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GLOBAL GOVERNANCE: RECONSTRUCTING THE WORLD ECONOMY

By

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About Professor Martin Daunton

Martin Daunton has been the master of Trinity Hall since 2004 and professor of economic history at the University of Cambridge since 1997. He is a fellow of the British Academy and president of the Royal Historical Society. He has been working on social and economic policy of Britain, the colonies and the United States. He is the author of several books including *Progress and poverty: an economic and social history of Britain, 1700-1850* (Oxford University Press, 1995), *Trusting Leviathan: the politics of taxation in Britain, 1799-1914* (Cambridge University Press, 2001), and *Wealth and Welfare: An Economic and Social History of Britain, 1851-1951* (Oxford, 2007).

He is currently researching on the circumstances leading to the Havana and Bretton Woods conferences and the emergence of global financial institutions.

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Introduction

The recent great recession has focussed attention on the ability of the World Trade Organization, the International Monetary Fund, and the groupings of G20 and G8 to respond to major issues of balance of payments disequilibria and currency misalignments. The Doha round of trade talks of the WTO is deadlocked, and has been for many years. Meanwhile, the IMF has failed to come up with a solution to the problem of currency realignment; and there has been talk of currency wars.

A major question we face is how to create effective and legitimate institutions of global governance – and how to balance those two contradictory ambitions. Can international organizations be legitimate without a loss of effectiveness? Can they be effective without a loss of legitimacy?

My concern here will be those institutions created in the aftermath of the Second World War which are still in existence (the IMF and International Bank of Recovery and Development, now the World Bank) and those which have evolved from the post-war system. The latter include the WTO which developed from the General Agreement on Tariffs and Trade, a supposedly preliminary step in 1947 towards the creation of an International Trade Organization but which was not ratified by the United States. The formation of these institutions during and just after the Second World War reflected the circumstances of the time. These circumstances created structures which

have proved difficult to adapt and which have led to considerable problems in the very different circumstances today.

The international institutions were also set up as a response to the great depression of the 1930s and the perception that there were no credible commitments to international economic stability. The pre-1914 gold standard had functioned reasonably well without any formal agreement beyond a contingent rule linking currencies to their gold value. If there was a serious economic problem, a country could suspend gold convertibility, but would expect to return at some point.¹ However, the situation changed between the two world wars, when the lack of any agreement that was binding on all parties led to beggar- my-neighbour policies.

The political dynamic had changed, and governments needed to pay much more attention to domestic considerations: the commitment became ever more contingent, and ever more likely to be broken, without any formal agreement to maintain exchange rates (or for that matter avoid trade restrictions). The Geneva consensus (so called after the location of the League of Nations) failed to maintain the voluntary commitment of the pre-1914 gold standard since there were no international institutions established

¹ Michael. D. Bordo and Anna. J. Schwartz, 'The operation of the specie standard: evidence from core and peripheral countries, 1880-1910', in J. B. de Macedo, B. Eichengreen and J. Reis (eds.), *Currency Convertibility: The Gold Standard and Beyond* (1996), p. 12.

by formal agreements.² In the Second World War, economists and politicians recognised the dangers in this situation and wished to create formal, binding commitments.

Were the rules created in the post-war period simply a reaction to the problems of the 1930s? Did these very rules in fact create difficulties for the future? A major problem had already become apparent in the disequilibrium of the late 1960s and the early 1970s between the under-valued yen and DM and the over-valued dollar. One post-war institution, the IMF, failed to provide any answer to this problem, leading to the breakdown of the system of fixed exchange rates and a decade of uncertainty. Can the IMF do any better now?

The circumstances in which these institutions – the International Monetary Fund, the International Bank for Recovery and Development or World Bank, the General Agreement on Tariffs and Trade and the putative International Trade Organization - were created need to be understood in order that we do not draw mistaken conclusions from the past, and that we understand the constraints on their actions. Let me take two examples of such references to the past by leading figures in the current debates.

² Harold James, *The End of Globalization: Lessons from the Great Depression* (Cambridge, Mass. 2001).

The first example is in the sphere of international currency policy. The debates of 1941-44 between the British and the Americans over international currency policies have been revisited in the recent economic crisis to suggest that the wrong decision was taken when the American solution of Harry Dexter White was adopted rather than the British proposals of John Maynard Keynes. In April 2009, Zhou Xiaochuan of the People's Bank of China proposed a 'super-sovereign reserve currency', and referred to Keynes's similar idea of 1941. The idea emanating from China is to create a basket of currencies to replace the dollar, thus allowing more international cooperation. It has much in common with Keynes's idea of supra-national money or 'Bancor'.³ If Keynes had succeeded, the post-war order would have taken a very different shape. There would have been less dependence on the dollar; and the IMF would have taken a very different form as the creator of international liquidity, allowing over-drafts to deficit countries and requiring surplus countries to take action. We need to know why this did not happen, and why the IMF took on the limited form which still hampers its response.

The second example comes from trade, where Pascal Lamy of the WTO in a speech in India in November 2010 referred to the conference at

³ See Fred Bergsten, 'We should listen to Beijing's currency idea', *Financial Times* 8 April 2009. Bergsten was involved in the collapse of the Bretton Woods system as assistant for international economic affairs to Dr. Henry Kissinger at the National Security Council in 1969-71.

Havana in 1947-8 which drew up the Charter of the ITO. Lamy stated that the key issue facing the world now is unemployment, just as was recognised in the Charter of 1948, and that it must again be given priority.⁴ What he did not point out was that the priority given to employment in 1947/8 led to the collapse of the whole enterprise, for the Charter was never ratified and the ITO did not come into existence. Arguably, the lesson to be drawn from the attempt to create the ITO is that all-encompassing proposals, such as those developed in 2001 as part of the Doha Development Agenda are likely to end in deadlock and failure. A more limited and feasible concentration on specific issues is more likely to succeed. We should not turn to the past as a guide to the future without understanding more about why particular outcomes were foreclosed and others adopted.

Let me now turn to the creation of the new institutions of global governance after the Second World War. Why did they take the form they did, and how did the circumstances of their creation shape their response to the current problems of the world economy? It is a tale of two conferences: the creation of the IMF and IBRD at Bretton Woods in the US in 1944, and the signing of the Charter of the ITO at Havana in 1948, which was subsequently not ratified by the participants.

⁴ Pascal Lamy, speech to the Federation of Indian Chambers of Commerce and Industry, New Delhi, 19 November 2010 at http://www.wto.org/english/news_e/sppl_e/sppl180_e.htm

Bretton Woods and the IMF

When 44 countries met at the Mount Washington Hotel at Bretton Woods in New Hampshire in 1944, they ratified an agreement that had largely emerged from bilateral negotiations over the previous two years between the USA and Britain. More accurately, the agreement was between one and a half countries, for Britain was in a weak financial position, and largely accepted the American plan of White rather than the proposals of Keynes.

Despite their disagreements, there was a considerable measure of consensus over what was needed for the post-war world.⁵

The Bretton Woods agreement is an example of embedded liberalism⁶ that grew out of a consensus of technical experts, many of whom were based at the League of Nations. Both sides concurred in the need to create financial stability by ending the competitive devaluations of the 1930s. Both agreed on the need for fixed exchange rates as a precondition for the recovery of trade. Both accepted that domestic prosperity should be a prime concern to prevent the resurgence of economic nationalism that marred the 1930s. In order to ensure that exchange rates were stable and domestic prosperity preserved,

⁵ The debates are set out in Robert Skidelsky, *John Maynard Keynes: Fighting for Britain, 1937-1946*. London: Macmillan, 2000.

⁶ John G Ruggie, 'International regimes, transactions and change: embedded liberalism in the postwar economic order', *International Organization*, (2) (36), (1982) 379-415.

they agreed on the need to limit capital mobility. They also agreed that the sudden movements of capital in the 1930s put pressure on the exchanges; and that changes in the interest rate for domestic reasons should not be threatened by capital inflows or outflows in search of the best return. Finally, they could also agree that international institutions were necessary to prevent the pursuit of narrow self-interest. The creation of binding, enforceable commitments limited nationalistic pressures which would, in any case, be weaker because domestic prosperity would now be reconciled with rather than sacrificed to the international economy. There was, then, a high level of consensus, reinforced by the fact that highly technical issues of international financial policy were not at the heart of electoral politics and could be largely left to technical experts.⁷

Nevertheless, there were differences of emphasis between Britain and the USA. In part, the difference arose from the countries' positions as creditor and debtor, and in part from their divergent banking systems. Keynes's

⁷ Neil De Marchi, "League of Nations Economists and the Ideal of Peaceful Change in the Decade of the Thirties". In *Economics and National Security: A History of their Interaction, Annual Supplement to Volume 23, History of Political Economy*, edited by C.D. Goodwin, 143-178. Durham NC and London: Duke University Press. 1991; G John Ikenberry, 'A world economy restored: expert consensus and the Anglo-American postwar consensus'. *International Organization*. (1) 46, (1989), 289-321.

proposal for a clearing union and 'Bancor' rested on his concern for Britain's position as a debtor, and he urged that the burdens of adjustment should also fall on the US as the leading creditor. In order to create liquidity in the world economy, and to remove deflationary pressure on debtors, Keynes proposed the creation of international money and the provision of overdrafts to debtor countries so that they were not compelled to deflate. White's stabilisation fund was more conservative: it did not allow for the creation of bank money, and instead limited the IMF to the quotas contributed by each member state.

Of course, the Americans felt that Britain as the debtor should take action to put its economy on a firm footing, without the dangers of inflation from the creation of Bancor. Equally, the British felt that the Americans lacked a full appreciation of their plight and were repeating the mistakes of the 1920s when too much of the burden of adjustment was passed to debtor countries, with disastrous consequences. The different approaches also reflected the banking practices of the two countries, for British banks allowed customers an overdraft facility – something that the Americans felt would lead to inflation and imprudence.

Britain had very little alternative except to agree to the American proposals. Despite the different starting points of Keynes and White, deadlock was avoided for three reasons. The first reason was that there was a basic agreement on what needed to happen. The second was that the British negotiators in the period leading to Bretton Woods were in a weak financial and economic position and had little option except to make concessions. And thirdly, domestic political interests did not intrude to any

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great extent – not only because of the highly technical nature of the issues, but also because of the circumstances of the war. Consequently, the problem of a two-level game at the international and national level, with the danger of asymmetry, did not arise.

The outcome for global governance was the exclusion of the voice of developing countries who were largely absent from Bretton Woods, and weighted voting which gave control to countries according to their quota. Further, the narrow agenda of Bretton Woods led to inflexibilities in face of the new problems which arose in the 1960s. The aim had been currency stability not realignment; thus the IMF was incapable of dealing with new problems as the dollar weakened and the yen and DM strengthened.

The narrow agenda of Bretton Woods led to the later creation of G77 by developing countries keen to press for compensatory finance rather than currency stability. The US was suspicious of the IMF, for the Europeans as a bloc had veto power, as well as holding the managing directorship. The emergence of G8 led to a potentially more manageable body to negotiate reform, but it was also dominated by Europeans which led to suspicion by the Americans. The institutional structure was not able to resolve the crisis, and in the end the only solution was ‘benign neglect’ - allowing a crisis to develop in the hope that it would create the opportunity for reform. Even when the crisis came in August 1971, no one had a solution and the outcome was a decade of uncertainty. The IMF was neither legitimate nor effective in dealing with the crisis in the 1970s, with a failure to agree on positive steps for

reform.⁸ The IMF has been no more effective in the recent problems with international finance, and has not escaped from the limitations of its creation.

Havana, GATT and the International Trade Organization

The outcome for trade was very different from that for currency policy. Discussion concerning matters of international trade was largely left until after the end of the war: many more countries were present, and they had a much greater voice which challenged the proposals put forward by the Americans. Furthermore, Britain had a chance to reopen some of the issues on which they had given ground in 1944, seeking redress for the problems of debtor countries that it failed to secure in the currency talks. The concessions made by the British in order to resolve the monetary problems were fought again in the negotiations over trade – and the politics of trade had much greater political resonance in both Britain and the USA. The result was a draft Charter for the ITO which was signed at Havana in 1948 but which did not stand a realistic chance of ratification: concessions in the international arena led to a document that alienated far too many groups at home. The two-level game was not resolved.

The failure of the ITO may be explained by the intrusion of domestic interests to a much greater extent than in the agreement made at Bretton

⁸ see Harold James, *International Monetary Co-operation since Bretton Woods*. New York: Oxford University Press, 1996.

Woods in 1944. Trade was intrinsically more liable to become a political issue, and the conference was differently constituted, with more and divergent voices. Above all, the problems of negotiating an acceptable Charter for the ITO were intensified by deeply divisive notions of fairness and justice which connected with domestic concerns. Indeed, the failure to establish the ITO was probably a desirable outcome for the future of multilateral trade negotiations: it was over-burdened with deeply contentious issues going far beyond trade. By contrast, the interim General Agreement on Tariffs and Trade could proceed to reduce tariffs on a more pragmatic basis without such a destructive presence of normative issues.

Discussion of the recreation of multilateral trade was crucial to the vision of the post-war world. The earlier outbreak of policies of self-interest following the introduction by the US of the Smoot-Hawley tariff of 1930 and the introduction of British imperial preference in the Ottawa agreement of 1932 marked a collapse of the world economy into economic nationalism and trade blocs based on bilateral deals. This development was known as Schactianism, after its main proponent, the president of the German central bank and economics minister under Hitler, Hjalmar Schacht.

The main opponent of Schactianism was Cordell Hull, the Secretary of State in the US between 1933 and 1944: he was the reincarnation of Richard Cobden who firmly believed that free trade meant both peace and prosperity. As Hull put it in his memoirs,

unhampered trade dovetailed with peace; high tariffs, trade barriers, and unfair competition, with war... if we could get a freer flow of trade

... so that one country would not be deadly jealous of another and the living standards of all countries might rise, thereby eliminating the economic dissatisfaction that breeds war, we might have a reasonable chance of lasting peace.⁹

He was particularly opposed to imperial preference which was worse, in his view, than high tariffs. Whereas tariffs fell on all countries equally, preferences were more distorting of world trade (and particularly hit American exports).

Hull's first achievement was the Reciprocal Trade Agreement Act of 1933 which depoliticised trade agreements by passing power from Congress (with the opportunity for special interests to press for favours) to the President within a set limit of a 50 per cent reduction in tariffs. The Act allowed bilateral deals with other countries to reduce tariffs, and Hull's aim during the war was to extend this approach to a more generalised system of multilateral negotiations as part of the reconstruction of the post-war economy on a new basis of open trade and prosperity. The RTAA had to be periodically renewed which became more difficult at the end of the war with rising Republican influence in Congress, so that the ambitions of Hull faced constant challenge – above all in the person of William Clayton, the assistant Secretary of State with responsibility for carrying on the task of creating a multilateral world economy. Moreover, the definition of multilateral trade was a matter of serious

⁹ Cordell Hull, *The Memoirs of Cordell Hull, Volume 1* London, 1948, pp. 81-3

dispute with the British government which started to develop its own policy on post-war trade.

In 1942, James Meade of the British Cabinet's Economic Section, produced a scheme for an international commercial union. He stressed that Britain more than any other country depended on multilateral trade; but he was also well aware that its post-war balance of payments deficit made it unwise to remove imperial preference at once.¹⁰ He therefore started to devise a particularly British approach to multilateralism which emerged in the context of negotiations over Lend-Lease – the provision of American munitions and resources to Britain without payment – which required (under article VII of the agreement) the dismantling of imperial preference. At once, there was a different definition of multilateral trade which affected negotiations.

The American side was anxious to complete the negotiations over article VII and the terms of any loan to Britain at the end of the war which contained a further obligation to reduce preferences before turning to the wider negotiations over trade. The British were reluctant to engage in the wider negotiations without dealing with preferences at the same time, so that

¹⁰ James Meade. 'A Proposal for an International Commercial Union [1942]'. In *The Collected Papers of James Meade: Vol. III, International Economics* edited by Susan Howson, 27-35 London, Unwin Hyman, 1988.

they could secure a *quid pro quo* of reductions in American tariffs. Furthermore, the war-time coalition government in Britain was reluctant to push the trade negotiations because of internal dissensions between Conservative imperialists who felt that the empire provided a secure market for British goods; the advocates of free trade; and Labour supporters of international planning. Consequently, the whole process of trade negotiations was delayed until the end of the war. This delay fundamentally changed the political dynamic from that experienced at Bretton Woods in 1944.

The American loan to Britain was agreed in December 1945, and on the same day the two governments published the *Proposals for Consideration by an International Conference on Trade and Employment*.¹¹ These *Proposals* led to a series of meetings and conference, starting with a preparatory meeting in London in 1946, continuing with a conference at Geneva in 1947. This conference led to the interim General Agreement on Tariffs and Trade, a draft Charter of the ITO, and culminated in the conference at Havana in 1947-48 which led to the signing of a revised Charter. Since the Charter was never ratified, the interim GATT survived until it was incorporated into the World Trade Organization in 1994. These post-

¹¹ British Parliamentary Paper. 1945. Cmnd. 6709, 'Proposals for Consideration by an International Conference on Trade and Employment', 6 Dec. 1945.

war negotiations involved more countries with fundamentally different agendas.

One area of fundamental difference was employment. In the case of Britain, Meade realized that dependence on trade would have to rise after the war in order to solve the deficit on the balance of payments. This would make Britain susceptible to any recession in the States. He feared that such a situation was dangerous, given the inherently unstable nature of American capitalism, and many Labour politicians and Treasury officials agreed. One Treasury official commented that:

We tie ourselves up to the highly peripatetic US economy – and, what is more, we agree to increase our dependence upon international trade.... We are, in fact, embarking upon a high import-high export policy with no safeguards at all about the stability in USA and with very limited powers to take protective action in co-operation with like-minded countries to ease the impact of US depression on our economy.¹²

In response to such fear, Meade worked up a plan in 1946 for international full employment as a complement to his scheme for a commercial union. A Treasury official explained that Meade's plan was 'good socialism and good sense': it was a way of securing what had not been possible in the Bretton Woods agreement, namely an obligation by the

¹² The National Archive, T236/702, 'International full employment', R.W.B. Clarke, 18 July 1946

creditor country to take action to adjust its economy and not to pass all of the burdens to the deficit economy.¹³

A commitment by every country to maintain domestic full employment would allow the reduction of trade barriers; and if any country – above all the US – had a serious recession and mass unemployment, other countries should be allowed to take defensive action. As one British official noted, ‘there is very considerable feeling everywhere that countries cannot afford to disarm if the elephant [the US] is going to run amok. Especially if the elephant then says that it is the only sane and virtuous animal in the zoo.’¹⁴

Not surprisingly, the American position was somewhat different, with considerable scepticism that socialism could be equated with good sense. In the United States, the more progressive policy of the Full Employment Bill of 1945 gave way to the more cautious Employment Act of 1946. The Full Employment Bill of 1945 assumed that unemployment was a natural consequence of free enterprise which was liable to ‘brief periods of growth and development culminating in peaks of prosperity that gave way to disastrous collapse’. The Bill proposed to supplement free enterprise by

¹³ TNA, T236/702, Commercial policy: talks with New Zealand, note of meeting, 17 June 1946; ‘International employment policy’, nd [June 1946]; S.D. Waley to B. Trend, 18 Oct. 1946; T236/704, S. D. Waley to P. J. Grigg, 28 October 1946.

¹⁴ The National Archive, T236/702, S.D. Waley to B. Trend, 18 Oct. 1946; T236/704, S. D. Waley to P. J. Grigg, 28 October 1946

setting the level of federal 'compensatory finance' in order to ensure that 'all Americans able to work and desiring to work are entitled to an opportunity for useful, remunerative, regular, and full-time employment'. Opponents of the Bill argued that inappropriate lessons were being drawn from the unusual conditions of the 1930s, and that in normal circumstances the economy tended to full employment. They felt that some unemployment was inevitable and even desirable: business cycles were an essential part of the process of economic adjustment as resources moved in response to changing consumer demand. Hence the Bill would slow down economic adjustment so that reduction of unemployment in the short term would only intensify it in the long run. At the same time, the pursuit of full employment 'would result in inflation of prices and an artificial boom, and then the very depression and unemployment we are trying to avoid'.¹⁵

The opponents of the Bill rejected the insertion of a right to employment into law as at best a pointless exercise since nothing could be done to enforce it; and at worst as a non-American exercise in socialism. The outcome was the Employment Act of 1946 – the change in title indicating a fundamental weakening of ambition. It dropped the right to employment and the federal government's responsibility to ensure full employment through 'compensatory finance'. The Act expressed an *intention* and not a

¹⁵ Gary J Santoni, 'The Employment Act of 1946: some history notes', *Federal Reserve of St Louis*, 1986 7-12

requirement to achieve the maximum useful employment for those able and willing to work, rather than a commitment to full employment for all.

The American approach was much more limited than the British wished, and the 'Proposals' became part of a very different intellectual framework in Britain. Clement Attlee, the Labour prime minister, admitted in 1946 that 'In certain specific points of world economic planning, we find the United States in agreement with us, but, generally speaking, they hold a capitalist philosophy which we do not accept'. Hugh Dalton, the Chancellor of the Exchequer, believed that multilateralism meant agreements between governments to create 'the most sensible forms of International Economic specialisation.... the *ultimate* goal, must, I think, be a kind of supreme International Economic Planning Body'.¹⁶ This was exactly what the Americans did not want. There was, in other words, a failure of consensus from the outset, and deep ideological divides over the meaning of multilateralism.

The disagreement between Britain and the States was as nothing compared with what was to happen. In attempting to tame the American elephant, other beasts were released from the zoo, and these scared the British government. The first beast that caused alarm came from within the

¹⁶ Richard Toye, 'The Labour Party's external economic policy in the 1940s'. *Historical Journal* 43 (1) 2000, 189-215

British empire, from Australia's Labour government which initially provided the lead for less developed countries in the discussions at London and Geneva.

The Australian White Paper on full employment of 1945 asserted that 'full employment can be maintained only as long as total expenditure provides a market for all goods and services turned out by Australian men and women, working with available equipment and materials, and fully employed after allowing for the need for leisure'. On this view, what was needed was the full utilisation of the resources of the world in order to ensure a market for primary products on which Australia relied. If 'dependent countries' – primary producers such as Australia – were required to abandon economic protectionism, they needed assurance that other countries fulfilled their 'basic obligation' to maintain effective demand. Failure to do so should permit the complainant to take action against the errant country – most probably the United States - in order to prevent the spread of depression.

The Australian Labour government's commitment to full employment was particularly important because of the politics of demobilization. There was long-standing opposition to conscription in Australia. This had split the Labour party in the First World War, and still led to serious disputes. In compensation for conscription and even more for compulsory service overseas, the Labour government promised that ex-soldiers would have priority in jobs, a concession that contradicted the long-standing union demand for a closed shop. Full employment was a means of satisfying both the trade unions and the opponents of conscription: if everyone had a job, the dilemma was resolved. Quite apart from the political appeal of full

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employment, the Australian government was well aware of the impact of the depression in primary products which had such devastating impact in the 1930s.¹⁷

The policy of the Australian Labour government alarmed even the British Labour government. The British felt that it 'is bound to cause resentment on the part of the Americans at whom it is obviously aimed', and decided that it was 'tactically wrong for us to put it forward' in the post-war conferences.¹⁸ Of course, the Australian policy would potentially hit Britain by increasing the price of primary products compared with manufactures, and so worsen the British balance of payments.

Matters took a still more alarming turn from the British and American point of view as other primary-producing or under-developed countries started to develop an even more radical position on employment issues. In the preparatory meetings in 1946, the Colombian representatives pointed out that the Americans assumed that a precondition for a high level of employment was the removal of regulations and practices impeding the free development of world trade. They were sceptical, arguing that full employment was

¹⁷ Shirley Jenkins, 'Australia plans full employment', *Far Eastern Survey* (17) 14 (1945), 240-2; Tim Rowse, 'Full employment and the discipline of labour: a chapter in the history of Australia social democracy', *The Drawing Board: An Australian Review of Public Affairs* 1 (2000), 1-13.

¹⁸ The National Archive, T236/703, S.D. Waley to B. Trend, 'International employment policy', 14 October 1946.

inseparable from two objectives: the encouragement of a variety of production; and the success of manufacturing industries which paid higher wages than extractive industries and helped to create 'a mentally and morally superior working class'. The Colombians argued that such an evolution could not be achieved 'by depriving young industries of all protection' and that 'a policy of trade freedom should be developed in harmony with the peculiar conditions prevailing in industrially-backward countries'.¹⁹

The theme was developed by the Indian delegates who complained that the Americans showed insufficient appreciation of the problems of less developed countries. Nehru put the Indian case most strongly and forcefully, contradicting American commitment to free enterprise and multilateral trade, and making a strong case for the economic policy of India as it moved towards political independence:

the obligation of countries with undeveloped economies to develop their resources could only be fulfilled by instruments such as developmental tariffs and quantitative controls, and by adequate safeguards. India was wedded to economic planning as opposed to

¹⁹ The National Archive, T236/704, United Nations, Economic and Social Council, Preparatory committee of the international conference of trade and employment: memorandum on the objectives of the international trade organization in respect to employment (submitted by the secretariat), London E/PC/T/W.18, 19 Oct. 1946.

free enterprise.... A developing country was ... likely to cause immediate unemployment in other countries in the industries it was developing. ... Developed countries should be obliged to make reasonable adjustments in their own industries.²⁰

The Indians were adamant that the Charter should allow countries to take action appropriate to their particular stage of development and to their social and political institutions. Political independence from the British would be a sham unless India could develop its economy and escape from the long-shadow of subservience to British economic needs.

The Cubans pressed yet another line, arguing that members of the ITO 'should be obliged to take every action against conditions detrimental to work-people, and towards raising their standard of living.' In their view, sweated labour contradicted the purpose of the ITO, and

tended to attract foreign investors who were not so much interested in improving the workers conditions as in profits. Goods produced under these circumstances would undersell in the world market those produced in countries with better workers' conditions and would ultimately have a detrimental effect on these conditions.

²⁰ The National Archive, T236/704, United Nations, Economic and Social Council, Preparatory committee of the international conference on trade and employment, Committee I, summary record of meetings, second meeting, part, two, 21 Oct. 1946, E/PC/T/CI/7, 22 Oct. 1946.

Consequently, the ITO 'should endeavour to establish a salary regime and general working conditions which would enable the workers to bear a dignified existence'.²¹

Clearly, these claims to special treatment and to dignified existence alarmed developed countries. The British feared that the draft charter on employment might become a threat rather than (as originally intended) a buffer against the power of the United States. As a Treasury official remarked, 'all under-developed countries are pressing for virtually unlimited rights to protect infant industries. This is of course completely unacceptable to us, but it is likely that the provision will have to be made under ITO for the promotion of such countries' economic development'.²² These issues were fought over in the preparatory meetings and conferences in 1946-8. Trade itself was contentious within both Britain – between the proponents of free trade and imperial preference – and in America, where the Republicans were suspicious of Hullite multilateralism. Trade was quite unlike the highly technical issues of

²¹ The National Archive, T236/704, United Nations, Economic and Social Council, Preparatory committee of the international conference on trade and employment, Committee I, summary record of meetings, second meeting, part two, 21 Oct. 1946, E/PC/T/CI/7, 22 Oct. 1946; T236/704, United Nations, Economic and Social Council, Preparatory committee of the international conference on trade and employment, observations by the Cuban delegation, E/PC/T/CI/10, 28 Oct. 1946.

²² The National Archive, T236/704, No 102 Eager 28 Oct. 1946

currency; and the conflicts were compounded by inserting deeply divisive considerations of distributive justice and employment.

The negotiators at Geneva and Havana were faced with huge difficulties in producing a text that all participants in the international conferences could accept – and success in creating a compromise in negotiations at an international level was highly unlikely to win support from domestic interests within the United States. The two-level game could not be reconciled, for in creating a deal at Havana the American negotiators were seeking to reconcile the views of other countries which were out of kilter with the domestic coalitions needed to secure ratification of the Charter in Congress.

The problem was made all the more intense by the shift in membership and voting rights between the conferences at Geneva and Havana. At the latter, undeveloped countries had a greater voice. The Bretton Woods agreement was largely determined by negotiations between the United States and Britain, and other participants at the conference signed a 'done deal'. Negotiations over trade took a very different form; many other countries took part. When detailed discussion over the path to multilateral trade started at Geneva in 1947, 23 countries comprising 80 per cent of world trade produced a draft Charter of the ITO and negotiated the General Agreement on Tariffs and Trade. The Geneva conference gave more voice to more countries than did Bretton Woods, but even so the negotiations at Geneva were dominated by developed countries. What would happen at Havana?

The Americans were anxious that voting rights should be limited to full members of the United Nations, but the British government disagreed, arguing that such a limitation rested on the 'completely misconceived idea that the prestige of the United Nations depended on exclusivity rather than on the successes it achieves'.²³ Of course, votes in the UN on security and general political issues were necessarily confined to members. In the case of functional specialised agencies, such as the International Labour Organization or World Health Organization, effectiveness meant including the greatest possible number of countries in the particular field. The British argued that the Charter of the ITO would affect the economy and trade of everyone, and would arouse opposition unless everyone invited to Havana could show their parliament and public opinion that they had a voice. Legitimacy, on this view, meant an inclusive approach.

In the end, the British won the argument and every country was allowed to attend and to vote. However, the Americans went much further than the British wished, abandoning the initial proposal of the British government that voting should be weighted by trade so as to ensure the dominance of the developed world. Instead, the Americans accepted a un-weighted franchise of one country, one vote as a way of securing wider adherence to the ITO. Rather than expressing gratitude, as was naively

²³ The National Archive, FO371/62312, S L Holmes (Board of Trade) to F W Marten (Foreign Office), 23 Aug 1947.

assumed, the majority of undeveloped countries instead pressed for greater concessions. The balance of power changed in favour of the under-developed countries which altered the dynamic of the two-level game: a compromise in international negotiations was more likely to result in concessions that alienated important domestic interests. Institutional design made ratification of the Charter more problematical.²⁴

The under-developed countries took it as axiomatic that the draft of the Charter agreed at Geneva was heavily weighted in favour of the 'big commercial countries'. In particular, the Latin American countries played a crucial role in securing revisions at Havana. They were concerned that America was turning its attention to the reconstruction of Europe through the Marshall Plan and, in the words of the Canadian report on the conference,

the fairy godmother of the North was deserting them in favour of Europe. Their acquaintance with socialist ideas had converted them to a form of international socialism in which the richer countries were under an obligation to the poorer countries to promote the economic

²⁴ The best account of the debates over institutional design is in the report from the Canadian delegation: *Documents on Canadian External Relations, Volume 14*: 581, Secretary of State for External Affairs to heads of post abroad, 4 June 1948 at <http://www.international.gc.ca/departement/history/dcer/details-en.asp?intRefid=10321>

development of these countries and to raise their standard of living up to that of the richer countries.²⁵

During the war, new industries developed in Latin America as a result of a reduction in imports from the United States and Europe. Once the war was over, Latin Americans feared the revival of European competition. Their aim was to maintain quantitative restrictions and preferential arrangements to encourage development within Latin America, based on economic integration and import-substituting industrialisation. Their approach was clearly expressed at Havana by the representative of Venezuela:

The equality embodied in the Charter must not be of the nineteenth-century type, which actually established disequality [sic] by making it impossible, for instance, for Latin American Countries to develop new economies. During that period they had furnished raw materials and had been a dumping ground for finished products. This had now been substituted by the just idea of economic interdependence for the welfare of all. A Charter would not be possible unless the old

²⁵ *Documents on Canadian External Relations, Volume 14*: 582, Chief delegate, delegation to the United Nations Conference on Trade and Employment to Secretary of State for External Affairs, 13 July 1948, at <http://www.international.gc.ca/departement/history/dcer/details-en.asp?intRefid=10322>

prejudices were discarded and instead modern dynamic principles of co-operation adopted.²⁶

Such a developmental approach clearly complicated Hull's and Clayton's panacea of multilateralism as a solution to the economic problems of the world. To secure a deal, they gave way: development quotas were allowed to restrict imports in order to support infant industries. New preferences were permitted on condition that they were within the same economic region and were needed for development. Since Britain was committed to ending its own preferences by the terms of Lend-Lease and the American loan of 1945, there was an obvious inequity if other countries were able to introduce new preferences at the expense of British export markets. The issue was finally resolved by inserting a footnote to the effect that an economic region could be defined in terms of integration as well as proximity, so covering the British empire. Hence imperial preferences could be preserved by the Charter of the ITO, marking a considerable loss for the American negotiators. Furthermore, the Charter allowed nationalisation and compensation for foreign capital on terms that seemed grossly inadequate to many American businessmen. Many critics came to the view that the Charter was more of a threat than an opportunity.

Whilst Clayton was busy pursuing multilateralism at Havana, domestic opposition was becoming apparent. Although the Republicans had been

²⁶ The National Archive, BT11/5206, seventh plenary meeting, 29 Nov. 1947

willing to accept the renewal of the RTAA, the ITO Charter was quite another matter. Congress did not ratify the ITO which fell foul simultaneously of two groups. On the one side were the 'perfectionists' who felt it was insufficiently committed to free trade; on the other side were the 'protectionists' who felt that it surrendered too much.²⁷ The Charter of the ITO had become overburdened with conflicting and unrealisable ambitions so that the limited scope of the GATT was more realistic.

The failure of the ITO and survival of GATT was, in the words of a recent commentator

a blessing in disguise: with a multifaceted agenda ranging from restrictive business practices to intergovernmental commodity agreements, the ITO risked evolving into a large bureaucracy that would have institutionalized and sanctioned state regulation of international commerce as much as it would have freed trade from such controls.... The narrow focus of the GATT served the process of trade liberalization ... well because the GATT's mission was simple and straightforward. The GATT had no autonomous power, independent leverage, or financial sanction. The GATT, in some

²⁷ William Diebold, 'The end of the ITO', *Essays in International Finance* 16, Princeton University, 1952.

sense, did not exist beyond the commitment of its members ... to reach certain goals through a negotiated consensus.²⁸

The Havana conference showed the dangers of wide representation. It was clear that this led to serious difficulties in solving the two-level game. Success at Havana meant failure on Capitol Hill.

Pascal Lamy is not correct to suggest that adding employment to current trade negotiations will break the deadlock. Indeed, the experience of Havana suggests that it might lead to even greater failure. The story of the ITO charter suggests that overloading the negotiations as in the Doha Development Agenda is not practical politics; that a democratic voting structure might lead to legitimacy but it also threatens effectiveness.

CONCLUSION

The experiences of the monetary conference at Bretton Woods and the trade conferences at Geneva and Havana were very different. In the first case, the two-level game was relatively simple. Both Britain and the US administrations wished to resolve the problems of currency instability, and they had a high level of agreement on the basic requirements for success. There were different emphases between the proposals of Keynes for Britain

²⁸ Kym Anderson and Bernard M Hoekman, *The Global Trading System*, London: I.B.

Tauris, 2002: p. 221

and White for the US, but these did not prove to be insurmountable because both sides realised that there was too much at stake, and because the Americans could impose their wishes on a much weaker partner. The British took comfort from any concessions by the Americans, realising their parlous position.

At Bretton Woods, the agreement reached between these two unequal partners was acceded to by the other 42 countries. After all, the dollar and sterling were the two key international currencies so that the United States and Britain had the major say. Furthermore, international negotiations were insulated from domestic politics. The issues were highly technical and difficult to explain – not least during the exigencies of war and other more immediate concerns. Popular political debate focused instead on issues such as the nature of the post-war welfare system and on full employment – and it was these issues that contributed to difficulties in negotiating the post-war deal on trade.

The post-war conferences on trade faced much greater difficulties at both the international and intra-national level. Trade was intrinsically more politicised and more immediately understood by electors and by various interest groups. In the closing stages of the war, trade politics intersected with policies on full employment and welfare in a manner that created fissures both within countries (as in the debates over the Full Employment Bill in the US) and between them (as over the divergent approaches of Britain, US and less developed countries). The negotiations over trade and the wider issues of equity between developed and under-developed countries started with fewer

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countries (23) but they all had some voice; and by the time of the conference at Havana, more representatives with widely disparate views had greater voice with the shift to wider participation and the replacement of weighted voting by one member, one vote.

The dispute over institutional design raised major issues of what was politically realistic and feasible. The final draft Charter of the ITO was hard-won at Havana, but the deals struck there did not command support from domestic interests where another pattern of coalitions and trade-offs was needed. The solution at Bretton Woods rested on a separation between domestic and international concerns; this was not feasible in the debate over the ITO. Although the RTAA created something of a buffer between domestic and international concerns in the United States, it was only partially successful: it helped to limit the intrusion of Congressional politics in tariff reduction; it was not likely to succeed on the wider normative issues of full employment and justice in international economic relations.

The example of Havana shows that a wider membership and more democratic franchise are deeply problematic if combined with an extremely broad agenda. The draft Charter of the ITO raised major normative issues of justice and equity on which compromise was extremely difficult. The attempt to create a consensus between the extremely diverse parties at the conference meant that domestic acceptance was more difficult within the US, which was what really mattered if the Charter were to have any credibility.

The relationship between agenda-setting and representation was crucial. The British wanted a wider agenda to control the 'elephant' of the US,

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with the danger that the agenda was then captured by less developed countries and taken in a radical direction. The British also wanted wider membership to legitimate the agreement, though with a less democratic franchise than desired by the Americans. Could a wide agenda and wide membership be reconciled? The evidence of the two conferences at Bretton Woods and Havana suggests that success was more likely when the agenda was limited and representation was narrower: GATT and tariff cuts survived, whereas the ITO failed. But did the failure of the ITO matter? In fact, it was probably beneficial for the future of trade negotiations by passing the large normative issues of distribution were passed to the UN Economic and Social committee where they could be debated apart from the practical trade issues decided at GATT. Compartmentalisation proved beneficial.

This is the lesson that Pascal Lamy has not learned. The moral to be drawn from the current failure of the Doha Development Agenda is not, as Lamy suggests, that the wider issues should be inserted into trade talks as they were at Havana. Rather, it is that an over-loaded agenda is unlikely to succeed. The final collapse of the Doha Development Agenda might be a blessing in disguise, as was the abandonment of the Charter of the ITO.

Of course, the politics of the two organizations – the IMF and GATT – changed over the next 20 or 30 years, leading to continued tension between legitimacy and effectiveness. The IMF was effective in meeting a very limited post-war agenda of currency stability, but proved incapable of dealing with the problems of disequilibrium in the world economy that led to the suspension of the regime of exchange rates created at the end of the Second World War.

Its agenda was too narrow and its structure too rigid to cope with new challenges; and it lacked legitimacy because of the weighted voting system and the dominance of a few countries at its inception. Much the same could be said at the present time. Meanwhile, GATT was denounced as a 'rich man's club' and the policies of the less developed countries were articulated through G77 and the United Nations Conference on Trade and Development. Questions of legitimacy and agenda setting remained a matter of concern.

This longer story is one that I will be addressing in my forthcoming book which takes the story to the present – but for the moment, I would suggest that we need a clear understanding of the circumstances under which institutions emerged during and after the Second World War. It was at this time that they took on characteristics that have shaped the governance of the world economy over the last 70 or 80 years, and have proved remarkably resistance to change. How to bring about their redesign is not an easy task.