

Transatlantic Economic Relations in the Post-Cold War Era

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Table of Contents

1. Introduction
(Barry Eichengreen)
2. Openness and Diversity: Thinking About Transatlantic Economic Relations
(David Soskice)
3. Whither U.S.-EU Trade Relations?
(Jeffrey Schott)
4. European Monetary Unification and International Monetary Cooperation
(Barry Eichengreen and Fabio Ghironi)
5. European Migration Policies in an American Mirror
(Ricardo Fainni)

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Introduction

With the decline of tariffs, capital controls and transport costs, interaction between the US and European economies has grown increasingly intense. Economists may dispute the implications of economic globalization, but there is no question that US and European firms are in increasingly direct competition. The growth of cross-border banking, securities trading and other international capital flows has made it more difficult to think about the two regions' financial markets as economically distinct. Policies on one side of the Atlantic -- be these central bank decisions over the interest rate, congressional and parliamentary decisions about the budget, or government decisions on competition and regulatory policy -- have growing repercussions on the other.

The scope for conflict is considerable. US producers and policymakers complain about EU farm subsidies and food product standards (such as restrictions on hormone-treated meat). Europeans object to US restrictions on trade and investment in the financial, telecommunications and transport sectors. When US anti-trust authorities decide whether or not to let Boeing and McDonnell-Douglas merge, they are little concerned about the implications for the competitive position of Airbus Industrie. When the member states of the European Union decide whether or not to form a monetary union, they pay little attention to the implications for the reserve currency status and exchange rate of the dollar.

And yet policymakers on the two sides of the Atlantic continue to work toward common goals. Even while pursuing regional initiatives (enlargement and deepening of the European Union, ratification of the North American Free Trade Agreement), US and European governments have continued to press for the expansion and liberalization of the multilateral trading system. It was US and European support that ultimately pushed the Uruguay Round to its successful conclusion. US and European governments support one another's efforts to secure improved market access in Japan and the developing countries. They collaborate through the G-10 and the Bank for International

Settlements to limit instability in financial markets. They work through the World Bank and IMF to support stabilization and liberalization in transforming economies around the world.

The four chapters of this book, written by American and European authors, consider four aspects of the transatlantic economic relationship. They ask whether conflict or cooperation will dominate in coming years. Will the growing interdependence of the two continents' economies heighten policymakers' mutual interests and encourage them to collaborate in the pursuit of common goals? Or will competition lead to conflict and recrimination? How will the postwar tradition of economic policy collaboration adapt now that the glue of a common Cold War enemy has dissolved?

One scenario is a conflictual race to the bottom, in which deregulatory trends in the United States force European countries to cut wages and benefits, abolish training and apprenticeship schemes, and more generally dismantle social protection in order to meet "cut-rate" American competition. The European tradition of relationship banking, in which banks and firms establish long-term connections around a range of financial services, may similarly crumble as US financial institutions enter to skim off the financial cream. The only way for Europe to prevent the spread of "MacJobs" and the rise of US-style income inequality, by this interpretation, will be to limit American firms' access to European markets. This gloomy perspective, predicated on the notion that the United States and Western Europe societies have fundamentally incompatible visions of how their political economies should be organized, does not bode well for the transatlantic relationship.

The first chapter, by David Soskice, challenges this pessimism. Soskice acknowledges that the political economies of Western Europe and the United States have evolved along different lines, European societies supporting collective values through networks and institutions of social regulation, the United States emphasizing individualism and market orientation. (In many respects the United Kingdom might be grouped with the

United States; Soskice refers to the Anglo-Saxon model.) These different value systems, given concrete reality by government policy, private-sector action and historical inheritance, have produced distinct forms of economic organization on the two sides of the Atlantic: different modes of financial organization, different institutions of education and vocational training, different industrial-relations systems, and different mechanisms for technology transfer.

In most Northern European countries, large enterprises collectively contribute to elaborate systems of apprenticeship and vocational training. Workers obtain narrowly applicable vocational and professional skills. Unions, employers associations and governments discourage firms from poaching workers trained by their competitors (a practice which would erode the incentive for firms to underwrite skill formation), while firms provide the long-term employment commitment necessary to persuade trainees to participate in this investment. In the United States, where job security is less and no such collective responsibility is acknowledged (and even if it were, mechanisms for enforcing it would be lacking), employers do not underwrite comparable levels of training. The vocational knowledge conveyed by institutions of public education tends to be of more general applicability. Europe's bank-based financial systems allow managers to adopt long-term horizons useful for strategic planning but are miserly with finance for start-ups. While America's market-based financial system is generous with venture capital, the tyranny of the stock market sometimes prevents management from seeing beyond the next quarterly profit statement.

Thus, there may in fact be no race to the bottom. US and European institutional forms each have comparative advantages. The advantage of the United States is in new industries characterized by rapidly changing technologies, whose exploitation requires maximum market flexibility. Europe's comparative advantage lies in tailoring goods to the market and in incremental product and process innovation, which rely on a stable labor force and long-term customer relations. It is simply not true that the United

States and Europe are converging to a common model. Both the American and European forms of economic organization can survive and prosper because there exist markets both for radically new products (based on the electronic and biochemical technologies of Silicon Valley, for example) and for established products whose economic viability is sustained by incremental change (the machine tools of Southern Germany and textiles of Northern Italy). Openness can reinforce the viability of this institutional diversity by increasing the gains from specialization. In an open world economy, both the US and European economies can specialize in producing what they produce best without regard to the constraints of domestic demand. There is no need for policymakers on one side of the Atlantic to insist that the other adopt their preferred form of economic organization. It is not necessary for Americans, as a precondition for negotiating a Transatlantic Free Trade Area (TAFTA), to demand that Europe adopt a uniform deregulated economic system along US lines, or for EU policymakers to insist that the United States adopt European levels of social protection. Both systems can flourish in competition with one another. And the more open the competition, the stronger the gains from institutional diversity. But if a TAFTA is accompanied by US pressure for changes in European competition policy, corporate governance and labor relations, the viability of the European model could be threatened. The desirability of further transatlantic integration thus depends on the particular form it takes.

This concern provides a bridge to Jeffrey Schott's chapter on US-EU trade relations. Schott notes that the US and EU together account for more than half of global imports and exports. While conflicts over industrial policy and agricultural subsidies have festered for years, by and large the two economies have worked harmoniously for the expansion of the multilateral trading system. They have used the General Agreement on Tariffs and Trade for defusing conflicts that have proven intractable in bilateral negotiations.

But with the end of the Cold War and the rise of regionalism, there is new reason to worry about the stability of the bilateral trade relationship. The

end of the Cold War removes a powerful incentive for the US and the EU to paper over their differences. It allows security concerns on their respective doorsteps (in the US case, to the South, in the European case, to the East) to replace global goals once pursued in multilateral fora. These facts provide one rationale for a TAFTA, namely, to refocus attention on the transatlantic trade relationship.

Schott challenges the notion that a TAFTA is necessarily the best way to address bilateral trade tensions. US complaints over European policies toward agriculture, intellectual property rights, standards, certification requirements, financial services and investment all fall within the purview of the World Trade Organization. The same is true of EU complaints about US restrictions on trade and investment in financial, telecommunications and transport services and environmental policies. It would make more sense for the US and Europe to invest in strengthening the WTO than to create a separate venue for bilateral negotiations. Bilateral consultations through, *inter alia*, the Transatlantic Business Dialogue can contribute to this process, but only if they do not detract from investment in and compliance with WTO rules and procedures.

The chapter by Barry Eichengreen and Fabio Ghironi shifts the focus from trade to monetary relations. Transatlantic collaboration in this issue area has been less systematic and regular than in trade, while institutional flux is more pronounced. The EU is making a concerted push for monetary unification, and a monetary union comprising at least a subset of member states now seems likely before the turn of the century. Eichengreen and Ghironi emphasize two consequences which may limit policy coordination. First, the institutions of international monetary cooperation will be disturbed. G-7 summits will be complicated when responsibility for the monetary policies of France and Germany are assumed by an institution that also determines interest rates for Austria, Ireland and the Benelux countries (not G-7 members). The IMF will have to consider organizing parallel Article IV consultations with the Euro zone and each EU member state. Institutional

relations between Europe's fiscal and monetary authorities may grow increasingly difficult and uncertain, complicating cooperative initiatives that require adjustments of both fiscal and monetary policies.

Second, the advent of the European Central Bank and the single European currency may destroy that international consensus which currently exists on the question of how to respond to financial disturbances. With the completion of its Single Market and monetary union, Europe will become more of a large, closed economy and be less preoccupied by exchange rates and exchange-rate policy. So long as the European Central Bank is striving to establish the credibility of its commitment to price stability, it will not be inclined to participate in US-led initiatives for concerted intervention in the foreign exchange market. Its lender-of-last-resort responsibilities are ambiguous under the Maastricht Treaty; it may thus hesitate to participate in European lender-of-last-resort operations if these might be seen as conflicting with its responsibility for price stability, much less contribute to international lender-of-last-resort initiatives for countries like Mexico. In the past, international monetary cooperation involving the US, Europe and Japan has been limited to periods of serious dislocation, as when the dollar soared in the mid-1980s and slumped in 1994, and during exceptional crises like the Mexican meltdown of 1995. There is a danger, Eichengreen and Ghironi conclude, that even such limited initiatives will prove difficult to arrange in the initial years of Europe's monetary union.

The final chapter by Ricardo Fainni takes up an issue, migration, that is troublesome in both US and Europe but where European policies have relatively little impact on the US, and vice versa. Rather, each region's experience and policy response provides an optic for thinking about the experience and response of the other. A porous border with countries whose per capita incomes are only a tenth or a twentieth one's own has long been an economic fact of life in the United States. In contrast, it is only with the collapse of the Iron Curtain and the development of North African expatriate networks that the EU has developed similar concerns. Hence, Fainni uses the US as a

lens through which to view Europe's experience

The comparison suggests that Europeans, like Americans, may grow increasingly concerned about the impact of immigration on the distribution of income if the decline of centralized bargaining allows unskilled immigrants to bid down the wages of unskilled natives. As the fisc becomes more centralized at the level of the European Union, Europeans like Americans will grow increasingly preoccupied by the impact of immigration on the public finances. Neither of these observations necessarily implies that the costs of immigration exceed the benefits, only that the phenomenon is likely to give rise to growing political tension.

Those who wish to limit immigration, whether westward across the Oder or northward across the Rio Grande, can build fences or provide migrants an incentive to stay home. Fainni argues on the basis of both European and US experience that the two approaches are complements, not incompatible alternatives. Tighter border controls may be the only effective short term option, but incentives for economic development are likely to be the more cost-effective long-term strategy. Incomes need not be equalized to stem the flow of migrants; even limited prospects of better living standards may be enough to produce an accelerating decline in migration by individuals with a taste for established social relationships and local culture. But time is required before technical assistance, financial aid and market access begin to have discernible effects. NAFTA and EU enlargement may eventually ameliorate the developmental problems of Mexico and Eastern Europe, but the Mexican crisis of 1994-6 reminds us that economic integration provides no guarantee of immediate policy and political stability, while the debate over EU enlargement reminds us that there exist powerful vested interests prepared to delay such initiatives.

· Still, his chapter contains more than a few lessons for readers concerned with the prospects of the United States.

The picture that emerges from these essays is one of problems, not crises. Historically, crises have been necessary to provoke major transformations of the transatlantic institutional landscape. An undercurrent of economic conflict and tension has rarely prompted US and European policymakers to fundamentally reform their bilateral relationship. These essays thus point to incremental rather than revolutionary change. Still, were US and European officials to overlook the problem areas identified, the transatlantic economic relationship could deteriorate due to their neglect. This would be as regrettable as it is avoidable.