W. Keller, Foreign Office, 'Wirtschaftspolitik im Chemiebereich 1962/63'. PA, B53-III-A2, No. 283. *Chemische Industrie, Zeitschrift für die deutsche Chemiewirtschaft*, 'Hic Genf, hic salta. Das Selling Price System als Prüfstein der amerikanischen Einstellung zur Kennedy-Runde.', Vol. 65, 2, 49-50. PA, B53-III-A2, No. 278.

general, the German chemical industry approves the aims of the Trade Expansion Act, in as much as they are to provide for a far reaching removal of existing barriers to commodity exchange.”¹¹⁷ The German mechanical industry was also strongly interested in getting better access to export markets and therefore supported a liberal EEC position.

On the protectionist side, the German steel industry even asked for an increase in the German steel tariff.¹¹⁸ The German textile industry insisted on a special treatment of the textile trade because of the widespread praxis of what it called “abnormal prices”. It asked for the harmonization of anti-dumping regulations within the EEC and the imposition of quotas against textile imports.¹¹⁹ The aluminium, coal, glass and ceramics, and electrical sectors asked for exceptions from the linear cuts for specific products.¹²⁰ The agricultural association (*Deutscher Bauernverband*, DBV) had already been opposed to the free trade area proposal and skeptical about British accession to the EEC, and even feared French competition within the EEC. During the Kennedy Round, it tried to block the decision on a common grain price in the EEC, and thus led to a prolongation of the negotiations.¹²¹

¹¹⁷ Verband der deutschen Industrie, E.V. (1962) ‘Trade Expansion Act....Yes. American Selling Price System...No’.

¹¹⁸ This tariff was not yet harmonized in the European Coal and Steel Community.

¹¹⁹ Letter of the Gesamtverband der Textilindustrie in der Bundesrepublik Deutschland (association of German textile industries) to Legationsrat D. W. Keller (confidential), November 11, 1963. PA, B53-III-A2, No. 107.

¹²⁰ Internal paper of the economics ministry (February 1964). PA, B53-III-A2, No. 290.

¹²¹ Neunreither (1968), 371-2.

Following these interest-group demands, the German government was the most liberal within the EEC and supported the aims of the TEA from the beginning.¹²² While continuously trying to ensure the success of the Kennedy Round, it also strove to achieve the abolition of the most important barriers to trade in the U.S., such as the ASP. In the agricultural field, once again in accordance with German agricultural interests, the German government took a position that tried to ensure a high price for agricultural products but with guaranteed access for third countries.

The two governments determined the position of the EEC. Already on February 6, 1962, the EEC Council declared its willingness to negotiate for linear tariff cuts if the US government was able to obtain a negotiating mandate. This occurred even though top officials of the European Commission were concerned that further tariff cuts would undermine the identity of the EEC as a customs union. On May 9, 1963, finally, the Council of Ministers decided that the EEC would take part in Kennedy Round. This opened the way for the GATT ministerial meeting one week later, which decided to start the Kennedy Round in May 1964.

In both countries, the positions taken by interest groups and governments show a strong correlation. They also support the contention that these governments accepted negotiations because they felt that they were in a favorable position to get concessions from the U.S. Alternative explanations of the

¹²² Notes of a meeting in the economics ministry, Bonn, June 11, 1962. PA, B53-401, No.

European acceptance of trade negotiations maintain that either geopolitical interests or economic beliefs influenced the preference formation of the EEC governments. Europe was dependent on political and military support from the U.S. government. Rejecting the American invitation to trade negotiations might have had serious repercussions concerning these other issues. In the 1960s, however, the security situation was more stable than in the 1950s and late 1940s, when less trade liberalization was achieved. In 1961, the European reaction to the Berlin Wall crisis showed increasing confidence in the security of Western Europe. A view that stressed Soviet attempts to secure its sphere of influence replaced the expansionist view of the Soviet Union.¹²³ This sentiment made it possible that French President Charles de Gaulle pursued a policy of increasing independence from the U.S. An additional political reason for objecting transatlantic trade liberalization was that to a certain extent it counteracted European unification, as long as the preferential abolition of tariff barriers and the existence of a common external tariff were the major unifying factors.

Especially in Germany, economic beliefs seem to have favored trade liberalization. The Minister of Economics, Ludwig Erhard, was a declared free trader. This attitude was already important in Erhard's reaction to the creation of the EEC, when he favored a free trade area including Great Britain and was willing to sacrifice the EEC for this objective.¹²⁴ In France, however,

283.

¹²³ Geiger (1970), 19.

¹²⁴ Moravcsik (1998), 199.

protectionist economic beliefs were dominant. As these economic beliefs correlate with the interests expressed by domestic interest groups in the two countries, establishing an independent influence for ideas would be difficult. While these alternative hypotheses thus lead to unsatisfactory conclusions, the evidence largely supports the contention that Europe responded approvingly to the American initiative because European governments could hope for substantial concessions in international trade negotiations. They knew that this would guarantee them the support of export-oriented industries, while not alienating import-competing ones.

4. Conclusions

Contrary to other theories of trade-policy making, I have argued that political processes internal to a country do not solely determine trade policies of states. Often trade policies are reactions to the policies chosen by other countries. The paper shows that PTAs can influence the trade policies of excluded states and in turn the trade policies of member states. More significantly, I establish a mechanism by which PTAs influence the ensuing trade policies of excluded and of member countries. This mechanism works through the mobilization of exporters, the subsequent choice of strategy made by excluded governments, and the increase of issue-specific bargaining power of member countries. In the case of the creation of the EEC, American exporters lobbied their government to react to the potentially discriminatory effects of this PTA and made the U.S. engage in the Kennedy Round. European governments agreed to participate in tariff cutting

because they expected large concessions from the U.S. for a relatively small reduction of discrimination. As Pierre Uri stated already in the late 1960s, “The establishment of the European Community gave the initial impetus to the Kennedy Round; its bargaining power has thawed American tariffs which had remained frozen for twenty years; and its existence induced some of its members to accept massive cuts in their previous levels of protection.”¹²⁵ This seriously questions the focus by most theories of trade-policy making on factors internal to a specific country in explaining its trade-policy choices. More research (especially on a larger sample of cases) is required to establish how widespread the effects described in this paper are, but a first overview at least showed their importance and the plausibility of the theory developed here in explaining them.

The paper has implications for various debates that have a prominent position in the fields of International Political Economy and trade policy. With regard to the former, it contributes to current research that tries to combine comparative and international political economy, i.e., that seeks to combine the domestic and international determinants of foreign economic policies. It shows how international developments influence domestic political processes and how these domestic processes in turn influence international developments. As such, it questions the usefulness of the unitary-actor assumption that characterizes much of the International Relations literature. The study is also another piece in a chain

¹²⁵ Uri (1969), 215.

of studies in the field of International Political Economy that are looking at the past as laboratory to develop parsimonious theories.

With regard to debates in the literature on trade policy-making, the paper offers a convincing explanation for the trade liberalization that has characterized transatlantic trade relations over the last decades. Helen Milner argues that interest-group explanations of the world-wide rush to free trade have to “specify how an exogenous force shifted political influence away from protectionists and in favor of those preferring free trade.”¹²⁶ This paper offers such an explanation by pointing to the effect of discrimination on the mobilization of free-trade interests. In addition, the paper provides a more optimistic evaluation of the consequences of trade discrimination. Economists have hotly debated the question whether PTAs are “building blocks or stumbling blocks” for multilateral trade liberalization.¹²⁷ If the analysis in this paper is correct, PTAs can serve as building blocks even if they divert trade from excluded countries. The study also shows that especially for weaker countries, the creation of PTAs can have the positive consequence that they increase their bargaining power in multilateral negotiations. This influence, however, will probably become less important as the current reduction of trade barriers also diminishes the potential for trade diversion. Finally, it seems that also in the future preferential and non-preferential trade policies will continue as strategies in the policy-repertoire of developed

¹²⁶ Milner (1999), 97.

countries. Fears that the new wave of regionalism, which started in the 1980s, will result in a world divided up into a few competing regional blocs therefore seem unfounded.

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¹²⁷ See for example Lawrence (1991) who comes to an optimistic assessment of regionalism and Bhagwati/Panagariya (1996) who take a pessimistic stance. See also Winters (1999) and Panagariya (2000), 317-25.

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