

## CHAPTER 4

# **The United States and Multilateral Trade Liberalization, 1922–67**

As Japan, Britain, and Germany withdrew from the world trading system in the 1930s, the United States redoubled its commitment to MFN principles and embarked on a crusade to end discrimination in international commerce. In the process, the U.S. government reversed its historic protectionism. Soon after the Smoot-Hawley tariff, the Reciprocal Trade Agreements Act (RTAA) of 1934 launched a program of bilateral negotiations to liberalize tariffs and dissolve preferential arrangements. This policy culminated in the creation of the GATT, which achieved significant multilateral tariff reductions in six negotiating rounds from 1947 to 1967.

This chapter examines why the United States campaigned to reduce tariffs and restore the principle of nondiscrimination against the tide of protectionism and trading blocs. The book's analytical approach relates this policy shift to the economic interests of industries with large returns to scale. In contrast to industries abroad, which were slow to introduce techniques to increase throughput and lengthen production runs, U.S. industries achieved very large output volumes. Producers could effectively exploit scale economies in the enormous domestic market, usually without relying on foreign sales.

Because the leading firms in mass production industries were the largest in the world, they had little reason to support trade protection. This chapter shows that large-scale producers favored cuts in U.S. tariffs and reciprocal agreements to open markets abroad. These firms wanted liberalization world-wide, and they did not push for the creation of a trading bloc. In fact, firms with subsidiaries abroad consistently resisted bilateral arrangements with Canada. For industries with large returns to scale, liberalization and MFN were inseparable components of trade strategy.

However, postwar reconstruction in Europe and Japan narrowed international differences in scales of production, undercutting the dominant position

of U.S. firms. Discontent with unreciprocated tariff cuts festered in the 1950s, and more and more mass production industries expressed misgivings about further trade liberalization. In the Trade Expansion Act of 1962, several formerly protrade industries sought safeguards against foreign competition; a few others were openly protectionist. Regional initiatives also gained ground as firms moved manufacturing offshore and developed production-sharing networks. In 1964, the United States sought its first waiver under GATT Article XXIV to implement free trade in automotive products with Canada. In the twilight of the Kennedy Round, the liberal era in U.S. trade policy ended, and a new strategy—first protectionist, then regional in its approach—began to take shape.

### **From Smoot-Hawley to the GATT**

The U.S. government's quest for a global market free of trading blocs dates to the years after World War I. Until then, the United States had employed a conditional version of MFN, under which tariff reductions in bilateral agreements were not freely extended; instead, countries maintaining trade treaties with the United States had to "pay" for improved preferential rates with additional concessions. But conditional MFN, the USTC concluded in a series of postwar studies, encouraged foreign governments to discriminate against U.S. trade to allow bargaining room to obtain future tariff benefits. Unconditional MFN, the USTC argued, would promote an "open door" abroad through the enticement of a minimum tariff schedule for all countries practicing nondiscrimination. The Tariff Act of 1922 therefore approved the use of an unconditional MFN clause in commercial treaties, and equal tariff treatment became a central tenet of foreign economic policy (Parrini 1969, 19–22, 227–37).

But even as the United States shifted to unconditional MFN, it also raised duties on a range of agricultural goods and manufactures, established protection for "war baby" industries deemed critical to national security, and introduced measures to combat dumping, exchange depreciation, and price deflation in the war's aftermath. In 1930, Congress passed the Smoot-Hawley tariff, commonly described as the highest tariff in U.S. history. Initially conceived as relief for farmers, this bill hiked duties on thousands of items and extended generous rates of protection to many sectors of manufacturing (Taussig 1931, chaps. 10–11).

After Smoot-Hawley, however, the United States reversed its longstanding policy of trade protection. During President Franklin Roosevelt's first term, Secretary of State Cordell Hull advanced a trade agreements program built on

tariff reciprocity and unconditional MFN. Hull wanted to scale back U.S. tariffs, but he recognized that this could not be done unilaterally. In the wake of the failed 1933 World Economic Conference, Hull also doubted the prospects for “a worthwhile multilateral undertaking.” Bilateral negotiations, he concluded, offered the best means for the United States to reduce its tariffs, engage other countries in the process of liberalizing trade, and promote the open door abroad (Gardner 1964, 40–46; Evans 1971, 5–7).

Congress approved Hull’s initiative in the RTAA, which permitted the Roosevelt administration to reduce tariffs by up to 50 percent. In contrast to the 1922 Tariff Act, which failed to stimulate trade negotiations and thus left no breaches in the tariff wall (Parrini 1969, 237–46), the State Department used RTAA authority to conclude twenty-three treaties by 1940 and nine more during World War II. Diplomats from the United States focused their efforts on Hull’s great nemesis, Imperial Preference in the British Commonwealth. In trade negotiations with Canada in 1935 and with Britain and Canada in 1938, the United States pushed for concessions on items with the greatest discrimination against U.S. goods to reduce trade preferences. Yet the State Department rarely insisted on equivalent tariff reciprocity, as it accepted a number of tariff bindings, rather than tariff cuts, in return for real reductions in U.S. duties. Thus, the primary achievement of the RTAA was substantial, enduring trade liberalization in the United States, rather than the opening of foreign markets. By 1945, U.S. tariffs had been reduced 44 percent to their lowest level since 1913 (Eckes 1995, 141–51).

During and after World War II, the State Department intensified its campaign to break up empires and dissolve trading blocs. In the 1941 Atlantic Charter, U.S. officials pushed Britain to accept trade “without discrimination and on equal terms” as a crucial postwar objective. The Lend-Lease Agreements reinforced this commitment: in return for wartime assistance, Article VII required U.S. allies to pledge support for “the elimination of all forms of discriminatory treatment in international commerce, and . . . the reduction of tariffs and other trade barriers.” Britain again promised to end tariff preferences as a condition for postwar loans in the Anglo-American Financial Agreement of 1945 (Gardner 1969, 41–67, 107–8, 152–57).

The State Department laid out the procedure to fulfill these obligations in its *Proposals for an International Conference on Trade and Employment*, which stated: “members should enter into arrangements for the substantial reduction of tariffs and for the elimination of tariff preferences, action for the elimination of tariff preferences being taken in conjunction with adequate measures for the substantial reduction of barriers to world trade” (Notter 1949, 629).

Under this formula, allied nations would reach an agreement to liberalize tariffs and empire preferences. In the meantime, Britain and the other colonial powers could not raise existing margins of preference or introduce new ones. Moreover, while the *Proposals* envisioned “mutually advantageous” results through reciprocal bargaining (that is, the United States would ease trade barriers to compensate empires for lower margins of preference), nondiscrimination took primacy over trade liberalization, as preferences would have to be “eliminated” while tariffs only needed to be “reduced.”

The United States pursued these objectives at parallel conferences in Geneva and Havana in 1947–48. The main obstacle in these negotiations was Britain’s insistence on preserving Imperial Preference and currency controls. Ultimately the State Department conceded these points: both the GATT treaty of October 1947 and the Havana Charter of March 1948 exempted existing preferential systems from MFN rules; other provisions authorized governments to employ trade and currency controls, even if discriminatory, to alleviate balance of payments problems. In addition, Article XXIV of the GATT permitted further departures from MFN for customs unions and free trade agreements. Finally, the tariff schedules in the GATT treaty committed the United States to cuts of up to 50 percent on a wide range of goods, in return for small reductions or mere bindings of foreign tariffs and margins of preference (Zeiler 1999, 108–26).

The State Department’s efforts to promote free trade multilateralism faced a second obstacle as well: protectionist sentiment among segments of U.S. society and Republicans in Congress. Protectionists denounced the Havana Charter as too much liberalization too quickly, while perfectionists objected to the treaty’s myriad loopholes and exceptions to free trade principles and MFN rules. When President Harry Truman withdrew the Havana Charter from consideration in the Senate in 1950, the provisional GATT treaty became the de facto international trade regime. Moreover, the sweeping power to liberalize tariffs conferred in early versions of the RTAA was curtailed. After 1947, RTAA bills restricted negotiating authority to one or two years and limited tariff cuts to 10–20 percent. Congress also added an escape clause to revoke tariff concessions that confronted domestic producers with surges of import competition, and it introduced peril point provisions to prohibit tariff cuts the USTC deemed harmful to domestic industry.<sup>1</sup> Weighed down by these constraints, the next four GATT rounds to 1960 yielded less significant tariff reductions than those negotiated at Geneva in 1947 (Pastor 1980, 99–103; Evans 1971, 11–20).

1. The peril point soon lapsed but was reinstated in 1951.

The Trade Expansion Act of 1962 temporarily boosted the slowing pace of multilateral liberalization, as President John F. Kennedy won congressional authority to cut tariffs up to 50 percent across the board. The Kennedy Round of the GATT reduced tariffs by 35 percent. But to win the right to launch a new trade round, Kennedy first had to appease protectionist pressures from labor-intensive industries and low-skill workers by tightening quantitative restrictions on textiles, raising tariffs on glassware and carpets, and introducing Trade Adjustment Assistance for workers and firms uprooted by trade (Zeiler 1992, 87–129).

The Kennedy Round's completion in 1967 marked the apex of the GATT. Discontent in the United States with what many regarded as unreciprocated tariff cuts festered throughout the 1950s and into the 1960s. The U.S. government had not pushed Britain to immediately end Imperial Preference; it had tolerated discrimination against U.S. goods by encouraging Europe to liberalize internally and form the EC; it had not aggressively pushed Japan to dismantle protectionist barriers. As reconstruction in these countries advanced, U.S. industry faced growing competition. With the trade surpluses of the early postwar period eroding, arguments that the United States could no longer accept uneven tariff bargains gained ground. Calls for reciprocity to open markets abroad and retaliation to punish unfair foreign trade barriers intensified.

Three important conclusions emerge from this overview of U.S. trade policy between 1922 and 1967. First, the United States steadfastly supported non-discrimination and multilateralism after its adoption of unconditional MFN. The RTAA automatically extended negotiated tariff concessions to all countries that had a trade treaty with the United States. In the years before World War II, the State Department sought to break down tariff margins in the British Empire; during the war it extracted pledges to eliminate these preferences altogether. Though provisions in the GATT treaty, the Havana Charter, and the Marshall Plan compromised these multilateral principles to facilitate European reconstruction and cold war unity, the U.S. government sought a waiver under GATT Article XXIV only once—the Automotive Products Trade Agreement (APTA) with Canada in 1964. For nearly half a century, the United States adhered to nondiscrimination even as others expanded empires and formed trading blocs.

Second, the United States reversed its historic protectionism soon after the Smoot-Hawley tariff. Duties paid as a percentage of manufactured imports declined from 40 percent in 1930 to less than 7 percent in 1967. In most of the treaties negotiated between 1934 and 1945, the United States accepted steep tariff cuts in return for concessions of little value. The first six rounds of the

GATT likewise exchanged significant reductions in U.S. tariffs for limited market-opening measures abroad. Though foreign governments emphasized, correctly, that the United States entered negotiations as a high-tariff country until 1948, tariff reductions were unequal both before and after this date. Legislation in the United States mandated *reciprocal* trade liberalization, but in practice trade liberalization was almost unilateral.

Third, enthusiasm for further tariff cuts waned after 1950. The U.S. government made limited tariff reductions in the four rounds that followed the inaugural GATT conference in 1947. Though the Kennedy Round produced comprehensive liberalization across the board, protectionist lobbying was building in the United States. Nontariff barriers spread to substitute for the tariffs previously bargained away. Pressure began to surface for retaliation to punish trade partners for unfair trade barriers and unreciprocated tariff cuts. All of this was a prelude to the changes that would overtake U.S. trade policy in the next decade.

### **Industry Groups and Trade Preferences**

The first part of the chapter generates expectations about trade preferences in industries with large returns to scale in two time periods, 1922–45 and 1945–67. In most of these industries, large-scale production created incentives for firms and business groups to support trade liberalization. Expectations about trade preferences are then compared to lobbying activity in the two periods. The analysis finds that throughout the eras under examination, most firms and business associations in industries with large returns to scale advocated tariff cuts and nondiscrimination. However, small-scale producers, principally in the chemical industry, sought to block trade liberalization in the years before the war, while industries whose scale position was declining after the war began to push for trade protection in the 1950s.

The second part of the chapter examines industry coalitions, party politics, and policy-making processes. While large-scale firms in heavy industry campaigned for trade liberalization, light industries pushed for the Smoot-Hawley tariff and sought to block trade liberalization in subsequent years. Institutional changes that shifted authority over tariffs from the legislative to the executive branch—factors outside the scope of the book’s theory—are critical to understanding the shift in U.S. policy during this period. Though some protectionist industries had the political clout to resist deep tariff cuts, no longer could they engage in the sort of tariff pork barreling that was typical before 1930. A statistical analysis of U.S. tariffs demonstrates that after three decades of liber-

alization, industries with large scales of production had low tariffs in 1964, while labor-intensive and geographically concentrated industries remained more heavily protected.

The chapter's final section evaluates why the United States never formed its own trading bloc when empires and preferential arrangements were expanding in the 1930s or when Europe and developing countries launched regional initiatives after 1950. Notably, growing cross-border trade and extensive FDI in Canada never stimulated discussions for a regional arrangement until 1964; in fact, U.S. firms with Canadian affiliates fought measures to liberalize regional trade throughout the period. This section argues that the enormous mass market in the United States made a trading bloc unnecessary. Instead, U.S. multinationals were content to invest behind Canada's high tariff walls, as long as the Canadian government did not modify the regulatory bargain for their branch plants.

#### The Scale of U.S. Industry after World War I

Writing in 1931, F. W. Taussig (1931, 473) noted: "the successful American industries are those turning out great quantities of a single product by large-scale methods." Almost all of the mass production industries in the United States enjoyed extraordinary advantages of large scale. The most prominent example is the automobile industry: between 1910 and 1914, Ford's production of passenger cars increased from 18,664 to 248,307. By 1929, both Ford and GM produced 1.5 million autos, while no European or Asian producer made as many as 80,000 (Wilkins and Hill 1964, 52–53). Companies in the United States also dominated global markets for most types of high-volume machinery: Singer, for example, produced 2.5 million sewing machines in 1913, two-thirds of world production (Davies 1976, 162); NCR sold 150,000 cash registers, a 75 percent market share (Cortada 1993, 70–73). On average, assembly lines in the United States turned out five times as many tractors, four times as many typewriters, and twice as many sewing machines as the largest plants overseas—in fact, the output of tractors, typewriters, and refrigerators *per plant* surpassed the total production of these items in Britain and Japan. Overall, the world's twelve largest automobile firms, nine farm machinery firms, and five office machinery firms were American.

Table 13 displays the scale of U.S. output for twenty-one products in 1929. In seventeen of these products, U.S. firms achieved the world's largest scales. Firms were most dominant in assembly-line consumer goods: average factory output was more than four times greater than in any country for automobiles,

typewriters, tractors, and sewing machines. In many producer goods as well, size advantages compensated for expensive labor due to steep cost curves, as U.S. plants generally maintained higher productivity while employing fewer workers than foreign factories. Steel mills in the United States, for instance, produced 1.5 times more than German plants and four times more than British factories, which helped to offset wages twice as high as Britain's and four times the German level (Berglund and Wright 1929, 56–62).

Only in chemicals was the United States at a disadvantage. Dye makers operated "little more than assembly plants . . . entirely dependent on intermediates imported from Germany" (Haynes 1945, 313). The combined output of the largest synthetic nitrogen producers, Allied Chemical and Dupont, was

**TABLE 13. Scale of Production in the United States, 1929**

Industry/Product	Output per Plant	Largest Competitor	Percentage of Largest Competitor's Output
<i>Transportation equipment</i>			
Automobiles	39,534	Germany	658.0
Trucks and buses	2,777	Germany <sup>a</sup>	
Aircraft	63	Germany	190.2
Tires	860,858	Germany	153.6
Locomotives	106	Germany	123.7
Motorcycles	4,058	Germany	121.7
<i>Electrical and machinery</i>			
Typewriters	36,909	Germany	496.2
Tractors	8,658	Germany	488.0
Sewing machines	34,511	Britain	425.2
Vacuum cleaners	54,124	Germany <sup>a</sup>	
Electric refrigerators	22,946	Germany <sup>a</sup>	
Electronic tubes	1,894,725	Britain	303.2
Radios	28,802	Germany	295.1
Lightbulbs	12,561,538	Germany	167.2
<i>Basic materials</i>			
Steel	196,421 tons	Germany	145.5
Pig iron	404,638 tons	Germany	137.5
<i>Chemicals and fibers</i>			
Explosives	5,578 thousand lb.	Germany <sup>a</sup>	
Rayon	4,021 thousand lb.	Japan	98.7
Alkalies and sodas	36,309 tons	Germany	88.2
Synthetic ammonia <sup>b</sup>	19,414 tons	Germany	20.5
Dyestuffs	2,063 thousand lb.	Germany	15.7

Sources: Data from U.S. Bureau of the Census 1930.

<sup>a</sup>Exact figure for Germany cannot be calculated due to industry definitions.

<sup>b</sup>USTC 1937.

one-fifth of IG Farben's capacity (Markham 1958, 102–3). European multinationals dominated the rayon market, as U.S. firms failed to keep pace with technological changes that increased MES production to seventy million pounds per plant (Markham 1952, 49–50).<sup>2</sup> In inorganic chemicals, efforts to implement mass production resulted in excess capacity and damaging price wars (Haber 1971, 176–77). Industrial chemistry in the United States simply lacked the economies of scale in production and R&D to compete with Germany and Britain. Moreover, the higher wage burden made the failure to achieve mass production very costly. In rayon, for instance, production costs exceeded Japan's by 177 percent, Italy's by 93 percent, Germany's by 40 percent, and Britain's by 20 percent, even though U.S. firms nearly matched European and Japanese producers in scale (Markham 1952, 171).

Where U.S. firms achieved a larger scale than foreign rivals, the large internal market was an enormous advantage. Automobiles are the prototypical case: Americans bought twenty-five times more cars in 1929 than consumers in any other country. Firms producing electrical appliances also achieved "unequaled levels of output" due to the "huge domestic market" (Backman 1962, 283). Domestic steel consumption supported forty-four steelworks with more than half a million tons of capacity and eighteen others over a million tons, whereas Germany had only eight with more than a million tons of capacity and Britain just three of more than half a million tons. In addition to the large population, high wages increased the demand for labor-saving industrial machinery and home appliances, long distances created a market for transportation and communications equipment, and abundant arable land enhanced the need for tractors and other farm machinery.

Table 14 shows that in most cases, the market in the United States allowed room for many plants with long production runs. For example, U.S. consumers purchased 4 million cars; with an MES of 500,000 autos per model, the market could support eight plants. By comparison, Britain, Germany, and Japan together consumed 307,000 autos, less than two-thirds of one MES plant. The domestic market was smaller than MES levels in only one product, motorcycles, as the popularity of the cheap automobile restricted sales. Consumption in the United States was more than twice as great as consumption in the next largest foreign market in every case except motorcycles, synthetic ammonia (because organic nitrates were abundant), and dyestuffs (where high prices choked off domestic sales).

2. Markham (1952, 7) notes: "The technology of rayon production is one of the few mass-production techniques wherein European scientists and industrialists have set the pace."

These figures explain why U.S. firms exported less than British, German, and Japanese firms, despite their larger scale. Chandler (1990, 52–53) notes:

Th[e] rapid, continuing rate of growth of consumer demand, like the geographical extent of the market, provided American entrepreneurs with more opportunities—in more industries—to exploit the economies of scale and scope than existed anywhere else in the world. . . . Because they had the world’s largest and fastest growing domestic market, American manufacturers were much less dependent on foreign trade than were those of Britain and Germany.

In most of the heavy and chemical industries, U.S. firms exported no more than 15 percent of sales, much less than firms in the same industries in other countries—not because of any disability in international competition but because domestic demand absorbed most of their production. Farm machinery producers, for instance, regarded exports as “sideline or incidental sales, to be welcomed. . . only if they did not interfere with domestic sales” (Broehl 1984, 597). With a mass market in which to exploit economies of scale, U.S. firms faced none of the handicaps that motivated industry groups in Japan, Britain, and Germany to push to expand protected markets in imperial trading blocs.

In sum, U.S. firms gained first-mover advantages in most industries with large returns to scale, as the enormous home market aided the development

**TABLE 14. Relative Size of the U.S. Market**

Product	MES Divided by U.S. Consumption	Largest Foreign Market	U.S. Consumption Divided by Foreign Consumption
Motorcycles	8.10	Germany	0.1
Sewing machines	0.93	Britain <sup>a</sup>	3.4
Synthetic ammonia	0.92	Germany	0.8
Typewriters	0.91	Germany	3.4
Tractors	0.54	Germany	9.7
Electric motors	0.52	Britain <sup>a</sup>	14.4
Trucks and buses	0.40	Britain <sup>a</sup>	9.3
Rayon	0.30	Germany	2.6
Dyestuffs	0.24	Germany	1.1
Radios	0.21	Germany	2.8
Oil engines	0.14	Britain <sup>a</sup>	6.7
Automobiles	0.12	Britain	25.4
Tires	0.08	Germany	4.9
Steel	0.05	Germany	4.1

Source: Data from U.S. Bureau of the Census 1930; U.S. Bureau of Foreign and Domestic Commerce 1930.

<sup>a</sup>Data for Germany are not available.

and use of mass production techniques in the years around World War I. With these advantages, U.S. industries had little reason to seek trade protection. They also had no need for a trading bloc: they controlled a market of continental proportions, which facilitated cost reduction to levels low enough to allow sales abroad when local demand could not absorb surplus output. Preferential arrangements would only encourage more of the discrimination that already limited U.S. goods in colonial empires and continental Europe by the 1920s. Trade liberalization to open these foreign markets therefore was best achieved on a nondiscriminatory basis.

### Mass Production Industries: Trade Preferences, 1922–45

Producers of automobiles, farm implements, and office and sewing machinery emerged as forceful advocates of trade liberalization well before the RTAA in 1934. Because firms in these industries had exploited the potential economies of scale, they declined to seek tariff increases on their goods and opposed trade protection for others during the 1920s, as hypothesis 5 anticipates.

Automakers were the most actively involved in trade lobbying. In 1929, the National Automobile Chamber of Commerce asked Congress to reduce automobile tariffs from 25 percent to 10 percent (U.S. Senate 1929 3:821–47). Ford sought to eliminate these duties, and it “vigorously opposed” Smoot-Hawley, which executives believed would incite retaliation abroad (Wilkins and Hill 1964, 205–6). In 1932, the auto industry launched a media campaign on the virtues of tariff reductions and reciprocal trade treaties.<sup>3</sup> The Automobile Manufacturers Association (AMA) pushed for “compensatory liberalization from those countries which offered potential outlets” (Gardner 1964, 39), and the group later supported Hull’s trade program enthusiastically.<sup>4</sup>

Firms and trade associations in other assembly-line industries echoed these views. Singer pushed to move sewing machines to the free list and expressed fears of foreign retaliation against U.S. tariffs.<sup>5</sup> Office machinery firms publicly deplored Smoot-Hawley because tariffs prevented foreigners from earning dollars to buy U.S. goods. NCR sought liberalization to alleviate “tariff barriers,

3. “Reciprocal Tariffs Urged,” *New York Times*, January 13, 1932, 21; “Auto Group Seeks Reforms on Tariff,” *New York Times*, July 31, 1932, sec. 4, 1.

4. “Auto Makers Back Hull on Exports,” *New York Times*, November 9, 1934, 38.

5. Singer communicated with policy makers privately and declined to testify at tariff hearings. Small firms in the Independent Family Sewing Machine Manufacturers raised the specter of import competition from Singer’s foreign affiliates, which were “everywhere behind the tariff wall and secure,” to defend the tariff as necessary protection against foreign competition *and* Singer (Davies 1976, 159–62).

trade restrictions and money complications,” which injured “productivity [at the Dayton factory]” (Cortada 1993, 179). Typewriter companies supported reciprocal trade negotiations “earnestly and unanimously” (U.S. House of Representatives 1943, 1075). Farm equipment producers such as International Harvester and Caterpillar also pushed for trade agreements (U.S. House of Representatives 1945 2:2878). Other industries favoring the RTAA included producers of tires, aircraft, radios, telephones, and electrical appliances.<sup>6</sup>

Among the industries producing on a large scale, as shown in table 15, the steel industry’s failure to seek trade liberalization is the principal inconsistency with hypothesis 5. Historically, steelmakers sought tariffs so imports would not undermine cartel prices—hence the nineteenth-century aphorism, popularized by steel-using industries, that the tariff was the “mother of trusts.” After the turn of the century, however, the steel industry limited its protectionist demands (Berglund and Wright 1929, 224). Testifying to Congress in 1929, the American Iron and Steel Institute (AISI) recommended tariff increases only for pig iron and certain classes of bar iron. The group added: “we have complacently accepted the reduction in duty on the finished product [since 1909]” (U.S. Senate 1929 3:6).<sup>7</sup> But in the depths of the depression in 1932, the AISI campaigned against foreign subsidies, dumping, and exchange depreciation.<sup>8</sup> Though it never testified to Congress on any of the five RTAA bills up to 1945, the AISI protested lower steel duties in treaties with Belgium and Britain in hearings of the Committee for Reciprocity Information.<sup>9</sup>

Small-scale producers, table 16 demonstrates, mostly pushed for tariff increases and actively opposed trade agreements (the exception being the motorcycle industry). Dye manufacturers were the leading protectionists. The American Dye Institute lobbied for a restrictive system of tariffs and import licenses during World War I, with levies based on domestic prices rather than import prices to safeguard against dumping and exchange depreciation. In 1922, the group pushed to increase these barriers to block German firms from reentering the U.S. market. In 1929, the Synthetic Organic Chemical Manufacturers Association (SOCMA) defended its high tariffs of 55–60 percent with

6. “Divide on Treaty for French Trade,” *New York Times*, June 26, 1935, 6. GE and Westinghouse supported lower tariffs for all of their products except lightbulbs (U.S. House of Representatives 1940 2:1202–3).

7. One producer pushed for duties higher than those requested by AISI but conceded that, unlike U.S. Steel and Bethlehem, “my plant is a small one and, consequently, I have not that volume of business” (U.S. House of Representatives 1929 3:1875).

8. “Steel Imports Cited in Drive on Dumping,” *New York Times*, May 8, 1932, sec. 2, 7.

9. “Steel Men Decry New Tariff Cuts,” *New York Times*, April 7, 1935, sec. 5, 1, 6; “Jobs Lost to 3,900 by Steel Imports,” *New York Times*, July 15, 1935, 15.

additional specific duties per pound (U.S. House of Representatives 1929 1:68–76; Bidwell 1956, 188–90).

The rayon industry also was active in the protectionist cause. Producers sought higher tariffs in 1922 and pushed, without success, for a valuation system like the one for dyestuffs (USTC 1922, 420–21). In 1929, the Rayon Institute asked Congress to raise duties—which averaged 45 percent plus specific levies by weight—to save small plants from bankruptcy (U.S. Senate 1929 13:55–72). Firms producing ammonium sulfate and explosives sought greater trade protection as well (USTC 1922, 47, 543–45; U.S. House of Representatives 1929 1:309–13). Only companies making alkalies such as soda ash and caustic soda declined to seek higher tariffs, as they found existing rates “adequate” even

**TABLE 15. Trade Lobbying in Large-Scale U.S. Industries, 1922–45**

Industry/Lobby Group	Position on the RTAA and Tariff Cuts: Support (+) or Oppose (–)
<i>Automobiles</i>	
National Automobile Chamber of Commerce; Ford; GM (1929)	+
AMA (1934–45)	+
<i>Office machinery</i>	
American, Michigan, and St. Louis Cash Register (1922)	–
Office Equipment Manufacturers Institute; Typewriter Manufacturers Export Association (1940–45)	+
<i>Sewing machines</i>	
Independent Family Sewing Machine Manufacturers (1922)	–
<i>Farm machinery</i>	
Caterpillar (1935)	+
International Harvester (1945)	+
<i>Trucks and buses</i>	
Ford; GM; Mack; International Harvester; White Motor (1929)	+
<i>Electrical appliances</i>	
National Electrical Manufacturers Association (1929)	+/–
<i>Aircraft</i>	
Aeronautical Chamber of Commerce (1940)	+
<i>Tires</i>	
Rubber Association of America (1922)	+
Goodyear (1940)	+
<i>Steel</i>	
AISI (1929–35)	–

**TABLE 16. Trade Lobbying in Small-Scale U.S. Industries, 1922–45**

Industry/Lobby Group	Position on the RTAA and Tariff Cuts: Support (+) or Oppose (–)
<i>Motorcycles</i>	
Harley-Davidson; Motorcycle Manufacturers of America (1922)	+
<i>Explosives</i>	
Trojan Powder (1922)	–
Sporting Arms and Ammunition Manufacturers Institute (1945)	–
<i>Rayon</i>	
Tubize Rayon (1922)	–
Rayon Institute; Delaware Rayon (1929)	–
Rayon and Synthetic Yarn Producing Industries (1935)	–
Dupont; five other rayon firms (1945)	–
<i>Alkalies and sodas</i>	
Monsanto; Hooker Electrochemical; ten other firms (1922)	–
MCA (1934–45)	–
<i>Synthetic ammonia</i>	
Committee of Byproduct Coke Producers (1922–29)	–
Shell Chemical; Koppers (1933)	–
<i>Dyestuffs</i>	
SOCMA (1929–45)	–

though “foreign chemical trusts” paid lower wages (U.S. House of Representatives 1929 1:841–44).

After 1934, the chemical industry fought trade treaties and repeatedly challenged the constitutionality of the RTAA. The leading firms, such as Dupont, Allied Chemical, American Cyanamid, Monsanto, Dow, and Hooker Electrochemical, were openly hostile to tariff cuts, and SOCMA and the Manufacturing Chemists Association (MCA) testified against all five RTAA bills up to 1945. The dye industry vigorously defended American valuation and objected when the USTC recommended a cut in dye tariffs in negotiations with Switzerland (Bidwell 1956, 159–61; Haynes 1954, 60–61). Rayon producers complained that they could not survive a reduction in trade protection in treaties with European countries.<sup>10</sup> These firms argued for tariff hikes because even with the “rise in mass production of rayon” they still could not compete effec-

10. “Testimony of the Rayon and Synthetic Yarn Producing Industries,” March 8, 1935, Trade Agreements Program File, 1934–35, Box 7, RG 20.

tively due to wages four to ten times higher than in Japan and Germany (U.S. House of Representatives 1945 2:2540–43).

To summarize, only producers of chemicals, which were small in scale compared to European rivals, opposed trade liberalization. Most of heavy industry had no need for trade protection because of its high rate of output. Instead, these industries sought tariff reductions in the RTAA. Moreover, they supported liberalization on a nondiscriminatory basis to open foreign markets and dissolve imperial arrangements.

### The Scale of U.S. Industry after World War II

International differences in the scale of production were substantial immediately after the war but narrowed soon thereafter. In the 1950s, Britain, Western Europe, and Japan rebuilt their devastated industries and introduced new plant and equipment to replace assets destroyed in the war. This trend reduced—and occasionally eliminated—the cost advantages of U.S. firms. Nonetheless, most assembly-line industries in the United States remained world leaders, even when their relative scale of production was not as great as in 1929. Table 17, based on data from 1958, demonstrates that most U.S. factories still employed mass production techniques more effectively than those in other countries.

Still, there were prominent reversals of fortune. One such shift occurred in steel, as Hogan (1971 4:2092) noted:

companies in Europe and Japan . . . have grown in size . . . so that they can install large, modern facilities and take advantage of economies of scale in a manner which was not possible heretofore. . . . Before World War II, there were very few large strip mills in operation outside the United States. . . . With the growth of the industry abroad, this has changed radically, for now in place of companies with one-half million tons or at most two million tons of steelmaking capacity, there are companies capable of producing many millions of tons.

The problem for the steel industry was not only that production runs were comparable in the United States and abroad; firms with large sunk investments in open-hearth methods also were slow to adopt new blast oxygen furnace technologies. As a result, Japanese (and later Korean) companies with lower labor costs and more efficient manufacturing processes achieved higher productivity, even in slightly smaller plants.

Major changes also occurred in electrical machinery, office machinery, sewing machines, and motorcycles. By 1958, European and Asian firms manufactured

these goods on a comparable scale with cheaper labor. In electrical machinery, the United States maintained low costs for mass-produced motors and generators, but European firms moved ahead in heavy power-generating equipment, which could not be produced on an assembly line because custom craftsmanship to detailed specifications often was required (Bidwell 1956, 218, 233). In office machinery, U.S. firms gained leadership in electronic computers but lost their dominance in established products such as typewriters and calculators. Scale and cost advantages in sewing machines also declined rapidly.

In the chemical industry, however, U.S. firms improved their position. Strength in new petroleum-based chemicals helped to offset competitive weak-

**TABLE 17. Scale of Production in the United States, 1958**

Industry/Product	Output per Plant	Largest Competitor	Percentage of Largest Competitor's Output
<i>Transportation equipment</i>			
Aircraft	54	Britain	287.9
Trucks and buses	23,861	Britain <sup>a</sup>	261.7
Automobiles	77,856	Britain <sup>a</sup>	219.1
Tires	1,275,886	Britain	177.8
Motorcycles	3,343	Germany	79.9
<i>Electrical and Machinery</i>			
Electric refrigerators	116,838	Britain <sup>a</sup>	330.5
Lightbulbs	35,167,621	Britain <sup>a</sup>	311.6
Electronic tubes	4,960,635	Britain <sup>a</sup>	310.0
Computing machines	2,977	Britain <sup>a</sup>	296.6
Tractors	14,848	Britain <sup>a</sup>	125.9
Typewriters	68,397	Germany <sup>b</sup>	
Sewing machines <sup>c</sup>	16,347	Germany <sup>b</sup>	
<i>Basic materials</i>			
Steel	309,509 tons	Japan	91.6
<i>Chemicals and fibers</i>			
Explosives	9,083 thousand lb.	Britain <sup>a</sup>	148.9
Rayon	39,883 thousand lb.	Japan	124.5
Alkalies and sodas	122,316 tons	Germany <sup>b</sup>	
Synthetic ammonia	106,208 tons	Britain <sup>a</sup>	102.1
Dyestuffs <sup>d</sup>	1,211 thousand lb.	Britain <sup>a</sup>	81.4

Source: Data from U.S. Bureau of the Census 1961; Board of Trade 1963; Prime Minister's Office 1962; Statistisches Bundesamt 1965.

<sup>a</sup>Comparable data for Germany and Japan are not available due to industry definitions.

<sup>b</sup>Comparable data for Britain, Germany, and Japan are not available due to industry definitions.

<sup>c</sup>Data are for 1954.

<sup>d</sup>Data are for all coal tar chemicals.

ness in dyes, inorganic chemicals, and synthetic fibers. Mergers in the dye industry led to “lower costs through larger-scale production and economies in management” (Bidwell 1956, 182), but the German firms created out of the IG Farben trust remained world leaders. Synthetic nitrogen capacity per plant doubled between 1937 and 1955, despite the entry of several firms into the industry (Markham 1958, 106–7). Producers also increased output per plant in rayon and synthetic fibers such as nylon and polyester.

The book’s analytical framework predicts that changes in relative scale will alter industry trade preferences. While successful mass production industries should continue to favor tariff reductions and reciprocal trade agreements, protrade preferences should weaken in industries with declining relative scale. Specifically, producers of steel, office machinery, sewing machines, and motorcycles had incentives to drop out of the trade-liberalizing coalition. In contrast, lobbying for protection is expected to diminish in synthetic fibers, industrial chemicals, and agrochemicals. In dyestuffs, opposition to trade liberalization is likely to remain strong.

#### Mass Production Industries: Trade Preferences, 1945–67

Producers in large-scale industries generally continued to favor trade liberalization after 1945, as shown in table 18. As European and Japanese reconstruction proceeded, however, many began to concede that their competitive position was eroding. A Ford executive stated this succinctly: “the United States may not inherently retain any industrial advantage it now has by virtue of the size of our home market,” he explained to Congress in 1958, because European firms “have shown their ability to match and on occasion exceed us in deriving the benefits, technological and economic, from such large-scale production” (U.S. House of Representatives 1958b, 240). Even so, the AMA and the Big Four (GM, Ford, Chrysler, and American Motors) consistently backed trade liberalization (U.S. House of Representatives 1956b, 894–904; 1962 6:4080–91). Producers of mining and construction machinery advocated tariff reciprocity vigorously (U.S. Senate 1955 3:1824–34; U.S. House of Representatives 1956b, 1031–37). Caterpillar argued that there should be “no form of protection from competitive foreign machinery” because of “the great importance of exports as a means of accentuating the benefits of mass production” (U.S. House of Representatives 1958b, 253, 266). Firms making home appliances and electric lamps remained favorable to trade liberalization, as GE insisted the electrical industry would willingly “bear its fair share

**TABLE 18. Trade Lobbying in Large-Scale U.S. Industries, 1947–62**

Industry/Lobby Group	Position on the RTAA: Support (+) or Oppose (–)
<i>Automobiles</i> AMA; Ford; Chrysler; Studebaker (1947–62)	+
<i>Aerospace equipment</i> Aerospace Industries Association; United Aircraft; Champion Aircraft (1953–62)	+
<i>Electrical appliances</i> GE; Institute of Cooking and Heating Appliance Manufacturers (1947) Borg-Warner (1962)	+ +
<i>Consumer electronics</i> Radio-Television Manufacturers Association (1953–55)	+
<i>Semiconductors</i> EIA; Fairchild (1958–62)	+
<i>Telecommunications equipment</i> National Electrical Manufacturers Association (1955) ITT (1958–62)	– +
<i>Tires</i> U.S. Rubber (1951) Century Tire and Rubber (1958)	– +
<i>Farm and construction machinery</i> International Harvester; Caterpillar; Black and Decker; several small firms (1947–62)	+
<i>Locomotives and railway equipment</i> Baldwin Locomotive Works (1947) Union Tank Car (1962)	+ +
<i>Electrical machinery</i> GE; Westinghouse; Allis-Chalmers; other firms (1955–58)	–

in terms of tariff reduction [and] the consequent increased imports” (U.S. House of Representatives 1947, 713).<sup>11</sup>

In other industries, dissenting voices were heard. Some producers complained that multilateral tariff reduction increased import competition without improving market access abroad, while others sought stronger escape clause and peril point provisions in trade legislation. For example, the Elec-

11. Though GE’s household appliances and lamps divisions supported freer trade, its power-generating equipment section testified on behalf of the Buy American Act, as noted later in the chapter (Bauer, Pool, and Dexter 1963, 206–7).

tronic Industries Association (EIA) and the Radio-Television Manufacturers Association backed RTAA bills in the 1950s but grumbled about the absence of “true reciprocity” in GATT agreements. In hearings on the 1962 Trade Act, the EIA protested the use of nontariff barriers abroad to offset negotiated tariff cuts. In response, the group urged Congress to revise escape clause and peril point procedures (U.S. House of Representatives 1953 2:1449–55; 1958b 2:2846–47; U.S. Senate 1962 1:498–505). ITT continued to support the RTAA (U.S. Senate 1958 1:507–8), but the telephone equipment section of the National Electrical Manufacturers Association protested that reciprocal tariff concessions provided “no real reciprocity” due to regulatory barriers to entry in foreign telephone systems (U.S. House of Representatives 1955, 2582–83). Producers of tires for motor vehicles remained favorable to trade liberalization, but U.S. Rubber turned against the RTAA because of alleged German dumping of bicycle tires (U.S. Senate 1951 1:827).

Complaints from industries that had lost a once-dominant scale position, shown in table 19, were more intense. Though steelmakers did not oppose the RTAA in the 1950s, they criticized the State Department’s failure to secure equivalent tariff concessions from foreign countries. As competitive pressures increased, the AISI pushed for procedures to ensure that tariffs could be reinstated if conditions in the industry worsened (U.S. House of Representatives 1958b 2:1828–37; 1962 6:3983–87). Firms manufacturing heavy power-generating equipment protested preferential procurement by foreign governments. Westinghouse in particular launched a sweeping attack on the policy of reciprocal tariff reductions:

These rates are completely inadequate to protect us and our workers against foreign competition. . . . [T]here has been no trade liberalization abroad for the substantial tariff concessions we have made. . . . It is harder today to sell American-made electrical equipment in foreign countries . . . than it was either in the 1930s or just after the war. (U.S. House of Representatives 1955 1:1063)

Westinghouse organized a pressure group of producers of custom-made generators and transformers to lobby to exclude foreign rivals from public procurement in the United States (U.S. House of Representatives 1955 2:2030–38, 2052–57; 1958b 1:471–544). GE, on the other hand, carefully sought more favorable procurement practices without compromising its larger interest in trade liberalization, as executives emphasized that the firm’s support for “Buy American” provisions did not change its desire for “the gradual and selective revision of our tariffs” (U.S. House of Representatives 1955 1:885).

**TABLE 19. Trade Lobbying in Small-Scale U.S. Industries, 1947–62**

Industry/Lobby Group	Position on the RTAA: Support (+) or Oppose (–)
<i>Rayon</i>	
Rayon Yard Producers Group (1949)	–
American Viscose (1955)	–
Manmade Fiber Producers Association; Rayon Staple Fiber Producers Association (1962)	–
<i>Petrochemicals and plastic materials</i>	
Dupont; Monsanto; Dow (1955–62)	–
Texaco; other petroleum firms (1962)	+
<i>Alkalies and inorganic chemicals</i>	
MCA (1947–62)	–
Dupont; Monsanto; Dow (1955–62)	–
<i>Office machinery</i>	
Typewriter Manufacturers Export Association (1953)	+
Typewriter Manufacturers Export Association (1956)	–
Smith-Corona; Royal McBee (1959)	–
<i>Sewing machines</i>	
White Sewing Machine; Terry Sewing Machine (1955)	–
<i>Dyestuffs</i>	
SOCMA (1947–62)	–
American Cyanamid; Allied Chemical and Dye (1955)	–
Dupont; Koppers (1962)	–
<i>Steel</i>	
AISI (1958–62)	–
<i>Motorcycles</i>	
Harley-Davidson; Mustang; Indian Motorcyle (1951–55)	–

In motorcycles, typewriters, and sewing machines, firms turned against trade liberalization and lobbied to reinstate high tariffs on their products. Harley-Davidson, Mustang, and Indian petitioned for escape clause relief in 1951 to withdraw negotiated concessions on motorcycles (USTC 1953). Harley-Davidson argued that it could not survive without tariff protection because motorcycles, unlike automobiles, could not be mass-produced to compensate for low wages abroad.<sup>12</sup> The Typewriter Manufacturers Export Association, one of the

12. Harley-Davidson complained that foreign governments negated their tariff concessions through import licensing, exchange depreciation, and nontariff measures. The firm concluded, “reciprocity has hurt our motorcycle business . . . to the point where our home market is just about the only market we have left” (U.S. House of Representatives 1953 1:52–59).

groups most favorable to trade in the prewar era, also turned protectionist. The leading firms supported the RTAA until 1953, but then in 1956 they urged Congress to remove typewriters from the free list unless European countries offered steep tariff concessions (U.S. House of Representatives 1956a 3:1635–38). In 1959, Smith-Corona and Royal McBee sought escape clause relief (USTC 1960). Sewing machine producers “strongly opposed any further reduction in the duties on the importation of sewing machines,” especially from “cheap-labor countries” such as Japan. They too wanted escape clause relief, firms told Congress, but they doubted their application would be accepted (U.S. Senate 1951 2:1395–97; U.S. House of Representatives 1955 2:2097–2102).<sup>13</sup>

The chemical industry remained fiercely protectionist, despite the improvements made in industrial and agricultural chemicals after the war. The industry’s largest firm (Dupont), third-largest (Allied Chemical), fifth (Dow), sixth (American Cyanamid), eighth (Monsanto), and tenth (Koppers) all appeared before Congress at least once between 1947 and 1962 to oppose the RTAA, while SOCMA and the MCA lobbied against all six trade bills in this period. To limit the scope for further tariff cuts, these groups demanded that trade legislation stipulate escape clauses, peril points, and product-by-product negotiations involving “qualified industry advisors” (U.S. Senate 1962 2:718–23).

With the European chemical industry devastated after the war, U.S. chemical companies nonetheless maintained that they were disadvantaged by high wages and poor technological skill; high-volume production, they asserted, could be applied to standard bulk chemicals but not more advanced compounds (U.S. House of Representatives 1953 1:152–58, 226–34). By the late 1950s, firms further emphasized that the scale advantages of the early postwar period were quickly disappearing as Europe rebuilt:

[Foreign plants are now] comparable in size to those existing in the United States. . . . The economies of large-scale and modern technology, added to the advantages of lower wage and salary scales, result in substantially lower costs to European and Japanese chemical industries. . . . We are losing our past advantage due to larger volume output, as our competitors in Western Europe expand their operations. . . . Opening the U.S. market . . . will spur them to even further expansion. (U.S. House of Representatives 1962 5:3297–98)

13. Italian and Swiss affiliates importing components for final assembly in the United States urged Congress to dismiss these claims because “[t]he scale of production in the United States is larger, bringing about mass production economies not possible abroad” (U.S. House of Representatives 1955 2:2565).

Moreover, chemical industries in a reconstructed, integrated European market could appropriate scale economies more easily, according to Dupont executives:

[European integration] has provided market opportunities for foreign manufacturers comparable in size to those in the United States, and consequently big enough to support the construction of plants equal in size and operating efficiency to ours. . . . we are in the process of losing the advantages of size and advanced technology which have contributed so importantly to the chemical industry's favorable trade balance of recent years. (U.S. Senate 1962 3:1274)

As a result, the chemical industry argued, tariff cuts would allow foreign producers to increase market share in the United States, with no offsetting benefit for U.S. companies. "We are not concerned with exporting," a Monsanto executive explained: "We believe we will lose most of our chemical exports in time, when these foreign plants are finished. We are concerned with preserving our domestic market" (U.S. House of Representatives 1955 1:1090).

In short, even in the favorable market environment of the early postwar years, the chemical industry's ingrained protectionism was unshakable. Chemical companies not only opposed further trade liberalization for coal tar derivatives, dyes, synthetic fibers, and explosives, they also fought to defend American valuation and to extend it to other products. In opposing further liberalization, dye makers complained that tariff cuts "over our protest" in the 1951 GATT agreement would cause growing import penetration (U.S. House of Representatives 1953, 152). The Rayon Yarn Producers Group insisted that the 50 percent tariff cut imposed against the "pleading of the industry" in 1949 "exceeded . . . the peril limit" (U.S. House of Representatives 1949, 223–26). In 1960, producers filed, unsuccessfully, for escape clause relief for staple fibers (USTC 1961).

### **Domestic Coalitions, Institutions, and Party Politics**

The preceding analysis demonstrates that most U.S. industries with large returns to scale, with the exception of chemicals, dominated world markets after World War I. As expected, these producers generally opposed tariff increases in the 1920s, and after 1934 they advocated concessions to foreign countries in return for tariff reductions abroad.

The antitariff coalition of heavy industries competed with protectionist light industries for influence over policy. Businesses in textiles, clothing, footwear, pottery, glassware, and the like lacked global trade ties and feared for-

foreign competition. Firms in these industries manufactured in family shops or small factories because returns to scale were small. If left unprotected, these producers would suffer import competition from labor-rich countries. Labor-intensive industries therefore formed the backbone of the protariff movement, and they rallied the strongest resistance to reciprocal trade liberalization.

The puzzle in U.S. trade policy is why mass production industries failed to block tariff increases in 1922 and 1930 and why labor-intensive industries were unsuccessful in their efforts to defeat the RTAA between 1934 and 1962. To illuminate how group pressure and political influence shaped policy outcomes, the analysis considers the intervening effects of coalition formation, party politics, and political institutions.

### Smoot-Hawley

Cleavages between large-scale mass producers and labor-intensive industries first emerged in the debate over the 1922 tariff. Labor-intensive businesses coalesced in pressure groups such as the American Tariff League to push for higher duties to block imports and prevent deflationary gold outflows. Large companies in assembly-line industries lobbied through the National Foreign Trade Council and similar organizations to expand markets and promote nondiscrimination abroad. The “bargaining tariff” compromised these opposing interests, as large firms accepted higher duties designed to equalize domestic and foreign production costs in return for provisions to reduce these tariffs in reciprocal trade treaties through the operation of unconditional MFN.<sup>14</sup>

But the State Department negotiated no significant commercial treaties under the legislation, so bargaining tariffs failed to open markets or promote equal tariff treatment. By 1930, Wilson (1971, 94) writes:

business internationalists . . . were no longer willing, as they had been in 1922, to accept high duties in return for promises of downward revision through flexibility. . . . Consequently internationalists were much more outspoken in their criticism of the 1930 tariff than they had been of the Fordney-McCumber legislation.

Capital-intensive heavy industries joined export-oriented Midwest agriculture and Wall Street banks with overseas loans to form an antitariff coalition. A few

14. Big business regarded this as an “open door tariff,” as the double-column schedule could be used to reward countries practicing nondiscrimination with concessions and punish those using discrimination with high duties (Parrini 1969, 214–20, 234–35; Wilson 1971, 65–70).

big businesses (such as Ford) even lobbied Congress to lower duties on their products or to block tariff increases for others. On the opposite side, labor-intensive manufacturing, border farming, and small banks pushed for tariff hikes. This latter group dominated the congressional debate and successfully persuaded legislators to raise duties to unprecedented heights in the Smoot-Hawley tariff (Eichengreen 1989).

Two factors exogenous to the book's theory prevented mass production industries from realizing their trade preferences in policy. The first was party politics: the tariff hikes of 1922 and 1930 occurred in party-line votes during Republican control of the legislative and executive branches. Second, institutional procedures for setting tariff levels encouraged protectionist logrolling. As Schattschneider (1935) demonstrated, Smoot-Hawley exposed a basic defect in trade politics: protariff groups declined to oppose duties for one another in a game of "reciprocal noninterference," while free riding limited countervailing pressure from antitariff groups. This asymmetry in organizational skill made legislators prone to protectionist pork barreling to satisfy the constituents that mobilized on trade issues. Committee structures, legislative processes, and the final bill reflected this bias—members of Congress were assigned responsibility for the tariff schedules of interest to industry in their districts; committee hearings produced twenty thousand pages of testimony, mostly from protariff interests; and the Senate bill included 1,200 amendments. The implication was clear: for trade liberalization to occur, control over tariff making had to be transferred from congressional committees beholden to special interests to an executive capable of acting in the general interest.

### The RTAA

After 1930, mass production industries pushed more vigorously for trade liberalization, especially once the Great Depression's effects were felt (Wilson 1971, 97–98). Group pressure was necessary—though not sufficient—to trigger the shift to the RTAA. In addition, partisan change provided a permissive condition: the Democrats swept the 1932 national elections, as Roosevelt won the presidency and his party gained both houses of Congress. Though Roosevelt's cabinet included such protectionist figures as Secretary of Agriculture George Peek, Cordell Hull and other top officials hailed from the Democratic Party's antitariff wing. In fact, the most substantial liberalization under the RTAA coincided with the five terms served by Roosevelt and his successor, Harry Truman—a twenty-year stretch during which Democratic control of Congress was almost uninterrupted.

Partisan change made possible a second key shift: institutional innovation in trade policy-making. The RTAA, Haggard argues, defeated protectionist logrolling through two specific channels. First, Congress no longer set tariffs on specific goods; it merely voted on whether or not to continue delegation to the executive. Because the presidency served a broad national constituency, it could internalize the policy effects of pressures to satisfy narrow district interests. Second, reciprocal trade concessions linked tariff reduction at home to liberalization abroad. This motivated protrade groups to lobby for the RTAA to gain access to foreign markets. Over time, trade agreements expanded the size of the export sector, which led to more protrade lobbying (Haggard 1988).

Pastor (1980, 91) suggests that “there are few interest group political analyses of the 1934 Trade Act” because the influence of private interests “was not discernable either in hearings or in the final bill.” Instead, various accounts have emphasized the liberal philosophy of Hull’s State Department (Haggard 1988); the ideational connection between the Smoot-Hawley tariff and the Great Depression, which motivated officials to reform trade institutions (Goldstein 1993); and the Democratic Party’s desire to enact more permanent liberalization than it had accomplished previously (Bailey, Goldstein, and Weingast 1997). Still, these arguments lack a cogent theory of institutional change: the new policy-making structure seems to materialize spontaneously, while the politics that produced it remains opaque.

The brevity of the RTAA hearings in 1934 does not mean that private actors exerted no influence. Quite the contrary, Hiscox (1999) demonstrates that constituency interests—particularly, the growth of export interests in manufacturing—were the source of party positions and extant institutional structures. In fact, lobbying by firms and trade associations in mass production industries was a critical factor in the changes in the trade policy process. Advocates of tariff reduction argued that only the executive, not the Congress, could properly conduct foreign trade relations. This group recognized that trade liberalization required the insulation of tariff-making authority from protectionist interests. Protectionists countered that the RTAA was an unconstitutional delegation of authority to the president; they knew that the Smoot-Hawley system could survive only if Congress retained control over trade.

The political influence of these competing coalitions is not apparent in hearings in Congress or in the Committee for Reciprocity Information because of selection bias. In most hearings, roughly three-quarters of the witnesses testified against RTAA bills and tariff negotiations; representatives of mass production industries appeared infrequently. Opponents of trade liberalization had more incentives to speak publicly in an effort to amend (if not defeat) unfavorable

trade bills in Congress and spare themselves tariff cuts once their products had been placed on the table for negotiation. Supporters of trade liberalization had other channels of influence, for example through trade negotiators in the State Department, and they did not need special exceptions to suit their interests.

Thus, the RTAA by itself was no “magic bullet” (Hiscox 1999). Institutional changes “created the opportunity for free traders to implement their particular vision of economic policy,” but they “did not mandate the lowering of tariff levels” (Goldstein 1993, 140). Protariff groups could have persuaded the State Department to offer foreign countries only token concessions in 1934, but they didn’t; after 1937, delegation could have been ended at any time, but it wasn’t. In each extension of the RTAA legislation, policy questions (the length of trade-negotiating authority, the maximum level of tariff cuts, the principal supplier rule, the inclusion of escape clauses and peril points) masqueraded as institutional questions. The outcome of these debates hinged critically on the balance of political influence between protariff and antitariff groups. Representatives of labor-intensive industry testified to Congress in numbers disproportionate to their size and sway because they already had been defeated on the larger question of whether or not the United States would set tariffs through international negotiation. They could not defeat the legislation altogether; they could only hope to modify and dilute it to provide some refuge from harmful tariff cuts.

Institutional and partisan influences in trade policy lie outside the book’s theory, and it must be acknowledged that they have been introduced into the preceding discussion in a descriptively ad hoc fashion. This does not mean that the theory is wrong; rather, it suggests that while the preferences of domestic political actors play a significant role, they cannot fully explain policy outcomes. To systematically examine how economic interests affected trade policy at the industry level, the next section turns to statistical methods.

#### Statistical Analysis of U.S. Tariffs

The analysis examines U.S. tariffs in 1964, after several rounds of RTAA and GATT tariff reductions (though before the Kennedy Round agreements had been phased in). The dependent variable, *tariffs*, is the value of duties collected divided by total imports.<sup>15</sup> The units of analysis are three-digit Standard Industry Classification (SIC) industries, with independent variables measured for 1958.

To estimate the effects of scale economies, the analysis uses *scale*, which is

15. Tariff rates are an appropriate measure of trade protection for this period because anti-dumping duties and other nontariff barriers were rare outside of agriculture.

described in the appendix and employed in chapter 3.<sup>16</sup> *Import competition* and *export dependence* capture comparative cost considerations reflected in trade patterns. Because these two trade variables perform poorly, the models include an alternative measure of comparative costs, *labor intensity*, which is wages divided by value added. There are two proxies for collective action costs: *industry concentration* is the share of output in plants with more than one thousand workers; *geographic concentration* is the percentage of all workers located in the five states with the largest production.

The first column of table 20 includes all of the independent variables except *scale*. The best predictors of tariffs are *labor intensity* and *geographic concentration*. The strength of *labor intensity* suggests that elements of comparative costs not reflected in trade patterns were important in tariff setting. This makes sense since the U.S. economy was not heavily exposed to trade, and low import penetration in part reflected past industry success in securing tariff protection (hence the incorrect negative sign for *import competition*). The strong positive effect of *geographic concentration* also is predictable, since geographically localized protectionist industries such as textiles, apparel, and footwear should have been less vulnerable to free-rider problems (though some protrade industries, such as automobiles, were geographically concentrated too). *Export dependence* is weakly significant, and *industry concentration* has no effect on tariffs.

The second column adds *scale* to the model, and this variable is statistically significant with the correct positive sign. A likelihood ratio test rejects the null hypothesis that *scale* has no effect on *tariffs* at  $p < .05$  ( $\chi^2 = 4.19$ ). Table 21 shows how predicted tariffs change as relative scale and the returns to scale vary. The figures illustrate that tariff rates were sensitive to the scale position of industries and the size of the returns to scale. Holding returns to scale constant, tariffs fall as relative scale rises: moving from relative scales of 0.5 at the low end to 3 at the high end, tariffs decline by 7.6 percentage points at modest returns to scale, 14.6 percentage points at large returns to scale, and 21.2 percentage points at very large returns to scale. Variation in returns to scale magnifies the effect of relative scale, with a 6.1 percentage point tariff increase at very small scales and a 7.5 percentage point tariff decrease at very large scales.

This analysis confirms that even though party politics, institutional structures,

16. Again, note that when scale is small, this measure is greater than 1; when scale is large, it is less than 1. To preserve cases, industries with very small returns to scale were entered as 1 to represent a neutral effect of scale economies on unit costs. While this coding decision affects the coefficient estimates, and the results accordingly should be treated with caution, it is not likely to systematically bias the results because the true value will be underestimated in some cases and overestimated in others.

and foreign policy priorities were important factors in the pace and scope of liberalization in U.S. trade, factors operating at the industry level played a critical role in tariff setting.

### U.S. Trade and Canada

At the same time that the United States sought multilateral trade liberalization to pry open foreign empires and trading blocs, it abstained from forming pref-

**TABLE 20. OLS Regression Results for U.S. Tariffs**

Variable	Tariffs in 1964	
Scale		0.61** (0.30)
Import competition	-0.06 (0.13)	-0.09 (0.13)
Export dependence	-0.29* (0.16)	-0.25 (0.16)
Labor intensity	0.21*** (0.07)	0.22*** (0.07)
Industry concentration	-0.02 (0.03)	0.00 (0.03)
Geographic concentration	0.17*** (0.05)	0.16*** (0.05)
Constant	-0.00 (0.03)	-0.61** (0.30)
F-ratio	5.88***	5.69***
Adjusted R-squared	0.15	0.17

Note: Cell entries are OLS regression coefficients, with standard errors in parentheses.  $N = 137$ .

\*\*\* $p < .01$     \*\* $p < .05$     \* $p < .10$

**TABLE 21. Marginal Effects of Scale and Returns to Scale on U.S. Tariffs**

Relative Scale	Change in Unit Costs at One-Half MES			Marginal Effect of Returns to Scale
	5%	10%	15%	
0.50	16.5	19.5	22.5	6.1
0.75	14.7	15.9	17.0	2.4
1.00	13.4	13.4	13.4	0.0
1.50	11.7	10.1	8.6	-3.1
2.00	10.5	7.9	5.5	-5.0
3.00	8.9	4.9	1.3	-7.5
Marginal effect of relative scale	-7.6	-14.6	-21.2	

erential arrangements of its own. "Free trade multilateralism," Gardner (1969, 17) writes, reflected

the transformation of the United States into a major exporter of mass-produced industrial products. These products were particularly vulnerable to the impact of tariff preferences and other forms of discrimination. . . . [The country's] growing industrial efficiency might be progressively offset if American products were not guaranteed equal access to foreign markets.

Controlling a market of continental proportions allowed mass production industries to look to the world market rather than a regional sphere. Firms therefore wanted a general reduction in world trade barriers more than exclusive benefits in selected countries. Only in chemicals did competitors exploit scale economies better than U.S. companies. Yet there is no evidence that chemical producers desired exclusive privileges abroad, as these firms instead devoted their energies and political resources to defend the tariff at home. On the whole, industry showed no interest in a trading bloc.

Devotion to the principle of nondiscrimination is particularly evident in U.S. relations with neighboring Canada. In 1911, these two countries negotiated a reciprocity treaty that failed to pass the Canadian parliament. After 1911, preferential trade with Canada was a recurrent political issue. However, large U.S. companies consistently opposed such initiatives. Most had invested in Canadian manufacturing, and regional integration between the United States and Canada would harm these small-scale affiliates. As a result, U.S. heavy industry called for a rather incongruous policy of eliminating barriers to American goods everywhere except in Canada.

### The Branch Plant Movement

Investment by U.S. companies in foreign manufacturing dates to the late nineteenth century. Machinery firms such as Singer and International Harvester set up overseas outlets to perform product demonstrations and after-sales servicing; then suppliers of public utilities, such as ITT, moved abroad to secure foreign contracts that required local capacity; automakers began to manufacture abroad, followed by tire producers, before World War I; and after the war the electrical and electronic industries established foreign affiliates. The U.S. Bureau of Foreign and Domestic Commerce (1931, 11) noted that U.S. branch plants produced mostly in "large-scale industry, which gives scope for the application of American production methods, with the emphasis on the scale of production and high productivity per man." The motives were to circumvent

tariffs, nontariff barriers, and exchange controls; minimize transport costs; challenge foreign rivals on their home turf; and exploit monopolistic advantages in the control of proprietary assets.

The incentives to invest in Canada were simple: high tariffs made exporting difficult and local production attractive. Under Canada's National Policy, automobiles and farm machinery, two important U.S. exports, paid 35 percent duties, and engines and parts were taxed at 30 percent (Marshall, Southard, and Taylor 1936, 199–203). In response, U.S. automakers set up assembly plants in Windsor, just across Lake Ontario from Dearborn, Michigan, the hub of automobile production in the United States. By 1929, U.S. firms produced five and a half vehicles in Canada for each one imported from the United States. Producers of tires, tractors, farm implements, machinery, and electrical equipment soon followed in kind.

While the branch plants enjoyed generous trade protection, they also faced pressure to increase local content. For example, Canada increased tariffs on automobile parts in 1926 to force U.S. affiliates to produce components locally or develop linkages with domestic suppliers. When foreign investors complained that taxing parts at higher rates than finished vehicles encouraged imports at the expense of domestic production, the Canadian government introduced tariff rebates on imported parts for branch plants with 50 percent local content; foreign components used in exported vehicles received a full duty drawback. Firms equipped to meet this target (such as Ford) lobbied for and embraced the new rules, which raised entry barriers for competitors (Traves 1984, 137–47). In fact, several branch plants supported strict rules of origin for Imperial Preference on exports to the British Commonwealth. In contrast, those with “primitive assembly operations” sought to delay or block local content mandates (Marshall, Southard, and Taylor 1936, 275; Williams 1986, 85–88).

Inside the small Canadian market, branch plants generally manufactured broad product lines in low volumes. Under pressure from tariffs and local content rules, two-thirds of U.S. affiliates surpassed 75 percent Canadian content in 1932. Due to “the loss from reduced scale of operations, the lower efficiency of labor, and the duplication of plant and management” (U.S. Bureau of Foreign and Domestic Commerce 1931, 11), productivity was low: two out of every three U.S. affiliates in Canada reported higher unit costs than their corporate parents (Marshall, Southard, and Taylor 1936, 232–33). Even in the most efficient plants, an electrical industry executive stated,

[foreign] costs are approximately the same in spite of the fact that the foreign factories use American designed tooling, American production

methods, American “know-how,” and have wage costs about one-third to one-fourth of the United States wage costs. . . . The reason can be partly found in volume. . . . Specialized operations are so many times more expensive that the advantage of lower wage rates is more than offset. (Backman 1962, 297)

But FDI nevertheless was profitable because tariff walls and entry restrictions allowed branch plants to pass off elevated costs to Canadian customers by marking up prices 30–40 percent (Marshall, Southard, and Taylor 1936, 237–39).

This arrangement was stable as long as Canada did not cut tariffs after branch plants were locked in to increased production and local content. Several U.S. firms attained leading positions in the Canadian Manufacturers Association and joined together to defend trade protection before the Canadian Tariff Board (Marshall, Southard, and Taylor 1936, 275–76; Scheinberg 1973, 229–32). For example, Ford opposed proposals to reduce automobile tariffs, arguing that “the present margin of protection should be continued” since the industry was “still in the formative stage” (Wilkins and Hill 1964, 131–32). International Harvester and Deere, the leading producers of farm machinery, also turned protectionist once they had factories inside Canada’s tariff wall (Radosh 1967, 48–50; Wolman 1992, 91–92).

In the United States, these firms fought plans to liberalize bilateral trade—even as they pushed for reciprocal trade treaties with European countries and the British Empire (other than Canada). The USTC (1920, 76) reported, “American manufacturers with branch establishments in Canada were opposed to reciprocity because it promised to open the Canadian market to other American products in competing lines.” The Commerce Department advised against trade talks with Canada because “American capital invested in Canadian industries is due to the Canadian protective tariff policy” and “free trade . . . would naturally detract from the value of the investment” (Scheinberg 1973, 233). When President Roosevelt considered trade negotiations with Canada, advisers again warned that the “branch plants have tended to support the maintenance of a high tariff wall by Canada.”<sup>17</sup>

Trade agreements between the United States and Canada in 1935 and 1938 were carefully crafted to avoid upsetting this status quo. The State Department’s objective was not to liberalize Canada’s general tariff but to attack Imperial Preference. While Canadian duties against the United States helped the branch plants and harmed U.S.-based exporters, Imperial Preference exposed

17. “American Branch Plants in Canada,” August 1934, Country Files, 1933–35, Box 1, RG 20.

both to greater competition from Britain. Multinationals from the United States therefore pushed to reduce the preferences British goods enjoyed under the Ottawa Agreement. Some also sought to reduce Canadian duties on parts exported from the United States—but none wanted Canada opened to imports of finished goods.<sup>18</sup> Indeed, too much trade liberalization aroused protests from companies invested in the branch plant system: for instance, U.S. firms in the Canadian Automobile Chamber of Commerce petitioned the Tariff Board to reverse tariff cuts in the 1935 treaty and restore the old duties because, they argued, “reduced protection will undermine the stability of the industry.”<sup>19</sup>

### The Rise of Canadian Industrial Policy

The collapse of the multilateral payments network and the restructuring of the world economy during and after World War II disrupted Canada’s economy and the branch plant system. During the war, Canada accumulated sterling balances on exports to the British Commonwealth while payments for imports from the United States drained its foreign exchange. This problem worsened after the war, as European countries facing a dollar shortage continued wartime restrictions on the use of hard currency for imports. Without a system to transfer balances on exports to the British Empire to pay for imports from the United States, Canada needed either to export more to or import less from the United States to stem the loss of dollar reserves and prevent a balance of payments crisis.

The loss of imperial markets was troublesome for the branch plants. Before the war, firms used Canadian affiliates as export platforms and granted exclusive rights in commonwealth trade to gain scale economies.<sup>20</sup> After the war, U.S. multinationals opened new factories or enlarged existing ones in Britain

18. “Report of the Committee for Reciprocity Information in Connection with the Negotiation of a Reciprocal Trade Agreement with Canada,” Trade Agreements Program File, 1934–35, Box 7, RG 20.

19. “Auto Makers Ask Canada to Kill Treaty Auto Rates,” *New York Times*, December 17, 1935, 11. The petitioners were GM, Chrysler, Hudson-Essex, Studebaker, and International Harvester. Nash Motors and Willys-Overland, neither of which operated branch plants, complained that without tariff cuts they were “prevented from shipping . . . products into Canada on a fair and equitable basis” (“Report of the Committee for Reciprocity Information in Connection with the Negotiation of a Reciprocal Trade Agreement with Canada,” Trade Agreements Program File, 1934–35, Box 7, RG 20).

20. In the interwar period, Ford, GM, and Chrysler factories in Canada exported 25–50 percent of their production because sales to Australia, New Zealand, and South Africa boosted output during winter down periods. In fact, Ford-Canada exported three times more than Ford-U.S., even though it produced one-tenth as many cars (Wilkins and Hill 1964, 44, 120).

and Western Europe because they had to produce inside the sterling area and the European Payments Union to sell there. Export opportunities for Canadian branch plants evaporated (Safarian 1966, 116). In automobiles, the effect was dramatic: in 1948–49, Ford's exports from Windsor declined from 41,141 to 17,415.<sup>21</sup>

As U.S. affiliates confined their sales to the Canadian market while continuing to rely on imported parts, Canada's trade deficit soared. Some Canadian officials believed that this persistent strain on the balance of payments could be relieved if the branch plants could serve a wider market by specializing for export. Barriers to trade with the United States, the Department of Trade and Industry argued, perpetuated an inefficient industrial structure; removing these barriers would encourage branch plants to "develop specialized production in Canada for export to the U.S. domestic or export markets as an offset to Canadian industry's imports from the U.S." (Williams 1986, 110). Soon after the 1947 GATT conference, Canadian officials asked the U.S. government to negotiate "further tariff cuts, particularly in the manufacturing goods field, which would make possible a better balance in the enormous one-way trade associated with our branch plants" (quoted in Granatstein 1985, 39). Canadian nationalists and U.S. firms in the Canadian Manufacturers Association countered that without tariffs the branch plants lost their *raison d'être* and would simply migrate back home. Fearing a repeat of the 1911 Reciprocity Treaty debacle, Canada's prime minister Mackenzie King abruptly broke off these negotiations in the spring of 1948.

With trade policy unchanged, the "miniature replica" branch plant structure endured. The limited range of the Canadian market allowed room for only a few plants large enough to take advantage of scale economies. In many sectors, however, the leading U.S. firms all owned Canadian affiliates; once one entered the market, competitors followed so the first mover could not capture the benefits of producing behind the tariff while others had to export over it.<sup>22</sup> As a result, branch plants produced well short of U.S. output levels (Eastman and Stykolt 1967, 7–10; Task Force on the Structure of Canadian Industry 1968, 79–80, 136–37). Those with high unit costs reported that "production runs

21. In the same period, exports from Dearborn dropped from 88,559 to 53,700. Ford's United Kingdom factory received top priority in commonwealth markets previously serviced from the United States or Canada because mass production required exports of nearly 100,000 vehicles (Wilkins and Hill 1964, 374, 407–8).

22. For example, the Canadian market could not support a single MES plant for electric ranges and refrigerators, yet ten and twenty-three factories, respectively, produced these goods (Eastman and Stykolt 1967, 253–55).

were shorter, or volume was lower, or that these, in turn, led to relatively less tooling and mechanization” (Safarian 1966, 204–5).<sup>23</sup> As Ford-Canada’s chairman told the House of Commons in 1953: “Without the tariff, we could not possibly compete with the United States manufacturers, and the reason is solely one of volume. . . . Because the volume in the U.S. is thirteen times that in Canada, unit costs of production are substantially lower” (quoted in Dykes 1982, 26).

In an attempt to fix its balance of payments problems and reform its antiquated industrial structure, the Canadian government began to aggressively apply industrial policy after 1960. These moves upset the regulatory bargain that attracted FDI and, with growing frequency, caught the branch plants in the middle of disputes with the United States. As these conflicts threatened to provoke a trade war, efforts to reorganize the branch plant system and discipline Canada’s use of TRIMs gradually produced a formal governance structure to manage bilateral trade and investment. The automotive industry provides an early example of this dynamic at work.

#### The Automotive Products Trade Agreement

In 1962, the Canadian government established a duty remission program that offered automakers a dollar in tariff rebates for each dollar increase in exports over their monthly average for the previous year. The main purpose was to reduce Canada’s \$500 million deficit in automotive products, which accounted for one-third of its overall trade deficit. Subsequently the U.S. Treasury Department opened a countervailing duty inquiry when a radiator producer, Moline Manufacturing, complained that the duty remissions were unfair export subsidies. Treasury’s preliminary inquiry indicated that the refunds constituted illegal “bounties” or “grants” under U.S. law.

Eager to avoid a trade war, U.S. automakers urged the two governments to negotiate a bilateral agreement on automotive trade and investment.<sup>24</sup> In testi-

23. Eastman and Stykolt (1967, 13) explain:

[The] scale of output is below the modern best-practice scale. Runs of single products in Canadian factories are short, with the result that excessive time is used in changeover for each unit of output. The machinery used is often inefficient because indivisibilities in the use of the most modern methods of production can be overcome only at higher scales of production for individual plants than exist in Canada.

24. Officials in the United States emphasized that the law required them to impose countervailing duties if the duty remissions were found to be an export subsidy. In response, Canadian officials hinted they would increase local content requirements on automobiles if the United States

mony to a Canadian Royal Commission in 1961, Ford, GM, and American Motors advocated mutual tariff elimination so “the full cost benefits of U.S. mass production . . . would then be passed on to Canadian consumers” (Royal Commission on the Automotive Industry 1961, 40–41).<sup>25</sup> These firms also appealed to U.S. officials to negotiate a free trade agreement.<sup>26</sup> In contrast to 1935 and 1948, when automakers were satisfied with high Canadian tariffs, now they had strong motives to support free trade. Because of consolidation, only the Big Four remained in business (Studebaker had just closed its last U.S. factory), so high-cost Canadian affiliates no longer faced competition from automobiles exported from the United States. As a result, outsiders could be excluded from sharing in the benefits of free trade—provided that it was not extended to third countries through the MFN clause.

Initially the State Department was cool to the idea of a bilateral arrangement that would exclude third countries. One memo discerned a “progressive movement across national borders toward the integration of a particular industry” but concluded that a common market with Canada was not “in the cards” because “our economic interests are too broad geographically to make such an arrangement feasible.”<sup>27</sup> Another briefing paper amplified this concern: “getting around our most favored nation commitment could have some erosive impact on this basic element in our international trade policy. What is more important, perhaps, we could excite Congress to think of other and more far-reaching departures from MFN. We do not take this risk lightly.” But if the United States adhered to MFN, “the Europeans would get a free ride on \$300 million of finished

---

retaliated. According to U.S. firms, “such a decision by Canada would require them to make additional investments in Canada of several hundred million dollars, in order to protect the \$600 million investment they already have there. For this reason, Ford, GM and Chrysler have stated that they would be placed in serious difficulty by the imposition of countervailing duties” (Memorandum from Secretary of State Rusk to President Johnson, Washington, DC, September 18, 1964, U.S. Department of State 2001, 690).

25. These firms argued that tariffs perpetuated the assembly-plant structure because low volume forced branch plants to import components with large economies of scale, such as engine blocks and automatic transmissions. Without trade barriers, branch plants could specialize in a limited range of models for both markets and could import models not produced in Canada from the United States. (Canada’s tariffs were 17.5 percent on finished vehicles and up to 25 percent on parts; U.S. tariffs were 6.5 percent on complete vehicles and 8.5 percent on most parts.) The Royal Commission (1961, 50) agreed that bilateral free trade offered an “escape from low-volume production in Canada,” but the Canadian government instead chose the duty remission scheme.

26. Chrysler pushed for more tariff protection for its affiliates in its Royal Commission testimony, but it subsequently joined the majority and supported free trade.

27. “Memorandum of Conversation with R.A. Winter,” Regional Executive for Canada, Ford International Group, July 14, 1961, Lot File 65D493, Records relating to Economic Matters, 1956–66, Box 1, RG 59.

vehicle exports.” The State Department therefore decided that the United States should seek a waiver under GATT rules for automotive trade with Canada to ensure “that there would be no free riders, e.g. Volkswagen.”<sup>28</sup>

The sticking point in the negotiations was Canada’s longstanding concern that free trade would cause the branch plants to close. Without tariffs and industrial policy to guide investment, Canadian officials argued, production would concentrate in the larger market. To prevent automotive production from migrating back to the United States, they insisted on limiting free trade to original equipment manufacturers already in Canada. Canada also demanded production commitments from U.S. firms.<sup>29</sup> In separate letters of undertaking with the Canadian government, the Big Four agreed to maintain 60 percent Canadian value added in their domestic sales and to assemble one vehicle in Canada for every vehicle sold there.

Firms in the United States accepted production safeguards in return for free trade because in an uncertain trading environment they might face more restrictive measures. Thus, National Security Adviser McGeorge Bundy reported to President Lyndon Johnson: “The big companies are all in line, Ford and Chrysler with gusto.”<sup>30</sup> Ford executives told Congress that “the limited free-trade approach” was “entirely reasonable” given the risk of new regulations to shift production to Canada and increase exports to the United States. GM officials agreed that the APTA, while “not free of difficulties,” was a “workable plan” (U.S. House of Representatives 1965, 127–96). With restraints on entry and tariffs still in place on imports from outside North America, U.S. automakers could internalize the full benefits of free trade to compensate for the costs of reorganizing the division of labor between affiliates and the corporate parent.<sup>31</sup>

28. “Negotiations with Canada on Automobile Trade,” September 29, 1964, Lot File 65D493, Records relating to Economic Matters, 1956–66, Box 2, RG 59.

29. A Commerce Department official explained:

Because of the small size of their industry, the Canadians believed that unlimited free trade would result in their industry being swallowed up by the much larger and efficient industry south of the border. They therefore sought . . . assurances. . . . We on our side saw no such need because of the size of our industry, its very great efficiency, its lower cost, and its great ability to compete. (U.S. House of Representatives 1965, 104)

30. Memorandum from the president’s special assistant for National Security Affairs (Bundy) to President Johnson, Washington, DC, November 27, 1964, U.S. Department of State 2001, 692.

31. Auto parts producers protested that content rules and duty remissions for Canadian branch plants favored non-U.S. subcontractors. The United Automobile Workers (UAW) complained that Trade Adjustment Assistance for uprooted workers was inadequate, but it nonetheless expressed hope that free trade in automobiles would be extended to other sectors (U.S. House of Representatives 1965, 255–82).

The State Department accepted the production undertakings because, one memo stated, “Once we get to a free trade regime, it will have its own momentum—and we will all benefit from it.”<sup>32</sup> Multinationals such as Dupont, Procter and Gamble, U.S. Steel, and IBM already had issued calls for bilateral free trade,<sup>33</sup> and a few industry groups sought special tariff arrangements after the APTA was negotiated.<sup>34</sup> But for the most part, the *New York Times* observed, “U.S. subsidiaries have been organized as branch offices behind Canadian tariff walls and are little interested in, or equipped for, free trade.”<sup>35</sup> A comprehensive free trade agreement would have to wait another twenty years, as chapter 6 details.

### **Conclusion: Toward North American Free Trade**

The period marked by the conclusion of the Kennedy Round represented the end of an era in U.S. trade policy. From World War I to the 1950s, mass production industries enjoyed extraordinary cost advantages from large-scale manufacturing. As a result, firms in industries such as automobiles, farm machinery, sewing machines, office machinery, and electrical and electronic equipment opposed tariff increases in the 1920s and pushed for trade liberalization after 1930. These industries also supported unconditional MFN and pushed to eliminate trade discrimination, even as the world moved toward a closed system of regional blocs. Their political strength sustained the RTAA through successive rounds of the GATT after World War II, even though the tariff concessions of foreign countries were not as substantial as those made by the United States.

As large firms in mass production industries pushed for trade liberalization worldwide, they opposed regional integration between Canada and the United States. Most had chosen local production for the small, tariff-protected market in Canada, despite the high cost of manufacturing products with large returns to scale in small factories. Once these investments were sunk, U.S. firms had a

32. “Negotiations with Canada on Automobile Trade,” September 29, 1964, Lot File 65D493, Records relating to Economic Matters, 1956–66, Box 2, RG 59.

33. “Free Trade Envisioned,” *New York Times*, October 5, 1955, 54; “Market Tie Seen for U.S., Canada,” *New York Times*, February 14, 1961, 51; “More Ties Urged for U.S., Canada,” *New York Times*, January 24, 1965, 1; Williams 1986, 146.

34. The U.S. Embassy in Ottawa reported: “the greatest interest has been shown by the chemical and machinery industries” (“Functioning of U.S.-Canadian Automobile Arrangement and Possibility of Other Special Trade Arrangements,” U.S. Embassy Ottawa to Department of State, February 26, 1965, Subject Numeric Files, 1964–66, Box 991, RG 59).

35. “More Ties Urged for U.S., Canada,” *New York Times*, January 24, 1965, 7.

vested interest in preserving the trade barriers that separated Canada from the United States.

After 1950, the coalitional base of the RTAA began to fragment. Reconstruction in Europe and Japan enabled foreign producers to combine mass production techniques with low wages. More and more U.S. firms favored escape clauses and peril points in trade legislation to slow or reverse the pace of liberalization. At the same time, U.S. multinationals began to rethink their strategies toward Canadian manufacturing. As the branch plants became more exposed to foreign competition and Canada increasingly asserted its right to regulate FDI during the 1970s, the need for a more comprehensive trade agreement covering other sectors grew accordingly.

Two trends accelerated the transition to regionalism. First, U.S. companies began to move production offshore to alleviate high labor costs. Initiatives such as Mexico's Border Industrialization Program encouraged intrafirm trade and signaled a shift in production relationships within multinational companies in North America. Second, as tariffs dropped to insignificant levels by the end of the Kennedy Round, miniature replica production in separate national markets no longer made sense. Inefficient branch plants became a severe liability, but investments in fragmented manufacturing facilities already had been sunk. Rather than closing down foreign affiliates once the conditions that produced them disappeared, U.S. multinationals integrated them into regional supply networks. This created a constituency for the sorts of regionally oriented trade policies the United States previously had spurned and, in turn, planted the seeds for the NAFTA treaty, the subject of chapter 6.