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## CHALLENGES FOR WESTERN ECONOMIC COOPERATION

Address By

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Tucson, Arizona, June 5, 1986

441.21038

*In his speech the ambassador emphasized:*

- *that retaliatory and counterretaliatory measures of protectionism would in the end create additional damage to international trade and the world economy.*
- *that we have to try to reduce surplus production and subsidies in a step-by-step process.*
- *that the German economy is, at the moment, pulling Western Europe with it towards higher, non-inflationary and possibly sustained growth.*

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One month ago the world economic summit of the seven leading Western economic countries was held in Tokyo. Reviewing the developments of the world economy since their Bonn summit, the heads of state and government of Canada, France, the Federal Republic of Germany, Italy, Japan, the U.K. and the U.S., meeting in Tokyo, had some reasons for satisfaction. In the year since the Bonn summit we have been witnessing an increased awareness of the interdependence of our economies and correspondingly a greater willingness for cooperation and coordination of economic as well as monetary policies among the summit participants. An attitude of overemphasizing domestic considerations, of a kind of "benign neglect" of the international repercussions of national economic measures, has been replaced by a more outward-looking and cooperative approach. I refer to the meeting of the G 5 on September 22, 1985, in the New York Plaza Hotel starting coordinated interventions in the capital markets in order to bring the exchange rates of the dollar more in line with economic realities. I refer to the Baker plan on the promotion of economic growth in the debtor countries through increased public and private capital transfers linked to concrete efforts by the recipient countries to restructure their economies. Both these measures symbolize the changes which took place between the Bonn and Tokyo summits. U.S. leadership has been decisive in this context!

At present, the United States is addressing vigorously one of the major reasons for the remaining imbalances threatening the world economy today - the high U.S. budget deficit. While waiting for concrete results from Congress on the budget for fiscal year 1987, there is reason for some optimism. In the meantime some other summit participants have already made significant progress in reducing their deficits. The German budget deficit, which three years ago corresponded to more than 4 % of GNP, has in the meantime been more than halved. Correspondingly the demand of the German public sector for capital has been reduced, contributing to a significant lowering of interest rates in West Germany. Our discount rate today is as low as 3.5 % (compared to 6.5 % in the U.S.).

The heads of state and government of the Seven in Tokyo were able to recognize a growing convergence of the economic performances of their countries. While the U.S. economy at this moment seems to grow by approximately 3 % of GNP, with the possibility of a higher momentum in the second half of this year, economic growth in Germany in 1986 is projected at around 3.5 % of GNP. Also Japan can expect a growth rate of around 3 %. The rest of Western Europe also is confident of increased economic growth prospects (probably by about 2.5 % of GNP), helped by coordinated efforts of central banks, in particular of the Federal Reserve Board, the Bundesbank and the Japanese Central Bank, to reduce interest rates. All these efforts would not have yielded such positive results if they had not been accompanied by the spectacular decline of energy prices. The economies of the non-oil producing and energy-importing countries thus received an additional incentive for growth while inflation rates were reduced. Needless to say, declining energy prices and interest rates are providing significant relief also to the great majority of the indebted developing countries of the Third World. The oil-producing developing countries like Mexico, however, find themselves in serious difficulties and require urgent support from the multilateral finance institutions like the IMF and the World Bank as well as from the private banking sector.

These are the more positive aspects of the world economic scene as they presented themselves to the summit participants. There remain, however, a

number of serious imbalances, constituting difficult challenges for Western economic cooperation. Also after Tokyo, there exists no reason for complacency. The major threat to the whole fabric of international economic cooperation between the industrialized Western countries as well as vis-à-vis the developing world emanates from the growing forces of protectionism. In view of the high U.S. trade deficit and the forthcoming November elections these pressures are at this very moment particularly strong in the United States, though certainly not limited to this country. Under the label of "fair trade" the U.S. Congress is more and more acting as if the U.S. were an island of virtue surrounded by sinners in international trade. Unfortunately the EEC list of U.S. sins in trade is grosso modo as long as yours on our shortcomings and this being so, each side is now busily preparing to apply retaliatory, counterretaliatory, etc., measures, in the end creating through the spiraling effect of these measures additional damage to international trade and the whole world economy.

While we have not yet solved either the so-called citrus or pasta war between the U.S. and the EEC on the citrus preferences granted by the community to Mediterranean countries like Israel, Tunisia and Morocco, nor the conflict over possible consequences of the accession of Portugal and Spain to the Community for U.S. exports (of agricultural as well as manufactured goods), a new chapter in our already sufficiently complex trade relations was opened about two weeks ago: The U.S. asked not only Japan and Taiwan but also West Germany and Switzerland to limit their machine tool exports to the U.S. Since there exists no possibility for the U.S. to accuse us of using so-called "unfair" trade practices like subsidies, dumping etc., reasons of "national security" were invoked this time.

We appreciate the efforts of the U.S. administration to counter what President Reagan called a mindless protectionist stampede and to restore positive U.S. leadership towards a reduction of trade barriers and the promotion of worldwide free trade through a new multilateral round of trade negotiations within the GATT. My government fully supports this approach. Indeed, the whole EEC is willing to make a positive contribution towards the success of the ministerial meeting which in September in Punta del Este, Uruguay, will decide on the opening of the new GATT round, even though the present protectionist pressures, particularly in the U.S., do not facilitate the open-mindedness and constructive spirit which are a prerequisite for success. The new round will have to tackle difficult problems: How to strengthen the GATT system, in particular its rules for dispute settlement and safeguards, how to enlarge its scope and area of application (in addition to manufactured goods also services, agriculture, intellectual property rights, trade-related investment etc.

Trade in agriculture has become a particularly divisive subject. For the first time the Summit in Tokyo dealt with this important issue at such a high level. Of course, no solution could be found on this first occasion - as a matter of fact, it is doubtful whether we will ever be able to totally solve such difficult issues as surplus production, subsidies, price levels and import barriers.

But at least we have to try together to bring these threatening developments under control. Otherwise the support for our respective farmers will become even more expensive and we will end up weakening the very foundation of our alliance by waging trade wars against each other. In order to avoid this we shall have to develop coordinated policy guidelines and establish rules of conduct within GATT as well as OECD. This is going to be extremely

difficult and controversial - the common agricultural policy of the EEC has a strong component of social policy. 11 Million farmers, many of them owning small farms, depend in their existence on the price and income support they receive from Brussels (approx. 20 billion dollars annually, as much as the 2.5 million U.S. farmers receive). Farmers generally are conservative and constitute a strong political lobby. They fight against developments which they perceive as threatening their existence as independent farmers. The enlargement of the EEC, by which the agriculturally oriented Mediterranean countries of Greece, Portugal and Spain were admitted, does not make it politically easier to find a solution. But we shall have to try, because the alternatives are all worse. Reduction of surplus production and of subsidies in a step-by-step process is - in our mind - conceivable, provided patience is applied.

Patience, however, is precisely what appears to be in scarce supply these days. The spectacular decline of the value of the U.S. dollar in particular vis-à-vis the yen and the DM has laid the foundation for a significant reduction of the U.S. trade deficit. The growth of the U.S. trade deficit appears to have been arrested, while German exporters are beginning to feel the pain. The growth rate of our exports is reduced, our imports are increasing in volume. The reverse is developing in the U.S.: your exports are beginning to increase again. But, unfortunately, the real effects will become clearly visible only later, possibly only after the November elections. Soon we might even be faced with more protectionist demands than ever because, as a consequence of the declining dollar, your imports have become more expensive and, therefore, in nominal terms, not in volume, will increase, while ours will appear as if they were decreasing. In dollars, not in volume or real terms, our trade surplus at the end of this year could accordingly even appear to be bigger than ever!

That moment will also become a test case for another concrete achievement of the Tokyo summit, the so-called "enhanced surveillance" or improved coordination of economic policies and performances of the Seven, taking into account indicators such as GNP growth rates, fiscal deficit ratios, current account and trade balances, monetary growth rates, reserves and exchange rates. There certainly is room for increased cooperation and coordination in economic policy matters as well as in managing the floating of major Western currencies. My government is determined to make its contribution to a healthy world economy. At this moment we are pulling Western Europe with us towards higher, non-inflationary and, as it appears, sustained growth. With the exception of an unemployment rate of 9 % (2 % higher than the U.S. rate), our economic performance is very positive and balanced, also in comparison to those of the U.S. and Japan. We are ready to do what we regard as economically wise and politically feasible to stimulate our economy, including raising our interest rates, if appropriate. But we - and even more so our independent Bundesbank - have to remain the final judges of our actions. Otherwise, for example, we may no longer be able to fulfill adequately our role within the European Monetary System (EMS), one of the major achievements of European politics of the last decade.

Finally, we continue to be faced with the unsolved debt crisis in the Third World. Lower interest rates are helpful to all developing countries, lower energy prices to most of them. But even more important is free trade. When we deny the debtor countries free access to our markets, we not only hurt them but also ourselves. Likewise, we cannot on the one hand ask for addi-

tional trade concessions by the developing countries in the new GATT round regarding services, etc., and on the other hand take restrictive measures with regard to their textile exports in the ongoing negotiations on a renewed multi-fiber agreement. In addition, the Baker debt initiative requires urgent implementation. Financial incentives must be given in order to promote the necessary restructuring of the economies of Third World countries and thus facilitate their integration into the world economy. This task cannot only be left to the IMF and the World Bank. We must also encourage the commercial banks to do their share. As IMF managing director de Larosière put it recently: "No debt strategy can succeed without the broad and active participation of commercial banks. A resumption of net new lending at a reasonable pace...ultimately provides the best protection for the value of outstanding loans...." Likewise governments and parliaments are called upon to take a positive attitude towards the replenishment of the loan program of the International Development Association (IDA VIII) as well as towards a general capital increase of the World Bank. It is of great importance that the realization of the Gramm-Rudman-Hollings Amendment and the effort to reduce the U.S. budget deficit will be accompanied by U.S. determination of the right priorities.

The Tokyo summit signaled progress in international economic cooperation. But some quite dangerous imbalances and challenges remain to be overcome. This requires that we all continue to do our homework well and at the same time coordinate our efforts internationally. Only then will next year's economic summit in Italy be able to take note of a further improvement of the world economy.