Introduction

At a conference in the *Palais des Nations*, in Geneva, Switzerland, representatives of 23 countries met from April to October 1947 and established two key pillars of the postwar world trading system. First, they created a legal framework for commercial policy by finalizing the text of the General Agreement on Tariffs and Trade (GATT). Second, the Geneva participants negotiated numerous bilateral agreements to reduce import tariffs, the benefits of which were extended to other GATT parties through the unconditional most-favored nation (MFN) clause. As a result, this landmark meeting produced a framework for postwar commercial relations in which governments agreed to rules about the use of certain trade barriers and to negotiate tariff reductions with one another. This system of multilateral cooperation has proven to be an enduring regime under which international trade has flourished for over half a century.

This book examines the origins of the GATT. There are many studies of the GATT from legal and economic perspectives, but relatively few that examine how the GATT emerged from the ashes of World War II. The goal of our study is to appreciate the original goals and intentions of its founders by reviewing the diplomatic history that gave rise to this remarkable agreement, and to understand why the GATT took the particular shape and form that it did, in terms of the various provisions included in or excluded from the text.

Chapter 1 focuses on the negotiations between the United States, the United Kingdom, and other countries during and immediately following World War II that led to the Geneva conference. The GATT grew out of discussions between government officials from the United States and the United Kingdom during the war. After seeing international trade stifled under the weight of protectionist measures during the 1920s and 1930s, officials from both countries had a compelling interest in pursuing policies that would reduce trade barriers and help expand world trade after the war. They sought to foster a more liberal trade system by developing a broad set of rules that would restrict the arbitrary use of trade restrictions, as well as initiate the process of negotiating reductions in existing trade barriers.

While the U.S. and UK governments agreed on the most important and basic principles to be included in a trade agreement, they differed on many substantive details that affected the shape of the GATT. Once these two countries agreed on a document that could serve as a basis for negotiation, other countries were invited to participate in shaping the provisions of the GATT and the charter for an International Trade Organization. Drawing on archival documents, the diaries and memoirs of participants, published and unpublished cable traffic and government memoranda, as well as many secondary sources, we aim to shed light on the political constraints on both sides of the Atlantic that affected the commercial-policy discussions.

Chapter 2 examines the evolution of the GATT as a legal text. The first draft of a proposed charter for an International Trade Organization (ITO) emerged from the State Department in August 1944. The first publicly released draft of the charter was published by the State Department in December 1945 on the basis of bilateral U.S.-UK discussions during the British loan negotiations. A revised draft emerged at the conclusion of multilateral consultations in London from September-December 1946. Officials in London appointed a drafting committee, which met at Lake Success, New York, in January-February 1947, to produce a formal draft of both a General Agreement on Tariffs and Trade and a charter for an International Trade Organization for consideration at the April 1947 Geneva meeting. This chapter traces how the provisions of the GATT evolved as a result of these meetings, and how the composition of the countries involved at each stage affected the specific details in the GATT text and shaped the form that it ultimately took.

In Chapter 3, we assess the GATT in light of recent economic and political theories that seek to understand the specific rationale for the existence of trade agreements. These theories include the idea that the GATT is motivated by terms of trade externalities across countries, by governments seeking external commitments to reduce the power of domestic interest groups, and by broader foreign policy and national security considerations. This chapter uses the history developed in the previous chapters to enhance our understanding of the motivations (sometimes different across countries) for why they chose to sign an international agreement on commercial policy.

In addition, we present an annex with key official documents whereby the reader can trace the evolution of government proposals and negotiating strategies that eventually produced the GATT in 1947. Annex A consists of documents that give us important insight into the American and British positions regarding a trade agreement. This includes such items as a short memorandum prepared in

1942 by an economist working in the Economic Section of the War Cabinet, James Meade, which was perhaps the first official government document that explicitly envisioned a multilateral commercial agreement after the war, to various State Department cables that reveal the thinking of key officials as the negotiations evolved. Annex B includes the participants in the various committees and subcommittees that were established during the negotiation of the GATT.

The legal and diplomatic record of the 1940s is enormous and many interrelated issues were considered simultaneously by government officials. We strive to limit our focus to a narrow but important part of the bilateral U.S.-UK relationship, i.e., the commercial-policy discussions that led to the GATT. We do not address related issues, such as the 1944 Bretton Woods negotiations on the international monetary system, the British loan of 1945, or even the difficult 1947 Geneva negotiations over trade barriers and the major dispute over imperial preferences, except to provide background as they relate to the provisions of the GATT. Furthermore, given our exclusive focus on the GATT, we do not examine the ultimate failure of the ITO, a subject considered in greater detail by Diebold (1952), Aaronson (1996), Odell and Eichengreen (1996), and Zeiler (1999).

There is an abundance of excellent work on the GATT, yet many of the standard references take the GATT 1947 as their point of departure, giving only a cursory sketch of the events that gave rise to it. For example, the classic works of John Jackson (1969), Kenneth Dam (1970), and Robert Hudec (1975), have analyzed the GATT as an international legal text, and other important books, such as Gerard Curzon (1965) and Karin Koch (1969), have examined the early activities of the GATT as an international organization. Yet both types of work take the GATT as given and focus less on its origins or where the text originated.

Our work builds on the classic work of Richard Gardner, *Sterling-Dollar Diplomacy* (1956). Gardner was one of the first scholars to consider the Anglo-American economic negotiations during World War II, and his book has stood the test of time for clarity and insight. While he focuses on both the monetary and trade discussions, we focus exclusively, and in somewhat greater detail, on the trade negotiations and texts. Later works, particularly Thomas Zeiler's *Free Trade, Free World: The Advent of GATT* (1999), also examine in great detail the diplomatic maneuvering and national motivations in the negotiations that led to the GATT, as do Miller (2003) and Toye (2008). Susan Ariel Aaronson's *Trade and the American Dream: A Social History of Postwar Trade Policy* (1996) is also a notable, archival-based examination of U.S. trade-policy formation in the 1940s.[1] These works, however, tend to avoid discussion of the specific provisions

1 There are also several country studies of trade policy, such as for Australia (Capling 2001) and Canada (Hart 1993, Rasmussen 2001), that examine how these countries responded to U.S.-UK proposals during the 1940s.

Cambridge University Press
978-0-521-51561-0 - The Genesis of the GATT
Douglas A. Irwin, Petros C. Mavroidis and Alan O. Sykes
Excerpt
More information

that eventually comprised the GATT text. While our book also does not aim to be a definitive history of the origins of the GATT, we hope it provides a deeper understanding of the basis for this important agreement.

We also hope that this book, which has been published shortly after the 60th anniversary of the 1947 Geneva conference that established the GATT, serves as a reminder of the remarkable and long-lasting achievements made just a little over half a century ago.

1 The Creation of the GATT

1.1 After the First World War

To understand the origins of the GATT, one must appreciate the traumatic events of the 1920s and 1930s. The period between World War I and World War II was a political and economic disaster, scarred by the Great Depression and the rise of fascism. A strong desire to avoid repeating this experience after World War II, along with the abandonment of isolationism by the United States in favor of a leadership role in world affairs, fostered support around the world for a new approach to international economic cooperation.

The outbreak of World War I in 1914 interrupted what had been a period of growing worldwide economic prosperity with moderate tariffs and expanding world trade supported by a well-functioning international monetary system (the gold standard). After the shock of World War I, the international trade and payments system recovered very slowly during the 1920s. Most countries only gradually phased out wartime controls on trade, while tariff levels remained higher than before the war. The United Kingdom did not return to the gold standard until 1925, and other countries waited even longer before restoring the convertibility of their currencies. Under the auspices of the League of Nations, the World Economic Conference of 1927 aimed to return the world economy to its previous state of vigor. But the Conference only started an international discussion of matters such as tariff levels, most-favored-nation clauses, customs valuation, and the like.

The gradual restoration of the world economy was interrupted by a worldwide recession starting in 1929. This economic downturn was met by greater protectionism, which in turn further reduced world trade. Although monetary and financial factors were primarily responsible for allowing the recession to turn into the Great Depression of the early 1930s, the spread of trade restrictions aggravated the problem. The commercial policies of the 1930s became characterized as "beggar-thy-neighbor" policies because many countries sought to insulate their own economy from the economic downturn by raising trade barriers. Blocking imports proved to be a futile method of increasing domestic employment because one country's imports were another country's exports. The combined effect of this inward turn of policy was a collapse of international trade and a deepening of the slump in the world economy.[1]

The United States bore some responsibility for this turn of events. What started out in 1929 as a legislative attempt to protect farmers from falling agricultural prices led to the enactment of higher import duties across the board in 1930. The Hawley-Smoot tariff of that year pushed already high protective tariffs much higher and triggered a similar response by other countries. According to the League of Nations (1933, 193),

> the Hawley-Smoot tariff in the United States was the signal for an outburst of tariff-making activity in other countries, partly at least by way of reprisals.

Canada, Spain, Italy, and Switzerland took direct retaliatory trade actions against the United States, while other countries also adopted higher tariffs in an attempt to insulate themselves from the spreading economic decline. The United Kingdom made a sharp break from its traditional free-trade policies by imposing emergency tariffs in 1931 and enacting a more general Import Duties bill in 1932. France and other countries that remained on the gold standard long after others had abandoned it for more reflationary policies imposed import quotas and exchange restrictions in an attempt to safeguard their balance of payments and stimulate domestic economic activity.

Many countries also turned to discriminatory trade arrangements in the early 1930s, both for economic and political reasons. At a conference in Ottawa in 1932, the United Kingdom and its dominions (principally Australia, Canada, New Zealand, and South Africa) agreed to give preferential tariff treatment for one another's goods. This scheme of imperial preferences involved both higher duties on non-British Empire goods and lower duties on Dominion goods and drew the ire of excluded countries for discriminating against their trade. Meanwhile, under the guidance of Reichsbank President Hjalmar Schacht, Nazi Germany concluded a series of bilateral clearing arrangements with central European countries that effectively created a new trade bloc, orienting the trade of these countries toward Germany at the expense of others. In Asia, Japan created the

[1] See the League of Nations (1942), Kindleberger (1986), Kindleberger (1989), and James (2001).

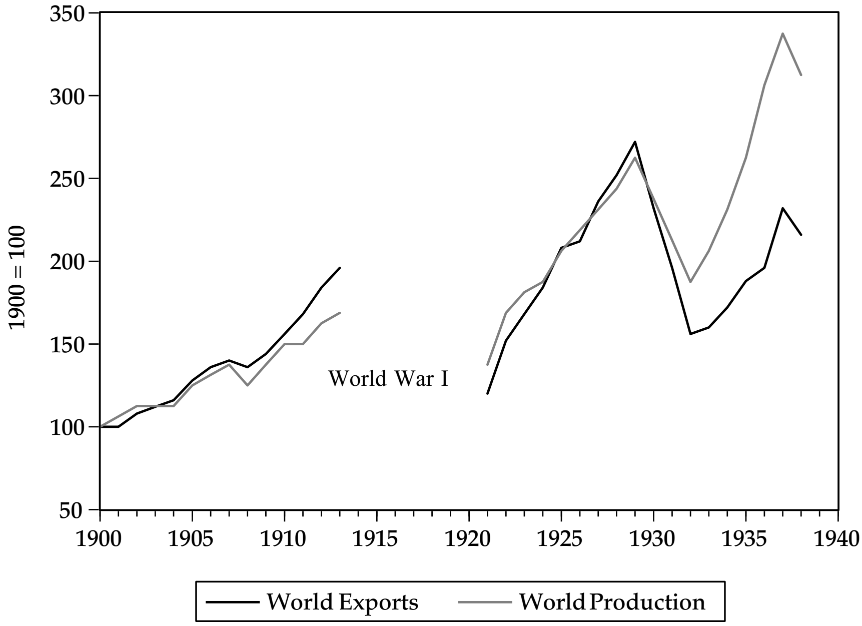

Figure 1.1. The Volume of World Trade and Production, 1900–1938. *Source:* Norbom (1962).

Greater East Asia Co-Prosperity sphere to extend its political and economic influence throughout the region and siphon off trade for its own benefit.

The outcome of these protectionist and discriminatory trade policies was not just a contraction of world trade, but a severe breakdown in the multilateral trade and payments system that the world economy had enjoyed prior to World War I and had started to revive in the late 1920s. Official conferences and multilateral meetings, notably the World Economic Conference in 1933, offered pronouncements to resist protectionism, but failed to stem the spread of inward-looking antitrade economic policies. The economic distress of the decade also had political consequences, undermining faith in democratic governments to manage their economies and hence abetting a turn to more authoritarian regimes in Germany and elsewhere.

Figure 1.1 shows the level of world exports and world production from 1900 to 1938. Although trade tended to grow faster than production prior to World War I and even in the 1920s, it collapsed to a much greater extent in the early 1930s. Even more important, having been saddled with a new and heavy layer of trade restrictions, world trade failed to rebound significantly after the recovery had begun. Even by 1938, world trade was still well below its 1929 peak. The growth of protectionist measures had stifled world trade and thereby, in the minds of many economic officials, hindered a full and complete recovery from the Depression.

However, having initiated the move toward greater protectionism in the 1930s, the United States also became one of the first countries to try to reverse these detrimental developments. For the first time in its history, the United States began to take a serious and active role in reducing trade barriers and expanding world trade in cooperation with other countries. After the Republican party that was responsible for the Hawley-Smoot tariff in 1930 was swept from office in the 1932 election, the Democratic administration of President Franklin D. Roosevelt formulated a new approach to trade policy. Recognizing that it could not undertake a unilateral reduction in American tariffs in the midst of the depression, the Roosevelt administration sought to negotiate bilateral trade agreements to reduce tariffs in concert with others. In 1934, the Democratic-majorities in Congress enacted the Reciprocal Trade Agreement Act (RTAA), which allowed the President to reduce American tariffs by up to 50 percent in the context of bilateral trade agreements that employed the unconditional most-favored-nation (MFN) clause. With this authority, originally granted for three years and subsequently renewed, the Roosevelt administration concluded more than 20 trade agreements during the 1930s.

Although these agreements had a limited effect in boosting world trade during the tumultuous 1930s, the RTAA marked a new beginning for U.S. trade policy, shifting it in a more liberal direction. The RTAA changed the course of American trade policy in several ways.[2] First, by enacting the RTAA, Congress effectively gave up the ability to legislate duties on specific goods when it delegated tariff negotiating power to the executive. Congressional votes on trade policy were now framed simply in terms of whether or not (and under what circumstances) the RTAA should be continued, so vote trading among particular import-competing interest groups was no longer possible. In addition, the national electoral base of the President is often thought to make the executive more likely to favor policies that could benefit the nation as a whole (such as open trade), whereas the narrower geographic representative structure of Congress would lead its members to have more parochial interests. For instance, the President may be more likely than Congress to take into account the broader foreign-policy ramifications of trade policy that affect the country as a whole.

Furthermore, the RTAA reduced the threshold of political support needed for members of Congress to approve executive tariff-reduction agreements. The renewal of the RTAA required a simple majority in Congress, whereas prior to the

2 The academic literature on the RTAA is quite large. See Haggard (1988), Bailey, Goldstein, and Weingast (1997), Hiscox (1999), Irwin and Kroszner (1999), and Schnietz (2000).

RTAA any foreign-trade treaty negotiated by the President had to be approved by two-thirds of the Senate. Tariff-reducing agreements thus needed only the support of the median legislator, not that in the 67th percentile. This meant that protectionist forces would have to muster greater support to block tariff-reduction agreements under the RTAA, by refusing to renew the legislation, than under a treaty, when a minority could (and frequently did) veto it.

Finally, the RTAA helped to bolster the bargaining and lobbying position of exporters in the political process. Previously, import-competing domestic producers were the main trade-related lobby group on Capitol Hill since the benefits to these producers of high tariffs was relatively concentrated. Exporters were harmed indirectly by these tariffs, but the cost to exporters of any particular duty was relatively diffuse, and therefore exporters failed to organize an effective political opposition. The RTAA bundled foreign tariff reductions that were beneficial to exporters with lower tariff protection for import-competing producers. By directly linking lower foreign tariffs to lower domestic tariffs, the RTAA may have fostered the development of exporters as an organized interest group opposed to high tariffs and supporting international trade agreements.

The key figure behind this shift in U.S. trade policy was Cordell Hull, Roosevelt's Secretary of State. Hull was a southern Democrat, a politician from a region and party that had traditionally and strongly supported low tariff barriers to trade. As a member of Congress during World War I, Hull grew to appreciate the global ramifications of domestic tariff policy. In his memoirs, Hull (1948, 84, 81) recalled:

> When the war came in 1914, I was very soon impressed with two points. . . . I saw that you could not separate the idea of commerce from the idea of war and peace. . . . [and] that wars were often largely caused by economic rivalry conducted unfairly. . . . But toward 1916 I embraced the philosophy that I carried throughout my twelve years as Secretary of State. . . . From then on, to me, unhampered trade dovetailed with peace; high tariffs, trade barriers, and unfair economic competition, with war. Though realizing that many other factors were involved, I reasoned that, if we could get a freer flow of trade – freer in the sense of fewer discriminations and obstructions – so that one country would not be deadly jealous of another and the living standards of all countries might rise, thereby eliminating the economic dissatisfaction that breeds war, we might have a reasonable chance for lasting peace.

As a result, Hull was an early advocate of international cooperation on trade matters. In 1916, he called for the establishment of a permanent international congress that would consider

> all international trade methods, practices, and policies which in their effects are calculated to create destructive commercial controversies or bitter

> economic wars, and to formulate agreements with respect thereto, designed to eliminate and avoid the injurious results and dangerous possibilities of economic warfare, and to promote fair and friendly trade relations among all the nations of the world (Hull 1948, 81–82).

The spread of illiberal trade policies and rise of international tensions in the 1920s and early 1930s confirmed to Hull the lessons he had learned during World War I. As he declared in 1937:

> I have never faltered, and I will never falter, in my belief that enduring peace and the welfare of nations are indissolubly connected with friendliness, fairness, equality and the maximum practicable degree of freedom in international trade (Dam 1970, 12).

Having been chosen by Roosevelt to serve as Secretary of State, Hull was uniquely positioned to pursue his belief that freer trade might lead to economic and political conditions that would be more favorable to peace. Hull fought a long and hard bureaucratic battle to ensure that the official U.S. government position on international-trade policy was his State Department's vision of a world more open to trade and free from discriminatory commercial policies.[3] Hull helped design the RTAA and led the fight for its passage by Congress. The administration requested Congressional authority to reduce tariffs by no more than 50 percent on a selective, product-by-product basis to avoid injuring domestic industries. The goal was not ''free trade'' in the sense of zero tariffs, then an inconceivable objective, but simply to reduce ''excessive'' tariffs and allow some additional growth in foreign trade.

Hull was an especially sharp critic of imperial preferences because of their adverse effect on U.S. exports, particularly to the United Kingdom and Canada, two of America's most important markets. Testifying before Congress in 1940, Hull called imperial preferences ''the greatest injury, in a commercial way, that has been inflicted on this country since I have been in public life'' (Gardner 1956, 19). Hull particularly desired a trade agreement with the United Kingdom and Canada to reduce the discriminatory effect against U.S. exports. In 1938, the United States and the United Kingdom signed a reciprocal trade agreement, but the negotiation was difficult and the results were limited. Despite Hull's best efforts, the agreement failed to put a dent in Britain's system of tariff preferences.

[3] At least initially, the Roosevelt administration was deeply divided between internationalists in the State Department, foremost among them Secretary Hull, and economic nationalists elsewhere who supported the New Deal program of government price supports (in agriculture and through industrial codes) that might be undermined without controls on imports. For a study of Hull and the early trade-agreements program, see Butler (1998). Allen (1953) also examines Hull's trade beliefs.