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U. S. ECONOMIC FOREIGN POLICY

A lecture delivered
at the Naval War College
on 26 October 1953 by
Professor Sumner H. Slichter

Thank you Captain Pederson.

I am glad to be here to discuss, with the emphasis rather strongly on the word "Economic," the Economic Aspects of Foreign Policy. My remarks will fall under the four principal headings: (I) The Principal Conditions That Mold American Foreign Economic Policy; (II) The Objectives of American Foreign Economic Policy; (III) The Accomplishments of American Foreign Economic Policy, and (IV) Where Do We Stand and What Should we do?

I. The Principal Conditions That Mold American Foreign Economic Policy.

Some of the conditions which mold American Foreign Economic Policy, or Economic Foreign Policy, are very ancient and some are very recent. Some of the most important molders of our Economic Foreign Policy are conditions and objectives which many people would regard as out-of-date. So there is a clash between various determinants of Economic Foreign Policy. In order to understand what is happening to our Economic Foreign Policy, it is important to see clearly this clash between old and new objectives — old objectives which we have inherited, and in which many people still believe, and newer influences and new objectives which are the result of the Second World War as well as other influences which I shall point out. This clash, this struggle over what Economic Foreign Policy should be is at the very heart of current discussions of our policy.

There are six principle conditions which make Economic Foreign Policy what it is in the United States. I am going to

take them up more or less in the chronological order of their emergence as influences on our foreign policy.

First, is the desire of the American people to protect manufacturing, agriculture, and other industries here from too severe foreign competition. That is a very ancient and powerful influence.

A second determinant is the extraordinarily high productivity of American industry. With this second determinant should be linked the wide diversity of American resources. Here, in this country, we have only 6% of the world's population but we turn out about 40% of the world's goods. Economically speaking, we are 40% of the world. This means that labor here is about nine times as productive as labor on the average outside of the United States. Our labor in an hour will turn out about nine times as much as labor in the rest of the world. It is about twice as productive as labor in England; it is about three times as productive as labor in France.

We are a big country and we happen to lie in the temperate zone where our size gives us a wide diversity of climates, and our bigness gives us a wide variety of natural resources. That means that we have an extraordinarily wide range of industries. We can grow oranges, cotton, and many semi-tropical things as well as wheat and other crops and animals that thrive in a fairly cool climate. The variety of our climates and the variety of our resources, combined with our efficiency, give us a superiority in a large number of industries and make it extremely difficult for other countries to sell us goods. The deficit in their sales to us over what they bought from us in the period 1946-1952 was about 34 billion dollars. This sort of circumstance is a second very important determinant of our Economic Foreign Policy.

A third important determinant may be described as the special economic problems created for many countries of the world by the Second World War, particularly the countries in Europe,

in the Near East, and in parts of Asia. These problems include the destruction of capital, the dislocation of established patterns of trade in accordance with which these countries had previously earned their living, and the creation of very difficult fiscal problems which have made it hard for the countries of Europe, the Near East, and Asia to restore and maintain stable currencies. Without a more or less stable currency, the economic processes are impaired in many respects.

A fourth fundamental determinant of our Economic Foreign Policy is the deep poverty of most of the world. Of the 2.4 billion people in the world, more than a billion (which is more than two-thirds of the population of the world outside the Iron Curtain) have an average income of \$80 a year compared to an average income of about \$450 a year in Western Europe (there are wide variations in Europe, but the average is around \$450 in Free Europe), and of around \$1600 in the United States. Among these more than a billion people, illiteracy runs 70% and about two out of three are sick a good part of the time or all of the time. They lack, roughly, about one-fifth of the food which is needed for minimum standards of nutrition if one measures nutrition in a way which I think is becoming out-of-date, by calories, and if one does not take account of some of the other important elements in nutrition. They do not get enough to eat. The problem of poverty is aggravated in many regions, particularly in Latin America and in parts of Southern Asia, by high birth rates. This means that if modern science reduces the death rate, there is a terrific upsurge of population, so rapid that the communities cannot provide enough savings to supply the increasing population with tools and equipment. It is interesting to note that a rapid increase in population is regarded as a favorable economic circumstance in the United States, but as an unfavorable one in Puerto Rico, Ceylon, or the Federated Malay States, and many other places. Whether a rapid growth of population is considered favorable or unfavorable depends largely upon whether the savings of the community are high enough so that the additions

to the labor force can be given enough tools and equipment with which to work.

A fifth basic influence on our Economic Foreign Policy is the existence of a powerful and aggressive Communist movement which endeavors to capitalize on the economic, political, and social problems of the rest of the world and to use discontent of any kind, from whatever source, to win converts to Communism.

Finally, a sixth basic determinant of our Economic Foreign Policy is the growing dependence of our rapidly expanding economy upon raw materials from abroad, some of these raw materials having strategic importance. I said that the United States produces about 40% of all the world's output. It produces half of the manufactured goods of the world outside of Russia, but it produces along with this half of manufactured goods only about one-third of the raw materials. Hence, we depend upon foreign sources of supply for about one-sixth of our raw materials. For certain important raw materials, we are very heavily dependent upon foreign sources. For example, we depend on foreign sources for all of our natural rubber, all of our manganese, all of our chromium and tin, about one-third of our lead and aluminum, and about one-quarter of our zinc and copper.

II. The Objectives of American Economic Foreign Policy.

What kind of objectives have these determinants of Economic Foreign Policy produced and what instruments have we developed for the purpose of pursuing these objectives? I am going to discuss the objectives and the instruments together because I think that will save a little time. As I have already indicated, these fundamental determinants have produced some conflicting objectives.

It seems to me that there are five principle objectives in our Economic Foreign Policy. Although there is conflict among these five objectives and although the pursuit of one objective

will interfere to some extent with the attainment of other objectives, all of these five objectives are simultaneously pursued. Perhaps we could get better results if we could narrow our objectives and concentrate upon some of these only. But you will readily understand that in a Democracy the narrowing of objectives is not easily done.

1. The protection of American industries from foreign competition. The first objective of American economic foreign policy is the protection of American industries from foreign competition. There are a number of principal instruments with which this objective is pursued. The first and most general instrument is, of course, the tariff.

A second instrument of protection is the "peril point" amendment to the Trade Agreement Acts of 1951. This amendment requires the President to submit to the Tariff Commission a list of products on which tariff concessions are being considered if we are in the process of attempting to negotiate a Reciprocal Trade Agreement with any other country. The Commission must submit its advance judgment as to how far the President may make tariff concessions without serious injury to domestic industry. If the President goes beyond the so-called "peril point," he must submit his reason to the Ways and Means Committee of the House.

A third instrument for protecting our industries from foreign competition is the "escape clause" amendment to the Trade Agreements Extension Act of 1951. This clause reserves the right to the United States to withdraw concessions if serious injury is caused or threatened to a domestic industry by tariff concessions. The amended law requires that an "escape clause" be included in all future trade agreements and that it be added as soon as practicable to all existing trade agreements.

The escape clause is a powerful instrument because no foreign manufacturer planning to enter the American market

knows how the clause will be interpreted; no foreign manufacturer planning to enter the American market knows what will be regarded as "serious injury." The idea of investing considerable time and money in setting up a sales organization in the United States, and doing business at a loss here for several years while he builds up enough accounts to carry the overhead, has very little attraction if he expects that his very success in selling motorcycles or bicycles in the United States will cause concessions to be withdrawn. So the "escape clause" amendment has done much to destroy the intended effect of the Reciprocal Trade Agreements. There is a clash among people in the United States over whether these Reciprocal Trade Agreements should be encouraged or whether they should be discouraged. This amendment, as well as the "peril point" amendment, represented victories for those of our citizens who think that the Reciprocal Trade Agreements should be discouraged.

A fourth instrument of protection is Section 22 of the Agricultural Adjustment Act, as amended, authorizing import fees and quotas when necessary to protect the Farm Price Support Program. We have a fee on almonds now and quotas on wheat and cotton. There are special acts imposing quotas: such as the Sugar Act of 1948, imposing quotas on sugar, and the Philippine Trade Act of 1946 which imposes quotas on products from the Philippines.

A fifth amendment of protection is the "Buy American" provision in various statutes. The original "Buy American" Act, which I think was passed in 1934, was intended to help some of our industries in the midst of depression. It directed governmental agencies to show preference to goods produced in this country unless the cost of domestic supplies were unreasonable. Reference to this Act has been written into a great deal of legislation since 1934 — into legislation passed in times of full employment rather than in times of depression. There is a "Buy American" provision in the Defense Appropriation Act of 1953. Even the Fed-

eral Housing Administration and the Rural Electrification Administration have "Buy American" requirements in their appropriations.

2. Raising standards of consumption in the United States.

The second objective of our Foreign Economic Policy conflicts very squarely with the first objective. The second objective is raising the standards of consumption in the United States. It is a much more recent objective, I think, than the objective of protecting our industries from foreign competition. I think the date of this second objective might be put for our convenience at 1934, when the Reciprocal Trade Agreements Act was passed. The idea behind this Act is that our industries would be more productive, and therefore our labor and capital would yield us a higher standard of living, if we concentrated on making the things which we are best able to make because of our "know-how," our climate, our resources, and imported the things which other parts of the world can make more cheaply than we can.

The new instrument for implementing this idea of using our Foreign Economic Policy to raise our own standard of consumption is the Trade Agreement Act of 1934 and the successive extension of that Act. Under the original Act, and its successors, the United States has entered into fifty Reciprocal Trade Agreements in which we reduced duties in return for other countries' reducing their duties. Six of these treaties have been terminated, but the others are in effect. This second objective of using Foreign Economic Policy to raise our standards of consumption and to concentrate our industries in the lines of production for which we are best adapted conflicts squarely with the much more recent objective of protecting American industries from foreign competition. The Reciprocal Trade Agreements involve reductions in our tariff which means, of course, exposing our industries to greater competition from abroad. But since more imports by the United States mean more foreign demand for our exports, The Reciprocal Trade Agreements help bring

about a shift of labor and capital from our less productive industries to our more productive ones, thus raising the average productivity of American industry as a whole.

3. Strengthening other economies. This third objective of our Economic Foreign Policy is also a recent one. Furthermore, it also conflicts with the first objective. We adopted the objective of strengthening other economies shortly after the Second World War. I think it has developed a bit in the last few years. When it was first adopted, it was regarded as a way of fighting the spread of Communism, of helping production revive so that other peoples could live better or could have the hope of living better. But I think more recently there has been added another aspect to the objective of helping other economies. As the 'cold war' has become more apparent to everyone, we have desired to strengthen other economies so that they would be better able to pay for their own defense and to pay for their own defense on a larger and more adequate scale. But you see this third objective is a very recent one; it does not go back before 1946.

The Reciprocal Trade Agreements Program, which was already in effect and which had been adopted for other reasons, has proved a useful instrument for promoting this third objective because this will make it easier for other countries to sell to us. If we open our own great domestic market (which is 40% of the world's markets) to other countries on more liberal terms, they can get the road machinery, the generators, the machine tools, the textile machinery, the tractors, and the other things that they need for increasing their production by selling us things which they are best at making. So our Reciprocal Trade Agreements Program not only has strengthened our own economy but it has strengthened other economies.

But we have never been able to go very far (as I shall point out in a few minutes) in liberalizing the duties which count. We made a lot of concessions which were not very important. But something had to be done on a big scale, and done in a hurry.

We were doing it under Lend-Lease and under UNRRA, but UNRRA was folding up. When the British announced early in 1947 that they no longer could support Greece and were going to pull out, and when the Russians made new demands on Turkey, President Truman appeared before Congress on March 12, 1947 with a proposal to send economic and military aid to Greece and Turkey. Here was an important new implement effectuating, or helping to effectuate, this third objective of our Foreign Economic Policy. And it was on June 5, 1947 that Mr. Marshall (then Secretary of State) proposed a much broader application of the so-called "Truman Policy." In the spring of 1948, as you all know, the Marshall Plan began operating. We have a number of other instruments which help us carry out this third objective of strengthening other economies. One of the important ones is the Export-Import Plan. And I suppose one should list the Bank for International Development because, though it is an international organization, most of the money in it comes from us and the bonds have been sold mainly in American markets.

The "aid" programs have gone through an evolution with which I am sure you are familiar, so I shall not dwell on them. The name of the aid programs has changed from time to time and the 'cold war' has led aid to take more and more a military form, but there has been no change in the fundamental principle of using credits and gifts in large volume because the help had to be given in a hurry and because there were political obstacles in addition to giving help through the form of trade. So we have had to give help on a large scale in the form of aid. That, of course, conflicted with our desire to raise our standard of consumption. We had to put our interests in conditions outside the United States ahead of our desire to obtain, at least in the short run, a maximum level of consumption. This aid which we have given, 40 billions of it since the end of the Second World War, has represented a 40 billion dollar lower standard of living for the American consumer.

Please do not infer that I am suggesting this money was not well spent. I am simply calling your attention to the fact, which is important for policy-makers to bear in mind, that we are dealing with objectives which are partly in conflict. Therefore, we must decide which compromise between these several objectives best promotes the national interest. I am not suggesting that the compromise which was made was a bad compromise, but I am emphasizing the fact that a compromise was necessary because we did have the desire to raise our standard of living and we also had the desire to fight Communism.

4. The development of foreign sources of supply of strategic materials. This fourth objective of our Economic Foreign Policy is also very recent — largely the result of the 'cold war.' Our Gift and Loan Program has done something to implement this fourth objective and so has our Stockpiling Program. We have discussed the implementation of this objective and other objectives by encouraging private investment abroad. There has been a fair amount of private investment abroad, and it has been done with the blessing of our government and in some cases with definite help from our government. But one cannot ascribe a great deal of encouragement to private investments from our public policies. Nevertheless, the expansion of our petroleum industry abroad, the development of important iron ore resources abroad, and the development of bauxite abroad — all by private investment — have helped to implement this fourth objective.

5. Restricting the flow of strategic materials from the Free World to Russia and her satellites. This is, of course, the most recent of all objectives of our Economic Foreign Policy. To implement this objective, we have the Export Control Act of 1949. As for as China and North Korea are concerned, we have the "Trading With The Enemy" Act of 1917. Finally, we have the Mutual Defense Assistance Control Act, known as the "Battle Act," which requires termination of the United States' aid to a coun-

try shipping materials of a primary strategic significance behind the Iron Curtain.

III. The Accomplishments of American Foreign Economic Policy.

Now, what has been accomplished by the Economic Foreign Policy of the United States? The simultaneous pursuit of conflicting objectives has, as one might expect, limited success in achieving some of these objectives. The first objective, the protection of American industries from foreign competition, has been rather successfully pursued, I think, in spite of all efforts to raise the standard of living in this country by encouraging imports. In the prewar period, 1936-1938, the percentage of merchandise imports to the commodity production in the United States (by "commodity production" I mean our total production minus services; I exclude the services because most services are not importable) was 4%; in 1952, it was 3.8%. So I think the subscribers to the "protectionist" objective have been quite successful in achieving their aim to keep bothersome competition from abroad out of our markets. In the manufacturing field in particular, where we have quite high duties, the concessions made in the Reciprocal Trade Agreements have been very meagre and minutely defined so that our imports of these manufactures today, after nearly twenty years of Reciprocal Trade Agreements, are only one-half of one per cent of our domestic factory output. We do not tolerate very much foreign competition in the field of manufacturing.

Incidentally, the method of using red tape to discourage imports has been developed. On June 30, 1952 there were almost 100,000 invoices that had been in the hands of appraisers for 90 days or more awaiting determination of the duty. At the close of 1952, the customs court had 63,010 appeals for reappraisals. It received 14,984 cases during the year; it decided 963. Cases were coming in just about fifteen times as fast as they were being decided. The number of undecided cases between the end

of 1948 and the close of 1952 had increased more than fourfold. So red tape has been developed into a pretty good method of keeping out goods.

Under the Reciprocal Trade Agreements Program, by which we have made efforts to achieve the second objective, the average rate of duty has been tremendously cut if one measures it by the ratio of duties collected to the value of dutiable imports. Of course there is a trick in that method of measurement, because a duty does not enter into the average if it is high enough to exclude imports. Hence, the very highest duties do not raise the average. Although the ratio of duties collected to the value of imports is a measure no statistician could possibly defend, it is the most convenient measure to use and we do use it time and again. In 1934, the duties collected were 46.7% of the value of dutiable imports; in 1951, they were only 12½%. That looks like a lot of progress in opening our markets to foreign trade but when you test the progress by the flow of trade you find that our Reciprocal Trade Agreements Program has been close to a flop; it has been a "paper" program rather than a real program.

Great progress has been made, I think, in achieving the third objective: strengthening other economies. At least this is true for Europe and one or two other countries like Turkey. For example, industrial production in Europe is about 40% above prewar. Real national income per capita in Western Germany, despite the terrific influx of population from Eastern Germany, is about as high as prewar; it is about the same as prewar in Italy; it has gone up around 10% in the Netherlands; it is up between 10%-15% in France, Denmark, and Britain, about 20% in Switzerland, and about 30% in Sweden.

So we have succeeded in greatly increasing production in Western Europe. Had we not succeeded I think the Communist Party, in France and Italy particularly, would be far stronger and more influential today than it is. I think that the money we

have spent has been well spent. It is easy to point to waste. Since time was of the essence, we could not always deliberate over the decisions to be made, but had to act quickly. Communism has lost ground in Western Europe, and one of the main reasons why it has lost ground has been the increase in production which aid from the United States helped to bring about.

Europe is much more independent of the rest of the world than it was before the war. Its physical volume of imports in 1951 was 10% below 1938, and its physical volume of exports was 40% greater. It had adjusted its trade to the loss of foreign investments and to the change in the terms of trade which are less favorable to Europe than they were before the war. But altogether it has succeeded in increasing its exports to the dollar area (that is, to this country, Canada, Cuba and Venezuela) by about 50% in physical terms, it still cannot sell enough to the dollar area to permit convertability of European currencies.

Our progress in the undeveloped, or so-called "underdeveloped," parts of the world has been slower. The Point Four Program really did not get going until 1952, or late 1951. The work of putting on demonstrations around the world, teaching primitive farmers better methods of farming, convincing them that other methods in farming would pay, is a slow business but it is a very important business. It has the merit of giving aid where aid is very important and giving aid with the expenditure of very few dollars on our part. What the rest of the world needs more than capital is knowledge. Many of these people need only a little in the way of better tools or fertilizer to raise their productivity considerably.

I do not think that I need to expand on the development of foreign sources of supply for strategic materials. I think our objective there is being attained fairly satisfactorily. Certainly the new supplies of iron ore have become available on a bigger scale and sooner than most of us dared hope for.

Finally, restricting the flow of strategic materials from the Free World to Russia has been achieved with reasonable success, although I think you know more about that than I do. You are well aware that this is a controversial topic and is bound to be because one cannot draw a sharp line and say: "This is where the materials begin to be strategic; on the other side of the line they are not." It is like the difference between day and night. The question is whether the trade between the two parts of the world is a trade which promotes our security relative to the strength of the other side. Any trade at all is bound to increase the strength of the other side. You cannot judge it by looking at the benefits which the Iron Curtain countries get. You can only judge it by comparing the benefits which they get with the benefits which we and our allies get.

IV. Where Do We Stand And What Should We Do?

Now we come to the question of where we stand and what we should do. I have indicated, I think, that the most important thing about where we stand is that the two conflicting objectives — our desire to protect ourselves from foreign competition and our desire to raise our standards of consumption — are more or less offsetting one another with the second losing out not completely but pretty completely to the first. In other words, we have this nineteenth century objective of protecting our industries from foreign competition being carried over into the twentieth century and still being a much stronger influence upon our Economic Foreign Policy than the twentieth century objective of raising our standard of consumption.

Our third objective of strengthening other economies more or less rests upon emergency means which are not desired as permanent means by the recipients of aid and credit and which are increasingly unpopular with American taxpayers. The need to strengthen other economies has diminished, at least in Europe, very considerably. But I doubt that it has diminished in the Near

East, in Latin America, or in southern and southeastern Asia. We are confronted, therefore, with the problem of replacing many of the instruments which we have used to promote our third objective.

I do not think we are confronted with any particular problem in respect to the fourth and fifth objectives. But we are not making very much progress in the pursuit of the second objective. And we are going to run into difficulties in pursuing the third objective in the future unless we develop to some extent new instruments for pursuing it.

The question of what to do about our foreign Economic Policy, how to modernize it, how to make an up-to-date twentieth century policy out of it, has been reviewed quite frequently of late. It was reviewed by the Gray Commission several years ago, which turned in an excellent report; it was reviewed again by the President's material Policy Commission, which turned in an excellent report, the so-called "Paley Commission," headed by Mr. Paley of the Columbia Broadcasting Company; it was reviewed by the Bell Commission, which turned in a splendid report in February of 1953; it was reviewed by Louis K. Douglas, who turned in a briefer report but a good one shortly after the Bell Commission. All of these reviews of our policies have produced essentially the same recommendations.

The problem is being reviewed today by a seventeen-man commission which will report next March, headed by Clarence Randall, Chairman of the Board of the Inland Steel Corporation. It has members of Congress upon it; it has businessmen; it has a very eminent economist, my colleague, Professor Williams. Obviously, we must make up our minds whether we are going to let our second objective be pretty much defeated by adherence to the nineteenth century first objective. If we regard the 'cold war' as important and if we regard Communism as a threat, then

we must devise new instruments for implementing our third objective because aid and credit will have to be used, I believe, on a considerably smaller scale in the near future.

The recommendations of the Randall Commission will be tremendously influential. If you will analyze its membership I think you will see that the Commission is so constituted that it can recommend no drastic departures from our present set of objectives, although it will undoubtedly recommend some changes. It is important that after the failure of Congress to pay any attention to the recommendations of the Gray Commission, after the failure of Congress to pay any attention to the recommendations of the Paley Commission, after the failure of Congress to pay any attention to the recommendations of the Bell Commission, after the failure of Congress to pay any attention to the recommendations of Mr. Douglas — it is important that we get a set of recommendations which will be sufficiently acceptable to the wide range of opinions in Congress so that at least modest steps can be taken in the very near future in modernizing and reforming our Economic Foreign Policy.

BIOGRAPHY

Dr. Sumner H. Slichter

Professor Sumner H. Slichter was born in Madison, Wisconsin, and educated at the University of Munich, the University of Wisconsin (A.B. 1913, A.M. 1914), the University of Chicago (Ph. D. 1918). He has served as Instructor of Economics at Princeton, Professor of Economics at Cornell, and Professor of Business Economics at Harvard, and on the staff of the Brookings Institution. Since 1940 he has been Lamont University Professor at Harvard. He has been the recipient of honorary degrees from Harvard, Wisconsin, Northwestern, Rochester, and Lehigh Universities.

In 1941 Professor Slichter was President of the American Economic Association, and in 1949 President of the Industrial Relations Research Association. He was a member of the Social Science Research Council from 1935 to 1938. He is now Economist for the Committee for Economic Development and a member of its advisory board. Professor Slichter was Chairman of the Board of Nine (3 public, 3 labor, 3 employer members) appointed by the Governor of Massachusetts in 1947 to advise the Governor on the labor laws of the Commonwealth. He was associate Chairman of the Advisory Council on Social Security established to advise the Committee on Finance in its study of the Social Security program. He has served as arbitrator in numerous labor disputes.

Professor Slichter is the author of: "Modern Economic Society," (1931); "Towards Stability," (1934); "Union Policies and Industrial Management," (1941); "The Challenge of Industrial Relations," (1947); "Trade Unions in a Free Society," (1947); "The American Economy: Its Problems and Prospects," (1948); "What's Ahead for American Business," (1951).