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On Milward's *Reconstruction of Western Europe*

Marcello de Cecco

As the huge armies of America and the Soviet Union met amongst the endless rubble of what had been Europe's largest economy and over the corpses of a government which had mocked the long history of European civilization and culture, no matter how heroic the sentiments expressed scarcely anyone could have believed that the small, shattered nations of western Europe were on the brink of the most prosperous, peaceful and one of the most creditable periods in their history. European capitalism, which many of its staunchest adherents had feared in the 1930s to be in its death throes, was not on the point of expiry but on the brink of more than two decades of remarkable vigour and success [1].

Indeed very few people had believed such an auspicious future lay at the doorstep of the shattered economies of Western Europe. A visionary like James Burnham had foreseen with great clarity, as early as 1941, a post-war world characterized by the demise of the British Empire, a Common Market including Britain, the emergence of three main economic areas, Europe, the U.S. and the Far East. There had also been the well known Nazi plans for the European Neue Ordnung. But the blueprints for the post-war world drawn in Britain and the United States failed almost invariably to include Europe. They foresaw the survival of the small European countries but, in the era of the Morgenthau Plan, a solution which would see once again Europe united around its natural pivot, a strong Germany, seemed utterly unthinkable.

American plans for the post-war world were much more worried about the establishment of free trade and a multilateral payments' system than about the reconstruction of Europe. For the immediate post-war

[1] A. S. Milward: *The Reconstruction of Western Europe, 1945-51*, London, Methuen, 1984, p. XV.

period, the Americans wanted to see the demolition of the Sterling area as a trade and currency bloc. They were also interested in an international monetary system which would allow U.S. banking and financial institutions to replace their British equivalent as the centre of international finance.

It is hard to recall those days, now that Britain is reduced to an economic size very near that of Italy. In the early 1940s, however, things were quite different. Before the War, the U.S. sent to the Sterling Area 27% of its exports, and the countries within the Sterling Area were the only ones which could guarantee a steady and sizable demand for manufactured goods. They represented the only reliable market for a United States still smarting under the memory of the dreadful Depression years and where public opinion expected the bad years to return, after the exhaustion of the war boom.

Early American post-war plans were thus aimed at preventing the Sterling Area from becoming a self-sufficient, protectionist trading and financial bloc. American worries were amply justified by news coming from Britain, where several highly influential voices were preaching a gospel of Planning at imperial level, a "benevolent" imitation of Hitler's European trading system.

While applying themselves with their British Ally to defeat the Axis, the Americans took the greatest pains in making sure that the blueprint of a self-sufficient Sterling Area would not leave the drawing board. They managed very successfully to replace it with their own alternative, based on multilateralism at both trade and financial levels.

To ensure the success of their plans, the Americans did not spare any effort, and pulled all levers available to them. The British reacted with great vehemence, but they worked under the considerable handicap of having to rely almost exclusively on the Americans to finance the war. After British gold and foreign exchange reserves were exhausted, the Americans came forth with the Lend Lease Agreement, but the Atlantic Charter, which gave birth to it, also contained a firm declaration by the British that they would, after the War, do all they could to ensure the return to a multilateral system of free trade and payments.

Early American Plans for an International Monetary System, to be launched at the end of hostilities, had shown great enthusiasm for dirigisme and étatisme. Harry Dexter White had baldly asserted that short-term capital movements, which had plagued the inter-war period and impeded the efficiency of national anti-cyclical policies, had to be controlled both by the countries which lost capital and by those where capital went.

White's Plan had been, on this essential subject, even stricter than Keynes' own. But, between the White Plan and the final Bretton Woods Charter, the American position evolved remarkably in the direction of unfettered laissez-faire in international relations. The influence of J. H. Williams, an archetypal realist, began to be felt more and more strongly in American government circles. He had an idea of the post-war world which was radically different from those of Keynes and White. He believed that, in a world dominated by the U.S. as the post-war one would be, the international monetary system would inevitably take its movements from the domestic monetary policy of the core country. He thought the post-war problem would be inflation, rather than the deflation feared by New Dealers and Keynesians. And inflation would have to be fought by a tough monetary stance in the U.S., coupled with a compatible policy adopted by the other core country, Great Britain.

The latter's role would be, in Williams' opinion, critical to the success of the new international monetary system he envisaged. Duly, if the monetary relations between the two centre-countries were reestablished on a viable equilibrium, the new international monetary system would succeed. Williams dismissed the possibility that an equilibrium dollar-sterling parity could be established by up-valuing the dollar or controlling incoming capital flows. He suggested, instead, that sterling be devalued to a more realistic level vis-à-vis the dollar and be brought back to effective convertibility. Looking at the actual cadence of events, we may conclude that Williams' advice was taken very seriously by the American Government. The promise of an early return of Sterling to convertibility at a realistic value was extracted from the British, and the Americans kept up their pressure until it was realised in 1947.

In these early plans for the post-war world the place of Europe is difficult to find, as they seemed to revolve almost exclusively on the choice between laisser-faire and dirigisme in the U.S. and Britain, and on the relative roles of the two victors in the post-war world economy.

The forces which, in the United States, called for an early liberalization of the international economic and monetary system, were the same as those which really wanted deregulation and liberalization in the U.S. But the degree of control which had prevailed there in the New Deal was hard to lighten or rescind. The partisans of laissez-faire decided that liberalization could be more easily reintroduced into the U.S. from the outside, as a need to conform to the rules of the new international economic order.

To the large New York banks, for instance, the policy of cheap money which had been initiated to finance the War effort was highly injurious. They had traditionally relied on a flow of deposits from regional U.S. banks, which they used to acquire assets on a much higher level than that granted by their own deposit base. With cheap money those inter-bank flows had dried up, as regional banks could invest their surplus deposits in safe governments bonds.

It was thus essential to terminate the cheap money policy as soon as this could be done without sacrificing the war effort.

The large New York banks also saw clearly written in their destiny that they were meant to replace the City of London as the world's premier financial centre. The dirigiste approach taken by White and Keynes with respect to short-term capital flows threatened to put an end to what they considered their legitimate aspiration to world financial supremacy.

Hence the transformation of the Bretton Woods Agreements into the laissez-faire version which they finally took. A far cry from the White and Keynes Plans, the final Agreement had a closer resemblance to the Williams Key Currencies Plan.

This world of Anglo-American agreements and disagreements, which seems to have had little worry about the fate of Europe, was radically transformed by the new realities represented by the Cold War and the crucial role which Europe was assigned to play in it.

As it dawned on both American and British statesmen that, while they were busy planning the future of the world, the Soviet Union had conquered Central and Eastern Europe by its military victories over Germany, and only a string of defeated and impoverished European countries stood between the Red Army and the Atlantic Ocean, a complete change of strategy occurred in Washington. While the destiny of the European countries had hitherto been of little worry to the Americans, and all they had really been interested in had been to convince or compel European countries to adhere to the Bretton Woods' blueprint for world trade and payments, as soon as the new reality of a victorious Soviet Union had sunk in, it occurred to the U.S. Government that, if they did not do some creative thinking rather fast, and act accordingly, Western and Southern Europe would soon be won to Communism.

That people became communists because of economic deprivation, unemployment and hunger had been a firmly held belief in America as well as in Britain. It had been the background to the victory of Keynesian and New Deal reformism. Now almost all Western and Southern Europe was reduced to conditions of utter economic deprivation, unemployment and hunger. And the working of the Bretton Woods system threatened to add to these evils, rather than take them away.

That these countries would be ready to fall to Communism was thus inevitable. The American Government convinced itself of the truth of the equation: unemployment + hunger = Communism. It determined very soon to act to prevent the realization of the menace. How to succeed in the task? It was obviously necessary that unemployment and hunger be swept away from Europe. This could only be done by a process of economic growth. The U.S. Government would do all it could to help induce growth in the European economies. But why had the European economies shown so little vocation for growth in the pre-war years? Because — the U.S. Government thought — European countries had destroyed, after the First World War, the network on intra-European free trade which had, before 1914, proved to be such a powerful engine of growth. They had closed themselves into a vicious circle of deflation leading to protection, leading to greater deflation.

To restart growth in Europe, the whole continent, west and south of the Yalta borders, had to unite into one economic area. This would unleash the power of economies of scale, bolster productivity, and initiate a virtuous circle of growth leading to employment, leading to more growth. U.S. experience lent itself as a powerful example to point to Europeans. The huge market represented by the United States had brought to it the prosperity that a United Europe could also achieve.

Under the flag of a United Europe one could also enclose the largest country of Europe, Germany. Without its economic and political rebirth the Americans thought no United Europe could survive. A strong Germany as the centre of a strong Europe thus became the new American strategy. The U.S. Government, once resolved, set out with great enthusiasm to bring this about with the help of the European governments.

This help had to be extorted, since only very seldom was it offered voluntarily. It is the main thesis of Alan Milward's book, and its main claim to originality, that the United States did not succeed in realising its European strategy. The enforcement of the Bretton Woods blueprint had meant for European countries, in the years between 1945 and 1947, a worsening of their early post-war problems. Most of these governments had post-war economic and political strategies — Milward successfully contends — that had little or nothing to do with a United Europe. Most countries, with the exception of Belgium and Italy, had adopted extensive economic planning as a way of life, not as a wartime emergency. They were reacting against the laissez-faire policies which had brought about the deflation and unemployment of the 1930s. European governments were determined not to see the atmosphere of the thirties reappear, and firmly intended to manage their own national economies in the most extensive fashion. France, in particular, was reacting to the shock of the German Blitzkrieg, with its demonstration of superior industrial power, by devising a very extensive Plan of National Renewal based on the reconstruction and reinforcement of the capital goods industry. The French government still accepted the Morgenthau Plan as its view of the future of Germany. It also believed very firmly in the need to keep control over former German coal production in order to boost its own steel industry.

Great Britain was completely immersed in its problems with the Sterling Area and the future of the Empire. It had to fend off the unwanted attempts by the Americans to dismantle both. In the new American strategy, the need to make Britain the engine of European unification superimposed itself on the previous demands, to run down the sterling balances and to return to sterling convertibility.

If we consider the new American strategy, however, we see that it had no great contradictions with the original American post-war plans. A greater role for European countries, as a United Europe, did not contradict a view of the world where free trade and currency convertibility were the main elements. A United Europe, with Britain in it, would reduce the Imperial temptations of the British. It would be a strong economic unit, more able to withstand competition with the U.S., thus less inclined to take refuge in isolationism, self-sufficiency and protectionism.

But the new American blueprint for a united Europe did go against the policies of most European countries. They had, very early after the end of the war, started their own national experiments to achieve prosperity. Milward contends that, between 1945 and 1947, they had been very successful in lifting themselves by their own bootstraps. The European economies were already well on their way to resurrection without any resort to grandiose plans to unite Europe, when the 1947 crisis errupted.

According to prevailing historical accounts of the post-war period, that crisis, or the American perception of it, directly induced the U.S. Government to introduce the Marshall Plan. Milward takes great pains to show how that crisis, far from being the deepest manifestation of destitution and despair it was painted to be in America was, in fact, a balance of payments crisis induced by the too rapid growth of the European economies.

It is impossible not to agree with the evidence Milward assembles to prove his thesis. On a model completely different from the American blueprint for the post-war world, the European economies had managed to lift themselves up at a remarkable speed. By doing so they had all encountered balance of payments difficulties with the U.S., enhanced by the sudden removal of price controls in that country. Those difficulties were induced by the disappearance of German industry as a supplier of capital goods and by the raw material intensity of their reconstruction effort.

Unlike Milward, I am convinced that the U.S. Government was aware of the nature of the European payments' crisis. But they also knew that European countries were going through a political crisis and they believed that throttling the boom would have meant a victory of the communists and their allies in Continental Europe. At the same time, they knew it would have been difficult to convince Congress of the need to help the European countries if what American Congressmen (and their constituents) considered as presents were known to go to people on their way to prosperity. It was much simpler to transform the true political crisis taking place in European countries into an economic crisis. The horrors and destruction of war were so near anyway, that the economic crisis could have looked credible to the much more prosperous Americans, who had been spared much misery.

Much more than Milward, I am therefore inclined to credit the American Government with a Machiavellian attitude towards its own citizens.

It was, anyway, only a question of timing. Had Marshall Aid not been offered, the payments crisis induced by the fast European recovery would have ended up in deflation and unemployment, and, according to the model which the U.S. Government believed in, the inevitable fall of Continental Europe to Communism. An equally bad alternative for the Americans would have been the adoption, by European countries, of managed trade and payments on a Continental level. A return to the dreaded European trading bloc. Alan Milward's belief in the honesty of the U.S. Government, when it introduced Marshall Aid is however understandable because it is based on his close study of the behaviour of the U.S. intellectuals and businesmen whom the U.S. Government put in charge of the administration of Marshall Aid. If we had only that team of administrators to represent the opinions of the U.S. Government, we would have to agree with Milward.

From top to bottom, they were a team of convinced Keynesians. Ironically enough, there was a lot in common between them and the European bureaucrats they had to deal with. But the Keynesianism of the Europeans was often more practical than theoretical, in the sense that they practised it without knowing it. And, more important, they did not have in mind the united, supranational, Europe the Americans had. They used Keynesian (or dirigiste, or mercantilist) methods to maximise economic growth in their respective countries within the normal nationalist frame of reference.

Compared to equally, or more, influential, American policy makers, the Administrators of the Marshall Plan were markedly more interventionist. They were convinced planners, and J. H. Williams' eyebrows would have been raised quite often had he read their position papers.

The history of post-war Europe, in fact, is the history of how this team of American planners, and their plans, were rendered more and more ineffective by the joint efforts of both European and American policy makers. Milward concentrates on the first half of the joint effort. This is perhaps wise, because the second half of the story has been told elsewhere. The original point of his study is to show how the European efforts to nullify the Marshall Planners' scheme came to coincide with what we have been used to calling "the construction of Europe".

As a work of demystification and of realistic history-writing, Milward's book cannot be praised too highly. As American public opinion was made to believe that, by the Marshall Plan, America came to the rescue of a starving, debilitated and stagnant Europe; the European public has been told and has come to believe, that the European Community was the crowning of a European supranational dream. Milward's thesis, which he convincingly demonstrates through 600 pages of closely argued and well documented prose, is that the European supranational dream was indeed there, but that it was the Marshall Planners who dreamt it, and that the real European Community as we know emerged from the unrelenting efforts of European governments to achieve integration in their own way, by negating the validity of the Marshall Planners' scheme, and by gradually replacing it (fighting from a position of weakness against their opponents, who held the strings to the Marshall Plan's purse) with measures, agreements and policies which were a realistic, if often algebraic, sum of traditional national aims.

Milward takes us through the fascinating phases of this process of retreat from an unacceptable supranational dream into a realistic process of integration. We see the OEEC, started by American will as a political, supranational Agency to administer Marshall Aid on a European scale, gradually become less and less a political entity, where national requests for aid are processed and granted on a more and more national basis. We are also shown, in great detail, how radically different from the original American-inspired Bretton Woods Plans the European Payments Union turned out to be.

Through Milward's precise documentation and arguments, we watch the rise of European integration as an oldfashioned pact among nations, endlessly negotiated by national bureaucracies and politicians, with almost no place for automatic mechanisms, for doctrinaire solutions, for traditional economic theory. A supranational solution is finally achieved, paradoxically, with the greatest deference to national sovereignty after, and perhaps because of, the failure of a declaredly supranational American grand scheme steeped in economic theory and imbued with abdications of national sovereignty.

As I have said, the thesis is very original, and the demonstration highly convincing. After Milward has completed his job, we are left thinking that things did go the way he tells us they did.

Still, he underplays, perhaps for the sake of consistency, the impact U.S. policy in the end had on the direction and shape of European affairs in those eventful years. It is undeniable that the Marshall Plan was motivated by strategic considerations, to contain a perceived Soviet threat in Western and Southern Europe. The new scenario painted by the U.S. gave a major role to a reconstructed Germany. It made it again the economic centre of Europe. It goes to French policy-makers' credit that, with great realism, they shifted their original policy stance of 180 degrees and gave life to the great Franco-German reconciliation. But this was done after it had been shown that it was the will of the Americans to see Germany once again as the heart of Europe.

It is also undeniable that, by the U.S. new strategic stance, Britain was left without any policy options. It had been deprived of the Sterling Area option when the U.S. had forced it to prematurely declare Sterling convertible in 1947. The greatest part of the Anglo-American loan had been burnt in trying to defend the parity in those six weeks that convertibility lasted. The Americans had subsequently tried to turn Britain into the promoter of European integration. But they could not expect it to embrace this option, as its economy was competitive with that of Germany, which was to be reconstructed anyway, while that of France was largely complementary to it, thus making the Franco-German alliance economically viable.

With the emasculation of the Sterling Area and the impossibility of finding a role in Europe, Britain was definitely finished as a great power by the Americans. Not unlike many of his countrymen, Alan Milward does not seem to be aware of this historical truth.

American action, however, did not stop at making the post-war world an impossible place for Britain. Again acting on the weakest ring in the chain, the U.S., by themselves and through the judicious use of their "specialised agency", as Peter Kenen later called the International Monetary Fund, insisted on Sterling Devaluation in 1949, and by it they obtained a Devaluation of all European currencies.

Around 1949, it had been realised that, by the skilled use of Marshall Aid, European countries were managing to re-equip their economies with capital goods and raw materials, but were not generating enough exports. The pattern of trade the European countries were developing looked far from satisfactory to the Americans. It did not show any permanent trend towards an enhanced integration between the European economies and that of the United States. Europe looked again as having the intention of relapsing, as soon as possible, and with the help of U.S. aid, into a self-contained bloc. Or at most into a trading area alternative to the United States. The only way of remedying that situation was to transform the European economies once again into export economies by a powerful re-alignment of European exchange rates. This was the logic of the Bretton Woods system, which Alan Milward perhaps too lightheartedly dismisses as having had no impact on the post-war economic history of Europe.

By keeping up the pressure in favour of devaluation on the Europeans, who did not have much enthusiasm, the Americans induced a speculative flight of money from the European currencies, and especially from Britain. It was useful to them that the Bretton Woods Agreements had been so lenient on the treatment of short-term capital movements, which both White and Keynes, but also continental Central Bankers and economists, thought had been responsible for the inter-war currency chaos.

With a 30% devaluation of Sterling, and similar devaluations for continental currencies, a powerful incentive was created to export to the United States. The European economies were once again transformed into export economies, and a general under-valuation of currencies vis-à-vis the Dollar was instituted, which was to last until 1971. Strong export lobbies came again to be formed in Europe, which could exert the pressure required to fend off all attempts to create a European economy not strongly linked by trade with the United States. At the same time, the over-valuation of the Dollar induced American investment in Europe, thus making the links between the two shores of the Atlantic stronger.

The total outcome was a world which satisfied, for a long period, both Europeans and Americans. It also sowed the seeds of its own long-run disequilibrium. But the main U.S. strategic objectives were assured. Europeans, rather than being tied by just loyalty, a very volatile feeling, had much more solid economic reasons to stick by the U.S., and refrain from dangerous dreams of neutrality.

Alan Milward does not seem to recognise this as a triumph of Bretton Woods' larger aims. This was the real scope of Bretton Woods. Up until 1971, it was achieved. The Bretton Woods system would have lived even longer, had the Agreements not been scrapped by the U.S. Government for what now appear clearly as reasons of domestic electoral expediency. Over-valuation of the currency which wants to be at the core of the international system seems to be a necessary requirement. Witness the events of the last five years. *Pace* Alan Milward, Bretton Woods is still very much with us. Only it must be seen for what it was and not for what it said it would be.

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