MONETARY

B. STRENGTHENING THE INTERNATIONAL MONETARY SYSTEM

1. Special Drawing Rights and the Adjustment Process

The years 1960 through 1963 saw a gold crisis and (1961) repeated speculation against the pound sterling and the dollar. There also were numerous international efforts to strengthen individual currencies and buttress the gold-exchange system. They included establishment of the London Gold Pool, in October 1961, and of the General Arrangements to Borrow, activated in October 1962 by the Group of Ten, i.e., major industrial members of the International Monetary Fund (IMF) which were associated in efforts to increase the financial resources available to defend the stability of the existing international monetary system.

In mid-1962 there was a substantial heightening of attention to the longer-term form and functioning of the international monetary system. New plans were proposed for modifying and reforming the existing structure, such as Britain's Maudling (Mutual Currency Account) Plan to improve currency support operations and international liquidity, and the Posthuma plan for harmonization of reserve asset use (aimed at avoiding speculative shifts from one type of reserve asset into another). In October 1963 the Group of Ten undertook an examination of the outlook for the functioning and probable liquidity needs of the international monetary system. This atmosphere of uncertainty, regarding both the short and long-term viability of the existing international monetary structure, prevailed at the time when the Johnson Administration began.

The United States was a very active participant in Group of Ten deliberations. Within the US Government the main forum for consideration of liquidity and adjustment process questions in the early stages was the Long Range International Payments Committee (LRIPC), formed in October 1962. The LRIPC included representation from the Department of State and Treasury, the Council of Economic Advisers and the Federal Reserve Board. The voluminous records of the LRIPC document abundantly the US Government deliberations on all aspects of these matters.[1/]

In 1964 the Group of Ten also recommended that a Working Party (WP-3) of the OECD conduct a study of the process of international balance of payments adjustment. Gradually this subject became the primary focus of the LRIPC, which concluded its meaningful functioning in June 1966, just prior to the completion of the WP-3 report on the adjustment process, issued in August 1966.[2/]

Meanwhile, the deepening difficulties of the pound sterling and the recurrent threats to international monetary

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1/ A brief summary of the five subsequent years of Group of 10 and IMF discussions and negotiations is contained in "Maintaining the Strength of the United States Dollar in a Strong Free World Economy," a Treasury publication, January 1968, pages 46-50. A fairly detailed account of the history and issues involved in these international discussions and negotiations is contained in a Department of State paper, "International Monetary Reform and the European Communities," Research Memorandum #REU-66, December 27, 1967 (~~SECRET/~~NO FOREIGN DISSEM/ CONTROLLED DISSEM).

2/ The Balance of Payments Adjustment Process. A Report by Working Party No. 3 of the Economic Policy Committee of the OECD, August 1966 (UNCLASSIFIED).

stability prompted the commencement of a contingency planning effort. This was initiated by President Johnson's Secret Memorandum of June 16, 1965.[3/] Aimed at intensification of the LRIPC efforts in the international monetary reform and liquidity fields, a special Study Group chaired by Treasury's Under Secretary for Monetary Affairs, Frederick L. Deming, was established with senior representation from five agencies including the Department of State (known as the Deming Group). In this more senior and much more restricted group, if an agency's principal representative were not available to attend, alternates were not permitted to substitute, so closely held were its deliberations. This Group consulted frequently with highly competent and respected professionals from academic and business circles, known formally as the Advisory Committee on International Monetary Arrangements and informally as the Dillon Committee, after its chairman, former Treasury Secretary C. Douglas Dillon.

3/ Memorandum from President Johnson to Treasury Secretary Henry Fowler dated June 16, 1965 ~~(SECRET)~~.

The State Department took an early lead in calling special attention to the problem of defining responsibility in the adjustment process, particularly with reference to the need of guidelines to encourage the surplus countries to take on a greater share of the balance of payments adjustment burden.[4/] Guidelines of this general nature were subsequently supported by the United States and through forceful representation of them were reflected also in the Report of Working Party 3 of the OECD on the adjustment process, issued in August 1966.

The Department of State pursued this matter of the adjustment process further when, late in 1965, it provided the LRIPC with a study showing the inconsistency of the balance of payments aims of OECD countries with the prospective increases in international liquidity under the existing monetary system.[5/] The Department of State

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4/ LRIPC Paper #88, November 21, 1963 "Responsibilities of Deficit and Surplus Countries" (LIMITED OFFICIAL USE).

5/ LRIPC 65-64, dated 12/3/65, "Brief Comments on Balance of Payments Aims" (LIMITED OFFICIAL USE).

stressed that these aims showed the importance of the current liquidity discussions and the need for the United States to press for procedures for international consultations on balance of payments objectives with a view to dealing with these inconsistencies.

In the initial stages of US deliberations on the liquidity problem, the Department contributed papers focusing on the problems of adapting the IMF to meet the liquidity needs and on the need for lengthening the maturities of financial assistance available to countries needing help in the adjustment process.[6/] As the Group of Ten Study Group neared completion of its report in early 1965 the Department was concerned over the fact that the US Government was lagging in the formulation of its own position on this subject. The Department first raised the matter in the LRIPC and urged

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6/ LRIPC 116, The IMF and World Liquidity, dated 12/31/63, (LIMITED OFFICIAL USE); LRIPC 117, Long-Term Lending and the International Monetary System, 12/31/63 (LIMITED OFFICIAL USE); LRIPC 64-24, The International Monetary Fund in the International Monetary System, 3/18/64 (LIMITED OFFICIAL USE).

that a position be developed before mid-year. Subsequently, Under Secretary George Ball discussed the question directly with Treasury Secretary Fowler.7/

On July 10, 1965, Secretary Fowler issued a call for an international conference to be convened on the subject of international liquidity. The Department of State at that time expressed its concern that any planning for creation of additional liquidity must provide for participation of less developed countries (LDCs) and make provision for their liquidity needs. A letter from Under Secretary Ball to Secretary Fowler dated August 24, 1965, provided the Department's views on organization of the conference with these aims in mind. The Department was particularly dissatisfied with the position generally espoused by members of the Dillon Committee that LDCs should not be full partners in such a liquidity plan. This position was rendered still

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7/ Memorandum from Assistant Secretary for Economic Affairs Anthony M. Solomon to Under Secretary George Ball, dated April 30, 1965 ~~(SECRET).~~

more disturbing by the fact that the Europeans were opposed to equal partnership of LDCs and that the Treasury Department, being more concerned with other issues involved, would, it was felt, be willing to yield to the Europeans on this point in bargaining for other objectives. An illustration of the Department of State's efforts to establish a firm US position on LDC participation was provided by a memorandum to the Committee by Assistant Secretary Solomon.[8/] In the event, the views of the Department of State prevailed.

Under Secretary Ball accompanied Secretary Fowler in August 1965 on a lengthy trip to all major Western European capitals, during which US views on the value of an international conference on liquidity were set forth to European financial authorities.

8/ Memorandum from Assistant Secretary of State Solomon to members of the Advisory Committee on International Monetary Arrangements dated October 18, 1965 (LIMITED OFFICIAL USE); further background on the Department's views is contained in a Solomon Memorandum to Under Secretary Ball dated October 15, 1965 (LIMITED OFFICIAL USE).

As negotiations progressed and increasingly technical matters came to the fore, the Department of State, while continuing to participate actively in policy formulation, found itself in general agreement with all but minor technical and tactical aspects of US policy as it was being developed under the leadership of the Treasury Department.

2. Supporting the Existing System

a. The Italian Crisis

In 1963 the Italian postwar economic "miracle" finally got out of hand. Inflation became rapid and excess demand spilled over into imports. Although Italy had ample reserves to deal with the immediate deficit (almost $4 billion at the beginning of 1963), doubts of its ability to apply the economic brakes and stop the outflow under a center-left government caused considerable nervousness and encouraged speculators. The country lost $1 billion in reserves between September 1963 and March 1964. Italy's Common Market partners insisted upon stronger deflationary measures as a condition to their support for the lira.

As a result, in mid-March of 1964, Bank of Italy Governor Carli came to the United States; and in Under Secretary of the Treasury Roosa's office a rescue package of $1 billion in US Treasury and European central bank standby credits was quickly put together. The US share of the standby credit (actually a Treasury rather than a Federal Reserve credit) was $550 million. At the same time, $200 million in Export-Import credits and $250 million credit line for Commodity Credit Corporation sales were also arranged.

This massive support, combined with the progress Italy was beginning to show in correcting its short-lived structural imbalance on trade account, quickly reversed the flow. The standby credits were never used, and only small amounts of the Export-Import and CCC credits were used. Thus the display of international financial solidarity sufficed to make a valuable contribution to international financial stability and order.

b. Defense of Sterling

US leadership in the defense of the pound sterling has been one of the most important continuing chapters in the history of postwar international economic cooperation. This defense is critical in view of the role of the pound as an important reserve currency under the fixed exchange rates of the gold-exchange standard. Under the security of fixed exchange rates, international trade has prospered in the postwar period as never before. Because of Britain's position as banker for the sterling area, the pound is a key currency in the international system, but Britain's inability to inspire confidence in its long-term economic future has led to recurrent speculation against the pound. Lack of confidence in or stability of the pound threatens the entire system of fixed exchange rates.

The sterling crisis of 1961 was followed by two years of improving UK balance of payments, but several factors, including unsupportably rapid growth at home, led to a deterioration in the balance of payments throughout 1964. For most of the year, this deterioration had little apparent effect on exchange-rate confidence; through most of the first three quarters of 1964 the pound stayed above $2.79 and required little support. The British Government, however, became sufficiently concerned with the trend to impose a 15 percent temporary surcharge on imports on October 26, 1964. The US Government recognized the necessity for this action and supported it, but both publicly and in bilateral consultations we expressed the hope that the British would remove the surcharge as soon as possible.

The international financial community soon felt that the surcharge alone was insufficient to protect the British balance of payments. In particular, it was felt that an increase in the bank rate from the existing 5 percent was required. When Thursday (the traditional day for announcing bank rate changes) November 18 passed without a change in the bank rate, the run on sterling began. On Tuesday the 23rd the rate was belatedly raised to 7 percent, but the move was too late and the hemorrhage continued. Hastily, the United States took the lead in arranging a $3 billion package of credits from the United States and other Group of Ten members plus Austria. The US share was $1 billion, of which $750 million was a swap of dollars for sterling by the Federal

Reserve, and $250 million an Export-Import Bank loan.

This massive support turned the speculative outflow into an inflow and saved the pound. In the course of a trip to Europe in September 1965, Under Secretary of State Ball personally took the initiative on behalf of the US Government in negotiating an additional $925 million package of credits furnished by the US and European central banks (excluding France, from which $75 million had been planned). The US share of this multilateral arrangement was $400 million.[9/] It was renewed in June 1966. By mid-1966, the British announced that they had repaid all their short-term debts to foreign central banks, but a variety of support-oriented credit from the United States still totaled around $500 million.

To strengthen its reserve position, the UK began in April 1965 to liquefy its portfolio of equity and long-term US securities. To "liquefy" meant converting a large part of its portfolio to short-term securities, thus exacerbating

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9/ Memorandum from Deputy Assistant Secretary Cooper to Assistant Secretary of State Solomon, October 8, 1965.

the US balance of payments outflow. For 1964 the impact was about \$650 million.[10/] On March 1, 1966, the UK announced that it was adding \$825 million obtained from such liquidations to its reserves. This left about \$500 million in its portfolio.

Although Britain's indebtedness position had improved, the first half of 1966 was disappointing from a balance of payments standpoint. The trade gap had widened ominously, and the pound was again under pressure. A large part of the pressure was the result of very high interest rates in the United States which made covered lending in Britain unattractive. Britain responded by a tough economic policy, including a six-month freeze on wage and dividend increases. The United States assisted the strengthening of the pound by increasing its swap line with the UK by \$600 million, to \$1,350 million, on August 31, 1966. The Department of State successfully resisted a Defense Department suggestion that the United

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10/ Memorandum from Deputy Assistant Secretary Cooper to Assistant Secretary of State Solomon, September 15, 1965.

States pick up the $200 million tab for Britain's East of Suez annual military expenditures in order to keep a UK presence there, despite the payments problem. In the State Department's view the proposal was unnecessary and the recommended course would probably have been ineffective.[11/]

Again the pound survived, and, partly as a result of the severe deflationary measures taken in the UK around mid-year, the balance of payments went into surplus towards the end of 1966.

For several reasons, the situation again reversed itself in the first half of 1967. The Arab-Israel war in June 1967 and its aftermath caused large withdrawals of sterling as well as increased import costs (largely for petroleum) and decreased exports. During the third quarter, Britain was compelled to support sterling very heavily, and in doing so drew $425 million on its swap lines with the United States, bringing the outstanding balance to $650 million. By November, speculative pressure against the pound had become intense

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11/ Assistant Secretary Solomon's Memorandum to Secretary Rusk, July 22, 1966.

and the British, after consultation with the United States, other Group of Ten countries and the IMF, decided it was impossible to hold the $2.80 rate any longer. On November 14 they set a new rate of $2.40. As part of the arrangements surrounding the devaluation, the United States increased the swap line to $1.5 billion on November 30 and in concert with central banks of some European countries extended a $250 million loan to enable Britain to repay the final installment on its 1964 IMF loan.

Once devaluation was accomplished, it became the concern of the United States to keep it confined to as few countries as possible so that the stability of the international monetary system would not be seriously threatened nor the advantage to the UK eroded. This effort was very successful; few countries outside the sterling area devalued and no major trading country followed Britain's lead.

Subsequently, the United States took the lead in an effort to give greater stability to the pound by a $2 billion contingency arrangement by the United States and 11 other countries plus the Bank for International Settlement to fund possible withdrawals by official holders of the sterling balances (presumably these are the more volatile parts of the sterling balances). Britain was to receive credits from the participating countries for declines in the sterling balances that could not be attributed to its own deficit.

c. The Gold Crisis of 1968

Prior to October 1961, exchanges of gold took place between monetary authorities in official transactions and also in free markets used by industrial buyers, speculators, hoarders and certain monetary authorities alike. In the latter markets, prices fluctuated in line and with supply and demand conditions. Particularly after 1958, the large US balance of payments deficits began to arouse concern in many quarters and to generate a feeling that corrective policies were needed. In addition, foreign governments and central banks became more reluctant to hold all of the dollars they were accumulating and, on occasion, they asked to buy gold from the United States. In late 1960 there were rumors about the possibility of an increase in the price of gold, which led to a very substantial increase in the demand for gold. The free market price of gold rose as high as $41 an ounce. The United States arranged for the Bank of England to sell US gold in London in order to stabilize gold markets and discourage speculative pressures. The gold price rally was fairly short-lived, but the US gold sales accelerated the rate of decline in our gold reserves, bringing a decline of $1 billion during the fourth quarter of that year alone, and $1.7 billion for the year 1960 as a whole. It was also in 1960 that the United States experienced its largest balance of payments deficit to date, of $3.9 billion.

In an effort to get other countries to share the burden of stabilizing the principal free gold market in London, the United States undertook negotiations which led to the formation in October 1961 of the Gold Pool of eight nations, which, in accordance with agreed shares, contributed gold for sales on the free market to keep the price there in line with the official monetary price of $35 an ounce. Subsequently the arrangement was expanded to cover purchases as well as sales. The Gold Pool was highly successful and in fact purchased more gold than it sold during the four years following its formation.

Only in 1965 did the Pool begin to make substantial net sales of gold, a trend that persisted through 1966 and on into 1967. Early in 1967 the Department of State began contingency studies of the problem, since it appeared that changes would eventually be necessary in international gold markets. One proposal studied in February 1967 involved a split price or two-price system of gold marketing. In the fall of 1967 interagency consideration of the gold market problem intensified as the result of growing pressures on sterling and discontent within the Gold Pool. In October Assistant Secretary of State Solomon sent a memorandum to Treasury Under Secretary Deming transmitting two proposals from the Department of State: one a proposing unitary price system, involving limitation on access to the major gold markets, and the other a proposing split price system.[12/] These proposals were considered by the Deming Group, but were not acted upon at that time.

During the fourth quarter of 1967, in connection with the sterling crisis and devaluation of sterling which took place during that period, the United States again suffered major gold losses, finally totaling more than $1 billion. In the early months of 1968 considerable speculation in gold continued, due to: (1) reaction to the record US fourth quarter balance of payments deficit of $1.7 billion; (2) scepticism as to the adequacy of UK measures to ensure the success of the British devaluation; and (3) growing rumors, encouraged by the French, about the possibility of an increase or even doubling of the price of gold. As the

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12/ Memorandum from Assistant Secretary of State for Economic Affairs Anthony M. Solomon to Treasury Under Secretary for Monetary Affairs Frederick L. Deming, "Alternative Proposals on Gold," October 27, 1967 ~~(CONFIDENTIAL).~~

crisis reached a climax in early March, Assistant Secretary Solomon met almost continuously with Treasury, White House and Federal Reserve Board officials. The outcome of these discussions was a decision to negotiate with the London Gold Pool members a two-tier system of gold transactions and pricing - an official monetary tier at $35.00 an ounce and a free market with a fluctuating gold price. This negotiation was successful; it led to the March 17 communique which announced the establishment of a two-tier system and stated the intention of the participants to consider the present monetary gold reserves adequate, as well as their judgment that it would not be necessary to add to these reserves through further purchases in the free market. The participants appealed at that time for the cooperation and participation of the monetary authorities of the world in this new system. The two-tier system as it was outlined in the communique was essentially the same as the split price system proposed six months earlier by the Department of State.

d. Support of the Franc

The strikes and general unrest in France during May 1968 caused a seriously aggravated deterioration of France's trade balance and an alarming flight from the franc. The French trade balance reversed itself from a $153 million surplus in the first half of 1967 to a $350 million deficit in the first half of 1968, while reserves declined by about $2 billion during May, June, and early July. To add to the resources available for the defense of the franc, the United States helped arrange in the first week of July a $1.3 billion standby credit to France in cooperation with British and continental central banks. The US share was $700 million, of which $100 million was the existing swap line.

Doubts about the ability of the French to spend their way out of domestic difficulties without severe balance of payments consequences led to massive speculation against the franc. The situation was exacerbated by the simultaneous strength of the German balance of payments surplus and widespread belief that an upward valuation of the deutsche mark was likely. French reserves dropped alarmingly. To defend the franc and calm financial markets, France drew heavily on the July swap arrangements. By the last week in November, such drawings totaled \$1.091 billion, of which \$571 million was from the United States. Beyond this, the Bank of France was swapping heavily with French commercial banks. The exact amount is unknown but it is believed to have reached between \$600 million and \$1 billion.

To stem the outflow of funds from France and into Germany, the Group of Ten countries met in a crisis atmosphere in Bonn from November 20 to 22. This meeting resulted in an additional central bank facility for France of \$2 billion. Germany's share was \$600 million and the US share \$500 million. It was generally assumed that the French would immediately devalue and for a short time this appeared inevitable. However, De Gaulle chose to maintain the existing parity and to defend it through domestic austerity measures, including a cut in budgetary spending, comprehensive exchange controls, wage and price restrictions and a vigorous income tax collection policy. Tax changes to favor exports and discourage imports were also introduced. Just previously, the German Government announced measures to reduce border tax adjustments on both exports and imports which had the effect of a 4 percent upward valuation on industrial trade account. Although as of January 1969 considerable skepticism remains of the ability of either the French or the Germans indefinitely to defend their exchange rate parities, the crisis atmosphere has subsided.

3. Maintaining the Strength of the Dollar

As the executive branch primarily responsible for the formulation and conduct of US foreign policy, the Department of State had adopted the position that measures undertaken to strengthen the dollar must neither violate fundamental political-military responsibilities nor impair our overall strategic objectives. Efforts were made to ensure that foreign policy considerations--both of a political and of an economic nature--would be taken into account in framing measures to reduce the balance of payments deficits. In general, the Department opposed reductions of aid and overseas military programs for purely balance of payments reasons, any consideration of import or tourism restrictions, and, until late 1967 when the situation became critical, restrictions on flows of private capital to less developed countries (LDCs). The Department consistently preferred measures to reduce private capital outflows to industrialized countries, especially western Europe.

When, by December 1964, it became evident that large deficits would continue despite the Interest Equalization Tax (IET) and reductions in the Government overseas account, the Treasury Department made several proposals, including re-examination of targets for reductions in AID and defense spending and measures to reduce private capital outflows.

In addition, the possibility of applying the IET to long-term bank loans and to Canadian issues was raised. Finally, to restrain the losses on travel account, it was proposed as a "major backstop" to devise a tax on overseas tourism for possible implementation if efforts to promote the "See America Now" program should prove unsuccessful.

Many of the basic principles of the Department's policies regarding balance of payments measures to strengthen the dollar were set forth in a memorandum of December 9, 1964. This paper pointed out that further savings from military and aid programs would require basic and far reaching policy decisions. Consequently, improvement should be sought in the capital account. While the Department would concur in any proposal to renew the IET, reservations were expressed on closing the exemption on Canadian borrowing until all other possible alternatives had been thoroughly explored. Moreover, it was pointed out, application of the IET to long-term bank loans would adversely affect Japan, and a thorough study would have to be made to avoid a crisis there. Finally, doubts were expressed whether significant savings could be achieved by levying a tax on tourism; the political implications of such a proposal needed to be carefully weighed before a final decision was reached.13/

Although the President's 10-point program of February 10, 1965, continued the effort by AID and the Department of Defense to cut overseas dollar costs, the Department of State's policy proposals had in general been accepted. Canada remained exempt from the IET, and Japan, at the Department's suggestion, was given an exemption on new securities issued or guaranteed by the Japanese Government up to $100 million each. No proposal was advanced for a travel tax, but further encouragement was given to the "See the USA" program. Direct foreign investment by business in advanced countries was to be placed under a voluntary restraint. Diplomatic and Consular Posts abroad were instructed to inform host

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13/ Memorandum to The Under Secretary of State from Assistant Secretary G. Griffith Johnson on Meeting of the Cabinet Committee on Balance of Payments, December 9, 1964 ~~(CONFIDENTIAL).~~

governments of the program and to explain its background and rationale.[14/]

During the following period the Department's policy remained within the framework of the December 9 memorandum. Attempts were made to modify Federal Reserve guidelines on Bank Lending Targets by exempting the less-developed countries from the 5 percent bank lending target,[15/] but this proposal was not accepted. Posts were subsequently informed, however, that Federal Reserve Guidelines called for the highest priority on bank loans to be given less developed countries in the granting of bank nonexport credits. Since primary responsibility for implementation of the President's programs rested with Commerce, Treasury and the Federal Reserve, the Department of State's principal concern was to ensure that the

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14/ Department of State Circular Telegrams 1457 (on Presidential Message on Balance of Payments), February 9, 1965 (LIMITED OFFICIAL USE) and 1642, March 8, 1965 (UNCLASSIFIED).

15/ Memorandum to Mr. Thomas Mann and Mr. David Bell from ARA/LA/ECP - Mr. Donald Palmer on Bank Lending Target, March 3, 1965 (LIMITED OFFICIAL USE).

effects of the restraint on capital outflows would be felt by those countries which could afford them--the surplus countries of Western Europe. Efforts were maintained to detect adverse effects on the UK, Canada and Japan in addition to the less-developed countries and to prevent changes in the program which would result in serious foreign relations problems.[16/] The Department continually noted that the weakest point in the President's program was a fast increasing total of private direct investment outflows and urged the need to tighten the voluntary guidelines of the Commerce program in the developed countries.[17/]

In 1964 the Fowler Task Force Report proposed, *inter alia*, a multilateral approach, particularly through the OECD, to review member countries' regulations relating to the

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16/ Memorandum to The Acting Secretary from Richard Cooper on Principals' Meeting on Balance of Payments, November 24, 1965 (LIMITED OFFICIAL USE).

17/ Memorandum to The Secretary of State from Assistant Secretary Solomon on Talking Points with President on US Balance of Payments, October 26, 1965 (LIMITED OFFICIAL USE).

investment portfolios of financial institutions and restrictions on capital movements; and to work for the gradual lowering of foreign barriers to ownership of US securities. US representatives in the OECD had played a key role in concentrating attention on the need to improve capital markets abroad. As a result of initial US urging, in mid-1967 a Report on the Improvement of Capital Markets was published. US representatives also continued to urge the Committee for Invisible Transactions to work for the relaxation of restrictions on capital flows. In addition, Ambassador Trezise and OECD mission officers in connection with the Atlantic Institute and a senior official of the First National City Bank formulated the idea of holding a major conference of private businessmen and bankers on capital market problems. With the support of the Department of State and Treasury, the Atlantic Institute/BIAC (OECD Business and Industry Advisory Committee) Conference on capital markets was held in Cannes, January 19-22, 1967.

During 1965, discussions were held within the US Government concerning travel policy in light of the continual deficit in the travel account. A study was made in the Department of State, primarily by the Office of Aviation and the Office of International Finance and Economic Analysis which strongly opposed a "travel US Flag" policy.[18/] It was pointed out that such a policy would have a negligible immediate effect on the balance of payments, and, in the long run, a negative one, because of possible retaliation against US airlines and aircraft sales. The conclusions were accepted by the Executive Committee on Balance of Payments in May 1965. Instead, the Department suggested several programs to increase tourism in the United States, including US Government support for low excursion fares for traffic originating in Europe and lower fares by local carriers in the United States to foreign travelers.[19/] Some

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18/ Memorandum to the Bureau of Economic Affairs - Mr. Jacobson, from OFE - William Miller and OA - Allen Ferguson, on Travel Policy and the Balance of Payments, May 5, 1965 (LIMITED OFFICIAL USE).

19/ Memorandum to The Under Secretary of State from Assistant Secretary Solomon on A Positive Approach to Improve the Effect of Travel on US Balance of Payments, October 27, 1965 (LIMITED OFFICIAL USE).

consideration was also given to the idea of restraining travel abroad through imposing either a flat rate or a progressive travel tax if the situation appeared to require some sort of mandatory program. Within the Department, however, some pointed out the dangers of possible economic and political retaliatory action by foreign governments. It was also noted that in the past the United States had argued with other countries that travel should not be restricted as a means to improve balance of payments problems, and that our adoption of such restrictions would be a complete reversal of previous US policy.[20]

After further examination, it was decided to oppose a subsequent Treasury proposal which would have taxed travelers $6 per day abroad for a maximum of 90 days. In addition to questions regarding the constitutionality of such a proposal, it was noted that the foreign policy repercussions from many

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20/ Memorandum to Assistant Secretary Solomon from Mr. Loy on Tourism - Possible Further Measures for Balance of Payments Improvement, February 24, 1966 ~~(SECRET)~~.

countries - especially Canada, Mexico and the UK - would undoubtedly be severe. Moreover, it was felt that any tax on travel should be in the context of mandatory restraints on investment flows.21/ The Department also opposed higher passport fees as ineffective, discriminatory (since passports are not required for travel to Canada or Mexico) and an infringement on the constitutional right to travel.22/

As part of its policy of encouraging voluntary restraints on foreign travel, the Department of State instructed its posts in April 1966 to utilize any opportunity which arose to suggest that business and other private organizations in the host country consider holding their annual meetings, conventions or conferences in the United States.23/ In addition, the Department enthusiastically

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21/ Memorandum to The Under Secretary from Mr. Solomon on Meeting of the Cabinet Committee on Balance of Payments on Treasury's Proposed "Tax on Tourist Travel," May 3, 1966 ~~(CONFIDENTIAL).~~

22/ Memorandum to The Under Secretary from Mr. Solomon on Meeting of Vice President's Travel Task Force on August 10, August 8, 1966 (LIMITED OFFICIAL USE).

23/ Department of State Circular Airgram CA-10063 on International Meetings and the US Balance of Payments Program, April 11, 1966 (LIMITED OFFICIAL USE).

endorsed the recommendations by the National Association of Manufacturers that the US Government sponsor package vacation tours to the United States by local national employees.[24/]

In the spring of 1966 because of the strains resulting from the heavy commitments and expenditures in Southeast Asia, consideration was given to approaching foreign governments directly benefiting from military expenditures in order to encourage them to hold reserves in the United States and to invest part of such reserves in long-term liabilities. Posts were requested to assess likely reactions to such a proposal. Moreover, views of various bureaus within the Department were sought on the prospects for obtaining prepayments on post-World War II indebtedness to the United States by nine developed countries.[25/] On the basis of replies from various posts, it was subsequently decided to send State/Treasury teams to several countries in different areas to

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24/ Department of State Circular Airgram CA-6701 on Proposed "See America" Program, March 7, 1967 (UNCLASSIFIED).

25/ Memorandum to E - Mr. Solomon from IMA - Mr. R. Cooper on Prospects for Further Repayment of Debts to US by Developed Countries ~~(SECRET).~~

explore alternative possibilities; i.e., debt prepayments, military offset arrangements, purchase special or other medium term US securities and reductions in short term liabilities to US commercial banks.[26/] Considerable success was met in many countries and efforts in this direction continued as the occasion arose.[27/]

By September 1966, discussions were inaugurated on a balance of payments program for the forthcoming year. In general, the Department's position was to question the need for any major new program. In addition to possible financial measures to encourage exports, and a Department-developed proposal for a possible NATO Military Payments Union (NMPU), the Department advocated a further tightening of the Commerce program on voluntary restraint of foreign direct investment in developed countries, by stipulating that investment during the period 1965-67 should not exceed

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26/ Department of State Circular Telegrams 2034, April 16, 1966 ~~(CONFIDENTIAL),~~ and 2236 and 2237, May 13, 1966 ~~(SECRET).~~

27/ Department of State Circular Airgram CA-5704, February 1, 1967 ~~(CONFIDENTIAL).~~

125 percent of a company's three-year investment in the 1962-64 base period.[28/] The Department of State advocated that, in the event voluntary controls could not be further tightened, serious discussion should be undertaken regarding the imposition of mandatory controls for direct investment, either by extension of the IET, a capital issue committee, or an auction quota scheme.[29/]

In December 1966, a number of proposals were advanced by the Treasury to discourage foreign travel by US citizens, including (1) an increase in passport fees; (2) reduction of the duty free allowance on tourist imports to $10 and (3) a Presidential appeal for voluntary restriction on personal travel. The Department of State successfully opposed both the passport and allowance proposals as likely to cause serious foreign policy problems. However, while reservations

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28/ Memorandum to Assistant Secretary Solomon from Mr. Cooper on Proposed Response to Treasury Memorandum on Balance of Payments Measures for 1967, August 26, 1966 ~~(SECRET).~~

29/ Memorandum to Mr. Rostow from Mr. Solomon on Meeting of Cabinet Committee on Balance of Payments, October 31 dated October 28, 1966 ~~(SECRET).~~

were expressed as to efficacity of any voluntary appeal, the Department supported it with the understanding that the Western Hemisphere be exempted.30/

In general, the Department of State opposed tax incentive measures as a vehicle for improving the US balance of payments, because they carried a high riskof foreign retaliation and would violate obligations under GATT.31/ During the summer of 1967 an interagency group met at the technical level to discuss export tax incentives. The State Department took the position that any export incentive program should focus on liberal overexpensing of export promotional costs and expanded non-tax incentives, and it strongly opposed tax incentives directly related to measures of export sale. The possibility of a rebate on all federal, state and local

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30/ Memorandum to Mr. Rostow from Mr. Solomon on January 4 Meeting of Cabinet Committee on Balance of Payments, January 3, 1967 ~~(CONFIDENTIAL).~~

31/ Memorandum: IMA - Cooper and Greenwald to Assistant Secretary of State Solomon, April 11, 1966 ~~(CONFIDENTIAL).~~

secondary indirect taxes consistent with the GATT was noted.[32/]

The question of indirect taxes was directly related to the "border tax" problem. At the July 1964 OECD Council Session the US representatives submitted a proposal calling for a standstill on existing border tax increases and asked for prior consultations before imposing changes in existing rates. US policy was to concentrate efforts in Working Party 4 to obtain a clear understanding and explicit or tacit acknowledgment that border tax adjustments were not trade-neutral, with the hope that some kind of agreed solution and guidelines for future changes could be developed.[33/] The US policy of working for a solution through the OECD, however, met with little success, and by the end of 1967 it became evident that a more forceful approach would have to be undertaken.

32/ Memorandum: IMA - Bergsten to Treasury - P. Schaffner, Export Tax Incentives, August 17, 1967 (LIMITED OFFICIAL USE).

33/ Department of State Circular Airgram CA-5947, December 3, 1965 ~~(CONFIDENTIAL).~~

After extensive interagency consultations and examination of various measures, it was decided that the United States would call for multilateral consultations under Article XXII of GATT on the ground that the current system of border tax adjustments and changes involved inequities which discriminated in favor of indirect-tax-oriented countries and had trade impairment effects. The Department reaffirmed its policy of opposing measures which would destroy GATT and lead to trade retaliations. In line with this policy the US representative was asked to call for a meeting of the GATT council and request establishment of a GATT task force to examine relevant GATT rules and member practices with a view toward recommending amendments or interpretations to neutralize the advantages which indirect-tax-oriented countries enjoyed under GATT border tax rules.34/

34/ Department of State Telegrams 127727, March 9, 1968 (LIMITED OFFICIAL USE) and 136053, March 26, 1968 ~~(CONFIDENTIAL)~~.

The Department's Bureau of Economic Affairs was often active in mediating the long-standing differences between AID and Treasury on measures to make US aid additional, i.e., to see that AID loans and grants resulted in equivalent dollar increases in US exports of goods and services. State Department personnel participated in the various field missions to Asia and Latin America and often raised with foreign governments the question of non-tariff barriers to US exports. The Department was particularly concerned with weighing the additionality benefits against the associated increases in AID program costs.

When, toward the end of 1967, it became evident that new and drastic measures would be needed to stem the balance of payments deficit and maintain the dollar as a reserve currency, reservations were still expressed within the Department regarding a new edition of the Treasury's March 1966 travel tax proposals, on grounds of both constitutionality and potential foreign political problems.[35/] The

35/ Memorandum, Ghiardi to Assistant Secretary Solomon, Tax Restrictions on Foreign Travel, December 20, 1967 ~~(CONFIDENTIAL)~~.

Department also opposed the idea of a Presidential appeal for voluntary restraint on travel, but its opposition was unsuccessful at the eleventh hour.

The Department remained in the forefront of those advocating mandatory measures for restricting direct capital outflows, preferably by extending the IET to direct investment. As the program for mandatory foreign investment restraints took shape toward the end of 1967, Assistant Secretary Solomon played an active role in the formulation of this Foreign Direct Investment Program (FDIP). In particular he was instrumental in obtaining the establishment of three different schedules of countries, with differing limitations on total investment by outflows from the United States and on use of retained earnings, so that the special needs of Less Developed Countries (Schedule A) and of other countries heavily dependent on US capital (e.g. the UK, Canada - Schedule B) would receive relatively more favorable treatment than the more restricted Schedule C countries. In this connection the Department also objected to FDIP proposals for holding LDC investments at 1967 levels.[36/] The Department was among those agencies successfully opposing complete exemption for Canada, but the crisis of confidence which afflicted the Canadian dollar in the first two months of 1968 forced reconsideration which resulted in Canadian exemption announced March 11.

The Department was also a strong and persistent supporter of greater efforts to improve our external payments position through liberalization of export credit policies. It participated actively in the "Okun Task Force" which met frequently in the fall of 1967 to explore such measures. The Department particularly espoused liberalization of the Federal Credit Insurance Association to permit a major expansion of export credit insurance and of the Export-Import Bank's rediscount facility. Though little was accomplished in mid-1967, subsequent inter-agency efforts led to the formulation of an

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36/ Memorandum to Assistant Secretary Solomon from Mr. Ghiardi on Balance of Payments, Supplemental Programs - Meeting with Secretary Fowler on December 19, dated December 19, 1967 ~~(SECRET).~~

Export Expansion Fund (EEF) within the Eximbank, and an Export Expansion Advisory Council to recommend to Exim appropriate financing assistance for transactions involving greater risk than normally accepted by Exim in its regular credit program. The State Department originally developed this EEF concept and thus in effect fathered this program.

Once Administration decisions were made on the final contents of the 1968 balance of payments program, it was essential that we inform our principal economic partners and consult with them on the implications of certain aspects of the program. This was particularly important in the case of Canada, which is extraordinarily affected by US external economic measures. Assistant Secretary of State for Economic Affairs Solomon telephoned Finance Minister Sharp in Ottawa and flew to Mexico to inform Canadian Prime Minister Lester Pearson who was vacationing there.

The President's Balance of Payments Program was announced January 1, 1968. It included mandatory controls on direct investment abroad and proposed taxation or other restrictive measures applicable to foreign travel. To counter adverse reactions abroad and explain the various programs, overseas posts were instructed on January 1 to inform heads of governments and central bankers of the new program. Intergovernmental teams headed by principal State Department officials again were sent abroad to discuss the program with key officials in numerous foreign capitals. Under Secretary Katzenbach headed a team to England, Germany, Switzerland, Belgium, The Netherlands, Italy, and France. Under Secretary Rostow headed a team which visited Australia, Japan and New Zealand. US Ambassador to the OECD Trezise carried out an extended series of visits to other European capitals. Of particular concern was the question of possible US measures to improve the trade account, which included consideration of a possible import surcharge/ export subsidy approach. As a result of a long series of consultations carried out by these teams and subsequent representations by the Department, a tentative agreement was reached with principal OECD trade partners that in order to forestall such US action, there would be an acceleration of Kennedy Round trade concessions by the OECD, and a deceleration of the schedule of implementation of these tariff cuts would be permitted the United States.

In the months following introduction of the new balance of payments program, the Department held the line against foreign pressures (Spain, Belgium) for exemption from the FDIP. In connection with development of legislation on a travel tax or other restrictive measures on foreign travel, the Department carefully pointed out aspects of these proposals which might cause embarrassment or serious repercussions abroad.[37/]

37/ Memorandum to Under Secretary Katzenbach from Assistant Secretary Solomon on Letter for the Under Secretary's Signature: Raising with Secretary Fowler Certain GATT Problems with Treasury's Travel Account Proposals, March 25, 1968 (LIMITED OFFICIAL USE).

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C. TRADE PREFERENCES FOR DEVELOPING COUNTRIES

1. A New Issue in US Foreign Policy

When the Johnson Administration took office in November 1963, the issue of trade preferences for developing countries was of relatively recent origin and appeared to be simply one of a series of trade policies being discussed in a rather undramatic way in several international forums. Over the course of the ensuing four years, the question of trade preferences became one of the major issues of US foreign economic policy, requiring the personal attention of the President on three separate occasions prior to his announcement in the spring of 1967 that the United States was prepared to consider a fundamental change in its 189-year-old trade policy of most-favored-nation treatment. In the course of four years, the Johnson Administration moved the US position from that of doctrinaire opposition, which had isolated the United States from all major countries of the world, to one of leadership of multilateral efforts to develop a workable system of preferences for all developing countries. These efforts were to continue well into 1969 before it could become clear whether a preference system acceptable to both the industrialized and developing countries was possible.

2. Evolution of the Preference Issue

A chronology of the key developments from 1963 through mid-1968 is presented below (Annex 1 to this section), together with citations of documents in the public domain relating to these developments. That chronology, of course, indicates only what happened and when. The purpose here, on the other hand, is to review (a) the elements underlying this sequence of events; (b) why United States policy shifted; and (c) how that shift was accomplished.

Particular emphasis will be placed on the last of these three points because the first two can be presented quite succinctly and have, moreover, been presented in considerably more detail in official documents and unofficial writings in the public domain.[1/] The basic elements in the preference issue and the external political developments which occasioned the basic review and shift of the US position can be summarized as follows:

-- concern on the part of developing countries over the future prospects for their export earnings, given their heavy dependence on primary products with generally poor growth prospects and their belief that newly-established industries in developing countries are unable to compete with established industries in highly developed countries;

1/ See especially the document cited below, in Annex 2, under the entry for July 12, 1967. A more thorough analysis of the history, economics, and international politics of the preference issue up to mid-1966 (i.e. prior to the shift of US policy) is authoritatively presented in "Trade Preferences for Less-Developed Countries: An Analysis of United States Policy" by Sidney Weintraub (Praeger, 1967).

-- dissatisfaction on the part of developing countries with the principle of most-favored-nation treatment, a policy they began to challenge as one imposed on them by the industrialized countries [2/] as a device to keep them in an inferior economic position: equality makes sense among equals, they argued, but Malawi and Germany are not equals nor are Peru and the United States equals; why should countries of such economic power be expected to overcome the same tariffs in major markets and still be able to compete on an equal footing?

-- the emergence of the United Nations Conference on Trade and Development (UNCTAD) as a forum where the views of the developing countries on this issue (and others) attracted more public attention and

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2/ The General Agreement on Tariffs and Trade (GATT) was drawn up in 1947 by 23 countries, most of them already industrialized countries; the GATT establishes the basic framework for world trade built on the principle of non-discrimination or most-favored-nation treatment.

where the developing countries' position appeared at least initially to be one of monolithic unity in favor of preferences for all developing countries;

-- the virtual isolation of the United States at the first UNCTAD Conference in 1964 as the only major industrialized country opposed to trade preferences in principle, a posture which made the United States the lightning rod for developing countries' growing dissatisfaction with their trade position and the rules of the game as embodied in the GATT;

-- the existence of numerous preferential trade arrangements among certain industrialized and developing countries which automatically involve discrimination among the developing countries (e.g. UK-Commonwealth preferences, various European-African preferences, US-Philippine preferences);

-- the gradual proliferation of the foregoing type of preferences (selective as to country beneficiaries) particularly between the countries of the European Economic Community and old and new African associates;

-- pronounced dissatisfaction on the part of Latin America as a result of its having no preferences in any major market (plus discrimination against Latin America in European markets) and consequent pressures on the United States for remedial action;

-- the gradual evolution of unanimity among the developing countries that the patchwork of selective preferences should be abandoned in favor of a system of preferences for all developing countries in the markets of all industrialized countries;

-- the continued isolation of the United States from 1964 until early 1967 as the only industrialized country opposed in principle to preferential trading arrangements, either selective or generalized;

-- the consequent loss of US influence over the course of external events, notably:

-- the further proliferation of selective arrangements which threaten to fragment world trade into closed blocs involving not only discrimination among developing countries (and against Latin America) but against the United States as well since most selective arrangements involve reciprocal preferences for industrialized countries in the markets of developing countries receiving selective preferences; and

-- the undermining of the basic rule of GATT reflected in the overwhelming approval (over US opposition) by the Contracting Parties of a waiver permitting Australia to extend a completely worthless system of preferences to developing countries, a step which opened the door to administrative anarchy in world trade with absolutely no benefit to anyone, least of all the developing countries.

All of these interrelated issues gradually merged into one policy issue: who was out-of-step, the United States or the rest of the world?

The preceding summary of the issue might imply that the answer is obvious and that it should be simple and non-controversial to shift US policy more in line with overwhelming world sentiment. Such a conclusion would underestimate the influence of a number of other major factors on the US position:

-- Congressional consideration. Trade preferences would be a basic departure from a policy dating back to the founding fathers (in conditional form) and explicitly precluded by all domestic trade legislation since 1922 (when the United States adopted the unconditional form of most-favored-nation treatment). The history of congressional jealousy over its prerogatives in the trade field, the frequently contentious partisan debates over trade policy throughout our history, the extreme scrutiny to which trade legislation is always subject -- all these made the prospect of going to the Congress for authority to extend preferences to developing countries something less than inviting. Moreover, there was concern that trade preferences might be interpreted by the Congress as giving something for nothing or as an aid substitute even if the preference authority could be obtained.

-- US business attitudes. No trade policy requiring congressional sanction can succeed without the support of the leaders of the US business community; the task of mobilizing public support for trade preferences appeared formidable indeed because preferences might seem to raise the spectre of a flood of "low-wage" imports and lead to actions to vitiate such a policy before its started (e.g. by strict quantitative limits such as are applied to imports of cotton textiles).

-- Impact on the Kennedy Round. The evolution of the preference issue coincided with the most important multilateral trade negotiations in history; fears were expressed that trade preferences might undermine the negotiations.

-- Balance of payments considerations. While this was not a major factor insofar as the preference issue was concerned in the early years of its evolution by 1967 it had become much more serious; in addition to all the economic uncertainties about the actual trade impact of a system of preferences, questions arose whether the United States could afford to take any chance that the trade (and balance of payments) impact might be adverse, given the erosion of our trade surplus.

-- Pressures for a special US-Latin American trade arrangement. A number of senior US Government officials and influential private businessmen supported the view of many Latin American leaders that the best answer to the proliferation of European-African preferences would be to establish a US-Latin American preferential trading area.

Finally, there is the subjective element of American pride in pragmatic approaches to policy issues: some fundamental questions had to be faced before deciding on purely political grounds that US policy should change. Would a system of trade preferences actually work in practice? Would the benefits outweigh the costs? Who would gain and who would lose? By how much? It was -- and remains -- much easier to pose these questions than to provide the answers.

3. How the West Was Won

A basic re-examination of US policy[3/] on preferences was initiated in the late spring of 1965 within the Department of State at the request of the newly-designated Assistant Secretary for Economic Affairs, Anthony M. Solomon. The

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3/ The most complete exposition of US policy as of May 1965 can be found in the UNCTAD Document cited in Annex 1 (entry of May 27).

conclusions of this first reappraisal (within the Economic Affairs Bureau alone) are reflected in the following excerpt from a covering memorandum of June 10, 1965, to Assistant Secretary Solomon transmitting a series of lengthy papers relating to the basic premises underlying preferences, the case for US-Latin American preferences, selective preferences, generalized preferences, and a review of preferential arrangements in operation at the time:

> 1) We continue to think that there is little in preferences, in trade terms, for the LDCs generally.
>
> 2) An effort to alter US legislation away from MFN to preferences for LDCs could have major costs, such as (a) engendering the feeling on the Hill and in the US generally that we should now focus on trade at the expense of aid and that the aid program could thereby be reduced drastically; and (b) that Congress might consent to preferential legislation only by coupling preferences with absolute import quotas on a wide range of dynamic LDC products.

3) Our stated support of MFN, however, has not been consistent, in the sense that we have not really opposed new preferential arrangements that have come along; and if our position is to continue to be in favor of MFN, we should also vigorously support this principle.

4) If, however, it becomes clear that there is no political disposition in the United States to oppose new preferential arrangements (such as those between the EEC and such places as Nigeria and the Maghreb states), or if our opposition goes unheeded internationally, then we believe the United States must consider a preferential system itself; the kind of system we have in mind would be a general one (i.e., to all LDCs except those which discriminate against us in favor of other developed countries, for all non-sensitive products where duties exist, with plenty of safeguards and room for unilateral maneuver by the United States), rather than one which picks and chooses among nations for what appears to be immediate political advantage. A proposal of this type is outlined along with alternative proposals.

Beginning in early July 1965, inter-bureau discussions within the State Department were initiated by the Bureau of Economic Affairs with the objective of finding some way to prevent the further proliferation of discriminatory preferential arrangements and, if possible, to develop a common approach among the major industrialized countries to the trade problems of developing countries. These discussions led to the transmission of the circular telegram reproduced as Annex 2.[4/] This message set the stage for a major effort within the framework of the Organization for Economic Cooperation and Development (OECD) to harmonize the divergent positions of the western industrialized countries on how to accelerate the trade and economic growth of developing countries. This matter became the main focus of the OECD Ministerial meeting

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4/ This telegram is somewhat unusual in that no drafting officer is indicated; instead, three different Bureau Office symbols appear as the "drafter." This reflects the extreme difficulty encountered over a period of 3 months in trying to reconcile mutually-conflicting opinions between the Bureaus of Economic, European, and African Affairs on what should be done. Innumerable drafts and counter-drafts were exchanged before the delicately-negotiated compromise language of Department of State Circular Telegram 428 was agreed. Other agencies presented no major problem once the Bureaus in State had resolved their differences.

November 25-26, 1965.[5/]

Agreement was reached by the OECD Ministers to establish a Special Group of senior trade policy officials representing the United States, the UK, France and Germany. The mandate for this Group, worked out in the OECD Council several weeks later, was to study problems regarding trade between developed and developing countries with the aim of formulating "constructive and concerted policies for encouraging increased export earnings by the developing countries."[6/] The work of this Group led to a substantial outpouring of memoranda and analyses of various facets of the preference issue by each of the four governments and the OECD Secretariat. In the early spring of 1966, after only a few meetings of the OECD Special Group, the French shifted their position to support of a generalized system of preferences built around

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5/ The text of the statement by Under Secretary of State Thomas C. Mann at the OECD Ministerial is contained in Airgram CEDTO A-316 dated November 27, 1965 from USOECD Paris (LIMITED OFFICIAL USE).

6/ OECD Document C(65)148, December 23, 1965 (RESTRICTED).

tariff quotas. (The French had previously opposed any kind of generalized preferences, maintaining that the special discriminatory arrangements between European countries and former colonial territories were better.) The French representatives gradually secured the support of Germany for this approach while the UK, which had always favored generalized preferences, was prepared to examine the tariff quota mechanism. The shift in the French position thus tended to solidify the position of all the major countries of Western Europe in favor of some kind of generalized preferences.

Misgivings in a number of Executive Branch agencies that the United States was becoming committed to the idea of preferences through the work of the OECD Special Group led to a meeting of senior officials, including members of the President's personal staff, and the drafting of explicit instructions defining what the US representative could and could not agree to at that stage. These instructions, reproduced as Annex 3 below, established many of the basic elements of the US position for the next two years.

The events listed in the chronology from August 1965 to August 1966 brought matters to a point where the Department of State considered it was time to seek the cooperation of other key agencies in devising a US trade policy strategy for the post-Kennedy Round years and to acquaint the President and other principal agencies with the broad lines of the Department's thinking. The GATT approval of the Australian preference waiver in March 1966 was a major contributing factor in convincing senior officials of the Department of the need to revise our policy on preferences: the Australian scheme had been thoroughly examined in the GATT and clearly exposed as a fraudulent device designed for no other purpose than to earn political points for Australia in the eyes of the developing countries. Bilateral diplomatic efforts were made to persuade the Australians to withdraw their plan, but to no avail. As the time for formal GATT action approached, efforts were made to devise a procedural way for all the industrialized countries to indicate their disdain for the

Australian fraud; the price was US agreement to abstain rather than vote against. The United States decided to vote against. When the final results ultimately became known (GATT votes are traditionally not revealed; the result is simply announced by the Director-General as approved or disapproved), the Department of State was genuinely shocked to learn that not a single other Contracting Party to the GATT was prepared to stand up for the principle of MFN embodied in Article I of the GATT. The vote on the Australian waiver was 51 in favor, one against -- the United States.

On August 12, 1966 Acting Secretary George Ball sent to the President the memorandum attached as Annex 4, below (memoranda to the Secretaries of Commerce and Labor and Governor Herter annexed thereto were sent a few days later after confirming through the President's Special Assistant that the President had no objection).

A restricted group of officials at the Assistant and Under Secretary levels of State, STR, Commerce, Agriculture, Labor, Treasury, and the President's Special Assistant for economic matters met periodically beginning in the latter part of the summer of 1966 to discuss the basic lines of a new trade strategy. No records were kept of these meetings. By early February 1967, a sufficient area of policy agreement was reached in this group to permit the Department of State to send a memorandum to the President outlining the main elements of a new trade policy (including preferences) and asking authorization to initiate Congressional consultations. This memorandum is reproduced as Annex 5.

With White House approval, these consultations took place in late March and early April with particular reference to a proposed statement on preferences the President was prepared to make at the Inter-American summit meeting scheduled for mid-April. The favorable results of these consultations are summarized in the Secretary of State's memorandum to the President on April 7, 1967 (Annex 6).

The President's statement at Punta del Este on April 13, 1967 that the United States was ready to explore the possibility of temporary preferences for all developing countries led to an acceleration of the pace of international consideration of generalized preferences. All of the key documents are in the public domain and are identified in the chronology -- Annex 1.

The support from the business community reflected in the recommendations of the US Chamber of Commerce and (to a lesser extent) the National Foreign Trade Convention were not, of course, spontaneous gestures. Senior economic officers of the Department of State spent many hours explaining the history of the preferences issue to key officers of these organizations and many other groups, including organized labor. The Secretary of State's memorandum to the President of November 27, 1967 (Annex 7) summarizes the results of these steps, including additional Congressional consultations.

This memorandum recommended the President authorize US support for the consensus statement on preferences, the result of nearly two years' work in the OECD Special Group.[7/]

7/ The text of the consensus statement is enclosure number 1 to the November 27 memorandum (Annex 7).

The President agreed, and at the OECD Ministerial Meeting November 30 - December 1, 1967, the following agreement was reached:

> ...Ministers agreed that the broad lines of the Group's work should serve as a common basis for Delegations of Member Governments at the Second United Nations Conference on Trade and Development and in future discussions of this matter.
>
> Ministers underlined that the envisaged arrangements should not imply the granting of reciprocal advantages by developing countries to the exports of developed countries.
>
> Some important questions regarding the arrangements for special tariff treatment remain open. Ministers instructed the Organization to continue to consider these problems in the light of the views expressed by developing countries.
>
> Several Ministers stated that a key element in such arrangements would be the phasing out, as rapidly as possible, of existing preferences extended by some developing countries to some developed countries. Other Ministers could not share this view, and stressed that the fundamental

aim of the arrangements contemplated was the granting of new advantages to the exports of developing countries.8/

The Second UNCTAD Conference in New Delhi (February-March 1968) found the United States no longer the target for developing countries' attack as the obstructionist to a policy of trade preferences. The shift in the US public posture contributed to some of the results which earlier memoranda had predicted: with the issue of principle out of the way, the hard realities of the details of a system of preferences had to be faced. The artificial unanimity of the developing countries quickly disappeared: differences between the Latin Americans and the Africans are as great or greater than those that still remain among the industrialized countries. It is clear that many policy and technical issues remain to be resolved if a mutually-acceptable generalized scheme of preferences is to materialize over the coming years.

8/ Excerpt from paragraph 7 of OECD Communique (OECD Document C(67) 131 - UNCLASSIFIED). The statement of the US representative at this meeting, Under Secretary of State Eugene V. Rostow, can be found in Airgram CEDTO A-304, December 4, 1967 from USOECD Paris (UNCLASSIFIED).

The United States is now deeply involved in this issue, as its world trade interests and political responsibilities dictate, rather than simply lamenting the disappearance of a principle that few if any other governments consider very relevant to the realities of economic relations between industrialized and developing countries.

A final observation concerning the impact on the American bureaucracy of how this particular shift in policy was accomplished may be of some interest: it is one of the ironies of the situation that the very technique which produced the shift is the one that poses the greatest threat to a conscientious follow-up. US opposition in principle to preferences would probably have been very difficult to change through normal staff channels and procedures -- the principle of MFN is too deeply imbedded in commercial policy officials in many agencies (and the pleas of the developing countries too remote a political factor) for the staff levels of these agencies to have recommended a proposal to modify the US position. Even at the policy level in other agencies, there was no deep conviction that moving the US position to support generalized preferences was positively desirable; it was more a reflection of reluctant recognition that the situation -- particularly with respect to proliferation of discriminatory arrangements -- was rapidly getting out of hand and no one had a better solution to put forward. The Department was the prime mover in securing the acquiescence by all agencies at the Under Secretary or Cabinet level.

ANNEX 1

Trade Preferences for Developing Countries: Chronology of Principal Developments

1963

February	At the first Preparatory Committee meeting of the UN Conference on Trade and Development, India suggested that trade preferences should be examined as a way of accelerating developing countries' export earnings.
April	India, with the support of other developing countries, advanced the same proposal in Committee III of the GATT.
May 21	GATT Ministers agree to establish a working party to study the granting of preferences on selected products by industrialized countries to less-developed countries as a whole. (GATT BISD, Twelfth Supplement, page 44.)
May 21-June 29	During the Second meeting of the Preparatory Committee of the UN Conference on Trade and Development, proposals were again put forward (and Secretariat studies were requested) concerning the granting of preferential tariff and quota treatment to the exports of manufactures for the developing countries. (Proceedings of the first UNCTAD, Volume VIII, pages 29, 32, and 45.)

July 20	Convention of Association between the European Economic Community and 18 African Associated States signed (Text available in GATT Document L/21/60/Add 1, April 7, 1964.)

1964

February 12	UNCTAD Secretary General Prebisch issues his report "Towards a New Trade Policy for Development" calling inter alia for a system of generalized preferences for manufactures and semi-manufactures from developing countries (UN Document E/CONF. 46/3, reprinted in Proceedings of the first UNCTAD, Volume II, pages 3-64.)
March 6	Eighteen Latin American countries adopt the "Charter of Alta Gracia" calling for the establishment by UNCTAD of a new structure of international trade based on preferential treatment for all developing countries. (IA-ECOSOC Document UP/CIES-7, 20 March 1964; also available in UNCTAD PREPCOM Document E/CONF. 46/100, April 10, 1964.)
June 1	The Second Committee of the first UNCTAD adopts (by a vote of 69 to 8 with 23 abstentions) a resolution calling for tariff preferences for manufactures and semi-manufactures (UNCTAD Final Act, Annex E, pages 154-155.)

June 13	The First UNCTAD Conference unanimously adopts a resolution calling for further examination of the issue of preferences (UNCTAD Final Act, Annex A. III. 5.)
November 24	GATT Working Party submits report on preferences containing no agreed conclusions. (GATT BISD, Thirteenth Supplement, pages 100-105.)

1965

January 26	Panama proposes US preferences for Panamanian goods as part of negotiations with respect to a new Panama Canal Treaty (Confidential internal State Department memoranda).
February 20	President of Peru publicly calls for US preferences for Latin America to offset effect of European-African preferences (Unclassified telegram 961 from Lima February 24).
May 19	Government of Australia announces intention to extend preferences to developing countries; GATT Council appoints Working Party to examine request for waiver (GATT Document L/2443).
May 27	UNCTAD Special Committee on Preferences completes its first meeting without unanimous agreement. (UNCTAD Document TD/B/C.2/1 and Addendum 1.)

August 10	Inter-American Committee on the Alliance for Progress addresses a recommendation to the Presidents of the OAS that a temporary defensive system of preferences be extended by the US to compensate Latin America for European-African preferences. (Unnumbered publication of the Pan American Union, August 10, 1965.)
December 17	OECD Council establishes a Special group (US, UK, Germany, and France) to formulate constructive and concerted policies for encouraging increased export earnings by the developing countries (OECD Document C (65) 148).

1966

March 28	GATT approves waiver for Australian preferences (GATT BISD, Fourteenth Supplement, page 23).
July 16	Nigeria and the European Economic Community sign as association agreement (Text available in GATT Document L/2774, April 26, 1967).
August 5	UNCTAD Group on Preferences issues a report on the salient points of a possible system of preferences without prejudice to positions of governments represented on Committee (UNCTAD Document TD/B/84, August 8, 1966).

August 11	OECD Special Group issues an interim report outlining two possible alternative approaches to a system of preferences (OECD Document TC (66) 25).
August 16	Presidents of Colombia, Venezuela, and Chile publicly call on US to give same preferential treatment to Latin America as Europeans give to Africans and Asians ("Declaration of Bogota" summarized in Unclassified telegram 820 from Bogota August 17, 1966).

1967

January-March	President Balaguer of the Dominican Republic issues numerous public appeals for preferential access to the US market for Dominican products.
April 12-13	President Johnson announces (at Inter-American Chiefs of State meeting) US readiness to explore the possibility of temporary preferences for all developing countries (Department of State Bulletin, Volume LVI, Number 1454, May 8, 1967).
May 31	UNCTAD Secretariat issues a detailed outline and analysis of a system of generalized preferences (UNCTAD TD/B/C-2/AC-1/7).
June	Inter-American Economic and Social Council adopts the Action Plan of Vina del Mar including inter alia, support for establishment of a system of generalized preferences (IA-ECOSOC Document 1306, June 24, 1967).

June 30	US Chamber of Commerce recommends US support for generalized preferences (Foreign Trade Policy Statement released July 9).
July 12	The US Administration's position on generalized preferences is presented to the Congress (Hearings before the Sub-committee on Foreign Economic Policy of the Joint Economic Committee, Ninetieth Congress, First Session, Volume I, pages 69-88 and 360-414).
July 19	UNCTAD Group on Preferences issues report on its second session (UNCTAD TD/B/C.2/38).
September	OECD Special Group recommends all OECD countries support certain principles which could form the basis for a system of generalized preferences (Text available in UNCTAD Document TD/56, January 29, 1968).
November 11	US National Foreign Trade Convention cautiously endorses idea of generalized preferences (Declaration of 54th NFTC Convention).
December 1	OECD Ministers approve the broad lines of the recommendations of the OECD Special Group (Paragraph 7 of OECD Communique, December 1, 1967).

1968

March 23	Second UNCTAD Conference adopts a resolution recognizing unanimous agreement in favor of the early establishment of a mutually-acceptable system of preferences and establishes

a Special Committee with the aim of settling the details of arrangements in the course of 1969. (UNCTAD TD/L/37, Annex 1, page 31).

ANNEX 2

COPY of TELEGRAM

ACTION: CIRCULAR 428 September 18, 1965

1. US is seriously concerned over multiple pressures tending to erode MFN trade principle among free world countries. Trend of recent developments involving trade relations particularly between developed and less-developed countries particularly disruptive because of departure from general commercial policy goals shared by major trading nations during most of post-war period, namely, gradual reduction of trade barriers, nondiscrimination between trading partners, and multilateral flows of trade. At present, however, more than 80% of total world trade still moves on non-preferential basis.

2. Proliferation of preferential agreements poses serious economic and political issues which so far have been dealt with piece-meal, primarily in limited commercial policy context in GATT and, within OECD, in context of coordinating developed countries' tactical positions for UNCTAD.

3. We believe matter should not be considered as urgent general policy issue by OECD community. Our present view is that it should be taken up at OECD Ministerial scheduled for November. We are cognizant of need so to maneuver as to support our Atlantic policies of maintaining and strengthening NATO, maintaining a close partnership with Europe, and reducing

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Drafted by: OT/RPE/AFI 9/17/65 Approved by: E-Anthony M.Solomon

Clearances:

EUR-Mr. Hinton	ARA-Mr. Palmer	AID-Mr. Saxe
AFI-Mr. Kling	Treasury-Mr. Ryss (sub)	Agric.-Mr. DeFelice (sub)
Commerce-Mr. McNeill (sub)	STR-Mr. Norwood	

trade barriers in the Kennedy Round as well as to improve the economies of LDCs.

4. US and other DCs now face important choices concerning way we organize trade and aid relationships. These decisions will have inevitable political implications. Trade policies, while recognizing transition necessary to take historical economic or political ties into account should be consistent with ultimate aims re world-wide DC-LDC relationships and US overall objectives.

5. Implicit consensus which existed earlier on policy objectives may no longer exist. Decisions taken in the Immediate future on specific cases of DC to LDC relations can set pattern for years ahead. Accordingly, US considers it important have full and frank international discussion at appropriate senior level so that ultimate course we all adopt, separately or jointly, is determined with full awareness of all implications and likely consequences.

6. Even though seems self-evident, we think worth repeating that preferential arrangements create problems for countries left on outside, particularly the LDCs, and increases pressure on such countries also seek similar arrangements with DCs including US.

7. Since trade in primary commodities accounts for 80% (not including petroleum) LDC foreign exchange earnings, clear that major improvement for LDCs now and for many years to come will have to be achieved in this area. Accordingly, we feel that OECD countries must address themselves more urgently than ever before to finding measures which will strengthen commodity markets on a commodity-by-commodity basis and at same time reduce dependence LDCs on primary commodity trade. For our part, we are giving these problems intensive attention in our policy planning. Experience leads us to doubt

that progress towards these objectives is furthered by trade preferences which encourage production for sheltered markets without regard to levels of world supply and demand, fragment world trade and aid relationships, and put one LDC at competitive disadvantage vis-a-vis its neighbor in major world markets for same product. Therefore, we would seek elimination of such trade barriers as well as reduction significant restraints on consumption as part commodity-by-commodity approach.

8. Since we recognize that preferential arrangements currently in existence cannot realistically be terminated overnight without serious impact on present LDC beneficiaries, we are anxious explore ways and means of giving effect to a policy recommendation formulated by the LDCs themselves at first UNCTAD Conference and accepted by all DCs, namely, that QTE preferential arrangements between developed countries and developing countries which involve discrimination against other developing countries . . . should be abolished pari passu with the effective application of international measures providing at least equivalent advantages for the said countries. END QTE

9. At same time we are tackling problem of increasing LDC earnings in primary commodity trade, we intend pursue vigorously efforts reduce developed countries' duties on items (both primary and processed products) of interest to LDCs. Best vehicle at moment for reducing barriers to LDC trade in Kennedy Round of trade negotiations. Benefits of tariff reductions among industrialized countries will be extended to LDCs without requirement of full reciprocity. In addition, we are urging DCs to give special attention to tariff reductions on items of particular interest to LDCs. Through these means we hope improve access to developed country markets for LDC goods and thus reduce further economic grounds for preferential treatment.

10. Our ultimate objective would be agreement in OECD on following points:

(a) Existing preferential arrangements should be phased out as rapidly as possible consistent with recommendations cited para 8 above. (In this connection, we would also continue seek early phase-out of Commonwealth preferences including those between developed Commonwealth members such as UK and Canada.)

(b) Wherever possible, preferences should be eliminated by reducing level of trade barriers rather than by raising preferential rates to present MFN level.

(c) Maximum use should be made of the Kennedy Round to reduce barriers to trade on products of interest to participating LDCs.

(d) Effects of loss existing selective preferences should be mitigated through improvement conditions of access by LDCs outside existing arrangements, as well as other appropriate measures of type cited paras 7 and 8 above, which could include financial assistance as well as diversification projects.

11. If others raise US-Philippine preferences or US-Canadian automotive agreement, we would take following positions. (1) US-Philippine preferences will continue be phased out and completely eliminated 1974. (2) While we consider US-Canadian auto agreement unique situation not prejudicial to interests of third countries (see Cirtel 10), US would nevertheless agree consider removal of automobile duties on MFN basis in light of results of Kennedy Round and other commercial policy developments.

12. Consistent with above, we would oppose provisions for preferential trade arrangements in any further EEC association negotiations with African states. FYI. We do,

however, attach particular importance to continuation and extension of EEC and French financial and technical assistance to African states. END FYI. Similarly, we would oppose extension preferential trade aspects of existing EEC/AOC arrangements beyond 1969, and would interpret EEC agreement to UNCTAD Resolution cited para 8 a declaration of intent.

13. FYI. In connection with para 12 above, the question whether the US should acquiesce in EEC preferences to Maghreb states (Subject to para 10 a) is under discussion within the US Government but no conclusion has yet been reached.

14. We appreciate need for careful preparations to avoid atmosphere of confrontation or crisis and obtain discussions in depth at OECD Ministerial meeting. We would hope combine discussion preferences problem with consideration of positive measures in commodity field to offer more comprehensive approach on DC-LDC trade and development relationships.

15. In contemplation of OECD November Ministerial meeting, US has already informally raised this range of subjects and possibility of Ministerial discussion trade preference problem with key delegates to OECD Trade Committee and with OECD SEC GEN. In response these soundings, Kristensen indicates he prepared to deal with question at Ministerial meeting. US has also informally requested Secretariat to do preliminary study of preference question bearing in mind that Article 1c of Convention states one aim of OECD shall be to promote policies designed QTE to contribute to the expansion of world trade on a multilateral, nondiscriminatory basis in accordance with international obligations. END QTE Important step in preparations will be meeting of OECD Secretary General in September with key Heads of Dels to begin preparations for Ministerial meeting. END FYI.

16. Action requested. Accordingly, USOECD (Brown) should concert with Sec Gen and with key Ambassadors to attain agreement on foregoing range problems as major substantive subject for Ministerial. US Representative should draw on US thoughts on this subject as per paras 1 to 12. He might well suggest formation special restricted group of Heads of Dels and senior trade officials to advance discussion to point where it could be generalized to entire membership in late October or early November. In meantime, other Missions may draw on paras 1 to 12 in replying queries and in general discussions US policy. If developments warrant, we may subsequently supplement OECD discussions with approach to Governments in capitals, possibly including visits by senior US officials to European capitals prior to OECD Ministerial.

END

SEND TO: ALL OECD CAPITALS
Amembassy PARIS for USOECD and Embassy
US Mission BRUSSELS for USEC and Embassy
US Mission GENEVA GATT

INFO: Amembassy LAGOS
" ALGIERS
" DAR-ES-SALAAM
" KAMPALA
" NAIROBI
" RABAT
" TUNIS
" BLANTYRE
" CANBERRA
" NEW DELHI (via pouch) per KWG

NOTE: Pouched by OC/T

ANNEX 3

US Position re Report of OECD Special Group on Trade with the LDCs

(Position paper prepared in the Department of State, Bureau of Economic Affairs, E/ITP, for presentation by the US Representative in the OECD Special Group.) *

The US representative on the OECD Special Group should be guided by the following informal discussions of the report of the OECD Special Group and in the drafting of the report:

1. The United States Government cannot, at this time, subscribe to definitive recommendations regarding the issue of preferences for LDCs.

a. We recognize the importance of achieving a concerted OECD position on the preference issue in advance of UNCTAD-II. However, a decision in favor of preferences would represent a major departure from US basic post-war commercial policy. This is an extremely important step and must be given the most careful consideration. The United States is continuing to review its policy.

b. Among the factors to be considered is the timing of a new trade policy initiative in relation to the progress of the Kennedy Round negotiations.

c. Further reflection is required on the deliberations and proposals which have emerged from the meetings of the Special Group.

*May 26, 1966

2. The US representative should, therefore, strive for the adoption of a report which

a. records the results of the Special Group's study of the economics of preferences and of the historical experience with preferential systems,

b. discusses the policy issues raised by preferential arrangements,

c. reflects certain principles which might govern any preferential system,

d. describes ways of dealing with the problems arising from trade in primary products, and

e. makes clear that the Special Group is not recommending a preferential system before there has been further study and consideration of the issue.

3. The US representative should ensure inclusion of the following points in the report (points a.i and ii are particularly important from the US point of view):

a. No preference scheme for manufactured and semi-manufactured products should be considered as potentially acceptable unless it is based on

i. the elimination of preferences now enjoyed by developed countries in certain LDCs.

ii. the phasing out of existing preferences granted by developed countries.

iii. the same tariff treatment for all LDCs without any reciprocal preferences for DCs.

iv. the application of any preferential system in the framework of continued reduction of m-f-n tariff, i.e. preferences should be degressive as a result of agreed cuts among the developed countries.

v. a time limit for new preferences.

b. Trade preferences should not be considered in any way as a substitute for continued foreign aid programs.

c. The developing countries should, in order to be able to take advantage of trade opportunities, institute internal measures, e.g. reform of currency over-valuation and protectionist import-substitution policies. The developing countries should also promote their economic development by reducing tariff and other trade barriers among themselves.

d. With respect to primary products, existing preferences should be eliminated. In addition, efforts should continue on a case-by-case basis to find effective means of stabilizing prices.

4. If the other members of the Special Group insist on recommending the institution of a system of preferences, either in general terms or a specific plan, the US representative should reserve his position on the ground that further study and discussion are required. If appropriate, he may also put on record comments regarding any specific proposal put forward by the other members of the group.

ANNEX 4

August 15, 1966

MEMORANDUM FOR THE PRESIDENT

Subject: Trade Policy--A Proposed Strategy for the United States

During the past several months, Secretary Rusk and I have become increasingly aware of the need to develop a new trade policy strategy for the United States after the Kennedy Round. You may recall that during your meeting with State Department Assistant Secretaries on May 31, Tony Solomon mentioned a possible US initiative in this area.

Our ideas have now become a bit clearer and I want to acquaint you with the direction of our thinking. Enclosed is a copy of a memorandum Secretary Rusk proposes to send Governor Herter, Secretary Connor, and Secretary Wirtz outlining our views as to the need for a new trade policy strategy and a possible way of meeting these needs. We are requesting the support and assistance of these key agencies in developing these ideas further so that an inter-agency proposal (in which Agriculture, Interior and Treasury would subsequently participate) can be submitted to you.

Speculation about possible changes in US trade policy could, I know, be a sensitive issue domestically. It could also have repercussions in the Kennedy Round negotiations which must remain our principal focus in the trade field over the coming months. However, I believe that by restricting inter-agency consideration of this matter to a very small group at the Assistant Secretary level, potentially embarrassing leaks can be prevented.

Although it is not likely that we will be seeking major new trade legislation in the next year, it is necessary that we begin now to develop a policy. What we propose is to refine a strategy which, with your approval, could be tested with Congressional leaders. You would then be in a position, if this seemed desirable, to use this as one element of a positive US program to help ensure a successful meeting of the Inter-American system.

(Signed George Ball)

Enclosure:

Proposed memorandum

MEMORANDUM FOR:

Governor Herter
Secretary Connor
Secretary Wirtz

SUBJECT: Trade Policy - A Proposed Strategy for the United States

I am deeply concerned that the world trading community appears to be drifting into regional blocs and discriminatory arrangements which, unchecked, would have serious political and economic consequences for the United States.

We need a new trade policy strategy following the Kennedy Round to check this drift. A sound strategy for the United States must, I believe, take account of:

-- The likelihood of increased discrimination against our exports as more countries in Western Europe associate themselves with the European Economic Community and form the largest market in the world with free trade among themselves and barriers against the United States and other outsiders.

-- The further proliferation of special trade arrangements which discriminate among poor countries, against Latin America, and against the United States.

-- The persistent appeal of the poor nations for preferred treatment for their exports. The countries of Southeast Asia as well as Africa and elsewhere will judge the sincerity of our interest in their progress by what we are prepared to do in the field of trade as well as aid.

-- The willingness of other industrialized countries to respond to this appeal which leaves the United States virtually isolated, a position which carries with it significant political costs.

United States political and economic interests require us to take the initiative and try to guide developments in a manner likely to advance our own national interests. We cannot let matters drift, leaving it to other nations to continue to work out ad hoc arrangements which adversely affect our interests.

This memorandum sets forth a possible way of meeting these challenges. I commend it to your personal attention and invite your support and assistance in developing it further so that an inter-agency proposal can be submitted to the President.

If our prognosis of a link between the EEC and most other Western European nations proves correct, the resulting continental trade wall against us would jeopardize our export position. We could, like Joshua, trumpet against such a wall and perhaps it would crumble. But prudence dictates that we arm ourselves with other tools. The only realistic way, in my view, is to move to the maximum extent possible toward free trade among all industrialized countries. This would be the first element in the proposed new trade strategy and would be in line with the authority to eliminate duties contained in the Trade Expansion Act but which could not be used because the United Kingdom did not join the EEC.

Appropriate legislation would be needed to enable us to enter into negotiations after the Kennedy Round. One approach would be to seek authority to negotiate the mutual reduction and possible elimination of trade barriers staged over an extended period, perhaps ten or fifteen years. An alternative would be to seek authority for another round of negotiations to reduce duties by a specific percentage as a further step toward our ultimate goal.

The second element of the proposed strategy would be to offer the poor countries of the world a "head start" in such a move toward ultimate free trade. The benefits of tariff reductions would be given to them immediately while reductions among industrialized countries are phased over a longer period. This would have a number of advantages for us:

-- It would improve our position vis-a-vis the developing countries.

-- It would, to the extent the developing countries support this approach, make it politically more difficult for other industrialized countries to resist the longer-term move to reduce barriers among themselves.

-- It would result in the phasing out of existing trade preferences which discriminate among developing countries, Latin America in particular.

-- It would strengthen our ability to insist on the elimination of preferences enjoyed by the European industrialized countries in the markets of some poor countries which discriminate against United States exports.

-- It would probably increase the trade earnings of the poor countries and assist in their economic development; they need trade as well as aid.

There is the problem, of course, of possible injury to US industry and labor arising from increased imports from low-wage countries. This may require additional safeguards and expanded adjustment assistance. Particularly sensitive items might be excluded entirely. In other cases, quantitative limitation on the amounts which could enter from developing countries at reduced rates might be appropriate.

No formal action should be taken which might divert attention from the Kennedy Round (which has to be substantially wrapped up by February-March 1967). We would not seek new authority until the basis for negotiations has been worked out with our trading partners. This process might take a year--from mid-1967 to mid-1968. In this event, the new program could be included in the 1969 State of the Union message. If the pre-negotiations moved faster and the traditional bias against trade legislation in an election year were overcome, the bill might be sent up in early 1968. In any case, for July 1967 (when the Kennedy Round is concluded), we would propose a simple one or two year extension of the period during which the existing authority under the Trade Expansion Act could be used.

These targets for submission of new legislation may seem far off, but we need to elaborate an inter-agency proposal so that we are in a position to:

-- Initiate consultations with Congressional leaders;

-- Refer to the direction of our thinking at the prospective meeting of Presidents of the Inter-American system toward the end of this year; and

-- Present a proposal in some detail at the Second United Nations Conference on Trade and Development in the summer or fall of 1967.

I believe the trade policy strategy outlined above is in the best interests of the United States because:

-- It offers the possibility of dealing realistically with the major commercial policy problem we face in the coming years, namely the strong likelihood of increased discrimination against our exports to Western Europe as these nations enter into various forms of associations with the Common Market;

-- It is responsive to the appeal of more than 100 poor nations for a special boost for their exports;

-- It would involve only a temporary departure from the basic objective of non-discrimination in world trade but simultaneously will enable us to obtain elimination of the invidious forms of discrimination which exist at present;

-- It would include adequate safeguards against injury to American producers and labor; and

-- It would help retain the historic US position of leadership in the trade policy field.

I would appreciate your designating a senior officer to meet with Assistant Secretary Solomon to develop further the proposed strategy so that an inter-agency proposal can be sent to the President within the reasonably near future. If the President agrees with this general approach, Congressional sentiment could then be tested.

Because of the sensitivity of this whole subject, I would appreciate your holding this memorandum closely within your respective agencies.

Enclosure 1

The Special Group recommended that Member Governments of the OECD support a statement on the following lines to be presented to the developing countries at the Second Conference of the UNCTAD. The United States Member of the Group stated that in his view it would be necessary for this statement to include, in addition, the point made by him on page 4.

(1) Temporary advantages in the form of generalized arrangements for special tariff treatment for developing countries in the markets of developed countries can assist the developing countries to increase their export earnings and so contribute to an acceleration in their rates of economic growth.

(2) The potential benefits for developing countries will be maximized by the largest possible participation of developed countries in arrangements for the grant of such special tariff treatment.

(3) Such new arrangements should aim to accord broadly equivalent opportunities in all developed countries to all developing countries.

(4) The arrangements should be designed so as to result in an equitable distribution among the developed countries of increased import opportunities to their markets.

(5) Any new arrangements for the grant of special tariff treatment cannot be put into effect without the support of the developing countries, and their views should be taken into account in the formulation of any such arrangements.

(6) The grant of temporary tariff advantages to developing countries would not constitute a binding commitment and should not in any way impede the reduction of tariffs on an m.f.n. basis, whether unilaterally or following an international tariff negotiation.

Discussions among Member Governments of the OECD have led to a broad measure of agreement on a number of key elements which might be included in arrangements for the grant of special tariff treatment.

A. Beneficiary Countries

Special tariff treatment should be given to the exports of any country, territory or area claiming developing status. This formula would get over the difficulty which would otherwise arise of reaching international agreement on objective criteria to determine relative stages of development.

Individual developed countries might, however, decline to accord special tariff treatment to a particular country claiming developing status on grounds which they hold to be compelling. Such ab initio exclusion of a particular country would not be based on competitive considerations (which would have to be dealt with by the procedures discussed under C and G below).

It is to be expected that no country will claim developing status unless there are bona fide grounds for it to do so; and that such a claim would be relinquished if those grounds ceased to exist.

B. Product Coverage

Special tariff treatment should apply in principle to all manufactured and semi-manufactured products. Other products could be included on a case-by-case basis.

C. Exceptions

In order to protect sensitive domestic industries it is probable that donor countries will find it necessary to exclude from the outset the benefit of the special tariff treatment a limited number of products in respect of which developing countries are already competitive.

D. Rules of Origin

The grant of special tariff treatment will require the application of rules of origin to determine the conditions under which imports shall qualify for admission at special rates of duty. It will be necessary to determine how best to achieve the objectives of ensuring that the rules are in accordance with the intentions of the new arrangements and of providing broadly equivalent new import opportunities into each developed market.

E. Duration

The special tariff treatment should be temporary and degressive. Margins of preferences would not be guaranteed. The initial arrangements should be for a period of ten years with provision for a major review before the end of this period to determine whether the special tariff treatment should be continued, modified or abolished. It is obvious that developed countries may wish before the ten-year period has elapsed to consider the feasibility of a further international negotiation to reduce tariffs on an m.f.n. basis. If they do so and the negotiations were successful, an element of degressivity would automatically be introduced into the arrangements for developing countries.

F. Depth of Cuts

The improved access for developing countries may take the form of duty-free treatment or substantial reductions below m.f.n. rates.

G. Safeguards and Adjustments

Any scheme of special tariff treatment must inevitably include some safeguard or adjustment arrangements to avoid the risks of dislocation of industry and labor. Safeguards may be either related to the possibility of withdrawal or modification of special tariff treatment when imports of particular products reach certain limits (defined in advance by reference to domestic production, consumption or imports); or they can be related to determination by the developed country concerned of the causing or the threat of injury to its domestic industry. These questions call for examination with a view to agreement among donor countries. It will be for the countries according special tariff treatment to ensure that safeguards are applied in a manner consonant with the principle of equitable sharing of improved access.

H. Preferences received by some developing countries in the markets of some developed countries

It is recognized that many countries would see as an important objective of the new arrangements a movement in the direction of equality of treatment for the exports of all developing countries in developed country markets. At the same time, developing countries presently receiving preferences in some such markets would expect the arrangements to provide them with increased export opportunities to compensate for their sharing of their present advantages.

I. Action by Countries with Centrally-Planned Economies

Both in order to maximize benefits for the developing countries and to provide for equitable distribution of appropriate measures among developed countries, the grant of special tariff treatment by developed countries with market economies should be matched by arrangements by countries with centrally-planned economies which would similarly increase the opportunities for the export to them of products from developing countries.

J. Action by Developing Countries

The arrangements should not involve the grant of reciprocal advantages by developing countries for the exports of developed countries. They should however be the occasion for developing countries to broaden market opportunities among themselves on a regional basis. It would also help if they agreed to take measures to encourage foreign investment as an additional spur to industrialization.

The United States Member stated that, in his view, a key element in any arrangements for the grant of special tariff treatment is the phasing out, as rapidly as possible, of existing preferences extended by some developing countries to some developed countries.

Enclosure 2

Consultations with Private Groups on Tariff Preference for Developing Countries

We have discussed the possibility of the United States joining with other developed countries in extending temporary generalized tariff preferences for developing countries with a number of key business, labor and public interests groups. While we have not sought or received specific endorsements, the reactions have been positive. Our consultations indicate widespread support for the effort to work out a system of generalized preferences. A summary of the most important of these consultations follows:

Business Groups

US Chamber of Commerce. In July 1967, the US Chamber of Commerce formally endorsed the extension of temporary tariff preferences by industrialized nations to developing countries. The conditions that the Chamber attached to this endorsement--that the preferences should be 1) extended all developing countries by all developed countries and 2) temporary--are both basic features of the US position.

National Foreign Trade Council and the National Foreign Trade Convention

On October 30 the National Foreign Trade Convention adopted a Declaration expressing concern about the growing proliferation of special discriminatory trading arrangements between developing countries and developed countries and about the effects of these special preferences on other countries, especially in Latin America. While re-affirming their support of trade liberalization on an m.f.n. basis, the Convention stated that, if preferences were to be instituted, they should be temporary and extended jointly by all developed countries to all developing countries.

National Association of Manufacturers. The NAM does not formally take a position on tariff matters. However, the Vice President of the International Affairs Department and others indicated a growing awareness of the trade and development problems of the LDCs. They thought the members interested in these matters would look favorably on a plan which would help developing countries and would remove existing discrimination.

Labor

AFL/CIO. The AFL/CIO several years ago endorsed preferences. Secretary Rusk recently discussed this problem with

George Meany. Mr. Meany reacted favorably to the Administration's approach subject to the following qualifications:

1. Preferences should be extended by all developed countries, or major developed countries, to all developing countries.

2. There should be adequate safeguards for American workers.

3. There should be agreement that the benefits of preferences should be passed on to the workers in the developing countries.

We are in full agreement with these points.

Public Interest Groups

Some of the public interest groups with whom we have discussed preferences are as follows:

The Council on Foreign Relations
League of Women Voters
American Association of University Women
Brookings Institution
Foreign Policy Association
Society for International Development

While these organizations may not all take formal positions on preferences, their reactions to our approach have been universally positive.

Enclosure 3

Consultations with Congressional Leaders on Preferences for Developing Countries

SENATE

Leadership:

Mansfield Dirksen

Senate Finance Committee:

Long Williams

(Tom Vail, Finance Committee staff) (November 27)

Foreign Relations:

Fulbright Hickenlooper

Others:

Javits

HOUSE

Leadership:

Speaker Ford

Albert

Ways and Means Committee:

Mills	Byrnes
Boggs	Curtis

Foreign Affairs Committee:

Morgan	Adair

(November 27)

August 12, 1966

TO: The Under Secretary

THRU: S/S

FROM: E - Anthony M. Solomon

SUBJECT: Memorandum to the President on Trade Policy - A Proposed Strategy for the United States
ACTION MEMORANDUM

Discussion:

Enclosed is the memorandum I have discussed with you which transmits to the President a copy of the Secretary's memorandum to Secretary Connor, Secretary Wirtz and Governor Herter, and explains that we are requesting the support and assistance of these agencies in developing an inter-agency proposal on trade policy for submission to the President.

Recommendation:

That you sign the attached memorandum to the President.

Attachment:

Tab A - Memorandum to the President

ANNEX 5

THE SECRETARY OF STATE

WASHINGTON

February 11, 1967

MEMORANDUM FOR THE PRESIDENT

Subject: A New Trade Policy for the United States

Recommendation

Last August George Ball sent you a memorandum outlining a new trade strategy designed to reverse current trends not in the United States interest and to maintain our leadership in free world trade policy in the post-Kennedy Round era. In accordance with your instruction, a small group led by Tony Solomon has examined these ideas further within the Executive Branch. We have consulted with Secretary Connor (and Acting Secretary Trowbridge) and with senior officers of Agriculture, Labor and Treasury. Ambassador Roth and Francis Bator also have taken part in the discussions. The result: unanimous agreement both on the need for a new United States trade policy and on the broad outlines of the policy itself.

We do not envisage a request for major new trade legislation before 1969. It is important, however, to consult informally with key Members of Congress now if we are to adopt a positive posture at several important international meetings over the next 12 months, including your meeting with the other Presidents of the Inter-American system. We must know soon whether the new policy direction -- described below -- can command the support of the Congress. If it does, the new policy should be taken up as the first order of business of a blue-ribbon public committee which Ambassador Roth will recommend be established to assist him in developing recommendations for trade legislation after the Trade Expansion Act expires on June 30.

You could then announce at the Latin American meeting in April that a major re-examination of our trade policy is under way with a view to improving the trade position of developing countries in ways that will further the historic United States objective of liberalizing world trade. This statement would be warmly welcomed by the Latin Americans and would, Linc Gordon feels, be a critically important contribution to a successful summit meeting. A careful statement along these lines would not arouse serious protectionist opposition, since only a general approach would be outlined at that time. Recently, Congressional leaders as diverse in their trade views as Senators Dirksen and Fulbright have commented on the unresponsiveness of the United States Government to the problem of the poor countries' declining share in world trade.

I recommend, therefore, that you approve informal soundings with key Congressional leaders.

Approve Congressional Consultations ________________

Disapprove ____

Discussion

The Need for a New United States Trade Policy

For the next few months our primary effort must be devoted to a successful conclusion of the Kennedy Round trade negotiations. At the same time, however, we must address ourselves to future United States policy -- to new problems which have arisen and to old problems which have acquired new dimensions. To meet these and to maintain our leadership in the field of trade policy, we must take into account:

-- the vital importance of maintaining our own export surplus;

-- the strong likelihood that the European Economic Community will be enlarged over the coming years, forming the largest market in the world with free trade among its members, but retaining substantial barriers against the United States and other outsiders;

-- the danger of further proliferations of special trade arrangements which discriminate:

-- among developing countries,

-- against Latin America, and

-- against the United States;

-- and, above all, the passionate and persistent appeal of the developing nations of the world for preferred tariff treatment for their exports. At the present time, the willingness of other industrialized countries to respond to the appeal leaves the United States virtually isolated in its opposition to preferences. For this we are paying significant political costs.

The challenge presented by these developments coincides with our need to obtain new trade legislation. After the Trade Expansion Act expires at the end of June, we will need a period of reflection and discussion with our trading partners. Thus, a simple extension of the Act for two years seems appropriate. But to exercise leadership and attract international support for a policy designed to meet these new circumstances, we need a new and flexible Congressional mandate.

Basic Elements of a New Trade Policy

1. To meet the objective of keeping open our commercial markets in developed countries, we propose:

-- That we seek legislation in 1969 which will enable us to urge the Europeans and other industrialized countries to join in a policy of progressive reduction and, where possible, elimination of trade barriers. Where agreements can be reached on specific products or groups of products, tariffs might be phased out over periods of five to twenty years.

2. To meet the twin problems of growing discrimination among poor countries and their appeal for tariff treatment more in keeping with their competitive abilities, we propose:

-- That the legislation enable us to offer the poor countries of the world a "head start" in the movement toward tariff disarmament among the advanced countries. The benefits of tariff reductions would be given to poor countries in advance of reductions among industrialized countries which would be phased over a longer period.

3. To meet the growing problem of regional bloc discrimination against United States exports, we propose:

-- That this approach be conditioned on agreement by the advanced countries to give up the preferential treatment they enjoy in the markets of associated developing countries.

4. To meet the problem of possible injury to United States industry and labor arising from increased imports from low-wage countries, we propose:

-- That the adjustment assistance provision be improved.

-- That there be an additional escape clause applicable to the special tariff treatment for the developing countries. Should difficulties arise, the advance cut might have to be withdrawn or, alternatively, a tariff quota might be established.

Dean Rusk

E:ITP:OT
2/9/67

ANNEX 6

MEMORANDUM FOR THE PRESIDENT

Subject: United States Trade Policy and the Inter-American Summit Meeting

Recommendation

In the light of Congressional sentiment in favor of the proposed course of action I suggested to you in early February, I recommend that at the Inter-American summit meeting you make a statement along the lines enclosed as Tab A and be prepared to accept the inclusion in the final Proclamation of a text along the lines enclosed as Tab B.

Approve ____________________

Disapprove ____________________

Discussion

In accordance with your authorization in early March, we have consulted the Leadership and key members of Congress concerning the broad outlines of a proposed new United States post-Kennedy Round trade policy. We have stressed to Congressional leaders our interest in formulating a joint trade policy with other industrialized countries which would give temporary trade advantages to all developing countries and in a way that would check and possibly eliminate completely the proliferation of trade arrangements which discriminate against Latin America, against other developing countries, and against the United States.

Congressional leaders have been advised that you contemplate making a statement outlining such a policy, provided they perceive no basic objection and, of course, on the understanding that if such a policy can be negotiated with other industrialized countries, specific legislation will have to be submitted for Congressional action at an appropriate later date, probably in 1969. The texts of a draft statement and a draft section which might be included in the final Proclamation at the conclusion of the summit meeting have been brought to the attention of Congressional leaders.

Nearly forty Senators and Congressmen have been contacted. Tony Solomon personally saw fourteen of these. Bill Roth and senior officers in the Bureau of Economic Affairs and Bill Macomber's Congressional Relations staff contacted the others. A complete list is attached as Tab C. In those cases where direct contact with the Congressional leader was not feasible, we have offered to arrange a further meeting if his Administrative Assistant found that his estimate of his principal's probable position was inaccurate.

I am pleased to be able to advise you that no objections have been raised with respect to your proposed statement or the draft Proclamation. Some members clearly favored temporary tariff preferences for all developing countries. Others gave their approval more cautiously, saying that at a later date they would like to consider the details of the proposal we hope to negotiate with other industrialized countries. Chairman Mills, one of the first Congressional leaders approached, personally proposed an amendment entirely consistent with our thinking which has the effect of strengthening your proposed statement. Several other leaders, including Senators Miller and Proxmire, also suggested improvements in the text.

The one reaction closest to a reservation was that of Senator Gore's Administrative Assistant who felt the Senator might have misgivings about departing from the principle of most-favored-nation although he thought the Senator would keep an open mind on the issue. This one cautious view is, however, overbalanced by the prevailing sentiment in favor of your proposed action at the summit meeting.

I therefore recommend that at the Inter-American summit meeting you make a statement along the lines enclosed as Tab A and be prepared to accept the inclusion in the final Proclamation of a text along the lines enclosed as Tab B.

Dean Rusk

Enclosures:

1. Outline of proposed Presidential statement on trade policy (Tab A).

2. Draft section of Inter-American President's Proclamation (Tab B).

3. List of Congressional leaders contacted on proposed trade policy actions at Inter-American summit (Tab C).

(Outline of Suggested Presidential Statement)

In the context of remarks about the importance of trade to development, the President might make the following points on US trade policy:

-- The process of freeing trade from unnecessary restrictions will not come to an end when the current and vitally important Kennedy Round negotiations are completed.

-- We have been examining the kind of trade initiatives the US should propose in the years ahead. We are convinced that our future trade policy must pay special attention to the needs of the developing countries in Latin America and elsewhere in the world.

-- We have been exploring with other major industrialized countries what practical steps can be taken to increase the export earnings of all developing countries. We recognize that comparable tariff treatment may not always permit developing countries to advance as rapidly as desired. Temporary tariff advantages for all developing countries by all industrialized countries would be one way to deal with this.

-- We think this idea is worth pursuing. We will be discussing it further with members of our Congress, with business and labor leaders, and will seek the cooperation of other governments in the world trading community to see whether a broad consensus can be reached along these lines.

DRAFT SUMMIT PROCLAMATION

The Presidents agreed that there is an urgent need for a fundamental re-examination of the trade policies of the industrialized countries with a view to expanding the export earnings of Latin American and other developing countries. The Presidents affirmed that they will:

(a) work for the maximum possible reduction in the Kennedy Round of trade barriers to the exports of the developing countries;

(b) seek the prompt elimination of all forms of discrimination against the exports of OAS Members in world markets.

The President of the United States stated that, consistent with its constitutional processes, the United States will consult with and seek the cooperation of other industrialized countries on the formulation of a joint policy which would give transitional trade advantages by them to all developing countries in ways which will not impede further movement toward the reduction of trade barriers on a world-wide basis.

KEY MEMBERS OF CONGRESS CONTACTED ON PROPOSED
HANDLING OF TRADE POLICY AT INTER-AMERICAN SUMMIT MEETING

	CONTACTED BY	COMMENT
SENATE		
Leadership		
Mansfield	Solomon 3/22	Reaction affirmative but cautioned he had only one vote.
Long (LA.)	Advised of proposed approach by letter from Roth 3/24. Solomon tried follow-up but unable reach Senator.	
Magnuson	Senior staff informed Senator's staff 3/23.	Staff said would inform Senator but certain he would strongly favor temporary tariff preferences for LDCs.
Dirksen	Solomon 4/4	Reaction affirmative.
Kuchel	Senior staff informed Senator's AA 3/23	AA said Senator on record in support of preferences for LA - would have no trouble with generalized preferences.

	CONTACTED BY	COMMENT
Hickenlooper	Solomon 3/30	Negotiability of proposals worth exploring but Latins should understand all industrialized countries must participate.
Morton	Solomon 4/5	Response affirmative.
Carlson	Roth & Solomon 3/23	Approach should be explored but questioned negotiability with Europeans.
Foreign Relations Committee		
Fulbright	Solomon 3/13	Favors proposal.
Sparkman	Senior staff 4/6	No problem with proposed approach.
Morse	Unable to contact	Already on record in favor of special trade advantages to developing countries.
Cooper	Senior staff 4/5	Reaction affirmative. Offered to do what is necessary to help.
Finance Committee		
Smathers	Senior staff informed Senator's AA 4/5	AA sees no problem. Will inform Senator.

	CONTACTED BY	COMMENT
Talmadge	Solomon & Roth 3/23	Approach worth exploring. No commitments should be made to other governments, pending Congressional consultation on specific proposal. Must protect domestic producers against possible injury.
McCarthy	Senior staff 3/29	Expressed general agreement. Emphasized need for continued close consultation with Congress.
Ribicoff	Advised of proposed approach by letter from Roth 3/24. Replied would like meet with Solomon but Senator could not be reached.	
Gore	Senior staff informed AA 3/30.	AA said Gore might have reservations about departure from MFN principle but thought he would keep open mind on subject.

	CONTACTED BY	COMMENT
Bennett	Senior staff 4/3	Generally positive reaction but doubts preferences would be temporary. Somewhat critical US trade policy.

HOUSE

Leadership

Speaker	Senior staff 4/6	No objection to proposed approach.
Albert	Senior staff informed AA 3/27	AA said he would bring to attention of Mr. Albert. Saw no particular problems except domestic industries which would want protection against possible injury.
Boggs	Solomon 4/4	Strongly favored. Thought proposal advantageous as means of reversing proliferation of discriminatory regional trade blocs.
Ford	Solomon 3/23	Response affirmative. Hoped legislative request would be separate from regular trade bill.

	CONTACTED BY	COMMENT
Arends	Senior staff 3/27	No objection but Congress would want to look at carefully.
Rhodes (Ariz.)	Senior staff 4/6	Rather cool to general approach for all LDCs but favored action for Latin America.

Foreign Affairs Committee

Morgan	Senior staff informed Cate. staff 4/3	Staff confident Chairman would have no problem.
Zablocki	Senior staff 4/3	No problem with proposed approach.
Belton	Senior staff 4/3	Reaction affirmative.
Adair	Senior staff 4/3	No problem with proposed approach.

Ways and Means Committee

Mills	Roth 3/21	Reaction affirmative.
Byrnes	Roth 3/21	Reaction affirmative.
Tom Curtis	Solomon 4/4	Affirmative response. Liked idea further trade liberalization after Kennedy Round.

	CONTACTED BY	COMMENT
Banking and Currency Committee		
Patman	Senior staff informed AA 3/25	AA said would give Chairman full report and would contact us if Chairman wanted further briefing.
Widnall	Senior staff 4/3	Regards proposed approach as positive stop.
JOINT ECONOMIC COMMITTEE		
Miller (Iowa)	Solomon 4/3	Strongly in favor. Made useful suggestion on language of proposed communique.
Javits	Solomon 4/5	All in favor.
Proxmire	Solomon 4/3	Response affirmative.
Bolling	Senior staff 4/5	Approach is fine.
Reuss	Senior staff 4/5	Fully supports proposed approach.

TO : The Secretary April 6, 1967

THROUGH: S/S

FROM : E - Anthony M. Solomon

SUBJECT: Trade Policy and the Inter-American Summit Meeting -- Memorandum for the President. ACTION MEMORANDUM

Consultations with Congressional leaders on the proposed statement by the President with respect to post-Kennedy Round trade policy, including transitional trade advantages for all developing countries, have gone very well. No opposition has been encountered. I believe the President can now be advised that the way is clear for him to handle the issue of trade preferences at the Inter-American summit meeting in the way we proposed in early February and with which the President concurred, subject to informal soundings of Congressional sentiment.

RECOMMENDATION

That you sign the Memorandum to the President attached as Tab 1.

E:ITP:OT:GCP:WECulbert:erg
4/6/67

Concurrence: ARA-Mr. Gordon
E/OT-Mr. Katz
H-Mr. Torbert

(Dated April 6, 1967, it was approved by the Secretary and signed by the President April 7, 1967.)

ANNEX 7

November 27, 1967

MEMORANDUM FOR THE PRESIDENT

Subject: United States Position on Tariff Preferences for Developing Countries

Recommendation:

Pursuing your initiative on preferences at Punta del Este, we have succeeded in achieving consensus on a set of principles under which all industrialized countries would extend temporary tariff advantages to all developing countries. In light of this consensus and the favorable reactions of business, labor, public, and congressional leaders, I recommend you authorize the United States representative to the OECD Ministerial meeting to support the consensus statement subject to a reservation on the elimination of reverse preferences unless our position on this issue is accepted.

Approve______________Disapprove_________

Discussion:

In accordance with your statement at Punta del Este, we have been pursuing in the OECD the possibility of reaching agreement on a temporary, generalized system of tariff preferences to be extended by all developed countries to all developing countries. A Special Group of experts from the United States, United Kingdom, Germany, and France worked out a draft set of broad principles or guidelines (Enclosure 1) which would serve as the basis for such an arrangement. The OECD Ministers, at their meeting November 30-December 1, are expected to take positions on the Special Group's Report and whether it can be presented to the Second United Nations Conference on Trade and Development (UNCTAD-II) as a joint position by developed OECD countries.

The following is a summary of the principles on which agreement was reached:

1. The preferences should be extended by all developed countries to all developing countries.

2. All the major developed countries must participate in order to insure an equitable distribution of increased import opportunities to their markets.

3. No preferences will be given on those products where developing countries are already competitive. There will also be safeguards or adjustment arrangements to avoid the risk of dislocation of industry and labor.

With one key exception, to which we have not agreed, the proposed guidelines are consistent with the objectives behind your initiative at Punta del Este. This exception concerns "reverse" preferences which are extended by certain developing countries to certain developed European countries. The United States will state at the OECD Ministerial that the United States believes that a key element in any preference plan would be the phasing out, as rapidly as possible, of such discriminatory reverse preferences. If the other OECD countries cannot accept our position, we will insist that it be included in the statement to be presented to the less-developed countries at UNCTAD-II.

The proposed guidelines leave unresolved a number of important issues affecting the implementation of a system of generalized preferences. These issues would have to be resolved to our satisfaction before we would make a decision about seeking legislation authorizing United States participation. We anticipate that discussion of the unresolved issues will last through 1968. United States support (there will be no formal vote, but the outcome will be reflected in a Ministerial communique) of the Special Group's Report is necessary in our continuing attempts to see if a workable system can be negotiated but retains the United States option not to grant preferences if an acceptable system cannot be agreed upon.

The other members of the OECD are expected to support adoption of the Special Group's Report although Japan may reserve its position with respect to specific language to deal with the possible trade diversionary effects of preferences.

The developing countries, at their meeting earlier this month, adopted the Charter of Algiers calling for a generalized system of tariff preferences to be extended by all developed countries to all developing countries. While the OECD proposal meets this request, there will undoubtedly be differences on many elements particularly since developing countries are seeking almost unrestricted access to developed countries' markets.

We have held extensive consultations with congressional, business, labor, and public leaders with respect to the Special Group's Report. The business and labor reaction (summarized in Enclosure 2) was highly favorable as evidenced by the formal endorsement of temporary, generalized preferences by the United States Chamber of Commerce. George Meany also endorsed the preference approach, subject to certain qualifications, all of which we have accepted.

The congressional reaction, while understandably more cautious, was generally favorable. (Enclosure 3 is a list of the congressional leaders consulted.) Even congressional leaders such as Congressman Gerry Ford, who could hardly be classed as an advocate of a liberal trade policy, favored our attempt to see if a workable system can be negotiated. Senator Dirksen has not yet given us his final reaction but, in a speech last year, he criticized the Administration for turning "a deaf ear to the pleas of these nations (LDCs) for preferential trading arrangements while offering no specific alternate solution to their problems". Other congressional leaders, such as Mills, Fulbright, Mansfield, Boggs, were favorably inclined. We intend to keep congressional leaders fully briefed of developments as the many presently unresolved issues are considered. We also expect to have congressional advisers on our delegation to UNCTAD-II.

Dean Rusk

Enclosures:

1. Special Group's Report.
2. Summary of business and labor reaction.
3. List of congressional leaders consulted.

DEPARTMENT OF STATE

Assistant Secretary

TO : The Secretary
The Under Secretary

November 24, 1967

THROUGH: S/S

FROM : E - Anthony M. Solomon

SUBJECT: US Position on Tariff Preferences for Developing Countries - ACTION MEMORANDUM

Consultations with Congressional, business, labor and public leaders with respect to the United States policy on tariff preferences for developing countries have gone very well. I believe you should now recommend to the President that he authorize the United States representative to the OECD Ministerial meeting November 30-December 1 to announce US willingness to join with other developed OECD countries at UNCTAD II next February in supporting a set of broad principles which would serve as the basis for a generalized system of tariff preferences extended by all developed countries to all developing countries.

The United States representative will state at the OECD Ministerial that the United States considers a key element in any preference plan would be the phasing out as rapidly as possible of reverse preference. If other countries are not prepared to agree to the US position on this issue, the US representative will insist that the US position be reflected in the OECD presentation to UNCTAD II.

The proposed guidelines leave unresolved a number of important issues affecting the implementation of a system of generalized preferences. These issues would have to be resolved to our satisfaction before we could make a decision about seeking legislation authorizing US participation. We anticipate that discussion of the unresolved issues will last through 1968. The United States decision to support the consensus statement is necessary in our continuing attempts to see if a workable system can be negotiated but retains the United States option not to grant preferences if an acceptable system cannot be agreed upon.

Recommendation:

That you sign the memorandum to the President attached at TAB A.

Attachment:

Memorandum to the President

Concurrences:

E/ITP-Mr. Greenwald
H-Mr. Macomber
EUR-Mr. Springsteen

E:ITP:OT:GCP:PWLande:cab