TOWARD A MOSAIC ECONOMY: ECONOMIC RELATIONS IN THE POST-COLD WAR ERA

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At the outset of the final decade of the twentieth century, the world economy has entered a critical period of transition. Change, as usual, is driven primarily by developments in the advanced industrial nations—the countries that for decades have dominated every aspect of international economic relations. Recent developments in the industrial world have been momentous: the emergence of Japan as a financial and commercial superpower, the revived pace of regional integration in Europe, the continued erosion of America's industrial competitiveness, not to mention the end of the cold war. Taken together, these developments suggest that fundamental changes may now be anticipated in the design and management of the global economic system.

Despite emerging strains, it will be possible to preserve the essential elements of the open, multilateral order erected after World War II. Tensions and friction will undoubtedly be amplified across a broad range of issues, but resistance to disruptive forces will also be strong, owing to certain enduring characteristics of the postwar system. If we are in transition to anything, it is toward a much more variegated and mutable order than we have grown accustomed to in the past, one which can best be described as a mosaic of international economic relationships.

Catalysts for a Changing Economic Order

In the aftermath of World War II, the industrial nations succeeded in creating a remarkably open and prosperous international economic order. Rising volumes of foreign trade and investment played a key role in promoting the continued growth of domestic economies. National markets, in turn, became increasingly integrated on a scale not previously seen in this century. Until now at least, the governments of industrial nations have succeeded in maintaining and even extending the liberal postwar order despite ever-lurking forces of parochial nationalism and particularist interest. Policy conflict has

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not been absent, for tensions and friction are endemic to any system of economic relations among sovereign states. The important point, however, is that for over four decades conflict has been kept manageable, as national policymakers have cooperated to avert any serious threat of disintegration or breakdown in the global economy such as occurred in the 1930s. The caliber of economic management may not be to everyone's taste, but it has contrived, by and large, to preserve the acknowledged benefits of commercial and financial interdependence.

As the decade of the 1990s begins, those benefits seem increasingly at risk as a result of two recent and dramatic developments in global affairs. The apparent ending of the cold war can be expected to alter significantly the calculations that citizens and governments of the industrial world are likely to make in dealing with their common economic problems. Additionally, the accelerating redistribution of economic power among western nations—in particular, America's relative eclipse in the shadows of a resurgent Europe and an increasingly assertive Japan—may affect both the ability and the willingness of the United States to bear its traditionally large share of the costs of economic leadership. Together these two developments threaten to shrink dramatically the supply of cooperative behavior in international economic relations even as the need for it increases in order to cope with a mounting array of troublesome issues.

The end of the cold war is a critical challenge because it removes one of the most important adhesives that, for forty-five years, held the western world together: the specter of a security threat from the Soviet Union. Europe, North America, and Japan may have been competitors in the marketplace, divided by their divergent commercial and financial interests, but they never permitted themselves to forget that they shared a common security interest as well. Because all industrial nations attached considerable value to the "public good" of collective security, economic rivalries, no matter how potentially explosive, were never allowed seriously to endanger the underlying foundations of the Western Alliance. All ultimately preferred to shelter themselves under their joint "security blanket."

With the waning of the Soviet threat, the perceived value of the postwar alliance system is bound to erode. Some common security interests will remain, as Saddam Hussein's invasion of Kuwait in the summer of 1990 clearly demonstrated. But nothing frightens like the danger of nuclear annihilation. Absent that threat, the value of the western security blanket will almost surely be considerably discounted, and this in turn will likely intensify the narrow egoism of key actors in each of the industrial nations, inside as well as outside of government. *Ceteris paribus,* greater weight will be attached to self-interest at the local or national level or, as in the European Community (EC), at the regional level. Correspondingly, nations will devote less attention to collective interests, and will increasingly be tempted to "free ride" in international economic relations. Resistance to concessions under present cooperative arrangements can certainly be expected to grow, and possibly there will even be unilateral defections from commitments previously made, risking greatly amplified tensions and friction across a broad range of issues in global economic relations.

The accelerating redistribution of economic power among the industrial nations represents a critical challenge because of its effect on the West's ability to contain the adverse consequences of increased free riding by individual governments. For many years nations relied, first and foremost, on the resolve and capacity of the United States to preserve the liberal postwar order against the corrosive effects of mutually uncooperative behavior. One does not have to be a fanatical devotee of the familiar "theory of hegemonic stability"[1] to acknowledge the extent to which the benefits of economic interdependence long depended on America's willingness to shoulder a disproportionate share of the burdens of leadership. This required timely concessions or sacrifices when necessary to resolve conflict and promote the welfare of its allies. In return for acknowledgement of America's dominant role in the western security system, Washington self-consciously accepted a special responsibility for management of economic affairs. In addition to providing relatively open markets for goods and capital and an abundant supply of the world's major international currency, America's most crucial contribution was strong and effective leadership in multilateral negotiations and in the major international organizations. An implicit bargain was struck in which Washington's allies acquiesced in a system that accorded the United States special privileges to act abroad unilaterally to promote US interests. The United States, in turn, condoned its allies' use of the system to promote their own economic prosperity, even if this happened to come in good part at the expense of the United States.

However, with the continued erosion of America's postwar economic predominance, best symbolized by its rapid transformation in the 1980s from the world's largest creditor nation to its largest net debtor,[2] the crucial assumption that the United States will not push its own private agenda to the point of fatally disrupting broader economic ties is beginning to look exceedingly complacent, if not downright unrealistic. The United States possesses neither the resolve nor the capacity it once had. The economic

1. The theory of hegemonic stability, which stresses the key role of a single dominant state in the maintenance of order in international economic relations, was developed more than a decade ago by Charles Kindleberger, Robert Gilpin, and Stephen Krasner. See Charles Kindleberger, *The World in Depression, 1929–1939* (Berkeley: University of California Press, 1973); Robert Gilpin, *U.S. Power and the Multinational Corporation* (New York: Basic Books, 1975); and Stephen D. Krasner, "State Power and the Structure of International Trade," *World Politics* Vol. 28, No. 3 (April 1976). The conventional appellation for the theory is attributed to Robert O. Keohane, "The Theory of Hegemonic Stability and Changes in International Economic Regimes," in *Change in the International System,* ed. Ole R. Holsti, Randolph M. Siverson, and Alexander L. George (Boulder, Colo.: Westview Press, 1980), 131–162. For a useful summary and evaluation of the theory, see Keohane, *After Hegemony: Cooperation and Discord in the World Political Economy* (Princeton: Princeton University Press, 1984), especially Ch. 3.

2. From a peak creditor rank of some $140 billion in 1981, according to official sources, America's international investment position declined to near balance in 1984 and to an estimated $665 billion of net debt by the end of 1989, reflecting the extraordinary deterioration of the current account of the US balance of payments that began in 1982. See *Survey of Current Business* Vol. 69 No. 6 (June 1989); and Vol. 70, No. 6 (June 1990).

ascendancy of Europe and Japan has sapped not only America's ability but, more importantly, its willingness to make painful sacrifices for the common interest. Increasingly, the burdens of economic leadership are being abandoned or rejected as too costly. Concessions on trade or monetary issues are now less freely offered, and foreign discriminatory practices less readily tolerated. Demands and threats are both more numerous and more frequently escalated and tend to be increasingly assertive, even aggressive, in tone. The infamous "Super 301" procedure of the 1980 Omnibus Trade Act, with its threat of possible retaliatory measures against nations labeled unfair traders, is indicative of this tougher attitude.[3] US Trade Representative Carla Hills has called Super 301 her "crowbar" to pry open the markets of Japan and other targeted countries.[4]

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Washington now looks to other industrial nations to shoulder more of the costs of economic stewardship. The United States has urged Japan, for example, to provide the bulk of the funds needed to underwrite the Brady Plan for Third World debt that was first announced in March 1989.[5] Later in 1989 the United States pressured the EC to take principal responsibility for organizing the West's financial contribution to the reconstruction of the newly liberalizing economies of Eastern Europe.[6] And in 1990 America pressed both the Japanese and the Europeans to make major trade concessions in an unsuccessful attempt to ensure a satisfactory conclusion to the Uruguay Round of the General Agreement on Tariffs and Trade (GATT) negotiations.[7] In effect, the United States has grown weary of being the main bulwark against free

3. The Super 301 procedure (actually set out in Section 310 of the 1988 Act) is an expanded version of Section 301 of the Trade Act of 1974. The toughest such measure yet legislated by Congress, it calls for identification by the Trade Representative of unfair trading countries and practices and sets out timetables for negotiation and possible retaliation. For a discussion of Super 301 see Jagdish N. Bhagwati, "United States Trade Policy at the Crossroads," *The World Economy* Vol. 12, No. 4 (December 1989): 463–467.
4. Clyde H. Farnsworth, "Why Trade Remains a Jumble," *The New York Times,* 29 January 1989, IV, F4.
5. Steven R. Weisman, "Japan Takes a Leading Role in the Third-World Debt Crises," *The New York Times,* 17 April 1989, A1.
6. See for example, "An Expanding Universe: A Survey of the European Community," *The Economist,* 7 July 1990, 19–20. The EC now coordinates the aid of twenty-four industrial nations under what has come to be known as the Phare program (after the French word for lighthouse). The membership of this new Group of Twenty-Four is identical to that of the OECD.
7. See for example, "Nothing to Lose But its Chains: A Survey of World Trade," *The Economist,* 22 September 1990, 29–37.

riding by others, becoming increasingly intemperate in its own pursuit of economic self-interest. This compounds the already heightened risk of amplified tensions and friction in economic relations resulting from the ending of the cold war. The key question for the industrial nations today is whether the liberal postwar order can still be preserved in the face of these critical challenges to mutually cooperative behavior.

The Prospects for Continued Economic Cooperation

In some quarters, it has become fashionable to take a rather pessimistic view on this question. Fears generated by the obvious erosion of America's economic predominance have of course already been in vogue for some time. Some scholars, labeled "declinists" by Samuel Huntington,[8] are persuaded of the irreversibility of present trends in favor of Europe and Japan. Not all analysts agree that the relative eclipse of the United States is permanent. Indeed, some authors have recently argued that America's apparent decline, as measured by various indicators of comparative economic performance, either has been greatly exaggerated or else can be more or less easily corrected.[9] Yet even most of these so-called "revivalists"[10] concede that the balance of power among western economies has in fact grown more diffuse and that this spreading of influence is almost certain to make collective management of commercial and financial affairs more difficult. Few would disagree with the cogent observation of Theodore Geiger:

> Just as the hegemonic role of the United States was one of the necessary conditions for the unprecedentedly high levels of economic integration and political coordination that characterized the international system (outside the Soviet hegemony) during the postwar period, so the waning power and influence of the United States in the present period are in part responsible for the system's gradually declining integration and coordination.[11]

The end of the cold war seems to exacerbate this trend. Though still a comparatively recent development, the sudden waning of the Soviet threat at the end of the 1980s has already provoked an anguished chorus of concern, not to say alarm, from informed specialists stressing the dangers of removing

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8. Samuel P. Huntington, "The U.S. Decline or Renewal?" *Foreign Affairs* Vol. 67, No. 2 (Winter 1988/89): 76–96. Among the authors specifically cited by Huntington are David P. Calleo, *Beyond American Hegemony* (New York: Basic Books, 1987); and, above all, Paul Kennedy, *The Rise and Fall of the Great Powers: Economic Change and Military Conflict from 1500 to 2000* (New York: Random House, 1987).
9. See for example, Henry R. Nau, *The Myth of America's Decline: Leading the World Economy into the 1990s* (New York: Oxford University Press, 1990); Joseph S. Nye, Jr., *Bound to Lead: The Changing Nature of American Power* (New York: Basic Books, 1990); and Richard Rosencrance, *America's Economic Resurgence: A Bold New Strategy* (New York: Harper and Row, 1990).
10. The term is Paul Kennedy's. See Paul Kennedy, "Fin-de-Siècle America," *The New York Review of Books,* 28 June 1990, 31–40.
11. Theodore Geiger, *The Future of the International System: The United States and the World Political Economy* (Boston: Unwin Hyman, 1988), xii.

the security blanket from western economic relations. Shafiqul Islam of the Council on Foreign Relations has written that "[t]he decline of the West's old common enemy of communism . . . is sowing the seeds of a capitalist cold war."[12] And Fred Bergsten of the Institute for International Economics has asserted that "the end of the Cold War could sharply heighten the prospect of a trade war."[13] For such commentators, it is almost as if the clock has now simply been turned back to the interwar period, or even to the nineteenth century, when economic rivalries were similarly unconstrained by a common security threat. The denouements of those earlier eras—first the Great War, then the Great Depression—certainly give little ground for optimism about the prospects for relations among the industrial nations in the future.

But is such pessimism justified? Is the liberal postwar order today really threatened with disintegration or breakdown? Or are such fears perhaps more than a little exaggerated? Certainly it is not implausible to argue that the postwar order, based as it was on the bipolar cold war, constituted a rather exceptional interlude in the broad sweep of global history. As political theorist Joanne Gowa has formally demonstrated, bipolar international systems are far more conducive to openness and stability in alliance economic relations than are their multipolar counterparts, since stronger incentives for intra-alliance cooperation exist in a bipolar world.[14] Hence it is not unlikely, as she suggests, that "the opening of postwar western markets" can indeed be attributed "to the transition from a multipolar to a bipolar international security system that occurred simultaneously."[15] The success of the postwar order can plausibly be said to have been the product of a very special set of historical circumstances.

Even so, the end of bipolarism hardly justifies alarmist pessimism about what is to come next. Not all the gains of the remarkable postwar interlude must inevitably be lost as we move once again toward multipolarism in international affairs. And the reason, quite simply, is that not all other relevant circumstances are being reversed at the same time, in tandem with the recent dramatic developments in superpower relations. The clock has not simply been turned back to an earlier, less cooperative era. In reality many other fundamental changes have also occurred in the world economy over the last forty-five years that will not disappear even with the end of both the cold war and US economic predominance. A good number of these changes act as countervailing forces to help lock in many of the benefits of commercial and financial interdependence that have been achieved since 1945. The success of the postwar order may not be so fragile after all.

At the systemic level, for instance, a variety of international regime structures[16] have been set in place to help promote collective economic man-

12. Shafiqul Islam, "Capitalism in Conflict," *Foreign Affairs* Vol. 69, No. 1 (1989/90): 172.
13. C. Fred Bergsten, "The World Economy after the Cold War," *Foreign Affairs* Vol. 69, No. 3 (Summer 1990): 96.
14. Joanne Gowa, "Bipolarity, Multipolarity, and Free Trade," *American Political Science Review* Vol. 83, No. 4 (December 1989): 1245–1256.
15. Ibid., 1253.
16. The standard definition of an international regime is a set of "implicit or explicit principles, norms, rules,

agement. These are often formally institutionalized in multilateral organizations like the International Monetary Fund (IMF) and the GATT or in regularized procedures such as the annual economic summits of the so-called Group of Seven.[17] The existence of international regimes by no means guarantees that all state behavior will be mutually cooperative, but it certainly does increase the probability that the tensions and friction so endemic in international economic relations will generally be successfully contained. International regimes facilitate cooperation by reducing uncertainty and transaction costs. They also help to suppress parochial nationalism by underscoring the importance of reputation and, if necessary, by providing collective enforcement mechanisms. Most importantly, as Robert Keohane has pointed out, they are easy to maintain once established. Hence international regimes tend to resist erosion, often for very long periods of time, even after the circumstances responsible for their creation, such as America's postwar predominance, have passed.[18] In Keohane's words: "The decline of hegemony does not necessarily sound cooperation's death knell."[19] On the contrary, the persistence of existing regime structures for trade, money, and the like suggests that the benefits of economic interdependence probably are in fact rather more robust than they might seem at first glance.

Similarly, at the state level, a variety of influential domestic and transnational constituencies have been created by the integration of national economies that now have an important stake in the maintenance of open markets for international commerce and finance. Particularist interests have always played a role in determining the foreign economic policies of sovereign governments, but where traditionally the balance of political forces at home might have tended to encourage protectionist restrictions and increased free riding abroad, today the reverse is often true. Equally powerful pressures on the "anti-protection" side of policy debates have emerged, often spurred by firms and industries now dependent on exports, imports, or multinational production and investments for a substantial portion of their earnings. As Helen Milner has argued: "Increased economic integration of advanced industrial states into the world economy [has] altered the domestic politics of trade."[20] The result is an augmented line of defense within every western nation against any assault on the cohesion and viability of the system as a

and decision-making procedures around which actors' expectations converge in a given area of international relations." See Stephen D. Krasner, *International Regimes* (Ithaca, N.Y.: Cornell University Press, 1983), 2.

17. The Group of Seven comprises the United States, Canada, Japan, Great Britain, France, Germany, and Italy. Meetings of the finance ministers of the Group of Seven also take place on a regular basis, though for some purposes consultations are limited to the Group of Five (excluding Canada and Italy) or even smaller configurations (e.g., the United States, Germany, and Japan).
18. Keohane, *After Hegemony,* 100–103.
19. Ibid., 9.
20. Helen V. Milner, *Resisting Protection: Global Industries and the Politics of International Trade* (Princeton: Princeton University Press, 1988), 290. See also I.M. Destler and John S. Odell, *Anti-Protection: Changing Forces in United States Trade Politics,* Policy Analyses in International Economics, No. 21 (Washington: Institute for International Economics, September 1987).

whole. These internal defenses are likely to persist and remain effective as countervailing forces even after the circumstances responsible for their creation have passed.

Finally, at the cognitive level, a variety of attitudinal changes have been bred by the achievements of the liberal postwar order that can also be expected to oppose any shrinkage in the supply of cooperative behavior in economic relations. Nearly half a century of successful experience with growing commercial and financial interdependence has clearly altered the dominant "economic culture"[21] in all the advanced industrial nations. Social values and perceptions have quite obviously shifted in favor of greater appreciation of the benefits of mutual restraint and open markets in international affairs. No longer is free riding accorded the same legitimacy as it was in the nineteenth century or interwar period. Today the burden of proof is on those who would disrupt foreign economic ties rather than those who would preserve them. There seems little reason why these changes as well should not persist and remain influential even in the new circumstances of the 1990s.

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Precisely *how* influential any countervailing forces are likely to be is difficult to say. In principle, international regimes, domestic politics, and social values all matter greatly to policymakers. In practice, however, their effectiveness in determining state behavior clearly varies from one issue to another and even, for any single issue, from one time to another. Thus prospects for relations among the industrial nations in this period of transition are also likely to vary both across issues and across time, depending on the relative strength of disintegrative and countervailing forces in each individual instance.

In short, the basic message is that no uniform or predictable pattern of change in the liberal postwar order should be expected in the post-cold war era. Global economic relations have of course always been messily ambiguous and differentiated to some extent. But now they are likely to become even more variegated and multi-layered than ever—growing closer in some instances, widening in others, and occasionally even reversing direction under

21. Economic culture has been defined as "a base of consensual knowledge of a non-factual nature, a set of values and beliefs about social economics which guides and legitimates policymaking. . . . [with] shared perceptions of reality and prescription forming the foundation of policy." See Paul Egon Rohrlich, "Economic Culture and Foreign Policy: The Cognitive Analysis of Economic Policy Making," *International Organization* Vol. 41, No. 1 (Winter 1987): 71.

the pressure of events. Increasingly the system will take on the characteristics of a colorful and complex mosaic, creating a world not easily reduced to simple aggregative analysis or broad facile generalization.

Issues of Agreement and Contention

The message of cooperation and conflict is clear in the pattern of relations between the United States and each of its major economic allies. The threat of amplified tensions and friction among the industrial nations in coming years is obviously very real. So too, however, is the promise of forceful resistance to disintegration or breakdown of the close economic ties that have been carefully cultivated since the end of World War II.

Competing American and Japanese Interests

By the end of the 1980s the atmosphere between the United States and Japan had grown highly acrimonious. Clearly the most contentious issue was the persistent imbalance in their mutual balance of trade. During the 1980s Japan's bilateral surplus with the United States soared above $50 billion a year, generating a rising tide of resentment and complaints from American business and labor. Americans criticized the Japanese for their habitual strategy of massive penetration of the US market in relatively narrow product lines which often caused severe injury to America's domestic producers.

In the early 1980s most US actions to counter the imbalance in trade stressed negotiation of so-called "voluntary" restraint agreements on Japanese shipments of such products as automobiles, textiles, finished steel, and machine tools. More recently, however, the major focus has been to promote increased American market penetration in Japan. In effect, Washington has cast itself in the role of *demandeur,* repeatedly assaulting the Japanese over allegedly unfair trade practices and, in the name of reciprocity, pressuring Tokyo for a variety of unilateral policy concessions. One commentator has labelled this America's "blame-thy-neighbor policy."[22] The objective, ostensibly, is to ensure equal opportunity for US firms and products in the Japanese market—the proverbial "level playing field."

Japanese reactions to all these pressures, not surprisingly, have tended to become increasingly testy over time. Gradually abandoning their customary diplomatic deference, Japanese officials and businessmen have begun to lash back, citing their own grievances against the United States, such as discriminatory government procurement programs, restrictions on the sale of Alaskan oil, and arbitrary interpretations of existing anti-dumping and countervailing duty regulations. America, they correctly point out, employs a wide array of tariffs and nontarriff barriers of its own to tilt the playing field in its favor.[23]

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22. Islam, 179. For a detailed critique, see Bhagwati, especially 454–463.
23. Perhaps the most detailed evidence for this is provided in annual reports on US trade practices published by the Commission of the European Community. In 1990 the Commission identified nearly 50 import barriers that illustrate, according to a senior Commission official, "that although the United States is in

Many Japanese feel that their country is as much sinned against as sinner and, as an emerging economic superpower, should stand up more firmly to Washington's persistent demands.

A Resurgent Europe

In the 1990s the US-Europe relationship is likely to be dominated by three key interrelated developments: the reunification of Germany, the revived pace of integration in the EC, and the reform and reconstruction of Eastern Europe. All three developments entail dramatic changes in the ordering of commercial and financial relations on the European continent. The risk inherent in each of them is that they could tend to turn Europe inward, tempting its governments to promote their own regional interests at the expense of outsiders like the United States.

Germany's reunification certainly alters the balance of economic power among the industrial nations. Germany's net creditor position in the world economy is exceeded only by Japan's and the Deutsche mark is more widely used internationally than any money other than the US dollar. Even before political reunification was formally complete, the Germans were already beginning to assert themselves more forcefully in various international economic forums. As the new era advances, there seems little reason to suppose that the Germans might shrink from further exploitation of their new-found commercial and financial leverage.

Moreover, the Germans are not alone. They are also part of the broader European Community, whose remarkable revival since the mid-1980s has served to further accelerate the redistribution of economic power. The launching of the EC's "1992" program triggered ambitious initiatives at the start of the 1990s for monetary unification and perhaps even some form of political union.[24] The deeper the process goes, the greater ultimately will be the EC's impact on commercial and financial affairs. One observer has likened the single-market project to "an economic earthquake in the making."[25] If a reunified Germany alone poses new challenges for the world economy, what of a reinvigorated and truly integrated Community? Together, the Twelve have a population of some 325 million and can boast of levels of production and trade that are already larger even than America's. Increasingly, Europe will become essential to foreign business as a market for goods or capital and as a magnet for investment; its influence in international economic negotiations

general terms a comparatively open economy, it nevertheless maintains numerous unfair or discriminatory practices and legislative provisions which impede and distort trade." "U.S. Assailed Over Trade," *The New York Times*, 19 April 1990, D8.

24. For a sequential portrait of the gathering impact of the single-market project, see "After the Fireworks: A Survey of Europe's Internal Market," *The Economist*, 9 July 1988, supplement; "What Are They Building?," *The Economist*, 8 July 1989, supplement; and "An Expanding Universe," *The Economist*, 7 July 1990, 19–20.

25. Christopher Huhne, "The 1992 Earthquake: Do You Hear a Rumble?" *The International Economy* (July/August 1988): 93.

and organizations is bound to rise as it continues to centralize major elements of policymaking in Community institutions. Outsiders are already treating the EC less like a disparate collection of separate states and more like a coherent entity that is a force in itself. Conversely, almost from the moment the single-market project was launched, fears were expressed about the possibility of an insular "Fortress Europe" in the making.

Then there are the former Communist nations of Eastern Europe, also in effect new actors on the world economic stage. Following the momentous events of 1989, all of the Soviet Union's erstwhile Warsaw Pact allies, as well as Yugoslavia, have embarked on programs of extensive liberalization and regeneration of their economies. All have declared their intention to rejoin Europe by moving as close as possible to the European Community (East Germany, of course, being a special case by reuniting with West Germany). None of the Eastern European states has a particularly large economy: taken together, their output amounts to less than one-tenth that of the EC.[26] But given their needs and the prospective costs of their reconstruction,[27] their reform efforts will surely add to the flux of intra-European relations in the 1990s, particularly if over the course of the decade they are joined even by parts of the Soviet Union itself. Given such profound changes, there is a risk that the Europeans will attach a higher priority to their own agenda of regional problems than to issues of concern elsewhere. Furthermore, there could be a temptation to ease the transition or resolve local conflicts of interest by deliberately discriminating against outside commercial and financial rivals.

Maintaining the Balance

Despite increasing possibilities for conflict among the advanced industrial nations, it hardly follows that in the 1990s governments will necessarily choose the path of overt enmity or trade warfare. One must not forget that there are also many countervailing forces working in the opposite direction to limit acrimony and keep interdependent relationships intact. All sides are tied together by an extensive network of overlapping bilateral and multilateral regime structures as well as a broad heritage of shared values. At the market level, these economies have become highly dependent on their mutual prosperity, and powerful business constituencies have emerged with a vested interest in promoting and preserving even closer economic ties.[28] All have

26. Institute of International Finance, *Building Free Market Economies in Central and Eastern Europe: Challenges and Realities* (Washington: April 1990), 7.

27. For some discussion, see ibid. and "East of Eden: A Survey of Eastern Europe," *The Economist,* 12 August 1989, supplement.

28. Dennis J. Encarnation and Mark Mason, for example, cite the key role played by Japanese corporations, rather than the Japanese or American governments, in determining "both the timing and the substance of their country's long march toward capital liberalization." See Dennis J. Encarnation and Mark Mason, "Neither MITI nor America: The Political Economy of Capital Liberalization in Japan," *International Organization* Vol. 44, No. 1 (Winter 1990), 25–54. Furthermore, Jeffry Frieden makes the point that "the groups that have been leading the charge for EC92 are not provincial, protectionist sectors within the EC but rather some of the more internationally oriented forces in Europe. Very few of them would support EC92 as a prelude to closure of global markets." Private correspondence with author, 8 October 1990.

long become accustomed to the occasional storms in their not-always-sunny relationships that somehow manage to pass without lasting damage. For all these reasons, it appears more probable that these countries will simply end up continuing down the familiar path already travelled for more than four decades—a passage marked by intermittent tensions and conflict, sometimes quite serious, but with few irreversible detours or dead-ends.

The Vital Years Ahead

Clearly, with the the fading of the cold war and growing diffusion of economic power among the industrial nations, amplified tensions and friction must be anticipated. Yet across the Pacific and the Atlantic powerful countervailing forces are also at work to limit any damage to the liberal postwar order. Prospects seem good that essentially cooperative relationships can be preserved, but not without much effort and certainly with a lot of contention over individual issues. In principle, four broad options may be identified in this period of transition: multilateralism, minilateralism, regionalism, and unilateralism.

A strategy of multilateralism would involve a renewed commitment to the liberal trade and payments regimes established after World War II, stressing the broadest possible participation of all nations and a reinvigorated role for the GATT, IMF, and other key international economic organizations. Principal emphasis would be on collective management of common problems to suppress economic conflict and promote policy cooperation. The rationale for such an approach is the same as it has been ever since the start of the postwar era: a non-fragmented global economy is the best possible guarantor of enduring prosperity and world order.

Like multilateralism, minilateralism[29] would also involve a renewed commitment to liberal trade and payments arrangements and collective management of common problems. Initially limited to an "inner club" of industrial nations, the participants in a minilateralist scheme would be willing to go beyond the lowest common denominator that can be accomplished in broader global forums. Principal emphasis here would be on a presumed trade-off between inclusiveness and achievement. The argument is that much more progress is possible over a wider range of issues when cooperation is restricted to a like-minded and relatively homogeneous group of countries.

Taking the logic of minilateralism one step further, regionalism would involve mutual commitments limited to even smaller groups of partners, on the model of the European Community or the US-Canada Free Trade Agreement (FTA). Here too emphasis is on the presumed trade-off between inclusiveness and achievement but with a more explicitly defensive rationale: to safeguard national interests against the risk of discrimination by inward-

29. The term "minilateralism" is not universally accepted. Another term to describe the same phenomenon is "plurilateralism." See "A Fresh Look at Trade Policy," in *The Free Trade Debate,* Reports of the Twentieth Century Fund Task Force on the Future of American Trade Policy (New York: Priority Press, 1989), 33.

looking blocs elsewhere. The main targets of such an approach would be an emergent "Fortress Europe" or a possibly insular "yen bloc" in the Pacific.[30]

Finally, unilateralism would eschew collective approaches altogether in favor of a more narrowly defined policy of national self-interest in commercial and financial affairs. The emphasis here would be on intensifying the kind of assertive and even aggressive tone that has already become evident recently in a growing range of economic initiatives by the United States and others. The rationale would essentially be one of despair: in a world of amplifying tensions and friction, *sauve qui peut.*

In the new "post-postwar era" of the 1990s tolerance for American free riding is likely to prove notably less reliable.

Of these four options, unilateralism clearly represents the highest-risk strategy insofar as it heightens the danger of non-cooperation or even retaliation by others. The more countries reject concessions in economic negotiations, or make unilateral demands on other governments, the more they are likely to provoke precisely the same egoistic behavior elsewhere, thus jeopardizing many of the benefits of interdependence for all. In the past that risk seemed rather less acute. Owing to the West's common security imperative and America's economic predominance, unilateralist impulses, particularly from the United States, generally encountered only limited resistance or complaint. This was certainly evident in the trade field, where US blame-thy-neighbor policies have time and again resulted in policy reforms, reluctant but resigned, from Japan or the EC. It has also been evident in the macroeconomic area, where no amount of reproach from other western nations in the Group of Seven or other forums has sufficed to alter America's domestically oriented fiscal or monetary priorities. But this is no longer the postwar era. In the new "post-postwar era" of the 1990s such tolerance for American free riding is likely to prove notably less reliable. Washington will not always be able to count on the patience and forebearance of its economic rivals.

Non-cooperation or retaliation obviously would be most likely if US unilateralism were to take the form of old-fashioned protectionism, as advocated *inter alia* by the American labor movement today. Even ostensibly more liberal policies, such as Washington's repeated market-opening initiatives promoting reciprocity and level playing fields, may generate conflict rather than compliance. Neither the Japanese nor the Europeans are persuaded that America faces

30. On the possibility of the latter, see "Together Under the Sun: A Survey of the Yen Block," *The Economist*, 15 July 1989, supplement.

as much unfair discrimination in international trade as it insists. Both Japan and the EC now seem more prepared than ever to respond in kind to any retaliatory measures undertaken by the United States. Although strong countervailing forces may be at work to rein in acrimony across the Pacific and Atlantic, a strategy deliberately designed to test the limits of those forces hardly seems the most promising way to keep America's balancing acts from tumbling. As Raymond Vernon and Debora Spar have argued:

> Unilateral measures are downright perilous. The United States cannot altogether rule out the use of threats and tit-for-tat in its efforts to open up foreign markets, but it must also recognize . . . that any unsubtle or extensive use of threats is likely to produce bitter reactions, hurtful to all parties involved.[31]

Much more attractive would be multilateralism, a renewed commitment to the basic principles of the increasingly threatened postwar order. Still accorded greatest respectability by the dominant economic culture, multilateralism continues to be widely championed in US policy debates.[32] America, urges economist Jagdish Bhagwati, must "save the multilateral trading system which has served the United States and the world economy so well in the post-World War II period."[33] Worthy as the goal may be, however, such entreaties essentially beg the question. Can the liberal postwar order as a general system be saved in the altered circumstances of the post-postwar era? In practice, a much more differentiated outcome must be anticipated in the mosaic economy of the 1990s. On many issues, from agriculture to high technology, disintegrative forces will almost certainly dominate international economic relations. It is obviously desirable that Washington should continue to promote collective management of common problems, based on the broadest possible participation and backed by the key international organizations: the greater the supply of cooperative behavior, the better. But a policy that nailed its flag solely to the mast of multilateralism would be sadly unrealistic and could even prove irrelevant.

More realistic, and certainly more relevant, would be increased emphasis on the minilateralist and regionalist options,[34] albeit as supplements to and not substitutes for the goal of a broad liberal order. On many issues there is indeed a trade-off between inclusiveness and achievement. In order to promote further openness in commercial or financial relations or simply to prevent

31. Raymond Vernon and Debora Spar, *Beyond Globalism: Remaking American Foreign Economic Policy* (New York: Free Press, 1989), 189.
32. See, for example, Robert Z. Lawrence and Charles L. Schultze, "Evaluating the Options," and Anne O. Krueger, "Free Trade is the Best Policy," in *An American Trade Strategy: Options for the 1990s*, ed. Lawrence and Schultze (Washington: Brookings Institution, 1990).
33. Bhagwati, 471.
34. For a prominent exposition of the minilateralist option see Gary Clyde Hufbauer, "Background Paper," in *The Free Trade Debate* and his article "Beyond Gatt," *Foreign Policy* No. 77 (Winter 1989–90): 64–76. For a discussion of the regionalist option see Rudiger Dornbusch, "Policy Options for Freer Trade: The Case for Bilateralism," in *An American Trade Strategy*, 106–34.

backsliding toward regressive behaviour, it may indeed be necessary to confine initiatives to smaller groups of nations prepared to join together in common commitments. But such progress should never be sought at the expense of the wider structure of interdependence. The slogan should be: multilateralism where possible, minilateralism or regionalism where necessary, and unilateralism only as the very last resort. Policy should be designed in modular form in order to conform to the complexity of a mosaic economy.

To some extent policy in the industrial nations has always been effectively modular, operating on several tracks at once. Certainly this is true of the United States. Even while promoting broad multilateralism in such settings as the IMF and GATT, Washington has by no means neglected the other strategic options available. Minilateralism has been evident in the wide variety of informal groupings that Washington has occasionally helped bring together to deal with specific problems. These have included the Paris Club (representing official creditors of developing countries), the Cooke Committee of the Bank for International Settlements (comprising banking supervisors and regulators), and the new Group of Twenty Four organized to help underwrite the economic reconstruction of Eastern Europe. Regionalism was obviously apparent in the US-Canada FTA, and unilateralism has certainly been evident in the Super 301 crowbar and other recent US trade initiatives.

To be successful, however, modular policies must be implemented with a clear sense of strategic design as well as with the tactical subtlety and finesse needed to fit existing resource means to ends. Most governments are not well organized to formulate and implement coherent economic strategies and will be challenged by the need to adapt more systemically to the altered economic and political circumstances of the 1990s. If policies are to operate on several tracks at once, they must all be programmed to arrive at the same destination.

Toward that objective, two conditions are critical. First nations must clearly communicate the hierarchy of their preferences in economic relations. There must be no mistaking that the highest priority remains an open world economy on the broadest possible basis. Perhaps the best way to assure this purpose would be to insist that any arrangements worked out on a more limited basis be strictly non-exclusionary in structure. They should be open-ended, allowing for participation by nations prepared to make the same commitments. One possible model is provided by several "codes of conduct," each dealing with a separate substantive issue, drafted during the Tokyo Round of GATT negotiations in the late 1970s. While each code is legally binding for all governments that become formal signatories, adherence itself is purely voluntary. An alternative model might be provided by Gary Hufbauer's far broader and more ambitious proposal for a comprehensive free trade and investment area for all twenty-four members of the OECD—an OECD Free Trade and Investment Area (FTIA).[35] This proposal would be attractive,

35. Gary Hufbauer, "Background Paper" and "Beyond GATT." The idea of an OECD FTIA, as Hufbauer freely admits, actually dates back to a 1974 study group of the Atlantic Council. See *GATT PLUS: A Proposal for Trade Reform* (Washington: Atlantic Council, 1974).

Hufbauer argues, in part because it "would have soft boundaries, not hard edges," and hence "could eventually succeed in realizing the goals of free and open trade that have so long inspired and frustrated the GATT."[36]

The second condition is that the United States must clearly communicate its readiness to share its traditional leadership role more fully with the other industrial nations. This means not only looking to others to bear more of the costs of stewardship, as Washington has already begun to do, but also acknowledging, in deed and not just in word, that the distribution of economic power is becoming more diffuse. The United States must learn that it can no longer frame policies solely in terms of domestically oriented priorities; nor can it still achieve its goals abroad simply by asserting demands more aggressively. Above all, the United States must be prepared to give more direct recognition to the role of the Japanese and Europeans as fully equal co-managers of the global economic system.

Sharing leadership does not mean going so far as to establish an explicit triumvirate of blocs led by the Big Three—the United States, Japan, and Germany—as some have advocated for the future[37] and others have suggested exists even now.[38] That would be carrying a desirable objective to an undesirable extreme. A formalized Big Three system would emphasize the mutual exclusiveness of emerging economic alignments rather than the reciprocal interests that exist among all western nations, and could even crystallize into mutual antagonisms and conflict. Far more preferable would be a more informal reallocation of responsibilities through the many international regime structures that are already in place, institutionalized where appropriate by a more equitable distribution of voting rights and positions of influence in the major economic organizations. In effect, the emerging mosaic of the world economy should lead to a mosaic of authority as well. Again, the principle should be multilateralism where possible, minilateralism or regionalism where necessary, and unilateralism only as a last resort. The industrial nations are on their way to a more complex set of relations than has ever existed. The best strategy would be to aid rather than resist the transition.

36. Hufbauer, "Beyond GATT," 72, 76.

37. See, for example, C. Fred Bergsten, "The World Economy," and Peter Tarnoff, "America's New Special Relationships," *Foreign Affairs* Vol. 69, No. 3 (Summer 1990): 67–80.

38. Said no less a personage than Britain's Margaret Thatcher after the Houston economic summit in July 1990: "There are three regional groups at this summit, one based on the dollar, one based on the yen, one on the Deutsche mark." As quoted in *The New York Times,* 12 July 1990, A1.