

## Beneath the Commerce of Nations: A Theory of International Economic Structures

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Drawing upon the theory of hegemonic stability, this paper advances a theory of international economic structures. It places particular emphasis on analyzing the whole structure of the international economy, and not simply the absence or presence of hegemony. It finds that there is no axiomatic relationship between hegemony and free trade or declining hegemony and protection. By differentiating between non-hegemonic structures, moreover, the theory of international economic structures also calls into question the appropriateness of the 'British' or '1930' analogy for the future of the present international economy. Finally, the theory is briefly examined through the cases of American trade policy in the inter-war period and the 1970s and early 1980s. The conclusion argues against simplistic analogies between the two periods and maintains that a considerable potential does exist for collective leadership of the international economy in the 1980s.

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Drawing upon the decline of the *Pax Britannica* in the late 19th century and the inter-war period, current variants of the theory of hegemonic stability predict that America's declining hegemony will lead to increased economic instability, international conflict and national protectionism. Gilpin, in particular, has argued that there are three possible scenarios for the present and future international economy.

The first is that the original core [i.e., the United States] somehow manages to retain or reassert its dominant position relative to the emergent cores; it continues to set the rules . . . . The second possibility is a shift from a hierarchically organized international economic system to one composed of relatively equal cores; the several cores together negotiate the rules governing trade, money, and investment . . . . Finally, the system can break down and fragment into conflicting imperial systems or regional blocs . . . . Although none of these possibilities is inevitable . . . the third possibility is most likely (1975:72).

Two years later, Gilpin reflected upon this same point.

Drawing parallels between the contemporary period and past eras is obviously a risky undertaking . . . . Yet, the strains and tensions of the present are there, and the

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experience and lessons of the past indicate cause for concern over the future of the international economic order in an era of weakened international and domestic leadership (1977:61).

Both Krasner (1976) and Kindleberger (1973), although less directly, echo Gilpin's apparent pessimism for the future of the liberal international economy constructed under the *Pax Americana*.

With the growing popularity of the theory, the views of these authors have been reduced to a simpler and more axiomatic form. Keohane (1980: 132), for example, states that the theory

holds that hegemonic structures of power, dominated by a single country, are most conducive to the development of strong international regimes whose rules are relatively precise and well obeyed. According to the theory, the decline of hegemonic structures of power can be expected to presage a decline in the strength of corresponding international economic regimes.

Keohane's simplified account of the theory of hegemonic stability has since been subjected to several varied tests, with mixed results (*see* Cowhey and Long, 1983; Lawson, 1983).

In this paper I examine the appropriateness of the 'British' or '1930' analogy for the present period of declining American hegemony. I argue that both the original variants and subsequent tests of the theory of hegemonic stability suffer from an inadequate conceptualization of the *international economic structure* (IES). By failing to distinguish between the structurally derived interests of non-hegemonic nations, past studies have been unable to discern differences between non-hegemonic international economic structures. Differentiating between such structures is, I believe, necessary for a proper understanding of the politics and processes of the international economy. Once it is recognized that differences between non-hegemonic structures may exist, the assumed parallel between the decline of the *Pax Britannica* and the decline of the *Pax Americana* becomes questionable. In fact, as I shall try to show, the analogy is quite misleading.

My plan is to proceed by first reviewing the principal variants of the theory of hegemonic stability. Second, I present a summarized version of a theory of international economic structures. In subsequent sections I examine the IES and American trade strategy during the 1920s and 1930s, and then during the late 1960s and 1970s. Finally, I conclude by suggesting some lessons for the present international economy that may be drawn from past experiences.

### **The Theory of Hegemonic Stability**

There are two principal variants of the theory of hegemonic stability, both of which address the question: 'Why does a liberal international economy—that is, an economy characterized by relatively free trade, currency convertibility, and freedom of capital movement—remain intact rather than fragment into autarkic national economies and regional or imperial groupings?' (Gilpin, 1975:39) The first variant, associated with Kindleberger's (1973), *The World in Depression, 1929–1939*, focuses on the provision of the collective good of international stability, where instability is defined as a condition in which small disruptions (e.g., the 1929 Stock Market Crash) have large consequences (the 'Great Depression'). Predicated on the assumption that markets are inherently unstable (or non-homeostatic systems) and tend toward stagnation and fragmentation, Kindleberger argues that the international economy will be stable only if a single leader

is willing to assume responsibility for '(a) maintaining a relatively open market for distress goods; (b) providing counter-cyclical long-term lending; and (c) (re-) discounting in a crisis' (1973:292). Kindleberger has since added that the leader must also undertake to (d) 'manage, in some degree, the structure of foreign-exchange rates' and (e) 'provide a degree of coordination of domestic monetary policies' (1981:247).

The second variant, drawn from the writings of Gilpin (1975, 1977) and Krasner (1976), attempts to explain the strength and content of international economic regimes. Both authors share Kindleberger's assumption that markets are non-homeostatic systems. Yet, according to this variant, liberal regimes collapse not only because of inherent flaws in the self-regulating international market mechanism, but also because nations often pursue goals other than aggregate national income and welfare. Krasner suggests nations may also be interested in the additional goals of social stability, political power and economic growth (1976:319). Gilpin takes a similar position, arguing that 'Other than in a few . . . exceptional circumstances, societies . . . have placed much greater emphasis on security values such as social stability or self-sufficiency than on income gains from the free operation of markets' (1977:22). Consequently, the political task facing a nation is not only one of curing market disfunction through hegemonial market intervention, but also of creating an international regime which meets the security needs of nations so that they can pursue the gains from freer trade.<sup>1</sup> Both Gilpin and Krasner argue that strong liberal international economic regimes are most likely to be created when a single hegemonic leader exists within the international economy.

Despite the similarity of their conclusions, each of the authors defines the IES differently. Kindleberger defines the IES by the single dimension of relative size, which he divides into three categories: small, middle and large sized countries (1981:249-51). Gilpin defines the IES by political-military power and relative efficiency (1977:22) and he identifies three categories of nations within the international economy: hegemonic leaders, peripheral states and growth nodes (1975). Like Gilpin, Krasner defines the IES along two dimensions, but focuses instead on the degree of equality (or inequality) in both the level of development and size of nations, dimensions along which he suggests six hypothetical distributions of potential economic power (1976:323).

### A Theory of International Economic Structures

Of the three authors, Gilpin's definition of the IES provides the best framework for investigating the relationship between the IES and the trade strategy of individual nations over time. As recently noted by Ruggie (1982), Kindleberger's focus on the single dimension of relative size ignores the 'dimension of social purpose.' This narrowly delimited conception of the IES, Ruggie continues, can explain only 'the *form* of the international order, but not its *content*' (1982:382). As a result, relative size can explain only the necessary, but not the sufficient, conditions for the emergence of a liberal international economy. Krasner's definition of the IES, because it applies to the level of the system only, is of limited usefulness in specifying the interests of individual nations within the international economy.

Although Gilpin's definition allows the IES to be analytically dissolved into its constituent parts, there are two problems with his dimensions. First, despite the obvious relationship between the political-military power of the United Kingdom and the United States, and their ability to organize a liberal international economy, the relationship between political-military strength and economic influence diminishes as the analysis is extended beyond the category of hegemonic leadership. The Federal

Republic of Germany and Japan, for instance, possess much greater influence over the international economic regime today than their political-military strength would indicate. And despite the large arms purchases of some, much the same is true of the OPEC nations. As a result, Gilpin's first dimension would appear to be of only limited explanatory capability. By drawing upon Kindleberger, we can find a more appropriate indicator of international economic influence in relative size operationalized by issue area.<sup>2</sup>

The second problem with Gilpin's analytical framework is his use of the term 'efficiency'. Strictly defined, efficiency indicates the least wasteful means of production. It thus applies to *production* processes, and not to the nation as a whole. The concept Gilpin appears to be referring to when he uses 'efficiency' is actually productivity, or output per unit of input.

In this study, the IES is defined by the two dimensions of relative size and relative productivity. As the focus is on the international trade issue area, relative size will be measured by a nation's proportion of world trade. Relative productivity will be measured by national output per man-hour relative to the average national output per man-hour in the other middle and large sized nations. In the remainder of this section I consider in some detail how each dimension of the IES affects the international economy and trade strategy in individual countries.

#### *Relative Size*

Relative size affects both a nation's ability and, because of the free rider problem, its willingness to assume responsibility for stabilizing the international economy and creating or maintaining a strong international regime. 'Small states,' Kindleberger writes, 'have no economic power. At the same time they have no responsibility for the economic system, nor any necessity to exert leadership.' Small states, in other words, are free riders. Middle sized countries are, by contrast, '[b]ig enough to do damage to the system, but not substantial enough to stabilize it . . . ' (1981:249-251) Since they tend to act as if they were small free riders, middle sized countries are extremely destabilizing and are the 'spoilers' of the system. Only large states, Kindleberger concludes, have both the capability *and* responsibility for leading the international economy: 'The main lesson of the inter-war years,' he argues, is 'that for the world economy to be stabilized, there must be a stabilizer, one stabilizer.' (1973:305)

Kindleberger's analysis is similar to that developed by Olson and Zeckhauser in 'An Economic Theory of Alliances' (1966). Olson and Zeckhauser argue that in the provision of any collective good, there is a strong tendency for the largest members of the group to bear a disproportionate share of the burden of providing the good because they place a higher absolute value upon it. Likewise it can be argued that a hegemonic leader will place a greater absolute value upon a liberal international economy than others and, as a result, will undertake to stabilize the international economy and construct a strong regime in order to achieve this goal.

Kindleberger argues that it is precisely because international economic cooperation is unstable that only a single hegemonic nation can lead an international economy. 'With a duumvirate, a troika, or slightly wider forms of collective responsibility,' he states, 'the buck has no place to stop' (1973:299-300). But the willingness of nations to participate in the provision of a collective good is also affected by the content of state interests and the degree of uncertainty within the international economy, and under certain specifiable conditions, collective action may well occur in non-hegemonic structures.

A nation's willingness to participate in the provision of a collective good will be

influenced by both the costs and benefits of providing the good and the costs and benefits of *not* providing it. The difference between the net gain if the good is provided and the net loss if it is not is determined by the nation's relative productivity (which shall be discussed shortly). Here it is sufficient to note that the larger the cost of *not* providing the good, the greater is the probability that the nation will participate in its collective provision.

Decisions to participate in collective action are also affected by the actors' perceptions of whether or not the collective good will be provided (Kimber, 1981). If any actor is certain that others will provide the necessary good, no incentive exists for it to participate in collective action. Some uncertainty is necessary, therefore, to stimulate cooperation. High uncertainty, on the other hand, decreases the incentives for collective action by exciting fears that other actors may defect from the cooperative endeavor or fail to perform their responsibilities. These fears may even become self-fulfilling prophecies as nations become paralyzed and unable to act because of the fear of defection. International cooperation, as a result, is most likely to occur under conditions of moderate uncertainty.

An international economy in which a hegemonic leader is present may approximate conditions of low uncertainty, where nations can be reasonably confident that the leader will maintain stability and a liberal regime.<sup>3</sup> Under these conditions, however, little incentive for collective actions exists and free riding will be prevalent. Non-hegemonic structures, on the other hand, contain a moderate level of uncertainty. Each nation's confidence that the collective good will be provided despite its free riding is eroded and the incentives for collective action are thereby increased.

Greater uncertainty can also be introduced into any IES through non-structural changes, such as a major reorientation of the pattern of trade or currency instability. To an extent, non-structurally induced uncertainty may actually facilitate cooperation in hegemonic structures as it tends to make free riding less attractive. On the other hand, greater uncertainty in non-hegemonic structures, because they lack a clearly defined leader and rely upon the willingness of nations to cooperate, may actually hinder cooperation by increasing defections or the possibility of defections from collective action.

In short, a hegemonic leader is most likely to stabilize the international economy and create or maintain a strong regime. And while collective action in non-hegemonic structures is problematic, middle sized nations, which face high net costs for not providing the collective good and conditions of only moderate uncertainty, may also be able to cooperate sufficiently to obtain these goals.

#### *Relative Productivity*

Drawing upon classical economic theory, Kindleberger assumes that once stability is created a liberal international economy will emerge through the self-seeking behavior of utility maximizing nations. When offered the opportunities of international trade and the division of labor, however, not all nations will choose to accept them.<sup>4</sup> Some countries may decide to remain outside the international economy entirely, and others may choose to participate only when offered additional inducements.

Central to the arguments of Krasner and Gilpin is the assumption that nations are power maximizers. Because power is a relative concept—one nation's gain is another nation's loss—a power maximizing nation is concerned not only with his own absolute gain from trade, but also with the differential between his gain and that of others. This differential is referred to here as the *relative gain* from trade.

At the core of Gilpin's writings, and to a lesser extent Krasner's, is a second assumption that markets work to the relative advantage of some nations and to the relative disadvantage of others—thereby producing differences in the relative gains from trade. Drawing upon the writings of Myrdal and Hirschman, Gilpin writes

Although most states tend to benefit in absolute terms from the operation of the world market economy, the more efficient and technologically advanced states tend to benefit relatively more than other states. They enjoy higher rates of profit and more favorable terms of trade. As a consequence, a market economy tends, up to a point, to concentrate wealth in the more advanced economies. (1981:138)

The efficiency and technological sophistication of a nation do not directly affect the country's return from the market, but rather, become important through their effects on the nation's labor productivity—which determines its areas of comparative advantage and its relative gains from trade. Productivity, or output per unit of labor input, is a function of the supply of labor relative to that of land, capital and technology. An increase in any of these latter factors of production, *Ceteris paribus*, will increase labor productivity. In the early nineteenth century, Ricardo demonstrated that the absolute gains from international trade did not depend upon absolute differences in productivity between countries. Even if one country was more productive in the production of all goods (absolute advantage), Ricardo showed that the two countries could still gain from trade by specializing in the production of those goods in which they were most productive (comparative advantage) and exchanging through international trade. There is nothing within this classical argument, however, which demonstrates that these two countries will gain equally. One nation may enjoy relatively greater gains than the other.

Gilpin (1975, 1981) attempts to move beyond the comparative statics of classical economics and develop a dynamic conception of international trade in which the differential benefits can be assessed more clearly.<sup>5</sup> An increase in the technological stock of a country (or capital or land), such as occurred with the invention of the steam engine, the cotton gin, or the techniques of assembly line production, will increase the productivity of labor in the manufacture of one or more goods ( $X$ ), shifting the comparative advantage of the nation to good  $X$ , increasing the value added, and expanding the net wealth of the country. As the innovating country begins to expand the sale of  $X$  in foreign markets, it increases production and attracts capital and labor from less productive occupations—increasing domestic demand, investment and profits. The higher rate of growth stimulated by increased exports and the net expansion of wealth increases the national capital stock and provides the wherewithal for additional research and development. As a result, a new increase in labor productivity is spawned which initiates a second round of the cycle. This process has been referred to as both *backwash* (Myrdal) and *polarization* (Hirschman).<sup>6</sup> As the process of concentration is subject to the law of diminishing returns, the growth curve stimulated by any one technological innovation (or increase in capital or land) eventually levels off (*see* Gilpin, 1981:156–185).

Throughout this process, labor productivity in the non-innovating country remains static, although its areas of comparative advantage shift in response to changes in the innovating country. The non-innovating country enjoys new growth as it increases its specialization in new product lines and begins to supply markets formerly met by production in the innovating country. Labor and capital are both attracted to the new industry and driven out of older product lines because of the availability of now cheaper

goods from the innovating country. The increased profits and growth engendered in the non-innovating country through increased specialization are offset to an extent by the loss of profits and income in the failing industries. This process is referred to as *spread* (Myrdal) and, more optimistically, *trickle-down* (Hirschman). The net result of this process is unclear and a matter of considerable debate,<sup>7</sup> but Gilpin assumes that in the short run, the backwash process dominates the spread effect.<sup>8</sup>

The free functioning of the international market is therefore assumed to concentrate wealth in nations of high productivity. Under this assumption highly productive nations will give free play to the functioning of the international market and will favor free trade because they enjoy disproportionate benefits from such trade. Yet even highly productive nations possess some internationally uncompetitive industries, and under certain conditions (discussed shortly) they will desire to protect these industries while maintaining their general commitment to free trade.

Nations of low productivity, on the other hand, do not benefit from the functioning of the market to this same extent as highly productive countries. This handicap has cumulative effects, so that nations of low productivity fall further behind their more productive counterparts over time. To break this cycle, relatively unproductive nations will attempt to develop the advantages of backwardness through government-led alterations in the nation's industrial structure so as to compete with the more productive nations upon a more equal basis.<sup>9</sup>

Historically, protectionist policies—by providing the opportunity to develop economies of scale and domestic market stability—have been an important and perhaps necessary component of government-led strategies of economic restructuring. Thus, it follows logically from the assumption that the backwash process dominates the spread effects that nations of low relative productivity will favor protection at home. Despite their strong interest in protection as a means of enhancing their competitive advantage, the static law of comparative advantage still applies for nations of low relative productivity. At any single point in time, they each remain internationally competitive in the production of one or more goods. As a result, nations of low relative productivity will desire at least a modicum of openness abroad so as to market the good(s) in which they currently possess a comparative advantage.

## **The Dynamics of the International Economic Structure**

### *Assumptions and Propositions*

Briefly, there are five basic assumptions that underlie the theory of hegemonic stability. These assumptions also form the basis for the theory of international economic structures summarized here. They are:

1. The international system is anarchical and based upon the principle of self-help.
2. Nation-states are the dominant actors within this international system.
3. The international market is a non-homeostatic system.
4. Within this market, the backwash process dominates the spread process (at least in the short run).
5. In descending order, nations seek to maximize their (a) relative gains from trade, (b) economic security, and (c) absolute gains from trade.

Each of these assumptions address particular aspects of the IES. The first two assumptions concern the nature of the international system as a whole.<sup>10</sup> The third and fourth assumptions address the behavior of the international market. The fifth

assumption concerns the behavior of nations. Drawing upon the first assumption, assumption five asserts that nations are power maximizers and therefore give primacy to their relative gains from trade, or the difference between the absolute gains from trade of themselves and all others. Additionally, it asserts that economic stability is a prior and, perhaps, necessary requirement for a nation's pursuit of its absolute gains from trade. Thus, nations may adopt protection in order to stabilize their economies even though it diminishes their absolute gains from trade. To the extent that classical economics has recognized national interests other than the maximization of the absolute gains from trade, the theory developed here reverses the ranking of these interests which that approach sets forth.<sup>11</sup> This has important implications for the argument set forth below.

There are also two central theoretical propositions. First, the larger the nation within the international economy, the greater is its willingness to stabilize this economy and construct a strong international economic regime. In general, only the largest nations are willing to undertake these tasks. Middle sized nations may also be willing to stabilize the international economy and construct a strong regime, but usually only where they face high net costs of not providing these collective goods. Second, the greater the relative productivity of the nation, the stronger is its interest in free trade. Yet even the most productive nations will attempt to protect their least competitive industries and even the least productive nations will desire some free trade abroad. Given these assumptions, the two theoretical propositions, and the interaction between the two propositions, it is possible to identify at least six different categories of nations within the two dimensions of relative size and relative productivity. These six categories are defined graphically in Figure 1.<sup>12</sup>

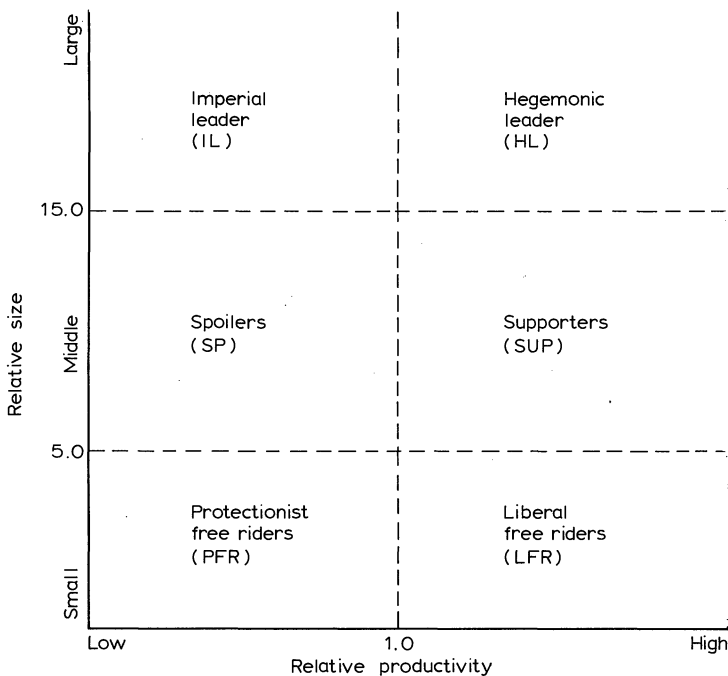


FIG. 1. Six categories of international economic actors.



There are three categories of nations of low relative productivity. In order of increasing relative size, they are *protectionist free riders* (PFR), *spoilers* (SP), and *imperial leaders* (IL). As they lose disproportionately from free trade, nations of low relative productivity possess a strong preference for protection at home. Yet, because they retain some comparative advantage, they also desire a limited amount of free trade abroad. This desire will not be strong, may be limited to seeking special trade preferences, and—because of their concern for the relative gains from trade—will remain secondary in importance to the desire for protection at home. Even though protection and free trade are continuous concepts, the choices available to a nation can be simplified to *greater free trade* ( $FT$ ) or *greater protection* ( $P$ ) for itself (first term) and all others (second term). Within this schema, the preferences of PFRs, SPs, and ILs can be ranked as  $P/FT > P/P > FT/FT > FT/P$ . This preference function asserts that despite the importance of dynamic comparative advantage and the relative gains from trade, ILs, SPs and PFRs also desire and will seek to obtain the gains from trade which can be acquired through static comparative advantage. Thus,  $P/FT$  is preferred over  $P/P$ . It can also be argued, however, that ILs, SPs, and PFRs—because of their focus on the relative gains from trade—may prefer to penalize their more productive trade rivals (who benefit from free trade abroad) and benefit their less productive counterparts (who like themselves are harmed relatively by free trade). If so, their preference function would be  $P/P > P/FT > FT/P > FT/FT$ . While the first preference function is used throughout the analysis developed here, either could be used without significantly affecting the dynamics of the IES discussed below. In both functions, ILs, SPs, and PFRs possess a dominant strategy of protection at home.

PFRs, as a result of their small size and lack of international influence, will be largely indifferent to the international economy. They possess little ability to affect the policies of others. Rather, their attention will be directed inward and focused on their own economic development. Most Third World nations and several of the less productive European nations today would be classified as PFRs upon the basis of their relative size and relative productivity.

SPs, or nations of relatively low productivity and middle size, do affect the degree of stability and the strength of the regime through their protectionist behavior. Consciously or unconsciously, they may even undermine the international economy by their protectionism. France and Germany in the late 19th century (*see* Table 1) and France and Japan throughout most of the post-World War II era (*see* Table 2) would be classified as SPs by their positions within the IES.

ILs, like hegemonic leaders discussed below, possess sufficient capabilities to lead the international economy. An IL, however, because of its low relative productivity, has little incentive to stabilize the international economy or create a strong regime. ILs instead will seek to limit international trade to essential raw materials or goods that cannot be produced at home. Furthermore, they will attempt to organize this trade through a mercantilist or administered trade regime. Since the industrial revolution, no ILs have existed within the global economy.<sup>13</sup>

There are also three categories of nations of high relative productivity: *liberal free riders* (LFR), *supporters* (SUP), and *hegemonic leaders* (HL). The burden of leadership in the international economy falls upon HLs because of their large relative size. It is from their high relative productivity, on the other hand, that HLs derive their interest in creating or maintaining a *liberal* international economy. While HLs could benefit at times from protecting their least productive industries, doing so would undermine their ability to lead the international economy towards greater openness because they constitute such a

large proportion of world trade. Their preferences, as a result, can be ranked as  $FT/FT > FT/P > P/FT > P/P$ . It can also be argued that instead of eschewing protection at home in order to more effectively lead the international economy, HLs may prefer  $P/FT$  over  $FT/P$  so as to protect their least competitive industries, yielding a preference function of  $FT/FT > P/FT > FT/P > P/P$ . In light of the largely unchallengeable economic position of a HL, however, the gains from protection are not likely to outweigh the costs inherent in undermining the state's leadership ability. Assuming that HLs recognize this trade-off, their preferences are more accurately captured in the first function. Again, the choice of preference function will not significantly affect the dynamics of the IES as HLs possess a dominant strategy of free trade under either function. The United Kingdom in the mid-19th century and the United States in the mid-20th century are the only two post-industrial revolution examples of hegemonic leaders.<sup>5</sup>

LFRs and SUPs possess only a moderate to strong interest in free trade. Unlike HLs, they do not possess the capacity to lead the international economy and, as a consequence, face no inherent constraints on protecting their least competitive industries. SUPs and LFRs protect these industries whenever possible. They will desire, in other words, a minimum level of protection at home. Although the protection/free trade dichotomy overstates their interest in domestic protection, their preferences can be ranked as  $P/FT > FT/FT > P/P > FT/P$ . LFRs and SUPs do not possess a clearly dominant strategy of either free trade or protection. What is of primary importance to these nations is the presence of free trade abroad, which is necessary for them to reap the export advantages derived from their high relative productivity. While SUPs and LFRs value export markets more than protection at home, they will sacrifice the latter only if necessary to obtain the former.

LFRs possess little influence over the international economy or the actions of other nations. They can free ride (adopt  $P/FT$ ) with impunity. Belgium and Sweden today would be classified as LFRs within the IES.

As SUPs possess only moderate influence within the international economy, their mixed interests create the tendency and their middle size the ability to free ride when a HL is present to maintain the liberal international economy. During periods of declining hegemony, as we shall see shortly, SUPs become critical in determining the continued openness or closure of the international economy. The United States was a SUP from the early 19th century until World War II. After a brief two decades as an HL, the United States returned to this category in the mid-1960s. The Federal Republic of Germany and France joined the United States in approximately 1965 and 1975 respectively (see Table 2). If present trends continue, Japan will also become a SUP by the early 1990s.

International economic structures are distinguished by the number of middle and large sized nations present in the international economy and the categories into which they are classified. Changes in the IES are of two kinds: changes within a structure and changes of a structure.<sup>14</sup> Changes *within* a structure occur within specific categories. A HL's ability to stabilize the international economy is affected as its relative size increases or decreases, even though it may remain in a position of hegemony. Likewise, rapid productivity growth in one nation which alters its rank within the international economy from second to first most productive nation will effect the foreign trade strategies of both the nation experiencing the growth and the one displaced, even though neither nation changes category. More importantly, changes *of* structure occur when any middle or large sized nation changes category. The decline of a HL into a SP, the rise of a LFR into a SUP, or the transformation of a SP into a SUP would each constitute a

change of structure. Since the mid-19th century, there have been six distinct international economic structures: two of hegemonic leadership (United Kingdom, early 19th century–1912, and the United States, 1945–1965), two of bilateral supportership (United States and the United Kingdom, 1912–1932, and the United States and the Federal Republic of Germany, 1965–1975), one of unilateral supportership (United States from approximately 1932–1945), and one of multilateral supportership (United States, the Federal Republic of Germany, and France, 1975–present). Each structure has its own dynamics for resolving the conflicting preferences of nations.

*Structure and Strategy*

Before examining the politics and processes of non-hegemonic structures, the preference functions identified above will be used to clarify the logic of hegemonic leadership within the international economy. A hegemonic IES is depicted in Figure 2.

As can be seen from Figure 2, a hegemonic structure will not axiomatically lead to a liberal international economy: universal free trade (*FT/FT*) is not the equilibrium outcome for any bilateral relationship. In every interaction between a HL and a SUP, LFR, SP or PFR, the equilibrium outcome is *FT/P* (or *P/FT* from the perspective of the

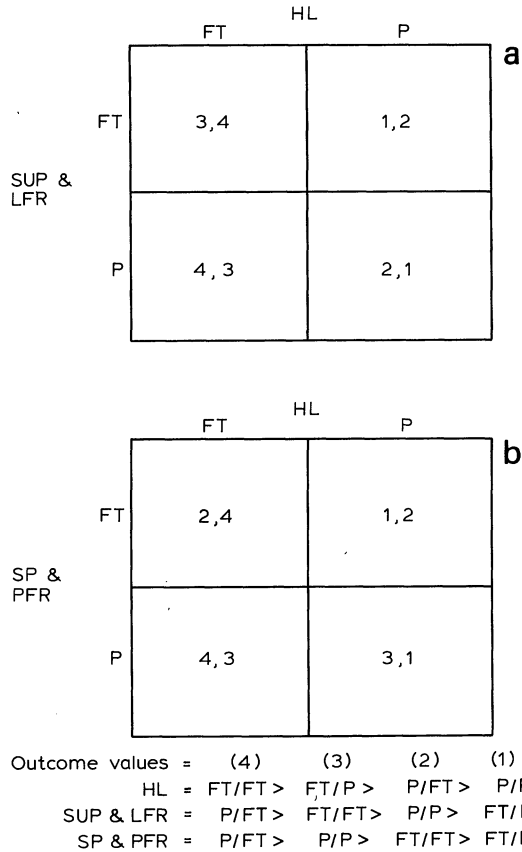


Fig. 2. A hegemonic international economic structure.

middle and small sized countries). In each case, the HL must impose (or offer) greater or lesser positive or negative sanctions (or side-payments) to obtain the nation's compliance with universal free trade under a liberal international economic regime. In other words, the hegemonic leader must directly alter the costs and benefits of free trade that SPs, PFRs, SPs, and LFRs face as a result of their position within the IES.

The sanctions imposed (offered) by the HL for compliance with a liberal regime must be at least equal to if not greater than the difference between the best payoff obtainable by nations in the absence of compliance and the free trade payoff. In cases of PFRs, SPs, LFRs and SUPs the size of the sanction (or the price of compliance,  $PC$ ) must be equal to or greater than  $P/FT - FT/FT$ . The price of compliance is likely to be high for SPs and PFRs (difference between first and third choices) and moderate for SUPs and LFRs (difference between first and second choices).

The sanctions imposed (offered) by the HL can take the form of threatening to close its market to the goods of the non-complying country, absorbing the costs of adjustment, or accepting a measure of protection in some areas to secure compliance in others. Historically, HLs may have also drawn upon their political-military power to ensure compliance by others to a free trade regime.<sup>15</sup>

In addition to paying the price of compliance, a HL must also stabilize the international economy. The ability of a nation to fulfill this task is determined by the resources available to it for regulation relative to the size of the disturbance it must control.<sup>16</sup> Regulation, or the process of maintaining equilibrium in the international economy, is at the core of Kindleberger's (1973) conception of stability. Given that disturbances are largely exogenous to the IES (e.g., the accelerating pace of technological advance which led to the rapid decline in prices during the late nineteenth century), the ability of nations to regulate disturbances successfully is determined by two factors: the absolute level of resources available to the nation for regulation; and the efficiency with which it can use these resources. Each of these factors can compensate for the other. A nation with large resources may be able to successfully regulate a disturbance even though its application of resources is inefficient. Conversely, a nation with smaller resources may be successful in regulating a similar disturbance if it uses resources more efficiently. The cost of regulating the international economy is referred to here as the *price of stability* ( $PS$ ). As disturbances can differ in magnitude and assuming that nations differ in their ability to manage their resources, it is not axiomatic that a hegemonic leader will be able successfully to regulate or stabilize the international economy.

Whether a liberal international economy is established or maintained depends, first, on the price of stability, and second, on the resources of the HL available for influencing other nations relative to the sum of the individual prices of compliance. The total resources available to the HL are limited to the difference between the outcome derived from the independent decisionmaking of sovereign nations ( $FT/P$ ) and the free trade outcome ( $FT/FT$ ). These resources, less the price of stability, must be equal to or greater than the sum of the individual prices of compliance, or

$$(FT/FT - FT/P)_{HL} - PS \geq \sum (P/FT - FT/FT)_{SUP, LFR, SP \& PFR}$$

for free trade to be established. It is not necessary that hegemony lead to a liberal international economy. In an IES composed only of a HL and SPs, for example, the price of compliance would be likely to exceed the benefits of universal free trade received by the HL.

An IES of bilateral supportership is shown in Figure 3. A structure of multilateral

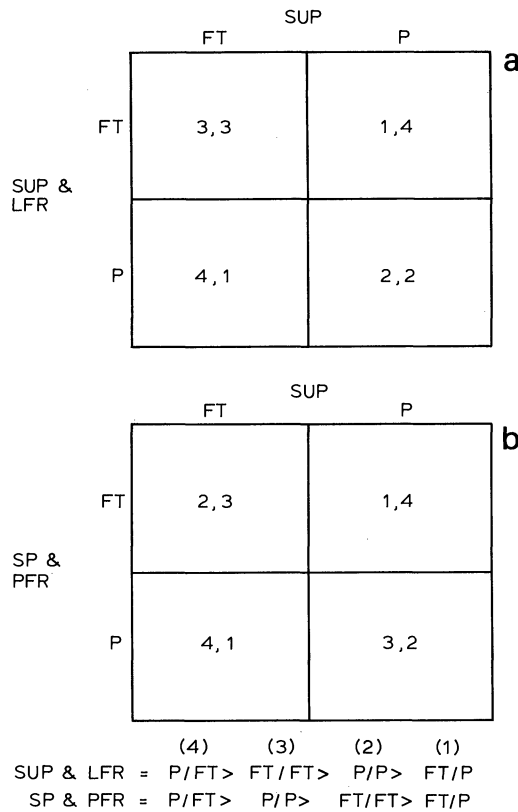


FIG. 3. An international economic structure of bilateral supportership.

supportership is similar to this bilateral variant and the dynamics of the two structures are identical. When two or more SUPs exist in the international economy, they confront a classic Prisoner's Dilemma. If each SUP attempts to maximize its individual gains ( $P/FT$ ) the net outcome will be suboptimal ( $P/P$ ). In the long run, each SUP can benefit from the cooperative provision of free trade ( $FT/FT$ ). The problem, however, lies in overcoming this 'dilemma of common interests'. Recently, Stein (1982:312) has argued that such dilemmas have been traditionally resolved through a 'collaborative regime,' which requires a highly formalized set of rules which 'specify what constitutes cooperation and what constitutes cheating' and procedures by which each party can 'be assured of its own ability to spot other's cheating immediately.'<sup>17</sup> In addition, the higher the cost of not obtaining free trade, the greater will be the incentives for nations to cooperate. SUPs and LFRs, although the latter will only marginally influence support for the regime, possess a moderate to strong interest in free trade because of their high relative productivity. The cost of not cooperating ( $P/P - FT/FT$ ) is likely to be significantly greater than the gain which would be acquired by protecting their least competitive industries ( $P/FT - FT/FT$ ). By imposing the necessary constraints upon the behavior of each other through a collaborative regime, SUPs can create a condition where free trade yields the highest obtainable long term payoff.

On the other hand, the universal free trade outcome is an unstable equilibrium. The

incentives and disincentives for cooperation are both strong. In this case, the IES is not wholly determining and the level of uncertainty within the international economy becomes particularly important. Because their strategies are interdependent, each SUP must be able to predict with some confidence the policies of others if cooperation is to occur. No SUP gains by continuing to pursue universal free trade ( $FT/FT$ ) if it believes that other SUPs are defecting or are about to defect from the cooperative solution. Only if it believes that others are pursuing and will continue to pursue free trade will a SUP be induced to cooperate. Moderate uncertainty, created by the absence of any clear leader, is likely to increase incentives for cooperation and reduce the free rider problem while at the same time not greatly undermining the ability of SUPs to predict each other's policies. High uncertainty, which can be created by non-structural changes, increases the likelihood that SUPs will adopt protectionism in order to stabilize their domestic economies and diminishes their predictive ability. As a result, the fear of defection may become self-fulfilling. A new, more stable, and sub-optimal equilibrium will form at the non-cooperative or universal protectionist outcome. In short, two equilibria are possible within a structure of bilateral support. Under conditions of moderate uncertainty, SUPs are likely to agree to cooperate in the mutual provision of universal free trade. If high uncertainty exists, however, cooperation is likely to be difficult to obtain and the SUPs may pursue more protectionist policies.

Due to the necessity of overcoming their dilemma of common interests, negotiations between SUPs, when they occur, will focus on the rules, norms and procedures of a liberal international economic regime. These negotiations, moreover, will center on obtaining an equitable distribution of costs. Because of their middle size, SUPs are unwilling to accept high short term costs for long term gains, as a HL might. Rather, they seek to balance their short term costs and benefits and prefer to bargain for collective movement towards specified goals. But despite the rational self-interest of SUPs in creating a liberal regime, it still may not be formed. Considerable costs will be incurred in negotiating such a regime precisely because it aims to constrain national behavior. If the negotiating costs exceed the benefits received by the SUPs from universal free trade, the regime will most likely fail. And even if successfully negotiated, the regime will be fragile. Each SUP faces a strong temptation to cheat as  $P/FT$  remains its first preference. For the same reason, the regime is likely to countenance greater protectionism than a hegemonically organized liberal regime. In addition, a collaborative regime will be slow to adapt or rule on the permissibility of changing national economic policies because of its necessarily explicit nature.

The final concern is the ability of bilateral or multilateral support successfully to regulate or stabilize the international economy. As for a single HL, the price of stability in a structure of bi- or multi-lateral support is a function of resources and the efficiency with which they are used. Two or more SUPs are likely to possess greater collective resources than a HL. The combined shares of world trade of the United States and United Kingdom were 25.2% in 1913 and 27.2% in 1929, the beginning and end of the period of bilateral support in the inter-war era, compared with the United Kingdom's 24.0% at the peak of its hegemony in 1870. Likewise, the United States, Federal Republic of Germany and France accounted for 33.4% of world trade in 1977, while the United States alone held only 18.4% in 1950. On the other hand, two or more SUPs will be unlikely to use their combined resources as efficiently as a single hegemonic leader. As in negotiating the regime, there will be costs involved in organizing the joint intervention necessary for the successful regulation of disturbances in the international economy.

In summary, a liberal international economy will arise in bi- or multi-lateral supportership only under conditions of moderate uncertainty where the net benefits of free trade for the SUPs, less the costs of negotiating the regime ( $NC$ ) and less the price of stability, exceeds the price of compliance of the other nations. In other words, universal free trade will occur in a non-hegemonic IES only if

$$\sum (FT/FT - P/P)_{SUP} - NC - PS \geq \sum (P/P - FT/FT)_{SP, PFR \& LFR}$$

Thus, the absence of hegemony does not necessarily mean the absence of leadership; under these conditions, effective collective leadership of a liberal international economy is possible and, indeed, probable.

An IES of unilateral supportership is depicted in Figure 4. The relationship between a SUP and LFRs is similar to that between two SUPs. Because of their small size, however, it is unlikely that LFRs can resist the temptations of free riding or supply the necessary constraints upon the SUP to prevent it from adopting protection.

The relationship between a SUP and one or more SPs and PFRs is paradoxical. A single SUP, which possesses a moderate to strong interest in free trade, and which might be expected to exert a moderating influence upon protectionism in the international

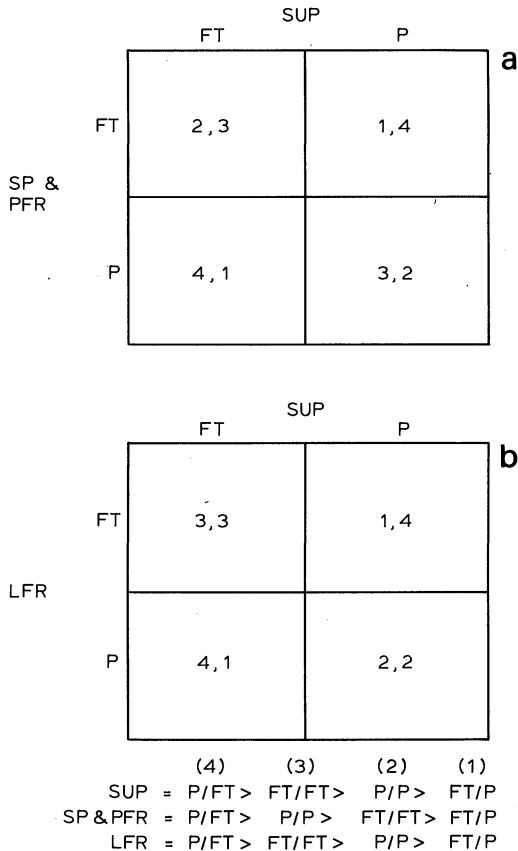


FIG. 4. An international economic structure of unilateral supportership.

economy, actually undermines the liberal regime in the short run. The dominant strategy of protection of SPs and PFRs ultimately forces the single SUP, which possesses only modest influence over the international economy, to accept its second worst payoff of  $P/P$ . There is no countervailing pressure upon the SUP to eschew its first preference of  $P/FT$  for a policy of free trade as there is under bi- or multi-lateral supportership. The core of the paradox is that a single SUP can achieve its highest payoff only by preempting the protectionist policies of SPs and PFRs, thereby creating a higher *relative* level of protection approximating its  $P/FT$  preference. By pre-emptively adopting a higher relative level of protection, the SUP channels imports formerly absorbed by its markets toward other countries (which are now relatively more open). In the short run, and to the extent that these now diverted goods are non-competitive, this action does not significantly reduce the SUP's potential export markets. The SUP therefore, obtains greater protection at home than it otherwise would have achieved and maintains its exports. In the long term, however, this strategy is counterproductive. The SUP's protectionist policies will lead to a tariff war in which, through a pattern of action and reaction, the SUP and SPs build higher and higher tariff walls around their economies.

As a result, this strategy will create benefits for the SUP only if implemented pre-emptively. If the SUP waits until other nations increase their level of protection, it will both lose its export markets and fail to gain additional protection for its own economy. On the other hand, this strategy is logical only if greater protectionism abroad is imminent. As the SUP gains from openness in the international economy, and since its pre-emptive protection will clearly act as a catalyst for closure, acting too soon or before protection abroad is imminent will cause an undue loss of exports for the SUP. Maximum benefits, therefore, require precise timing. But again, even with good timing, the pre-emptive strategy will provide benefits to the SUP only in the short run; its success is delimited to the time it takes other nations to retaliate.

Once tariff levels reach heights which prohibit international trade and nations become locked into an extreme  $P/P$  outcome, the interests of the SUP change. Any reduction in tariffs then benefits the SUP. While it cannot lead the international economy, a SUP will benefit from bargaining with other nations over tariff reductions. But because of its middle size, the influence of the single SUP will be limited and the actual reductions are likely to be moderate. Unlike negotiations between two or more SUPs, which focus on the regime itself, negotiations in a structure of unilateral supportership will center on the exchange of tangible concessions between countries. The SUP will attempt to make equitable bargains and will not accept unilateral costs, as would a HL. The movement back to openness within a structure of unilateral supportership will therefore be limited in scope and characterized by explicit bargaining.

We see, then, that hegemony is neither a necessary nor a sufficient condition for the creation of a liberal international economy. If the price of compliance and price of stability exceed the benefits of universal free trade, the hegemonic nation will be both unwilling and unable to lead the international economy toward greater openness. Conversely, two or more SUPs may be willing and able to construct or maintain a liberal international economy if certain conditions (specified above) are met. In an IES of bilateral or multilateral supportership, however, the international economy is likely to be more protectionist and more fragile, not because SPs, PFRs and LFRs behave differently than under hegemony, but because the SUPs themselves desire a measure of protection and possess a tendency to cheat—both of which may undermine their ability to cooperate. Finally, under a structure of unilateral supportership, the international



economy as a whole and policy within the SUP are likely to be unstable. When it confronts the imminent closure of its export markets, a single SUP will pre-empt protectionism in others, thereby initiating a new upward spiral of tariffs or other barriers to trade. And once the tariff walls are constructed the SUP can gain only by bargaining them away brick by brick.

**The IES and American Trade Strategy, 1913–1939<sup>18</sup>**

In the years immediately preceding World War I, the United Kingdom evolved from a HL into a SUP, creating a change of the IES from hegemony to bilateral supportership (see Table 1 and Figure 5). American trade strategy was affected in important ways by this transformation. Under conditions of only moderate uncertainty before the war, the

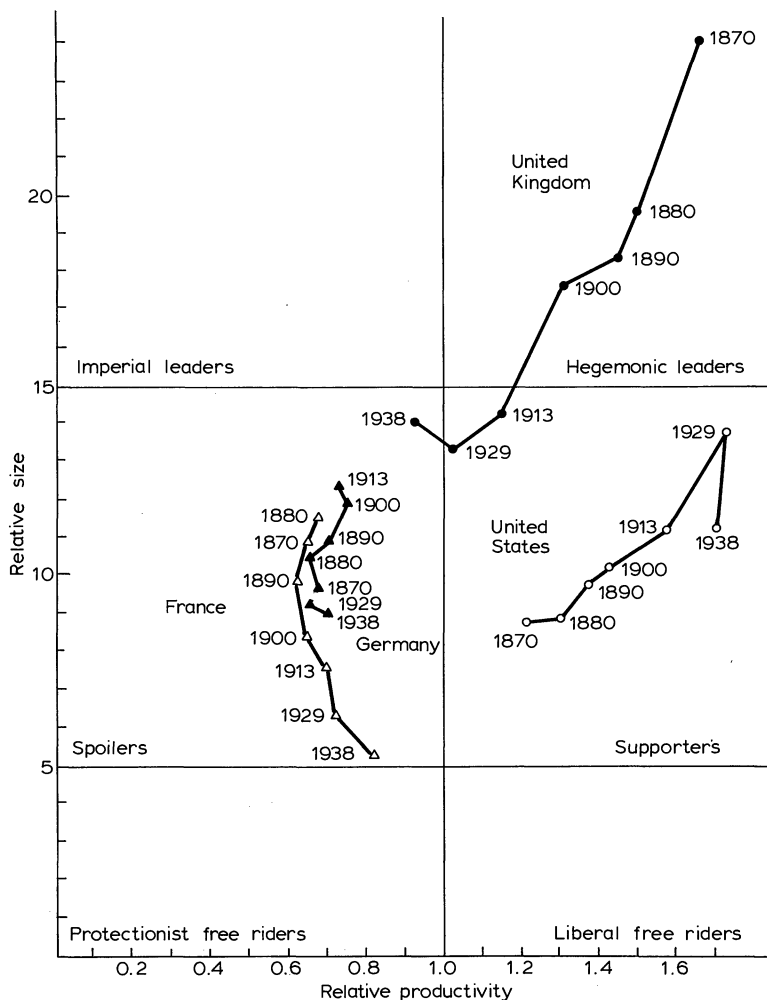


FIG. 5. The international economic structure 1870–1938.

TABLE 1. The International Economic Structure, 1870–1938.

Year	United States		United Kingdom		Germany		France	
	PWT*	ROMH†	PWT	ROMH	PWT	ROMH	PWT	ROMH
1870	8.8 <sup>a</sup>	1.22	24.0 <sup>a</sup>	1.63	9.7 <sup>1</sup>	0.66	10.8 <sup>a</sup>	0.65
1880	8.8 <sup>c</sup>	1.29	19.6 <sup>c</sup>	1.50	10.3 <sup>b</sup>	0.64	11.4 <sup>c</sup>	0.69
1890	9.7 <sup>d</sup>	1.37	18.5 <sup>d</sup>	1.45	10.9 <sup>d</sup>	0.69	10.0 <sup>d</sup>	0.63
1900	10.2 <sup>c</sup>	1.42	17.5 <sup>c</sup>	1.30	11.9 <sup>e</sup>	0.74	8.5 <sup>e</sup>	0.65
1913	11.1 <sup>f</sup>	1.56	14.1 <sup>f</sup>	1.15	12.2 <sup>f</sup>	0.73	7.5 <sup>f</sup>	0.68
1929	13.9 <sup>g</sup>	1.72	13.3 <sup>g</sup>	1.04	9.3 <sup>g</sup>	0.66	6.4 <sup>g</sup>	0.74
1938	11.3 <sup>h</sup>	1.71	14.0 <sup>h</sup>	0.92	9.0 <sup>h</sup>	0.69	5.2 <sup>h</sup>	0.82

\* Proportion of World Trade.

† Relative National Output per Man-hour (i.e. 'relative productivity').

<sup>a</sup> Mulhall data, 1870, 1880. See S. Kuznets, *Modern Economic Growth* (Yale University Press, 1966), p.306.

<sup>b</sup> Mulhall data, 1880, 1889. Kuznets, p.306.

<sup>c</sup> League of Nations data, 1876–80. League of Nations, *Industrialization and Foreign Trade* (League of Nations, 1945), pp.157-67.

<sup>d</sup> League of Nations data, 1886–90, in Kuznets, p.307.

<sup>e</sup> League of Nations data, 1896–1900, in Kuznets, p.307.

<sup>f</sup> League of Nations data, 1911–13, in Kuznets, p.307.

<sup>g</sup> League of Nations, *Review of World Trade*, 1927–29.

<sup>h</sup> *Ibid.*, 1936–38.

<sup>i</sup> Relative Productivity data derived from A. Maddison, 'Long Run Dynamics of Productivity Growth,' *Banca Nazionale del Lavoro Quarterly Review*, 128, (March 1979), p.43.

United States, recognizing the changing nature of the international economy and its position within it, adopted a liberal and active strategy. The nation significantly lowered its level of protection at home and created a mechanism, albeit one which was relatively weak, to accomplish a similar aim abroad. While desiring both protection and export expansion after 1912, the United States for the first time became willing clearly to subordinate the former goal to the dictates of the latter.

World War I, however, introduced a high level of non-structural uncertainty into the international economy. The patterns of trade and finance and the par values of the major currencies established during the period of British hegemony were disrupted. The war left in its wake a host of unsettled questions involving reparations, war debts, and the future role of Germany within Europe, all of which helped to politicize the international economy.

The United States reacted to this increased uncertainty in two ways. First, prompted by changes in European and particularly in British trade policy, the United States sought to insulate itself through higher protection. These tariff increases, on the other hand, were more moderate than they might have been because of the continuing constraints exerted by the IES of bilateral supporters. In addition, the United States also introduced a measure of administrative flexibility into the tariff in order to increase its ability to respond to changes in the international economy. Second, the United States, while recognizing that nations were more likely to be protectionist than in the past, sought to expand its exports through a more active trade policy and the adoption of the unconditional most-favored-nation (MFN) principle.

In game-theoretic terms, the United States in 1913, while still desiring  $P/FT$  (the first

choice of a SUP), recognized that within the structure of bilateral supportership *FT/FT* (second choice) was the best outcome it could reasonably hope to obtain. It achieved this result *de facto* with the United Kingdom by lowering its own tariff and establishing an unstable equilibrium in the north-west cell of Figure 3a. Through the reciprocity provision of the Underwood Act, the United States also created a mechanism through which to pursue this objective of universal free trade with others. In other words, the United States sought to shift its trading relationship with SPs and PFRs away from the equilibrium point in the southeast cell to the northwest cell of Figure 3b.

As previously noted, however, the universal free trade (*FT/FT*) outcome is an inherently unstable equilibrium: a partial defection from *FT/FT* or the possibility of greater defections in the future by either SUP will create an equivalent reaction in the other. In other words, if either SUP appears to be adopting greater protection at home or *P/FT* (its first choice), which from the perspective of the other SUP appears as *FT/P* (its last choice), the second SUP will also defect from the universal free trade outcome. Under the high uncertainty prevalent within the international economy during the post-World War I era, both the United States and the United Kingdom defected from free trade. Unfortunately, the free trade-protection dichotomy does not allow precise predictions to be made on the actual levels of tariffs. While the protectionist response is explicable within a structure of bilateral supportership under conditions of high uncertainty, America did not return to the high protectionism of the 1890s or, indeed, of the 1930s. Rather, it adopted a level of protection mid-way between the freer trade of 1913 and high protection of the 1890s because it was constrained at least in part by its continuing desire to export abroad and its fear of retaliation by other nations.

In 1932 or thereabouts, the United Kingdom evolved from a SUP into a SP, creating a second change of the IES from bilateral into unilateral supportership. This transformation and the years immediately preceding it constituted a period of acute instability in American trade strategy. Finding the constraints on its trade policy previously exerted by the structure of bilateral supportership loosened, the United States sharply increased its tariff in a strategy of pre-emptive protection in 1930. Additionally, while maintaining the instruments of an active trade policy, the United States turned inward upon itself. The rhetoric of American trade policy in the early 1930s was, in many ways, a reversion to the highly protectionist and mercantilist slogans of the early 1890s. The tariff was once again portrayed as a strictly domestic issue. Most importantly, the political leadership ceased to fear the threat of tariff retaliation. This factor, which had played an important role in restraining protectionist pressures within the United States during the period between 1913 and 1930, was not reflected in the tariff debates and failed to exert its moderating influence. The protectionist forces in Congress, as a result, were unleashed.

Between 1930 and 1934, largely as the result of America's pre-emptive action, the level of protection within the international economy rose precipitously. The United Kingdom, under pressure from its Empire, adopted a more protectionist policy in order to strengthen its imperial preference system. This was congruent with Britain's new status as a SP. Other nations more directly retaliated against the new tariff policy of the United States. By 1933, world trade had declined to 70% of its 1929 volume and to 35% of its value. American exports suffered disproportionately, declining to 52% of their 1929 volume and 32% of their value. With the drop in world trade, the United States could hope to regain its export markets only by reversing the trend toward higher tariffs abroad. It sought to accomplish this aim through the Reciprocal Trade Agreements Act (RTAA) of 1934. Yet the United States did not abandon protectionism in 1934, nor did

it perceive itself as acting in the long term interests of the international economy. Rather, American trade strategy remained narrow and explicitly self-seeking. The RTAA was seen as a complement to protection through which the United States could reopen foreign markets to its exports.

In 1930, confronting the imminent transformation of the IES from bilateral to unilateral supportership, the United States pursued a policy of pre-emptive protection as the theory summarized above would predict. By creating a higher relative level of protection at home, American policy approximated a SUP's first choice of protection at home and free trade abroad. In game-theoretic terms, the United States attempted through the Smoot-Hawley Act to obtain at least in the short run its first choice of  $P/FT$  by shifting the outcome from the south-east cells to the north-east cells of Figures 4a and 4b.

As world trade shrank under the pressure of sharply increased protection throughout the international economy, the trade policy interests of the United States changed from emphasizing protection at home to pursuing freer trade abroad. Formally stated, as other nations directly or indirectly retaliated against the Smoot-Hawley Act, the game-theoretic outcome returned to the far corner of the south-east cells of Figures 4a and 4b. From this position, any movement toward openness within the international economy would benefit a SUP. Given the limited influence of a single SUP, it is unlikely that it could induce or coerce other nations to move toward the north-east cells. Rather, it would be forced to bargain away its own tariffs, many of which would be superfluous, to induce other nations in a north-westerly direction. Again, as the resources available to a single SUP for influencing other nations are relatively modest, it would not be expected that a situation of universal free trade ( $FT/FT$ ) could be obtained. The final result would most likely lie somewhere between free trade and extreme protection. This was, indeed, the strategy adopted by the United States in the RTAA of 1934. By negotiating away limited amounts of its own protection, it sought to induce other nations to reduce their tariffs and other barriers to trade. While significant reductions occurred between 1934 and 1939, free trade was not contemplated. By the close of this era, tariff levels in the United States had been reduced only to the levels which obtained in 1922.

### **The IES and American Trade Strategy since 1965**

The present evolution of the IES is quite different from that experienced in the period just described. Where the hegemonic structure under Britain's leadership first evolved into bilateral supportership and then unilateral supportership, the current direction has been toward a proliferation of SUPs and multilateral supportership.

In the mid-1960s, the United States evolved from a HL into a SUP. From 15.3% in 1960, the United States declined to 14.4% of world trade in 1970. This percentage further declined to 13.4 in 1977 (*see* Table 2 and Figure 6). America's relative productivity also declined from 2.28 to 1.72 to 1.45 over the same period. In a series of rapid changes in the IES, the Federal Republic of Germany also evolved into a SUP in the mid-1960s as did France in the early to mid-1970s. The Federal Republic's share of world trade grew from 9.3 to 11.2% and its relative productivity increased from 0.95 to 1.06 between 1960 and 1970. These trends continued, reaching 13.5% and 1.15, respectively, in 1977. France's proportion of world trade was lower than that of the United States and the Federal Republic of Germany and grew slowly over the last two decades, rising from 5.7 in 1960 to 6.4% in 1970 and, finally, to 6.5% in 1977. On the other hand, France's relative productivity increased from 0.87 in 1960 to 0.96 in 1970,

and to 1.07 in 1977. Around 1975, as a result, a clear structure of multilateral supportership had emerged. If present trends in productivity growth continue, Japan is likely to join these nations as a SUP in the late 1980s or early 1990s.<sup>19</sup>

The present evolutionary trend within the international economy is not toward unilateral supportership as occurred during the decline of the *Pax Britannica*. Rather, the *Pax Americana* has evolved into multilateral supportership and is likely to remain so into the foreseeable future. It will be quite different from its historical predecessor. If the theory developed above is correct, the international economy—barring a major change in the level of uncertainty—will remain relatively open and stable despite the decline of American hegemony. The international economy, in other words, may resemble that which existed between 1913 and 1930, but we are unlikely to see a repetition of the economic collapse of the 1930s.

American trade strategy has been affected in three important ways by this change of structure from hegemonic leadership to multilateral supportership: first, pressures for protection generated by the nations' least competitive industries have increased; second, despite these pressures, the overall level of protection has risen only marginally; and third, the rules of the post-World War II trade regime have been both implicitly and explicitly altered often through multilateral negotiations so as to moderate domestic and foreign pressures from protection, even though this has required, in several cases, moving away from the liberal ideal of universal free trade.

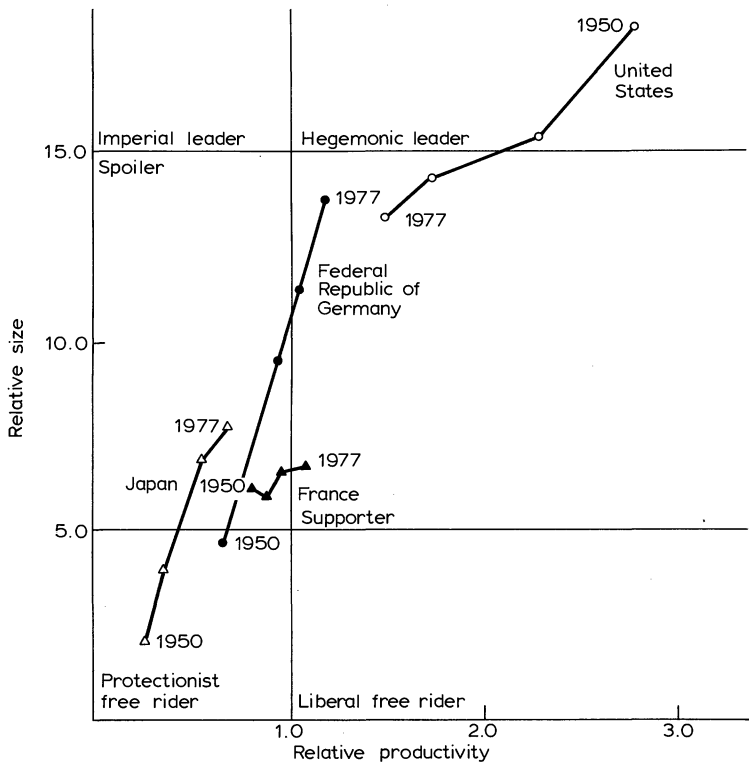


FIG. 6. The international economic structure 1950–1977 (excluding the United Kingdom).

TABLE 2. The International Economic Structure, 1950–1977.

Year	United States		Federal Republic of Germany		France		Japan		United Kingdom	
	PWT*	ROMH†	PWT	ROMH	PWT	ROMH	PWT	ROMH	PWT	ROMH
1950	18.4	2.77	4.5	0.66	5.9	0.80	1.7	0.25	13.1	1.15
1960	15.3	2.28	9.3	0.95	5.7	0.87	3.7	0.31	9.6	0.98
1970	14.4	1.72	11.2	1.06	6.4	0.96	6.7	0.55	7.2	0.86
1977	13.4	1.45	13.5	1.15	6.5	1.07	7.3	0.64	5.9	0.77

\* Proportion of World Trade.

† Relative National Output per Man-hour.

Sources: Relative Productivity data derived from A. Maddison, 'Long Run Dynamics of Productivity Growth,' *Banca Nazionale del Lavoro Quarterly Review*, 128 (March 1979), p.43. Proportion of World Trade Data for 1950 from Statistical Office of the United Nations, *Direction of International Trade*, Series T, 5, 8. For 1960, 1970 and 1977, Proportion of World Trade from United Nations, *Monthly Bulletin of Statistics*, selected years.

While protectionist pressures never entirely disappeared even at the height of America's economic hegemony, these pressures appear to have become stronger and the protectionists more vociferous over the last decade.<sup>20</sup> Significantly, in December 1982, an *Economist* headline queried 'Is Free Trade Dead?' The *National Journal* issued a similar headline one month later, asking 'The Protectionist Congress—Is This The Year That The Trade Barriers Go Up?' (Madison, 1983a: 18). Much of the recent concern over the future of the liberal international economy has centered on the highly protectionist Fair Practices in Automotive Products Act—better known as the domestic or local content bill—which has come to symbolize the growing protectionist pressures in Congress. This measure, passed by the House of Representatives in December 1982 by a majority of 215 to 188 but which died in a Senate Committee, would have required all automotive companies selling 500 000 or more cars annually in the United States to produce 90% of these vehicles in this country.<sup>21</sup> The percentage requirements decline for manufacturers selling fewer cars. Companies which sell less than 100 000 units annually in the United States would be exempted entirely. This bill resurfaced in Congress during the 1983 session where it again passed the House by a 219 to 199 margin. Other trade restricting issues pending before Congress include: reciprocity legislation which would encourage the President to retaliate against countries which do not maintain open markets for American exports, strengthening of the escape clause in the 1979 Trade Act, resistance to the continuation of the generalized system of preferences for less developed countries, and 'buy American' provisions in public works programs (Madison, 1983a: 18).

Despite these increased pressures for protection and the larger number of trade restrictive issues on the Congressional agenda, the level of protection in the United States has increased only marginally over the past decade. Through the success of the Kennedy and Tokyo Rounds of the General Agreement on Tariffs and Trade (GATT), the average tariff in the United States declined to 3% on all imports and 5% on dutiable imports in 1982.<sup>22</sup> Tariffs in the United States are currently at their lowest levels in history.

As tariffs have declined under the GATT, on the other hand, non-tariff barriers to trade (NTBs) have increased in importance. NTBs can be classified into two broad categories. First, indirect NTBs are laws or regulations which restrain trade but are not

primarily intended or designed for that purpose. They include environmental standards, health and safety regulations, and inspection procedures among a wide variety of such measures. Indirect NTBs have proliferated during the post-World War II era as governments have more frequently intervened in their domestic economies as a whole and production processes in particular. While they have increased in political saliency as tariffs have declined, indirect NTBs have most likely not increased significantly since America's transition from a hegemonic leader to supporter. Indeed, the Tokyo Round of the GATT addressed NTBs for the first time and adopted five codes on subsidies and countervailing duties, customs valuation, government procurement, technical barriers and standards, and import licensing procedures largely directed at standardizing or eliminating indirect NTBs (Krasner, 1979: 508).

Direct NTBs, or measures primarily designed to restrain imports, have increased in number and importance since the mid-1960s. Beginning with the Multi-fiber Agreement in 1962, the United States—and other nations as well—have increasingly resorted to voluntary export restraints (VERs), orderly marketing agreements (OMAs), and administrative regulations such as the Trigger Price Mechanism for steel in order to restrain imports. Between 1975 and 1981 alone, the United States imposed important quantitative restrictions on non-rubber footwear (OMA: Taiwan and South Korea), color televisions (OMA: Japan, Taiwan and South Korea), specialty steel (OMA: Japan; Quota: European Community, Sweden, Canada and others), textiles and apparel (bilateral agreements allowed under the Multi-fiber Agreement: Hong Kong, Japan, South Korea, Taiwan and others), automobiles (VER: Japan), and book printing and publishing (imports implicitly discouraged: all) (Morici and Megna, 1983: 15). In addition, during 1982, the major European steel producers agreed to limit carbon steel exports to the United States until 1985 (Cannon and Auerbach, 1982: A1,2 and 13).

In summary, the trend in American protection has been mixed. At the same time that it has been lowering duties within the GATT, the United States has been imposing bilateral protectionist measures, or direct NTBs, outside the framework of the GATT. On balance, the recent trend has probably been toward a small net increase in protection.

Both the increased pressures for protectionism and the only marginal substantive increases can be explained by the transformation of the United States from a hegemonic leader into a supporter and the constraints exerted upon American trade policy by the structure of multilateral supportership in which the nation is imbedded. As would be expected, when the United States evolved into a supporter it developed stronger interests in protecting its least competitive industries. Indeed, it has been in precisely those industries (textiles and apparel, steel, consumer electronics, and recently, automobiles) in which the advocates of protectionism have been most evident. In addition, as America's relative productivity has declined these pressures have grown and spread to a greater number of industries.

As in the period 1913–1930, however, the actual level of protection in the United States is constrained by the fear of retaliation. These constraints are clearly evident in the recent debate over the domestic content bill. Proponents of the measure de-emphasize its protective aspects and attempt to portray the bill as a means of achieving 'equity' in international trade and opening foreign markets to American exports. John D. Dingell (D-Mich.), the chief sponsor of the bill, argued during the House debate that its purpose was to send a message to the Japanese which 'says we are going to have our people treated fairly' (Madison: 1983a: 19). After noting that 31

countries including Japan possess domestic content requirements for automobiles, Representative Richard L. Ottinger (D-NY), a second major advocate, stated that the 'U.S. has been a sucker in this trade business and has generously given away free access' (Pastor, 1983:33). On the other hand, opponents warn of dire consequences for American exports if the measure is enacted into law in addition to questioning the domestic utility of protectionism. Drawing upon the specter of Smoot-Hawley, Special Trade Representative William Brock warned that if the domestic content bill was passed, "'We [would] begin walking down that path"' toward a deterioration of world trade' (Madison, 1983a:20). Critics also cite a Congressional Budget Office study which concluded that if other nations were to retaliate, there would be a net gain of only 70 000 auto jobs and a net loss of over 220 000 non-auto jobs by 1990 (cited in Pastor, 1983:33). Both proponents and opponents are sensitive to America's continued desire to export and aware of the potentially destabilizing consequences of protection in the United States. By depicting the issue as one of equity, the proponents seek to undermine the basis for retaliation by foreigners, but in any event see it as a risk worth taking. Opponents fear the effects of retaliation more. Despite their differences, both views reflect the concern over retaliation and the current constraints on American trade policy.

As a result of these constraints, two new departures have become evident in American trade policy which moderate pressures for protectionism. First, direct NTBs have been increasingly used to satisfy selected demands for even greater protection. The Reagan Administration, for instance, sought the renewal of the VER on Japanese autos despite its free market ideology in order, at least in part, to undermine support for the domestic content bill (Togo, 1983:A22; Madison, 1983a:18). While eroding the liberal ideal of universal free trade to a limited extent, direct NTBs are less overtly protectionist and less threatening to a liberal international economic regime than high tariffs or unilaterally imposed quotas. Both OMAs and VERs are established through diplomatic negotiations among the affected parties. While the importing country is often in an advantageous bargaining position because of its ultimate ability to act unilaterally, the pretext of negotiations does maintain a facade of voluntarism for the exporting nation. OMAs, modeled after the original Multi-fiber Agreement, are instruments of managed trade which either allow foreign countries a specified share of an expanding market or a particular rate of growth from a set import base. Even though they often yield some measure of protection to the domestic industry, OMAs usually allow for continued import growth. VERs, on the other hand, act like quotas and limit imports to a predefined level. More favorable to the exporting country than an equivalent tariff, however, VERs (like quotas) allow the exporter to reap the scarcity rent created by higher prices. Because of these characteristics, OMAs and VERs are more politically palatable to the exporting country than tariffs and quotas, even though they contravene the intent of a liberal international economic regime. In addition, by settling issues outside of the formal GATT framework, they allow the Geneva based organization to continue functioning as a trade liberalizing mechanism, rather than politicizing it by institutionalizing the cleavage between protectionists and free traders. They also avoid the need for a general tariff revision in the United States, concentrate activity in the Executive branch, which is less subject to protectionist pressures, and allow the administration to divide potential protectionist coalitions by dealing with import competition on a sector-by-sector basis.

The second departure in American trade policy is that, in a so far unsuccessful but no less significant attempt, the major trading nations have also sought to moderate protectionist pressures by coordinating their macroeconomic policies. In the locomotive



strategy adopted at the Bonn Economic Summit in 1978 and the convoy approach agreed upon the following year, the advanced industrialized nations linked their individual macroeconomic policies, so as to achieve mutual and balanced expansion of economic growth.<sup>23</sup> While the purposes were broader and despite the failure of these efforts, they were significant as an attempt to 'short-circuit' protectionism by reducing balance of trade deficits created by divergent growth rates.

We see, then, that in spite of the greater pressures for protection within the United States, barriers to trade have not increased significantly at least in part because of the constraints exerted by the structure of multilateral supportership. These pressures, moreover, have been moderated through the selective use of NTBs and attempts at macroeconomic policy coordination.

### Conclusion: Lessons of the Past

It should now be apparent that the 'British' or '1930' analogy is inappropriate as a guide to current changes in the international political economy. The evolutionary trend within the IES is not toward *unilateral* supportership, as in the earlier period, but toward *multilateral* supportership. American trade policy reflects this evolution. Even though pressures for protectionism have grown since the late 1960s and early 1970s, the actual level of protection within the United States has not risen appreciably. These pressures will continue to be restrained by the fear of retaliation in the future.

In light of past American policies and the structure of multilateral supportership in which the United States is currently imbedded, what is the likely future of the international economy, and what can American policymakers do to shape this future to align with the nation's perceived interests? The structure of multilateral supportership is likely to endure over the next several decades. There is little the United States can do to reassert its position of hegemonic leadership. Any industrial vitalization program which promises to strengthen America's competitive position is likely to be met by the efforts of the other supporters, whose own positions would be otherwise weakened.<sup>24</sup> The United States must learn to live, in short, as one trading nation among equals in a world in which the constant threat of a deteriorating trade regime exists.

This is not necessarily a cause for pessimism, however. As in the 1920s, the current level of uncertainty within the international economy has an important effect upon the trade policies of nations in a structure of bi- or multi-lateral supportership. Despite the oil shocks of the 1970s, the present international economy remains one of only relatively moderate uncertainty. While the patterns of trade and finance have been altered, the disruptions have not been on as large a scale as those which occurred during World War I. Indeed, the success of the advanced industrialized nations in regulating this disruption may demonstrate the potential of a structure of multilateral supportership. At least in the near term, nations are likely to continue basing their expectations of the future on the experiences of the recent past. This is a hopeful sign for the liberal international economy. It is this level of uncertainty, on the other hand, which policymakers can most directly affect. Most importantly, given the fragility of universal free trade under a structure of multilateral supportership, policymakers should resist any actions which threaten or imply that the United States may defect from its present commitment to free trade. In addition, a renewed emphasis on growth might mitigate some non-structurally induced uncertainty. As seen in the early 1920s, actual or feared protectionism in one supporter will stimulate similar action by others in return. This is, indeed, the lesson of the 1920s—and the danger for the 1980s.

### Notes

1. A strong international regime serves two other functions within the international economy. First, it facilitates the market intervention necessary to maintain stability. As Robert Keohane (1982: 338) has recently noted, regimes facilitate agreements between countries, improve the quantity and quality of information available to nations, and reduce transactions costs. Second, a strong regime constrains national behavior by its rules and norms and creates expectations about future behavior, both of which contribute to international stability. In this context, it is important to note that a liberal regime reinforces the equilibrating forces within the international market. By proscribing 'beggar-thy-neighbor' policies, which force the costs of adjustment to instability onto other nations, a liberal regime disperses the costs of instability across many nations helping prevent the concentration of destabilizing forces which can shatter an open international economy.
2. For an issue area based definition of relative size, see Keohane (1980).
3. Nations cannot be too confident, however, as hegemony does not axiomatically lead to an open international economy (see below). Thus, even under hegemony, a low level of structural uncertainty exists.
4. Gilpin (1975: 85) quotes Kuznets' wry comment: 'The greater power of the developed nations imposed upon the reluctant partners the opportunities of international trade and division of labor.'
5. Gilpin's argument has recently been supported by Zysman and Tyson (1983: 23-32) and Reich (1983). These authors dismiss the static conception of comparative advantage common to mainstream economics and argue that absolute advantage may be more fundamental to understanding international trade and national trade policies. In particular, Zysman and Tyson write:

[I]t is . . . necessary to distinguish between the notions of comparative advantage and competitive advantage. Comparative advantage refers to the relative export strength of a particular sector compared to other sectors in the same nation and is usually measured after adjusting for market-distorting government policies. For the purpose of discussion, competitive advantage refers to the relative export strength of the firms of one country compared to the firms of other countries selling in the same section in international markets. According to this interpretation, the competitive advantage of the firms of a particular country in a particular sector may be the result of that country's absolute advantage in that sector. In contrast to the usual notion of absolute advantage, however, the notion of competitive advantage allows for the presence of economic policies that help or hinder the international performance of different firms. Thus the competitive advantage of the firms of a particular country in a particular market may be the result either of real absolute advantage or of policy-induced and hence distorted absolute advantage. Indeed, policy-induced advantage can become real advantage over time (p.28).

Just as relative productivity determines the relative gains from trade in the backwash and spread processes, it also determines a nation's absolute advantage—which underlines Zysman and Tyson's conception of 'comparative' advantage.

6. See also Galtung's (1971) conception of 'spin-offs' from trade.
7. For an overview and empirical test of this debate see Chase-Dunn (1975) and Kaufman, Chernotsky and Geller (1975).
8. Gilpin, (1975: 57) also argues that in the long run, the spread process eventually dominates the backwash effect. This is logically inconsistent with an argument which traces free trade interests to the relative productivity of states, as nations of low productivity would then gain disproportionately from trade in the long run. This inconsistency may stem from an inadequate recognition of the cumulative nature of the differential gains from trade. It is important to note that Gilpin's examples of 'growth nodes,' the nations which principally benefit from the spread process, are also those nations which insulate themselves from the international economy (e.g., the United States and Germany in the 19th century), thereby violating the free functioning of the backwash and spread processes.
9. See Zysman and Tyson (1983: 23-32) for a discussion of the role of the state in this process of restructuring.
10. For a discussion of definitions and assumptions about the international system, see Waltz (1979).
11. Classical economics focuses almost exclusively on the absolute gains from trade. To the extent to which other factors are considered, this approach would most likely assume that nations, in descending order, seek to maximize their (a) absolute gains from trade, (b) economic stability, and (c) relative gains from trade.
12. The empirical demarcations between categories are guided by the theory of hegemonic stability but, in the end, remain somewhat tentative. The division between small and middle sized nations is placed at 5.0% of world trade. Over the last 100 years, this would place no more than five nations in the middle and large categories at any point in time. Nearly all of the nations traditionally regarded as major actors within the

- international system have been above this 5.0 level. Raising the cut off between small and middle sized countries by 1 or 2% would not dramatically affect the composition of the category. On the other hand, reducing this cut off point by 1 or 2% would greatly expand the number of nations within the middle sized category. For this category to be meaningful, it should be limited to those nations which do or can influence the international economy or the policies of others in some significant way. A division of 15.0% of world trade between middle and large sized countries places the United Kingdom from the early 19th century until 1912 and the United States from World War II until the mid-1960s in the large category. This is largely congruent with Gilpin and Krasner and was chosen for that reason. Most countries have been well below the 15.0% level. The precise division between the large and middle-sized categories is important in this study only for dating the transition of the United Kingdom from the former to the latter level. Given the rapid rate of decline in the British position before World War I, shifting the cut off point slightly in either direction would not have a major impact upon the analysis. The relative productivity of each country is calculated by dividing that country's absolute level of productivity by the average absolute level of productivity in the other middle and large sized nations. The 1.0 level, the demarcation between high and low relative productivity, indicates that productivity in the nation is exactly equal to the average of the others. Levels below 1.0 indicate that the country is of less than average productivity, while levels greater than 1.0 indicate that the nation is of higher than average productivity. This indicator and the 1.0 division between nations of high and low productivity, it is believed, accurately reflect the concept underlying the second theoretical proposition discussed above.
13. Chase-Dunn (1982) argues that the Netherlands was a hegemonic power in the 17th century. Insufficient data exist to classify the Netherlands within the dimensions of the IES specified here. For this reason, the examples and analysis are confined to the post-industrial revolution period.
  14. Gilpin (1981:39-49) makes a similar distinction between types of international change.
  15. Britain's role as the 'balancer' of the 19th century European state system and Napoleon III's need for British support for his Italian policy, for example, may have induced France, at least in part, to adopt a free trade policy in the Cobden-Chevalier Treaty of 1860 (see Iliasu, 1971).
  16. For a discussion of the concept of regulation see Rosecrance (1977:220-227).
  17. Similarly, Wagner (1983:330-334) has argued that in a continuous prisoner's dilemma, in which players choose one after the other, with full knowledge of each other's choices and where neither can count on having the last choice (circumstances which approximate the trade policy issue area), conditional cooperation (cooperate only so long as the other player cooperates) will be the optimizing strategy.
  18. Discussed more fully in Lake (1983 and 1984).
  19. Between 1960 and 1973, Japan's output per man-hour grew at an average annual rate of 9.9%, compared to 2.8% in the United States, 5.4% in the Federal Republic of Germany, and 5.9% in France. Between 1973 and 1979, Japan grew at a slower rate of 3.8% compared to 0.1% for the United States, 5.0% for the Federal Republic, and 4.8% for France (Magaziner and Reich, 1982:36).
  20. See Bergsten and Cline (1982:13) and Pastor (1983).
  21. Automobile production in Canada, for the purposes of this act, is considered to be within the United States.
  22. *Statistical Abstract of the United States* (1982-83:844). These low duties mask a variety of higher rates, see Weidenbaum *et al.*, (1983:29).
  23. For a concise history of the major developments at the various summits, see Madison (1983b:1173). For problems of economic coordination in general, see Morse and Wallin (1979:1-23).
  24. This not a rationale for not undertaking such a revitalization program, however. If it is assumed that other nations will pursue industrial advance to the best of their abilities, the United States must do likewise to stay in the same position within the IES. In short, the United States may have to run as fast as possible in the industrial adjustment/strategy area just to stand still.

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