

European University Institute  
Firenze  
Department of History and Civilization

HUBERT ZIMMERMANN

DOLLARS, POUNDS, AND TRANSATLANTIC SECURITY:  
CONVENTIONAL TROOPS AND MONETARY POLICY IN  
GERMANY'S RELATIONS  
TO THE UNITED STATES AND THE UNITED KINGDOM  
1955-1967

Thesis submitted for assessment with a view  
to obtaining the degree of doctor of the  
European University Institute

Florence, January 1997

Examining Jury:

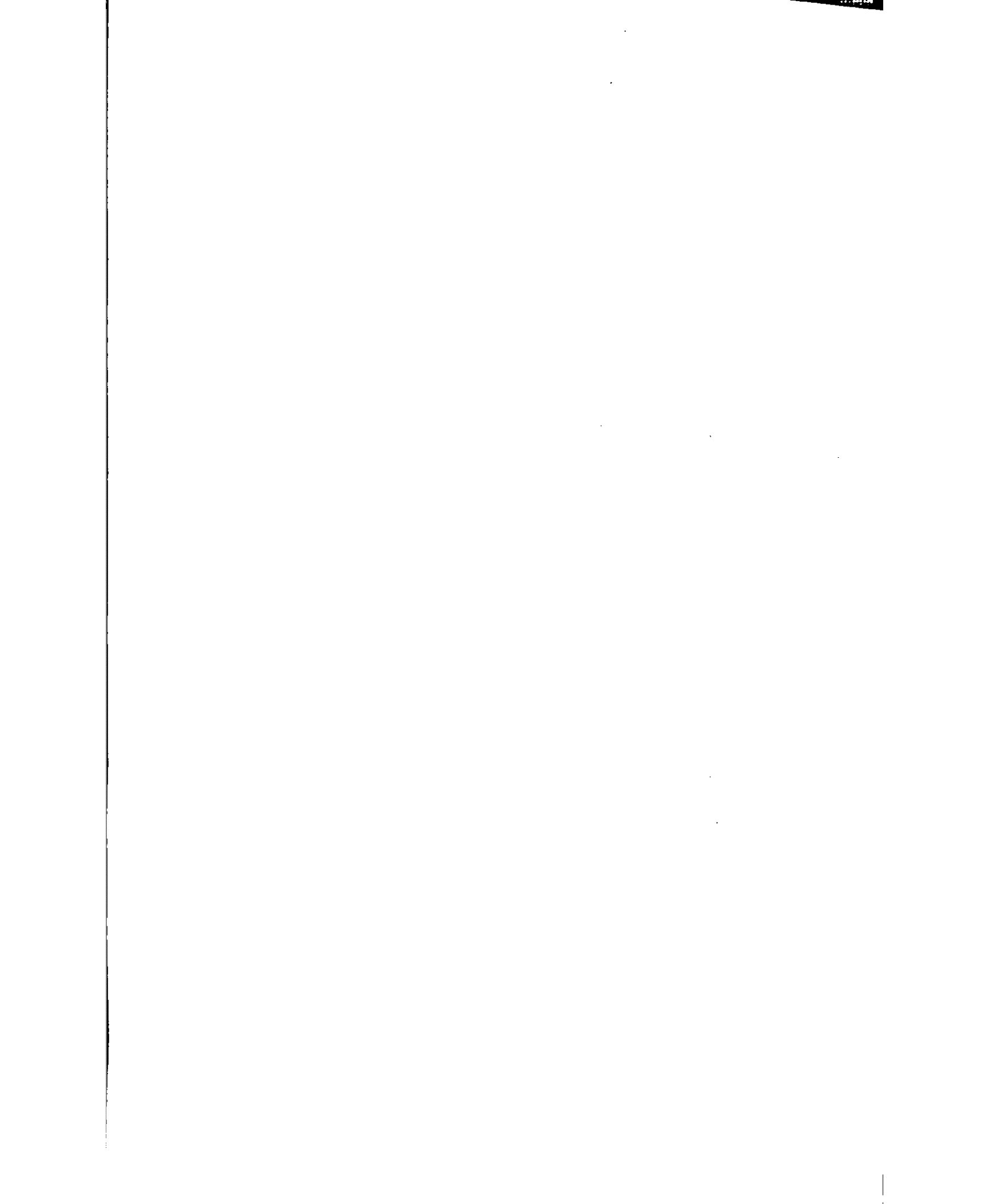
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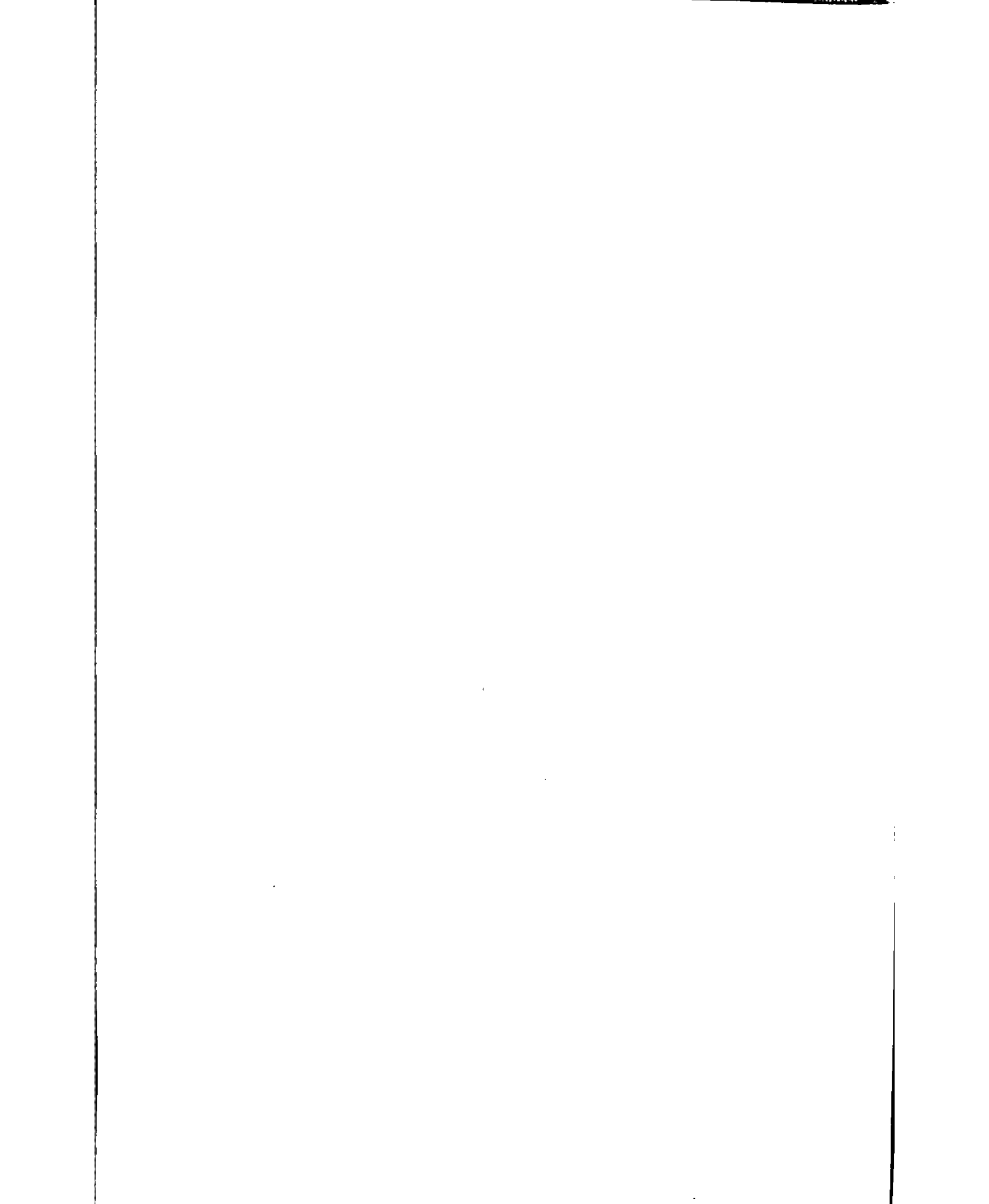
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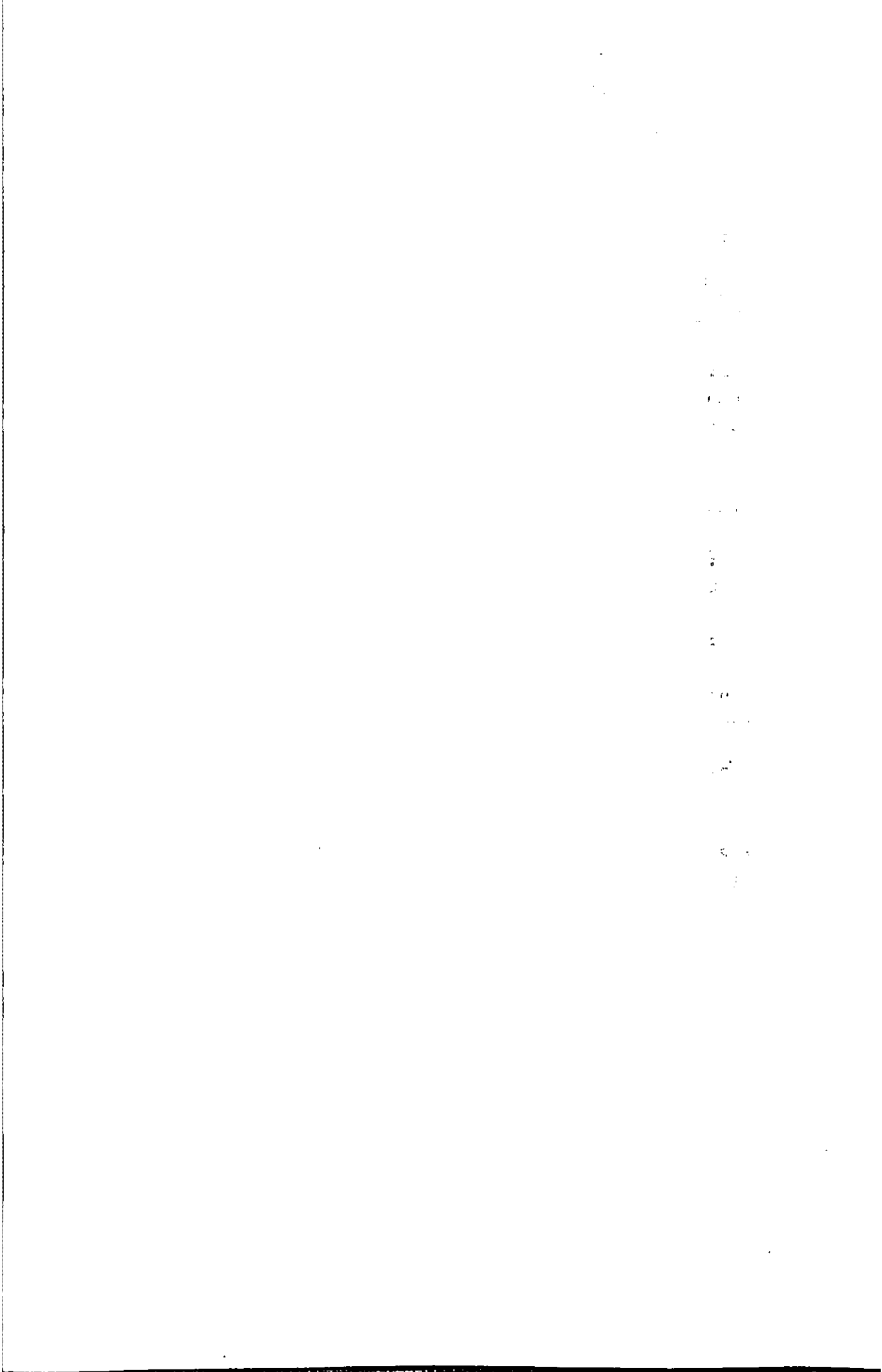
## LIST OF ABBREVIATIONS

AA	Auswärtiges Amt
AAPD	Akten zur Auswärtigen Politik der Bundesrepublik Deutschland
add	addition
amemb	American Embassy
APUZG	Aus Politik und Zeitgeschichte (journal)
BA	Bundesarchiv, Koblenz
BA-MA	Bundesarchiv Militärarchiv, Freiburg
BAOR	British Army on Rhine
BBA	Bundesbank-Archiv
BDI	Bund Deutscher Industrie
BEA	Bureau of European Affairs (DOS)
BGBL	Bundesgesetzblatt
BMF	Bundesfinanzministerium
BMVg	Bundesverteidigungsministerium
BMW	Bundeswirtschaftsministerium
bn	billion
BPI	Bulletin des Presse- und Informationsamts der Bundesregierung
CAB	PRO, Cabinet Papers
CDU	Christlich Demokratische Union
CEA	Council of Economic Advisers
ch	chapter
Cmnd	HMSO, Command Paper
CSU	Christlich Soziale Union
CY	Calendar Year
DAFR	Documents on American Foreign Relations
DDF	Documents Diplomatiques Francaises
DDRS	Declassified Documents Reference System
DEFE	PRO, Defense Ministry Files
DF	Decimal Files, NA
DOD	Department of Defense
DOS	Department of State
EA	Europa-Archiv
ECSC	European Coal and Steel Community
EDC	European Defence Community
EEC	European Economic Community
EFTA	European Free Trade Area
EPU	European Payments Union
FAZ	Frankfurter Allgemeine Zeitung
fn	footnote
FO	British Foreign Office
FR	Frankfurter Rundschau
FRG	Federal Republic of Germany
FRUS	Foreign Relations of the United States
FTA	Free Trade Area
FY	Fiscal Year
HMSO	Her Majesty's Stationery Office
IFZ	Institut für Zeitgeschichte, München
IHT	International Herald Tribune
IMF	International Monetary Fond
JCS	Joint Chiefs of Staff
JFKL	John F.Kennedy Library, Boston

KCA	Keesing's Contemporary Archives
KPPC	Kennedy's Presidential Press Conferences
LBJL	Lyndon Baines Johnson Library, Austin
LES	Ludwig Erhard Stiftung, Bonn
m	million
MAAG	Military Assistance Advisory Group (US)
MAC(G)	Mutual Aid Committee - Germany (UK)
MB	Ministerbüro
MC	Military Committee
MGFA I-III	Militärgeschichtliches Forschungsamt, Freiburg(ed), Anfänge westdeutscher Sicherheitspolitik, vols.I-III, München 1983-1993
MLF	Multilateral Force
NA	National Archives, Suitland (MD)
NHP	Nuclear History Program
NL	Nachlaß
NPG	Nuclear Planning Group
NPT	Non Proliferation Treaty
NSA	National Security Archive, Gelman Library, George Washington University, D.C.
NSAM	National Security Action Memorandum
NSC	National Security Council
NSF	National Security File
NYT	New York Times
NZZ	Neue Züricher Zeitung
OEEC	Organization for European Economic Cooperation
OECD	Organization for Economic Cooperation and Development
OHI	Oral History Interview
PA-AA	Politisches Archiv des Auswärtigen Amts, Bonn
POF	President's Office Files (JFKL, LBJL)
PP	Public Papers of the Presidents of the US
PPP	Pre-Presidential Papers (JFKL)
PREM	PRO, Files of the Prime Ministers' Office
PRO	Public Record Office, London
PSSD	Public Statements of the Secretaries of Defense (microfilm edition)
RAF	Royal Air Force (UK)
RAND	Research and Development Corporation (US)
Ref.	Referat (department of a German ministry)
RG	Record Group (NA)
SACEUR	Supreme Allied Commander Europe
SF	Subject Files, NA
SecState	US Secretary of State
SPD	Sozialdemokratische Partei Deutschlands
SZ	Süddeutsche Zeitung
T	PRO, Treasury Files
TAF	Tactical Air Force
telcon	telephone conversation
TIAS	US Treaties and Other International Agreements
VDB	Verhandlungen des Deutschen Bundestags, Protokolle
VIZ	Vierteljahreshefte für Zeitgeschichte
vol	volume
VPSF	Vice Presidential Security File (LBJL)
WEU	Western European Union
ZBR	Zentralbankrat (Bundesbank)

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## INTRODUCTION

### a) Research Goals

On 8 September 1994, in a pompous ceremony figuring Helmut Kohl, François Mitterand, John Major, and Warren Christopher, one of the last remnants of the Cold War was officially declared history: American, British, and French troops left Berlin. Similar ceremonies were held throughout Germany after 1989 as former allied troops, including the Russian forces, left the bases they had occupied for almost fifty years. The farewell speeches held on these occasions emphasized the bravery of the troops, the unparalleled success they had in fulfilling their mission of safeguarding the freedom of Germany, and the magnanimity of the sending countries (on the occasions of Russian troops leaving, tones were more muffled).<sup>1</sup>

The large-scale deployment of conventional troops of the hostile power-blocs at the Cold War frontline, both in West and East Germany, remains a remarkable and outstanding feature of European postwar history. On a diminished scale, despite the ceremonies referred to above, NATO troops are still present in many places in Germany. This continuity indicates that the troop's significance stretched well beyond the allocation of military security against the East. Allied troop stationing in the Federal Republic cannot be seen as in isolation from basic political and economic phenomena.

This study deals with the political impact and important economic consequences of American and British troop-maintenance in the Federal Republic of Germany from 1955 to 1967. It will concentrate particularly on the linkage between economic and security issues associated with Anglo-American troop maintenance. This linkage manifested itself in many ways during the endless conflicts about the foreign exchange expenditure of the troops. The research period has not been chosen randomly. 1955 was the date of West German sovereignty and the status of the troops on its soil changed from occupation forces to allies. 1967 marked the end of the most serious crisis concerning the continuation of allied troop maintenance under increasingly difficult financial conditions - and also the limit of availability of a sufficient archival base.

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<sup>1</sup> For the speeches held during the Berlin ceremonies see: EA 19/1994, D550-570.

However, many of the conflicts described in this thesis have shown a marked continuity and have still not yet been resolved.

Allied troop maintenance in Germany has not been the subject of extensive historical research despite it being one of the most conspicuous manifestations of the postwar military-political settlement in Europe. A large body of scholarly work exists which interprets allied troop-maintenance in Germany entirely within the framework of general strategic and political questions. Only the most recent of this literature is based on archival evidence.

The influence of strategic factors, above all nuclear strategy, on the conventional posture in the Alliance has been dealt with by whole school of historians.<sup>2</sup> A certain consensus has been reached in this respect which explains the long-term presence of the troops in Europe as a necessary complement of nuclear weapons and its value as depending on nuclear strategy. Their 'tripwire' function - they provide time to consider a nuclear response to an attack - figures as their most important role. However, it is evident that strategic factors explain only a small part of the continuity of allied troop-maintenance in Germany and that political factors played a far more important role.

The political foundations of allied troop stationing have also been extensively researched. The concept of 'double containment'<sup>3</sup>, that is the containment of both the Soviet-Union and Germany, provides a useful framework. The troops tied the United States and Britain to the defence of Western Europe, deterred local Soviet aggressions, and controlled the integration of Germany into the military and economic framework of the West.<sup>4</sup>

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<sup>2</sup> The most influential work is presumably Gaddis, *Strategies of Containment*, 1982. Other examples are Schwartz, *NATO's Nuclear Dilemmas*, 1982; Cioc, *Pax Atomica. The Nuclear Defense Debate in Germany*, 1988; Stromseth, *The Origins of Flexible Response*, 1988 and numerous articles in journals like *DIPLOMATIC HISTORY*. An assessment of the strategic debate in the Alliance is M.Trachtenberg's *History & Strategy*, 1991. For details of location, their structure, and changes over the years, see: Duke(ed), *US Military Forces and Installations in Europe*, 1988; Duke/Krieger(eds), *US Military Forces in Europe*, 1993; Lee Gordon, 'The Half-Forgotten Army. A Survey of British Forces in Germany', in: *THE ECONOMIST* 28.11.1970; Mahnke(ed), *Amerikaner in Deutschland*, 1991; Nelson, *A History of US Military Forces in Germany*, 1987.

<sup>3</sup> It is outlined in a very lucid way in Hanrieders, *Germany, America, Europe*, 1989.

<sup>4</sup> The literature on German rearmament covers all these aspects. See for a comprehensive treatment the three volumes of the MGFA(ed), *Anfänge westdeutscher Sicherheitspolitik 1945-1956*, 1982-1993 with exhaustive bibliography. For the political foundations of British and American troop maintenance in Germany, see ch.I and ch.VI.



Remarkably less research has been done on the major practical problem this troop-maintenance has posed for the sending countries and Germany: the problem of the cost and the impact of the financial problem on political-strategic questions as well as on the economic relations of the countries involved. At issue in particular was the foreign exchange need of the troops which was seen as causing a considerable drain on the reserves of the sending countries. This troop cost problem therefore did not only have a military and financial component, but it also became a major factor of the monetary relations of the affected countries. Historical research on this problem is rare, especially research based on archival sources.<sup>5</sup> This is surprising given that the history of allied troop maintenance is marked by an uninterrupted series of conflicts that arose on this issue. Disagreements about financial questions were much more frequent in the Western Alliance than strategic or political divergences. When the latter arose, they were often closely linked with the cost issue. It therefore seems rather arbitrary to simply separate strategic and political questions from their often complicated economic-monetary background. A comprehensive history of allied troop maintenance in Germany has to take this into account before it is possible to understand the particular role these troops played in postwar German and European history.

As a matter of fact, it is rather surprising that such an expensive kind of deterrence as large-scale conventional troop stationing was maintained during all these years, even though the main contributing countries -the United States, the United Kingdom and France- constantly

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<sup>5</sup> In the Anglo-German context only one specific article exists: Kaiser, 'Money, Money, Money', in: Schmidt(ed), *Zwischen Bündnissicherung und privilegierter Partnerschaft*, 1995, which provides an account with many facts but does not place the issue in a larger context. A few paragraphs, based on archival evidence, can be found in Schmidt G., *Großbritannien und Europa*, 1989; Mager, *Die Stationierung der britischen Rheinarmee*, 1990; Thoß, in: MGFA(ed), *Anfänge westdeutscher Sicherheitspolitik III: Die NATO Option*, 1994, p.198-210. The history of German-American Offset has been early on the object of some works of political scientists. The most comprehensive are: Thiel, *Dollar-Dominanz, Lastenteilung und Amerikanische Truppenpräsenz in Europa*, 1979, discusses the economic background extensively, suffers, however, strongly from the complete absence of archival material; Mendershausen, *Troop-Stationing in Germany. Value and Cost (RAND)*, 1968 provides a brief but well-informed analysis; Treverton, *The Dollar-Drain and American Forces in Germany*, 1978, based on interviews with participants in the events and on privileged access to government documents, is particularly strong on the 1966/67 crisis. Research based on archives is rare. The exceptions are: Wightman, 'Money and Security. Financing American Troops in Germany and the Trilateral Negotiations 1966/67', in: *Rivista di Storia Economica* 1/1988, p.26-77, with a similar approach to the one adopted in this thesis; Donfried, *The Political Economy of Alliance: Issue Linkage in the West-German American Relationship*, Ph.D.thesis, 1991, which deals mainly with the Anderson-Dillon episode; and Haftendorn, *Kernwaffen und die Glaubwürdigkeit der Allianz*, 1994 which places the issue in the larger context of the strategic discussion in NATO during the mid-1960s.

regarded it as only a temporary solution. Changes in strategic doctrines, the nuclearization of the Alliance, the build-up of a large conventional army, the *Bundeswehr*, and all the related economic problems did not decisively alter troop-levels. For an explanation of this continuity it is necessary to bridge the wide gap that often exists between disciplines in research on contemporary history. The analysis has to be extended beyond the narrow scope of a history of the troops and take into account fundamental political and economic aspects of the relations between the United States, the United Kingdom and Germany.<sup>6</sup>

As previously mentioned, this research originated from taking a closer look at a problem which plagued Bonn's relations to the countries maintaining troops on German soil: the problem of the foreign exchange cost of allied troops in Germany. The United States and the United Kingdom tried, during the so-called **offset- or support cost negotiations**<sup>7</sup>, to recover by various means the huge foreign-exchange losses caused by troop maintenance abroad. The potential of conflict in these negotiations was immense. The Germans regarded them as a discriminatory practice and as an outright symbol of their inferior status in the Alliance. In contrast, the United States and Great Britain saw them as an important means of ensuring German resources for the defence of the West and as a justified contribution to common defence. What lifted the conflict to an even higher plane was that both the US and the UK came to regard the troop's foreign exchange cost as a cause for fundamental monetary imbalances in the Western World. This interpretation was refuted by the Federal Republic. The diverging views led to numerous crises in mutual relations during the period 1955-1967.

Three basic approaches will be adopted in order to guide the analysis:

1) to write a history of the Support Cost- and Offset-negotiations and to link them to related phenomena in the economic and political relations of the United States, Great Britain and

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<sup>6</sup> The impact of the troops on German society from a sociological and "micro-historic" point of view has to be left aside, although it would be very interesting to look at it in more detail. Many German cities housed large foreign garrisons over decades. The troops played not only an important economic role in the region, but presumably also fostered a considerable exchange of values and attitudes. See: Signe S., *Die GIs. Amerikanische Soldaten in Deutschland*, 1985; Nelson D., *Defenders or Intruders? The Dilemmas of U.S. Forces in Germany*, 1987.

<sup>7</sup> Support Costs were direct, budgetary payments by the German government towards the cost of allied troops on its territory. Offset are measures short of direct payments which should offset the foreign exchange loss of the stationing countries, for example by placing weapon orders in those countries or by investing in their money markets. Occupation costs were German contributions to cover the expenses of the occupation forces in 1946-55.

Germany.

2) to show how economic, and in particular monetary, factors influenced security issues in relations between Germany, Europe and the United States.

3) to highlight changes in West Germany's relations with America and Britain in the period from 1955 until the Kiesinger/Brandt government's ascendancy to power in 1967, particularly regarding the role of economic diplomacy as reflected in the debate about the troops and their cost. Special attention will be given to tensions arising from the simultaneous integration of Germany in European institutions, in the Atlantic Alliance, and in the international monetary system. The objective of the following paragraphs is to clarify and narrow these three approaches.

#### b) The History of the Negotiations on Troop Costs

To write a history of the Support Cost- and Offset-negotiations is a self-evident purpose, given (i) the prominence and continuity of this problem during the first twenty years of West Germany's membership in NATO and (ii) the absence of related literature and the gaps in the few existing works. Reconstructing the events was therefore a first necessary step. However, I have not concentrated on the tiring technicalities and day-to-day work of the negotiations. It has also not been my intention to calculate how a fair offset or a fair sharing of the defence burden might have looked. Estimating the value of the troops is an essentially political assessment. Moreover, their overall cost is almost impossible to quantify.<sup>8</sup> The crucial task will be to attempt placing the negotiations in the context of numerous related issues such as the debates about troop levels, international monetary relations, armaments trade, military strategy, European questions, domestic political and economic factors, etc. The negotiations were forums in which such questions were dealt with and therefore provide an ideal starting point to take a fresh look at many issues. Generally the negotiations dragged on for many months and kept various departments of the respective governments busy, thereby producing abundant archival material. This provides a broad fundament to historical

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<sup>8</sup> See ch.I. In times of crises, like the Berlin crisis 1958-1961 the troops were naturally regarded as more 'valuable' than in times of detente. These fluctuations render it not astonishing that NATO never found a formula to institutionalize the distribution of the costs. Attempts by political scientists to calculate a fair burden-sharing miss this point completely. See for example: Olson/Zeckhauser, 'An Economic Theory of Alliances', in: REVIEW OF ECONOMICS AND STATISTICS 48/1966, p.266-79; Oneal/Elrod, 'NATO Burden-Sharing and the Forces of Change', in: INTERNATIONAL STUDIES QUARTERLY 33/1990, p.435-56; van Ypersele de Strihou, 'Sharing the Defense Burden among Western Allies', in: REVIEW OF ECONOMICS AND STATISTICS, 49, 4/1967, p.527-536.

analysis.

Offset or support costs payments had a direct connection with the level of allied troop-maintenance. Reductions were often justified by the insufficiency of German payments. The consistent emphasis of German governments on a stable troop level made the threat of redeployment an obvious means of pressure. Allied policies concerning troop levels are a focus of my research. The British reductions of 1958/59 and the American reductions in 1966/67 were intensely debated issues. Their connection with the negotiations and their economic, political and strategic reasons will be analysed in depth.

### c) The Link between Monetary and Security Policy

During a Congressional Hearing on the future of US troop maintenance in Europe, Martin Hillenbrand, Assistant Secretary of State for European Affairs, remarked that the US troop deployment had been conducive to a '*climate of receptivity toward American economic activity in Europe. I don't like to imply that our troops in effect are hostage to European good behaviour in the economic area, but obviously it would be foolish to deny at a psychological level that there is a certain relationship here.*'<sup>9</sup> Such statements which suggest a close link between economics and security in transatlantic relations have, in particular in connection with monetary affairs, found their way into a great number of very diverse scientific works on basic economic and political relations between the European countries, especially the FRG, and the United States.<sup>10</sup> The connection between political-military and economic-monetary factors has sparked increasing interest by many political scientists dealing with International Relations (IR) or International Political Economy (IPE) since the 1970s.<sup>11</sup> It is certainly no great novelty that security and economical issues were closely linked in

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<sup>9</sup> US Congress, House, Committee on Armed Services: Special Subcommittee on NATO Commitments, 92nd cong., 2nd sess., October 1971-March 1972, p.12574.

<sup>10</sup> For example: Calleo/Rowland, *America and the World Political Economy: Atlantic Dreams and National Realities*, 1974; Strange, *International Economic Relations of the Western World 1959-71*, 1976, p.270-75; Thiel (1979); Hannieder (1989), p.292; Costigliola and Borden, in: Paterson (ed), *Kennedy's Quest For Victory. American Foreign Policy 1961-63*, 1989, p.24-85.

<sup>11</sup> See for example: Bergsten/Keohane/Nye, 'International Economics and International Politics: a framework for analysis', in: Bergsten/Krause(eds), *World Politics and International Economics*, Washington 1975. For a recent attempt: Gowa, *Allies, Adversaries, and International Trade*, 1995.

international relations during the Cold War. However, empirical studies which thoroughly and systematically analyse these linkages are rare, particularly those which include a historical perspective.<sup>12</sup>

How did political-military factors in German-American and German-British relations influence their monetary relations and vice-versa? What exactly was the connection between the developments in the international monetary system and allied troop-maintenance in Germany? Those are basic themes of this research.

The most fundamental problem in the international monetary system from the 1950s to the 1970s was the increasing pressure on the currencies of the United Kingdom and, from 1958 on, of the United States. These problems moved inexorably to the forefront of political concerns and exerted an increasing impact on the politics in the Western Alliance. A major recipient of the huge Sterling and Dollar outflows was the Federal Republic of Germany. Monetary problems therefore assumed an increasingly important role in British-German relations since the early 1950's and in American-German relations from 1959 onwards. Germany's monetary policy was, despite the strength of its currency, in many ways restrained by the consequences of its commitment to the Western Alliance. The reality of the foreign troop maintenance in Germany turned out to be an important factor in this respect.

For the United States and Britain the situation was the reverse. Sterling and Dollar as suppliers of international liquidity created a strong burden on the balance-of-payments of both countries.<sup>13</sup> Washington and London were not willing to abandon the central role their currencies played in the world economy, for a variety of reasons. A stable balance of payments was a necessary precondition for these policies. Military expenditure abroad, of which troop stationing abroad was a major component, was in either case a conspicuous negative factor. Evidently, troop maintenance was not the only, nor even the main cause of the disequilibrium of the late 1950's and 1960's, but they were an easy and popular target for

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<sup>12</sup> Strange, 'Political Economy and International Relations', in: Booth/Smith(eds), *International Relations Theory Today*, 1995, p.154-74. One of the few exceptions is: Donfried (1991).

<sup>13</sup> see e.g. Triffin, *Gold and the Dollar Crisis*, 1960; Strange, *International Economic Relations of the Western World*, 1976, p.45-47.

demonstrating action on this problem. The USA and Britain saw themselves confronted with the dilemma of either assigning more relative value to the strengthening of the balance-of-payments or to harmonious relations with the Federal Republic which insisted on stable troop levels. This particular situation allows to address anew a whole range of issues which have been seen previously only in their purely political-military or monetary context.

Research on this theme will proceed alongside the following questions: 1. What was the influence of allied troop-maintenance on the monetary situation of Germany, the US and Britain? 2. How did monetary circumstances affect the attitude of these countries towards the conventional posture? 3. How were these influences converted to different policies towards the troop-levels? 4. How were monetary policies affected by political-military considerations? Finally, how did the troop cost issue spill over into other areas of mutual relations?

The significance of these problems for German postwar history remains to be evaluated. The concentration of historical research on either security policy or foreign economic policy prevents a balanced interpretation of these questions.<sup>14</sup>

#### d) Offset and German Postwar Foreign Policy

The 'German Question', understood as the problem of how a re-emerging, powerful Germany fits into the European structure of power, is a fundamental problem which underlies most research on German postwar foreign policy. Its long history stretches back centuries. Since the German reunification it is once more at the center of debate. The problem of Germany laid at the heart of many political issues in postwar Europe, and also formed an essential background of troop level and balance of payments debates.

The 'German Question' has to bear an exuberant amount of literature.<sup>15</sup> Research on it has

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<sup>14</sup> Döring-Manteuffel, 'Deutsche Zeitgeschichte nach 1945', in: VFZ Vol.41, 1/1993, p.1-30.

<sup>15</sup> For a critical reviews over much of the German literature see: Michalka(ed), *Die deutsche Frage in der Weltpolitik* (Neue Politische Literatur, Beiheft 3), 1986.

been traditionally marked by a certain ambiguity in the use of the term.<sup>16</sup> In the postwar period the problem of reunification was subsumed under the slogan and was much more accentuated than the continuity of the question of Germany's position in Europe.<sup>17</sup> It was assumed that only when reunification actually should take place, the problem of a German hegemonic position in Central Europe would arise anew.<sup>18</sup> In reality, the problem of German power in Europe never ceased to occupy the minds of West-European and American politicians after the war.<sup>19</sup>

How does this research figure in this context? First, as already mentioned, the significance of the Anglo-American troop stationing was twofold: control of the Soviet Union and control of Germany, 'double containment'. This control function was tacitly but widely acknowledged and substantial changes in troop-levels inevitably affected the credibility of this function.<sup>20</sup>

A second, and for this research even more important, aspect of the problem is the extent to which it became an economic one after 1955, when Germany was politically and militarily tightly connected to the Western camp. Twice in the twentieth century Germany had been able to transform an impressive economic resurgence in assertive, ultimately militarily aggressive, foreign policies. The most significant development in the Federal Republic, during and after the process of its inclusion into the Western alliance system, was the unprecedented economic success in the 1950's and 1960's, evoking apprehensions that the Federal Republic might use its sheer economic weight to pursue irresponsible policies. In the relationship towards its Western Allies the German problem expressed itself increasingly in an economic context. This historical process can be traced right up to today when the looming economic

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<sup>16</sup> Verheyen, *The German Question*, 1991, p.2-3, discerns four principal dimensions of the German Question: 1. the question of German identity, 2. the reunification issue, 3. the problem of Germany's place in the international environment, 4. the problem of German political and economic power in a narrower regional context.

<sup>17</sup> An example for this ambiguous treatment is provided by the articles in Schröder(ed), *Die Deutsche Frage als internationales Problem*, 1990.

<sup>18</sup> Heß, *Westdeutsche Suche nach nationaler Identität*, in: Michalka (1986), p.28.

<sup>19</sup> Loth, *Der Historiker und die Deutsche Frage*, in: *Historisches Jahrbuch 112/1992*, p.366-382.

<sup>20</sup> See for example Wiggershaus, 'The Other "German Question". The Foundation of the Atlantic Pact and the Problem of Security against Germany', in: Di Nolfo(ed), *The Atlantic Pact 40 Years Later. A Historical Appraisal*, 1991, 111-126.

hegemony of Germany is a major question of European policy.<sup>21</sup>

Rising economic power and lasting security dependence gave the foreign policy of the Federal Republic a very particular shape in the 'post-sovereignty' period from 1955 onwards. The institutionalized constraints on Germany's sovereignty in the Paris Accords of 1955, and possibly even more the self-restraint Germany exerted on its foreign policy as a consequence of recent history, contrasted sharply with the spectacular economic rise of the Federal Republic. Surprisingly, the role of economic diplomacy has only recently attracted increasing attention in accounts of postwar German foreign policy.<sup>22</sup> The traditional concentration on 'classical' attributes of foreign policy (military and alliance politics) has led to a rather striking neglect of the more subtle instruments of foreign economic policy in furthering Germany's interests.<sup>23</sup> This is particularly conspicuous in the field of monetary policy. During the 1950s, the German mark became one of the strongest currencies in the world. It would be indeed curious if this spectacular development had not had a deep influence on foreign policy issues.

How did the allies cope with the new fact of the overwhelming German economic success? Was the control-function of the troops used as lever in economic conflicts with the Federal Republic? Did Germany's need for security provided by NATO (and this security was for the Germans as a consequence of the crude logic of the nuclear age guaranteed by the presence of allied conventional troops on German soil), influence the way it managed its foreign economic policy? Did Germany use its economic weight to further its goals during the Cold War period?

The comprehensive questions posed in the last paragraph can, of course, not be answered fully with the results of this thesis. The objective is to add new angles to this fundamental debate. Many of the arguments dealt with in the thesis reappear in one form or another in the

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<sup>21</sup> Schwarz, 'Germany's National and European Interests', in: Baring(ed), *Germany's New Position in Europe: problems and perspectives*, 1994, p.107-30.

<sup>22</sup> A good example is Hanrieder (1989).

<sup>23</sup> Schröder H.-J., 'Wirtschaftliche Aspekte deutscher Aussenpolitik in der Adenauer-Ära', in: Knipping/Müller (eds), *Aus der Ohnmacht zur Bündnismacht: das Machtproblem in der Bundesrepublik, 1945-60*, Paderborn 1995.



contemporary discussion about DM hegemony and similar - real or unreal - consequences of Germany's economic power.

The thesis will proceed chronologically, divided into two parts. The first part will deal with the problem of British-German support costs and its implications during the years 1955-60. The troop cost issue had no special importance for German-American relations during this period. The second part, 1960-67, analyses German-American offset problems. Every chapter in both parts will attempt to place the troop cost issue in one or several larger contexts which are outlined at the outset of the chapters.

#### e) Sources and Literature

The coverage of the research period (1955 - 1967) by both published primary sources and archival material is extensive. However, biographies, journals, and newspapers were a necessary complement. I attempted to avoid the parochial view of some archive-based research in which the authors were visibly infatuated by the 'importance' of key documents they had dug up whereas the material often repeats only the temporary position of a small part of the concerned government. Particularly, in order to understand the crucial domestic context of many issues, secondary sources were essential.

Even so, primary sources are the foundation on which this research rests. Some of them are available in edited form. For US policy, the FRUS edition and the microfiche collection of newly declassified documents, the Declassified Documents Reference System, are very useful. These editions provide a good documentation of major issues, but unavoidably lack detailed material related to the subject. American archives were therefore crucial for this study. Extensive research has been carried out in the presidential libraries (JFK Library/Boston, LBJ Library in Austin) and in the National Archives (Washington). All of them contain an enormous amount of documentation on relevant issues. I consulted also important smaller collections like the McGhee Papers (Georgetown University) and the National Security Archives (George Washington University, Washington DC).

Extensive published documentation is lacking in the case of Britain. The Public Record Office, however, provides an immense amount of most compelling and comprehensive

material for all questions related to offset and monetary policy. Material from the Prime Ministers Office (PREM), the Cabinet (CAB), the Foreign Office (FO), the Treasury (T) and Ministry of Defence (DEFE) files has been consulted. The files are open until 1965 and have been thoroughly evaluated. Unfortunately, documentation on British policy in 1966/67 is not yet available and the analysis of the British position during these years must remain very preliminary.

Published sources for the German side are limited.<sup>24</sup> Only recently, the publication of German diplomatic documents has begun which covers, however, only the years 1963-65. Archives which contain relevant material are spread all over Germany. The Politisches Archiv - Auswärtiges Amt/Bonn provides material on the details of the negotiations, though many of the high-level documents are still closed to research. The sources in the Bundesarchiv/Koblenz close most of the gaps. Highly rewarding are the papers of various involved politicians (Blankenhorn, v.Brentano, Etzel, Schäffer, von Guttenberg). The files of the Chancellory (B136) have proved extremely useful. The central files of the Finance and Economics Ministry (B126/B107) also contain further extensive material.

Regarding the monetary side of the question some documentation in the Bundesbankarchiv (Frankfurt) was available and very helpful. Smaller collections such as the Defence Ministry sources which have been declassified for the Nuclear History Project (Prof.Krieger/Marburg), the Ludwig-Erhard Stiftung (Bonn) and the Institut für Zeitgeschichte (München) have been consulted. Significantly important, particularly for the crucial year 1966, is the Military Diary by former Defence Minister von Hassel. The files of the Defence Ministry in the Bundesarchiv/Militärarchiv in Freiburg, however, are almost useless for the period of this research due to the lamentable state of declassification.

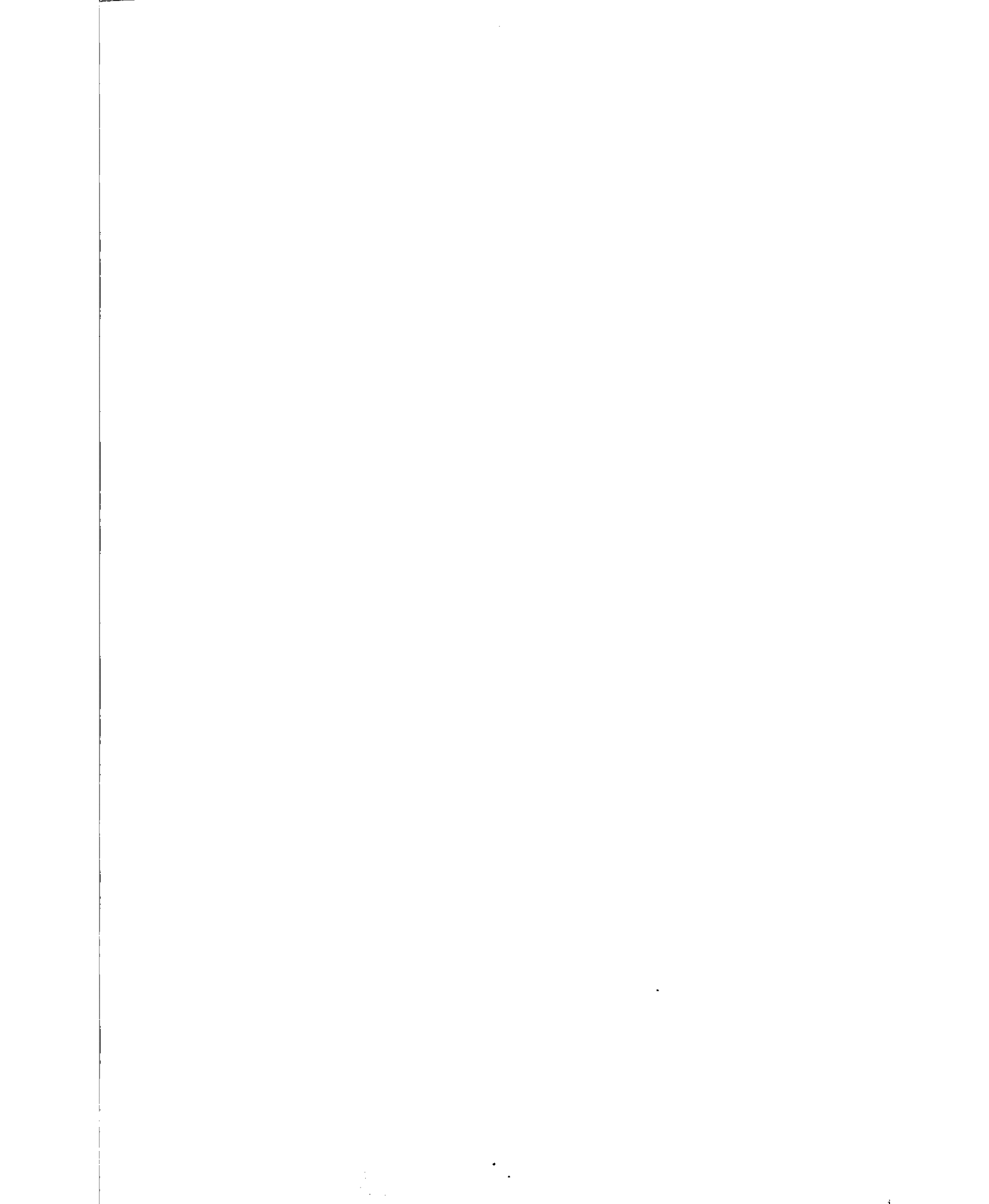
For the period 1964-67, the archival base is somewhat unbalanced because of the thirty years rule. The American side is comprehensively documented, the German sufficiently (although crucial documentation can not yet be quoted), and the British only very sketchily. This

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<sup>24</sup> Of limited value are Adenauers *Teegespräche (1950-1963)*, ed. Schwarz/Morsey, 1984-1992; editions of correspondence (like *"Sehr Geehrter Herr Bundeskanzler. Von Brentano Briefwechsel mit Adenauer*, ed. Baring, 1974; *Heuss/Adenauer 1948-1963*, ed. Mensing, 1989), the *Protokolle of the CDU Bundesvorstand 1953-1959*, ed. Buchstab, 1990, and the various memoirs.

affected particularly the last chapter.

Specific difficulties were presented by the statistical material. Official statistics for many of the questions posed in this thesis are hardly available and often unreliable. The influence of the troop maintenance on the balance of payments is a question that depends very much on interpretation. Balance of payments statistics are subject to numerous revisions by governments and the accounting method varies from country to country. Additionally, they were often manipulated for the sake of political reasons. Reservations regarding the reliability of the statistical material quoted in the thesis are mentioned where necessary.



**PART I**

**THE TROOP COST PROBLEM IN  
BRITISH-GERMAN RELATIONS 1955-1960**



CHAPTER I  
**AMERICAN AND BRITISH TROOPS IN GERMANY  
 AND THE FIRST SUPPORT COST AGREEMENT**

a) German Rearmament and Allied Troop Maintenance in Germany

When in May 1955 the Paris Accords came into effect, the great dispute about German rearmament which had dragged on for over five years finally came to an end. The result was spectacular, encompassing the establishment of West Germany's sovereignty and its inclusion among NATO only ten years after World War II. These events were accompanied by the continuation of large scale NATO troop stationing on German soil. American, British, French, Canadian, Dutch, Belgian, and Danish troops changed their status from occupiers to protectors. The diplomatic process leading up to the Paris Accords as well as the political and military causes and implications have been researched in much detail.<sup>1</sup> There are, however, still many gaps as to the economic foundations of these events -crucial for understanding the results- and as to how the plans, embattled for such a long time, were implemented in practice.<sup>2</sup> The following paragraphs briefly review the origins of allied troop maintenance in Germany and of West German rearmament, emphasizing the link between these two developments, within the perspective of economic burden-sharing.

In a way, the events leading up to the Paris Accords can be interpreted as an enormous undertaking of multinational burden-sharing initiated by the United States of America. Very soon after World War II, the Americans felt the need to find a way of using German resources in the increasingly costly pursuit of the Cold War. However, only the outbreak of the Korean War in 1950, and the lessons drawn from it, created the necessary political

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<sup>1</sup> The three volumes of the MGFA (ed), *Anfänge Westdeutscher Sicherheitspolitik*, (München 1982, 1990, 1993) provide a meticulous account with references to the vast literature about the issue. Recent collective volumes containing many excellent articles on German rearmament and related issues are: Heller/Gillingham(eds), *NATO: The Founding of the Alliance and the Integration of Europe*, 1992; Wiggershaus/Maier(eds), *Das Nordatlantische Bündnis*, 1993; Diefendorf/Frohn/Rupieper, *American Policy and the Reconstruction of West Germany, 1945-55*, 1993. See further: Schwartz, *America's Germany. John J. McCloy and the Federal Republic of Germany*, 1991; Rupieper, *Der besetzte Verbündete. Die amerikanische Deutschlandpolitik 1949-55*, 1991; May, *The American Commitment to Germany, 1949-55*, in: DH 13/1989, p.431-60. The following paragraphs are based on this literature.

<sup>2</sup> The publication of the fourth volume of the MGFA's *Anfänge Westdeutscher Sicherheitspolitik* by W. Abelshäuser will close a huge gap regarding the financial conditions of German rearmament.

preconditions. One of the consequences was that the United States themselves undertook a significant expansion of their commitment to Europe. The American government came to see the various economic aid schemes, like the Marshall Plan, as incapable to achieve a stabilization of the critical situation in Europe. Economic aid was replaced by military aid on a large scale.<sup>3</sup> Even this was seen as insufficient. The presence of a large conventional force in Europe seemed imperative from a military point of view in order to deter another Communist aggression. As long as the economic and political situation of the European democracies remained fundamentally unstable and the Soviet threat imminent, the only rapid way to achieve this objective was the stationing of American forces in Europe. Precisely that was also urgently requested by the Europeans.

The massive reinforcement of the small remaining US force in Europe was approved by Congress only in 1951, after bitter controversies.<sup>4</sup> The acrimonious debate showed that an extended US troop engagement was perceived as a major shift in US foreign policy. For the first time, American forces were deployed during peacetime in Europe. Nobody at that time, however, thought that the American troop presence in Europe would outlast even the existence of the Soviet Union. In all probability, the commitment had been approved by Congress only because the administration gave credible assurances that the measure would be of a temporary nature and the financial burden on the US would last only during a certain transitional period: namely until the Europeans had rebuilt their own forces. Undoubtedly, the government itself believed in this prospect, as Eisenhower later recalled: *'After all, when we deployed our six divisions to NATO, the deployment was never intended to be permanent and we informed congress that this was a temporary measure, particularly related to the build-up of West German forces'*.<sup>5</sup> The decision for an American troop commitment gave a strong impetus to the idea of German rearmament which had been considered by military planners already for some time.

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<sup>3</sup> Pollard, *Economic Security and the Origins of the Cold War, 1945-50*, 1985, p.241.

<sup>4</sup> On the 'Great Debate' about a prolonged massive US military presence in Europe see: Williams, *The Senate and US Troops in Europe*, 1985; Carpenter, 'US Nato Policy at Crossroads. The 'Great Debate' of 1950-51', in: *International History Review* 8/1986, p.389-414; Thoss, 'The Presence of American Troops in Germany, 1949-56', in: Diefendorf/Frohn/Rupieper(eds), 1993, p.411-32.

<sup>5</sup> FRUS 1958-60, VII, Memo of Discussion at the 390th NSC meeting, 11 December 1958, p.367.



The Americans were not at all eager to shoulder the burden of Europe's conventional defence alone. In 1949/50, the cost of economic aid and military commitments made themselves increasingly felt in the American budget - without any reasonable prospect of an imminent decline, quite the contrary.<sup>6</sup> The fear that the US would have to settle the bill alone was not unjustified. Britain and France were increasingly engaged in the defence of their shaken colonial empires, and other NATO countries lacked the necessary resources. The only country which had the potential to relieve the US significantly of their burden by means of conventional troops and financial support was the still occupied West Germany. The idea of rearming Germany was therefore in many ways linked to the US troop commitment and it was this 'Burden-Sharing' component which was a decisive element driving the debate.

In late 1949, the US Secretary of State, Acheson, confronted the NATO partners with the American intention to permit and pursue the partial reconstruction of Germany's military potential in order to use these resources for the defence of the West. His first proposal was a 'package deal', explicitly linking US troop commitments to West German rearmament.<sup>7</sup> However, European opposition, due to their still fresh wartime memories, proved to be even stronger than anticipated. The reconstruction of a German military and the inherent restoration of German sovereignty were difficult to swallow so shortly after the war. French resistance, in particular, was almost insurmountable. Only the danger of American disengagement or a stop of its military and financial support overcame this opposition. In an attempt to contain the German military potential, whose reemergence was obviously unavoidable, with a control scheme as narrow as possible, France in 1950 launched the Pleven Plan for an integrated European army. Four years of intensive, protracted negotiations and diplomatic arm-twisting on the subject of the proposed EDC (European Defence Community) followed.<sup>8</sup> Finally, in August 1954, the French parliament voted the project down. The plans for Germany's integration into Western defence organizations were void. The Federal Republic which had hoped to gain sovereignty, once it accepted to contribute to the European army and continued

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<sup>6</sup> Leffler, *A Preponderance of Power*, 1992, p.304-11; Pollard (1985), p.222-42.

<sup>7</sup> Acheson, *Present at the Creation*, 1970, p.437-440.

<sup>8</sup> On the EDC, apart from the MGFA-volumes cited above, see for example: Gersdorff, *Adenauer's Aussenpolitik gegenüber den Siegermächten 1954*, 1994; Fursdon, *The EDC. A History*, 1980; Volkmann/Schwengler (eds), *Die Europäische Verteidigungsgemeinschaft. Stand und Probleme der Forschung*, 1985.

close control by the Western Alliance, saw its foreign policy in shambles.

Despite the negative vote, the USA and Britain continued with vigorous efforts to find a new scheme which made German rearmament acceptable to France. Finally, France agreed to West Germany's accession to NATO and to the revived Western European Union (WEU), founded in 1948 by Britain, France and the Benelux countries. Numerous control mechanisms were included in the treaties to prevent autonomous military action by Germany. The politically most important controlling steps, however, were the American and British pledges to remain with their forces in Germany.<sup>9</sup> This was, in a way, an ironic result: the political framework of German rearmament required, instead of relieving the US and the UK of military burdens, a costly commitment, even if this was intended to last only for a short period.

The Paris Accords of 1954 which codified these events also meant the end of occupation for West Germany. It regained most of its sovereignty. The foundations for a German contribution to Western defence were in place, and American and British objectives seemed fulfilled. Their sighs of relief proved premature. The first years of Germany in NATO were overshadowed by various frictions between the new partner and its allies about the size and form of the German contribution to common defence. Apart from the twelve divisions the Germans promised to provide for conventional defence, few of the earlier plans for rearmament were still valid in 1955. This was a result of the turmoil following the defeat of the EDC. The absence of precise commitments and various political and economic obstacles prevented a rapid build-up of German forces. The quarrel between West Germany and its NATO partners about the exact form of the German contribution began. How much of the burden of common defence would the Federal Republic have to shoulder? This lasting controversy over burden-sharing became one of the most important issues of NATO policy.

To sum up: The fervour and the urgency with which the US and the UK had pushed forward the debate about a German defence contribution from 1950-1954 resulted not only from the need to tie Germany to the Western camp or from military exigencies, as the otherwise useful

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<sup>9</sup> The American, British, and Canadian assurances to continue maintaining their troops in Europe are printed in: FRUS 1952-54, V/2, p.1351.

concept of 'double containment' implies.<sup>10</sup> The pressing burden of defence expenditure and the obligation to pay large conventional armies abroad made the utilisation of German resources indispensable, if there was to be any hope of ever reducing this burden and maintaining simultaneously a credible defence posture in Europe.<sup>11</sup> The political circumstances of German rearmament, on the other side, required the prolonged presence of American and British forces as controlling factor against a re-awakening of dangerous German policies. These, in a way, contradicting objectives form an essential background to the conflicts analysed in this thesis.

#### b) The End of the Occupation Regime and the Financing of Allied Troops

The burden of conventional defence in Europe during these Cold War years was enormous, especially for the three powers which bore the major part of the cost -the United States, the United Kingdom, and Germany. In 1955, the United States maintained an army of 261.000 men in Germany, about 10% of total US military personnel.<sup>12</sup> The United Kingdom, in the WEU-Treaty, committed itself to keeping four divisions and the 2nd tactical Air-Force in Germany, altogether 105.000 men. Those were about 15% of all British troops under arms. For both countries the cost of these commitments was only part of the resources which went into the defence of Europe.

It is very important to distinguish between the actual cost falling on the budget and the share of this budgetary cost arising in foreign currencies. The budgetary cost, according to NATO rules, was to be assumed by the country which maintained the forces, wherever they were stationed. Precise figures as to the budgetary cost of the American and British European commitments are difficult to find because usually they were not specified in the military budgets, contrary to the foreign exchange cost. In November 1959, the US Budget Director

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<sup>10</sup> This formula which interprets US policy towards Germany as an attempt to combine the containment of Soviet power with the containment of any resurgence of aggressive German policies has been coined in one of the most thoughtful analyses of German-American postwar relations: Harrieder, *Germany, America, Europe*, 1989.

<sup>11</sup> See also: Peter, *Britain, the Cold War, and the Economics of German Rearmament, 1949-51*, in: Deighton(ed), *Britain and the First Cold War*, 1990, p.273-90.

<sup>12</sup> Mendershausen, *Troop Stationing in Germany. Value and Cost*, 1968, p.52. For allied troop levels 1955-67, see table 3, Appendix I.

estimated the cost of the American NATO commitment, including back-up, aid, etc. at \$4 billion, of which \$1.2 billion were converted in local currencies.<sup>13</sup> An 1970 estimate put the cost of US forces in Europe at between \$7-9.5bn of which \$1.9bn went across the exchanges.<sup>14</sup> The British published estimates on the budgetary cost only in the 1960s. In 1966, the budgetary cost was estimated at \$437.2m of which \$249.2m was DM-expenditure.<sup>15</sup>

Germany was under the obligation to contribute twelve divisions, to be built up until 1959. Cost estimates for the build-up of the army went up to between DM 50-80bn with a projected yearly allocation of DM9bn (see ch.II), that is about 30% of German budgets in the late 1950s. Initially, the funds for rearmament were expected to equal the occupation costs Germany had to pay after the war toward the expenses of the occupation forces. Those were formidable sums. In the early fifties, occupation costs and related expenditures absorbed about 15% of Germany's net social product and in some years 35% of all expenses in the Federal budget!<sup>16</sup>

The end of the occupation period added a particular factor of urgency to the debate about burden sharing in the Alliance. It implied the termination of these occupation costs.<sup>17</sup> They had covered the DM expenditure of allied troops on German soil almost completely (and a big part of the budgetary cost) and were the major contribution of Germany to the Cold War prior to joining NATO. The end of the occupation regime made the continuation of allied troop maintenance in Germany an expensive venture in financial terms and implied heavy

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<sup>13</sup> FRUS 1958-60, VII, 424th NSC Meeting, 12.11.1959, p.512.

<sup>14</sup> Roughly one third of the cost was spent on operations (personnel pay, supply, transport, maintenance) and the rest for equipment, constructions, administration, and training. See: Fried, 'The Financial Cost of Alliance', in: Newhouse(ed), *U.S.troops in Europe*, 1971, p.106-07, 129-30.

<sup>15</sup> KCA 1966, p.21266.

<sup>16</sup> Köllner, 'Die Entwicklung bundesdeutscher Militärausgaben in Vergangenheit und Zukunft', in: APUZG 22/84, 2 June 1984, p.29; Abelsbauser, 'The Causes and Consequences of the German Rearmament Crisis', in: Heller/Gillingham(eds), (1992), p.314; Köllner/Volkman, 'Finanzwissenschaftliche, finanzwirtschaftliche und finanzpolitische Aspekte eines deutschen Beitrags zur EVG', in: MGFA II (1990), p.748; Hardach, *Der Marshallplan*, 1994, p.238.

<sup>17</sup> This refers only to occupation payments in the Western zones. Berlin remained occupied territory until the 1990s and the Federal Republic paid the expenses of allied troops stationed in the city.

additional burdens to budgets and external balances of the sending countries.

Table 1:

Approximate Allocation of Occupation-Costs paid by the Federal Republic, 1948-56  
(in \$million)

paid to:	American Forces	British Forces	others*	Sum
1948/49	476.2	571.4	142.8	1190.4
1949/50	404.8	404.8	166.7	976.3
1950/51	547.6	404.8	285.7	1238.1
1951/52	547.6	309.5	289.5	1166.6
1952/53	762.3	434.3	517.7	1714.3
1953/54	762.3	434.3	517.7	1714.3
1954/55	762.3	434.3	517.7	1714.3
1955/56	350.2	199.5	212.1	761.9
1948/56	4612	3115	2574	10301

\* French, Belgium, Dutch, Danish, Canadian Forces; includes also from 1952 on Germany's contribution towards NATO infrastructure costs

Sources: until 1955: PRO, T 225/424, Treasury note on allocation of occupation costs, 5.8.1955  
1955/56: Keesings Contemporary Archives, p.13783.

note: This table offers approximate figures of the funds as paid by Germany, not as spent by the occupation forces. Exact figures about the amounts differ considerably from source to source. Firstly, this is due to a confusion on how much had been paid and how much had been actually spent (from the early 1950s on, the occupation powers were not able to spend all the money). Statistics on how much had been spent show often surprisingly huge variations from year to year. (See, for example, the figures on US receipts in: US Senate, 91.cong, sess.1, Subcommittee on US Security arrangements and Commitments abroad: US Forces in Europe, pt.10, 1970, p.2245). Secondly, the methods of calculation are obscure. German official estimates add all kind of different costs caused by the occupation troops. They cite an amount of about \$11048m as actual occupation costs in the mentioned period. (See: Leistungen der Bundesrepublik Deutschland für die ausländischen Streitkräfte, in: BPI 24/1961, 3 February 1961, p.221-24).

As has been already remarked, both the US and Britain had planned for only a temporary presence of their troops after signing the Paris Accords. These hopes were quickly shattered. The most important reason -in a long-term perspective- was that the troops acquired an eminent political importance which by far overshadowed their military significance. Their role in assuring the ratification of the Paris Accords is one example. The maintenance of American troops became a crucial element of postwar European policy. They guaranteed the control of German rearmament and economic reconstruction by the United States. This was of central importance to all European countries which had been at war with Germany. For Germany, on the other hand, the US troops were an essential piece of NATO's security guarantee. When

the US in 1956 gave first hints of considering redeployment the reaction made one thing definitively clear: US hopes for a short stay in Europe were too optimistic (For this episode, and a more extensive discussion of the political and strategic importance of the US troops, see ch.VI).

The lack of a firm British intention to provide troops for a European army had been a major factor in the defeat of EDC. Even after this disaster, when it became increasingly clear that some form of British commitment would be necessary to accomplish German rearmament as fast as possible and to save the Western defence cooperation, a vehement discussion split the British government and public.<sup>18</sup> Britain's hesitation over a formal commitment of troops was due more to financial considerations than to an unwillingness to commit forces to continental defence. Foreign Secretary Eden stated in a 1954 telegram to his American counterpart, Dulles: *'Once the EDC is in force and the Germans are bearing their full share of defence expenditure we must face the certainty that after what may not be a very long period we shall cease to receive any German contribution towards the costs of maintaining our forces in Germany . . . At present levels this would mean that we should have to finance an extra 80 million pounds in foreign exchange. This would present us with very great difficulties.'*<sup>19</sup> During the EDC debate, apprehensions that the Federal Republic would spend all its defence funds for its own forces, leaving the UK to foot the bill for its troops on the continent, were a major preoccupation of the British cabinet.<sup>20</sup> The tenor of the discussion was that the UK could not take on any additional burden on its balance of payments. Whether this could be avoided by reductions, US aid, further German payments, or administrative savings remained an open question as long as the EDC debate went on. When it became obvious that a British troop commitment was essential for the European security structure, the problem was still not resolved. In the internal discussion during 1954 about the commitment,

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<sup>18</sup> The most recent monographs on this subject are: Dockrill, *Britains Policy for West German Rearmament*, 1991; Jansen, *Großbritannien, das Scheitern der EVG, und der NATO Beitritt der BRD*, 1992; Mager, *Die Stationierung der britischen Rheinarmee*, 1990.

<sup>19</sup> PRO, T312/53, Tel.874: Eden to Dulles, 6 March 1954.

<sup>20</sup> See for example the following Cabinet Memoranda: PRO, CAB 129/ C(52)36, 13.2.1952; C(52)106, 4.4.1952; C(52)141, 3.5.1952; C(52)162, 14.5.1952; C(52)185, 9.6.1952; C(53)112, 23.3.1953.

arguments over cost therefore played a central role.<sup>21</sup>

These arguments were, however, overruled (as was the still strong opposition to participation in an organization like WEU where Britain had to delegate some sovereignty in defence matters). The political benefits of a British commitment seemed to outweigh the financial cost. Firstly, the troops were necessary to overcome the impasse in the German rearmament question because France, in particular, insisted on such a pledge. Secondly, they kept the US troops in Europe. This was a major objective of British foreign policy, particularly after Dulles' 'agonizing reappraisal' threat during the final stage of the EDC process. The Americans certainly also made their interest in a British commitment quite clear to HMG. Lastly, the troops could be useful in influencing continental politics given the abstinence of Britain from the new supra-national institutions in Europe, like the ECSC. This last point was the most ambiguous one because Britain never managed to achieve a clear idea of the role its troops should play on the continent, as we will see later on.

Rather grudgingly, Britain finally accepted the formal commitment of troops to continental European defence which was embodied in the WEU Treaty: '*...Britain...will continue to maintain on the mainland of Europe, including Germany,...four divisions and the Second Tactical Air Force...She undertakes not to withdraw these forces against the majority of the High Contracting Parties...This undertaking shall not, however, bind her in the event of an acute overseas emergency. If the maintenance of the UK forces on the mainland of Europe throws at any time too great a strain on the external finances of the United Kingdom, she will...invite the North Atlantic Council to review the financial conditions on which the UK forces are maintained*'.<sup>22</sup> When this declaration was made, it was hailed as a great success for British diplomacy. The inconvenience this pledge would cause for Britain in the years to come probably contributed greatly to her later reluctance to participate in other supranational institutions in Europe.

The longterm political implications of the American and British commitments were only

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<sup>21</sup> See Mager (1990), pp.121-145.

<sup>22</sup> Protocol No.II on Forces of WEU, Art VI, 23.10.1954, in: HMSO, Cmnd.9498, Treaty Series, 1955.

vaguely grasped in 1955/56. The immediate problem which seemed to prevent the United States and Britain from withdrawing their troops at an early point was another one. Both countries had expected that the Europeans would themselves shoulder the burden of conventional defence for their territories, especially when the German army was ready. But during late 1955 and 1956 it became clear that the build-up would proceed slower than expected and a reduction of the Anglo-American contingents appeared to be an unacceptable political and military risk as long as a direct threat from the Soviet Union was perceived. In this situation the extension of German financial contributions towards the cost of their troops in Germany seemed a justified request to the stationing countries. They were all faced with fierce domestic criticism about the high cost of their military commitments. In the case of the troops in Germany, the difficulty was less the sheer budgetary cost. The major problem for the sending countries was the huge loss of foreign exchange caused by conversion of dollars, pounds, etc. into DM to pay for services called upon by the troops. To justify the necessary extension of the troop maintenance this financial burden had to be kept within certain limits, or better, completely neutralized.

Certain delays in German rearmament had been foreseen by the stationing countries. As they were unwilling to assume all of a sudden the whole cost of their NATO commitment, they had insisted upon including a clause in the NATO Finance Convention, signed in Paris, which guaranteed an extension of occupation payments for one year (until mid-1956) to cover the period until West German rearmament gained momentum. This extended scheme obliged Germany to pay altogether \$762m in monthly allocations on a sliding scale.<sup>23</sup> The NATO Finance Convention reserved the right for the allies to negotiate a further extension. The Germans, however, understood May 1956 to be the end of this kind of payments. Wrongly, as it turned out. The stationing countries argued that if a German army was not forthcoming fast enough, the Federal Republic should continue to pay rather than have a free ride on the Western defence machinery.

However, one of Germany's major objectives during the EDC debate had been to get rid of

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<sup>23</sup> FRUS 1952-54, V/2, NATO Finance Convention (amended), p.1342-43. A widely overlooked, but very relevant consequence of this agreement was that these payments and all the following offset payments remained part of the budget of the Ministry of Defence. Consequently all of these costs were seen as part of the German defence effort.



the occupation costs. Numerous quarrels between Bonn and the occupying powers had originated from this issue.<sup>24</sup> The termination of occupation and the coming into effect of the Paris Accords made further voluntary payments - in whatever form - unacceptable to any German government. Widespread public protest against the dismantling of German industries and the confiscation of goods and facilities by the victorious powers after World War II were still a political issue. Reminiscences of the humiliating reparations scheme in the Versailles Treaty after the First World War added to the negative symbolic value of occupation costs in German public opinion. This background provides an adequate understanding of the dogged German resistance to payments after 1955. To the Germans it seemed as if the proposed equality in the Alliance existed only in theory because other NATO members with foreign troops on their soil did pay no such contributions. Thus the cost of American and British troop maintenance very soon became one of the most serious problems in Germany's relations with these countries affecting political relations, national budgets as well as financial markets.

The following paragraphs outline the first conflict arising on the question, as well as the background behind the positions. As the by far most serious repercussions were on British-German relations, the analysis will concentrate on this issue. The fundamental economic and political issues behind the British position will be scrutinized. Then, I will attempt an assessment of the troop's influence on the German balance of payments, to be followed by an account of the first support cost negotiations 1955/56.

### c) The Impact of Troop Stationing in Europe on the British Balance of Payments

In December 1955, participating for the first time officially at the annual NATO Council meeting, the German delegation was up to an unpleasant surprise. Arguing with the slow pace of German rearmament and the heavy burden on their balance of payments, Britain, France, and the US demanded the continuation of payments for foreign troop maintenance in the

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<sup>24</sup> The issue is largely neglected by historical research. For some hints, see: Schwartz (1991), 270-273; Henzler, Fritz Schäffer, 1945-67. *Eine biographische Studie*, 1994.

Federal Republic for the period after May 1956.<sup>25</sup> The German ministers were shocked. The British minutes recorded that the German Finance Minister '*Dr.Schäffer (who was beginning to get heated) had to say that such a request was quite unacceptable to the Federal Republic. There was no legal basis for it, and it was open discrimination.*'<sup>26</sup> Later, Schäffer embarrassed the allies with public announcements that the demands were not in accordance with the NATO-Treaty and that he would strictly oppose any further payments. He stirred up a considerable press campaign and the first open row on the troop cost issue started.<sup>27</sup> It became largely a British-German affair. The British arrived at the conclusion that their military commitment in Europe was a danger to their economy, and in particular to their balance of payments. The Americans, though faced with a numerically much higher cost, still profited from the overwhelming strength of their trade and regarded the dollar losses caused by their troops with relative equanimity, as long as the overall balance of payments was under control.

The completely negative attitude of Schäffer touched on a core point of British postwar economic policy. All through the postwar decades, Britain went to great effort to safeguard and strengthen the traditional role of sterling as an international reserve currency. This became a primary, if not the most important, objective of British foreign economic policy after the war.

Many, many volumes have been written on the wisdom and folly of this policy, centring on the question whether Sterling policy was a decisive factor in Britain's relative economic decline<sup>28</sup>, and throughout the thesis there will be numerous references to this debate. A

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<sup>25</sup> FRUS 1955-57, IV, p.44-49; BA, B126/S1520, Record of a meeting Schäffer/Blank-Allied Defence Ministers, 16 December 1956.

<sup>26</sup> PRO, CAB 134/1048, MAC(G)55; Record of Ministers Meeting in Paris, 16.12.1955.

<sup>27</sup> FAZ 7.2.1956; THE ECONOMIST, 11.2.1956; SPIEGEL, 22.2.1956.

<sup>28</sup> The following list is necessarily selective. Additional works on the subject will be referred to throughout the text: Alford, *British Economic Performance, 1945-75*, 1988; Cairncross/Eichengreen(eds) *Sterling in Decline: The Devaluations of 1931, 1949 and 1967*, 1983; Cairncross, *The British Economy since 1945*, 1992; Dow, *The Management of the British Economy, 1945-60*, 1970; Milward, *The European Rescue of the Nation State*, 1992, p.347-95; Pollard, *The Wasting of British Economy: British Economic Policy 1945 to the Present*, 1982; Strange, *Sterling and British Policy*, 1971.

comprehensive analysis of British monetary policy during the 1950s and 1960s is, however, well beyond the scope of this study. Previous research will be summed up and a closer look will be given to the link between British security and sterling policies. The following section attempts to assess the influence of Britain's military commitment in continental Europe on its balance of payments, placing it in the larger context of British monetary policy.

A review of British foreign policy, prepared in 1956 on the highest levels, stated after listing up Britain's fundamental foreign policy objectives: *'There are many areas or aspects of policy in which a failure could make it more difficult for us to attain these aims. But there is one, success in which is a matter of life or death to us as country. This is the maintenance of the international value of sterling ... Success in this is the greatest single contribution we can make to the maintenance of our position in world affairs and to the success of the policies which the free world is seeking to pursue'*.<sup>29</sup> The document shows the curious mix of sentimental commitment, political motivations, and economic reasoning which was characteristic of British postwar monetary policy. During the heyday of the British empire, the international role of sterling had been one of the mainstays of British influence in the world and a valuable source of income for the city of London. Until the mid-1950s about 50% of all international transactions were still conducted in sterling and Britain managed the reserves of numerous countries which formed the so-called Sterling Area.<sup>30</sup>

The financial consequences of World War II, however, had seriously undermined this position. From the conference of Bretton Woods on, British monetary policy was directed towards regaining for its currency the traditional position. The expected co-management of international monetary relations together with the Americans, however, proved to be beyond the strength of Britain's economy. A first disastrous attempt in 1947 to establish free convertibility with the dollar had ended in a rush out of sterling and had shown that the task

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<sup>29</sup> 'The Future of the UK in World Affairs', CAB 134/1315, PR(56)3, 1 June 1956; in: Goldsworthy(ed), *The Conservative Government and the End of Empire, 1951-57*, pt.1, 1994, p.62-63.

<sup>30</sup> James, *International Monetary Cooperation since Bretton Woods*, 1996, p.90. To the Sterling Area belonged the countries of the Colonial Empire and many former colonies, like Australia, South Africa, India, Ireland, New Zealand, etc. See: Tew, *International Monetary Cooperation 1945-70*, 1970, p.180. On British Sterling policy see also: Schmidt, 'Großbritannien, die Gründung der EWG und die Sicherheit des Westens: "The American Connection"', in: Salewski M.(ed), *Nationale Identität und Europäische Einigung*, 1991, 169-231.

would be extremely difficult to accomplish. Even the 1949 devaluation against the dollar did not reestablish confidence in the British currency. The move towards free convertibility in dollars, envisaged in Bretton Woods, had to be postponed for an indefinite period. In the meantime, the chronically weak British currency was shielded against trouble by American help and by the European Payments Union.<sup>31</sup> Britain's financial policies in the 1950s were designed to escape from this dependence on other nations, and to accomplish a safe move towards free convertibility.

These objectives were undermined by recurring balance of payments problems and frequent waves of currency speculation against the pound, impeding the buildup of a sufficient level of reserves. Devaluation as a way out of this situation was ruled out. A complex mix of considerations related both to foreign policy and domestic economic objectives led to the rejection of a flexible exchange rate for the pound in the early fifties.<sup>32</sup> In the mid-1950s, the British government gradually became strongly committed to the rate of \$2.80/pound. It was to defend this rate until 1967 despite the increasingly higher cost of doing so.<sup>33</sup> The commitment to Sterling's fixed exchange rate compelled the government to a series of restrictive economic measures in the domestic economy and to constant efforts of trimming its external commitments in order to restore confidence in the currency. None of these policies was a decisive success. Sterling remained fundamentally weak.<sup>34</sup>

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<sup>31</sup> The EPU was an intra-European financial clearing mechanism designed to facilitate trade in Europe by multilateralizing the settlement of payments imbalances. Every month, bilateral balances between the member countries were set off against each other so as to establish an overall position of each country towards EPU. When a country's position was negative, it had to settle it by a mixture of debts and hard currency payments. This was very advantageous for a country which tended to have a huge deficit with the EPU-countries, like Britain. In the absence of EPU, the deficits would have had to be settled entirely by dollars or gold. Recently, the EPU as research subject has seen a surge of interest: Kaplan/Schleiminger, *The European Payments Union*, 1989; Eichengreen, *Reconstructing Europe's Trade and Payments: The EPU*, 1993; Dickhaus, *Die Bundesbank im Westeuropäischen Wiederaufbau 1948-58*, 1996.

<sup>32</sup> Milward, 'The Origins of the Fixed-Rate Dollar System', in: Reis (ed), *International Monetary Systems in Historical Perspective*, 1995, p.135-151.

<sup>33</sup> A comprehensive answer as to the reasons for this position must await an archive-based study of British monetary history after 1955. Some continuing lines in the arguments against devaluation were, however, political considerations with regard to the US and the Sterling Area countries, which were both against devaluation; fear of adverse economic effects at home; prestige reasons; fear of political damage for the ruling party; and the influence of the City.

<sup>34</sup> HMSO, *UK Balance of Payments 1946-1954*, Cmnd.9430, 1955, p.32-33. For a recent overview over British economic policy after the war, see: Cairncross (1992).

In the British government there was no lack of explanations for this situation. One factor, however, took on a specific importance in government discussions after 1955: military commitments abroad, and specifically in Europe. Losses attributed to British troop maintenance elsewhere, mostly in countries belonging to the Sterling-area, involved no foreign exchange component because payments were made in sterling. The European commitment constituted a drain on British reserves because of the need for huge conversions to pay for local services, German civilian employees, allowances for the soldiers, etc. The British government estimated the average annual foreign exchange cost caused by troop-maintenance on the European continent at about \$180m.<sup>35</sup>

Already in 1952, the Chancellor of Exchequer had stated categorically that he could take on at most a burden of \$84m arising from the commitment in Germany.<sup>36</sup> In 1955, the situation was, if anything, even tighter. The WEU pledge had greatly enhanced Britain's prestige on the continent. Unfortunately, it seemed to endanger a central goal of British policy: the accomplishment of a sound and stable monetary position for the pound. British politicians like Macmillan came to assign to the troop cost problem a central role in their policy towards Europe, especially when Germany's payments seemed to stop after 1956. They regarded German support cost payments as a just means to get back the foreign exchange Britain lost through the provision of security for Europe. The Federal Republic appeared to benefit greatly from allied troop-maintenance, boasting an impressive balance of payments surplus and an ever stronger currency. Hence the dogged British insistence in this matter. The question was reduced to a simple choice: a stable currency or troops in Europe, or -formulated differently- the choice between the political merits of troop maintenance in Europe and the interest in sterling stability. Ultimately, the choice was decided for sterling stability. The British government would rather incur the odium of prolonged and acrimonious negotiations with the Germans than take on the cost for the sake of vague political benefits. A tough policy seemed justified as Germany's economy was booming while Britain's was dragging on, thus putting further pressure on the pound. In the following paragraphs I will try to analyse whether the

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<sup>35</sup> See Appendix I, table 4.

<sup>36</sup> CAB 129/55, C(52)320, Defence and Economic Policy. Cabinet memo by Mr Butler, 3 October 1952, in: Goldsworthy(ed), (1994), p.35.

diagnosis of British politicians -troops in Europe or Sterling stability- corresponded to reality.

Prior to 1955, the UK was able to cover the foreign exchange need of its troops by drawing on the DM accumulated in the account for German occupation costs. Those funds also covered most of the budgetary cost. Contrary to the foreign exchange expenditure, this cost would have been the same if the troops would have been stationed in Britain. It might have been even less due to various allowances granted to allied forces in Germany in the Status of Forces agreements<sup>37</sup> and to the lower cost of living in Germany at that time.<sup>38</sup> The only way to get rid of this burden, therefore, was to disband the troops altogether which would have involved even more political explosive than 'simply' redeploying them. To get help for its budget was therefore for the UK government only a side issue in the support cost negotiations.

The real issue was the foreign exchange cost. It was this cost in the first place which caused most of the apprehensions in the British government regarding the termination of German payments. For the first period after the cessation of occupation payments Britain was still able to draw on accumulated, unspent funds in the occupation cost account. However, these funds would be used up quickly and from then on the Bank of England would have to purchase DM on the London exchange market for use of its Rhine Army.<sup>39</sup> According to the British government, this factor influenced the British balance with European countries negatively, impeded the UK to earn reserves, and forced the British to equal the balance by payments in

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<sup>37</sup> Those agreements regulated the conditions for the stay of foreign troops in the Federal Republic and accorded to the troops allowances like free use of buildings and territory, reduced telecommunication tariffs, tax exemptions, duty free petrol, and German assumption of damages caused by the troops. See: BA, B126/34103, BFM, Abt. IIE: Truppenvertragskonferenz, 7 December 1959. For a summary of the treaties: KCA 1952, p.12226-7; KCA 1960, p.17849 (a full version is in: Verträge der BRD, Serie A, vol.7(1957), nr.64, p.42-171; nr.65, p.172-221; nr.67, p.366-75; Supplementary Agreement in: *ibid.*, vol.20(1965), nr.228, p.142-467).

<sup>38</sup> Fried, in: Newhouse (1971), p.125.

<sup>39</sup> The British and French acquired the marks needed for their troops on the free market. The Americans presented each month dollar cheques at the Bundesbank to acquire DM at an agreed upon rate of DM 4.20. When the dollar in the late 1950s came under pressure, the Bundesbank protested against the continuation of this method (in case the market price of dollars was only one Pfennig lower than this official price -most of the time it was even less- then the Bundesbank lost \$150.000 a month due to the discrepancy between the two prices). In the context of the offset negotiations in 1961, the Bundesbank managed to get a compromise which meant that the price for troop dollars was fixed anew at the beginning of each month. For documentation on these issues, see: NA, RG 59, DF 1960-63, 862a.13.

the framework of the EPU. The EPU deficits illustrated in the table below had to be covered mainly by gold and dollars. This caused a direct drain on scarce British currency reserves. Thus went the prevailing interpretation in the British government.<sup>40</sup>

How far did this British analysis conform to reality? What was the troops' real impact on the British balance of payments? The following table compares the foreign exchange cost of the troops with the yearly British EPU position, where balance of payments movements with Europe were reflected. German support cost payments have been added.

Table 2:

Local foreign-exchange cost of British troops in Germany as compared to contributions received from Germany and to the British EPU position (\$ million)

	local foreign exchange cost of British troops (1)	contribution received from Germany(2)	net UK annual EPU position(3)
1954-55	216	431	+136
1955-56	193	196	-327
1956-57	179	95	-225
1957-58	176	140	-317
1958-59	160	34	-267
1954-59	924	896	-1000

sources:

(1) see Appendix I, table 4. These data have been selected from British primary source material. The documents offer, however, a wide range of estimates. The data chosen are those cited most frequently in the sources. They can, however, be regarded only as approximations. The foreign-exchange cost of troop-stationing in Germany depends very much on the method of calculation.

(2) Keesings Contemporary Archives, various editions; BGBL II, 17, 21.4.1959; BGBL II, 22, 30.5.1959.

(3) The column shows deficits or surpluses for every year, not the accumulated position. EPU, Final Report 1951-1958, OEEC, Paris 1959, p.36.

The table seems to underline the necessity of a continuation of German payments if British apprehensions outlined above were not to come true. However, for the period 1956-59 it is obvious that even if the troop commitment had been terminated and this would have had a corresponding impact on the British balance with Europe, the British EPU position would

<sup>40</sup> See for ex.: PRO, CAB 134/1209, Committee on Services' Cost in Germany, CG (56)4, Memo by the Financial Secretary to the Treasury, 25 May 1956.

have remained strongly negative. There also seems no direct relation between the decline of German payments and the negative British EPU position. It is necessary to emphasize at this point that a straightforward comparison of one factor in the account with an overall payments measure (for example military expenditure abroad to overall deficits) is, in any case, a rather ambiguous indicator.

How much foreign exchange would Britain have saved if it had redeployed its troops? On this point unanimity was never achieved in the British government and the range of estimates is not astonishing, given the many variables which would have to be taken into account.<sup>41</sup> A redeployment of over large parts or the whole of the Rhine Army including equipment would have effected other subaccounts of the mutual payments statistics. A contraction of domestic demand in Germany might have set resources free for exports, and the opposite effect might have happened in Britain. In addition, Britain had itself substantial foreign-exchange earnings from foreign troops on its soil, namely American and Canadian troops. Their expense amounted to an annual average of about \$200m, which easily matched the British cost in Germany.<sup>42</sup> A British redeployment from the continent was likely to provoke a movement of these troops as a reinforcement of allied troops in Germany.

One further problem was the sheer cost of redeployment. It has been already noted that it is doubtful whether stationing its troops in Britain would have saved the government money. Allied troops in Germany benefitted from a series of allowances and German wages for civilian employees were lower. The cost of redeployment would have put a heavy one-time burden on the British balance of payments. Furthermore, German payments would have stopped which would have caused an additional drain on the British budget if the redeployed troops were kept active. This was very probable as the troops were assigned to NATO and their dissolution needed the consent of NATO authorities. Finally, after the first reduction of 8000 men in 1957 Britain already had serious difficulties in housing the men, and this was one of the main reasons for not going on with redeployment in 1959. Hence, even if

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<sup>41</sup> For an example of the difficulties of such an estimate see PRO, CAB 129/91, Report by Officials: Local Defence Costs in Germany, 8 January 1958.

<sup>42</sup> Balance of Payments 1946-1956, Cmnd.9871, HMSO, October 1956, p.44.  
Balance of Payments 1956-1959, Cmnd.861, HMSO, October 1959, p.18.



redeployment would have saved foreign exchange, it also was likely to cause heavy additional burdens on the British government budget (the Americans were to have similar problems in the 1960s). Imponderabilities such as those cited above make it impossible to arrive at an exact quantification of the foreign exchange impact of troop stationing abroad.

However, in the last analysis the real extent of the burden the troops placed on Britain's external balances can be assessed only if its placed in the larger context of British monetary problems. Strikingly enough, the official British balance of payments looked rather positive until the mid-1960s. This did not prevent frequent rushes of speculation against the pound. These attacks which hampered all efforts by the British government to stabilize the currency denoted a fundamental lack of confidence in sterling on the markets. One major reason for the uncertainty about the position of sterling was the calamitous gap between British reserves and liabilities, the latter being always four times the size of the former.

Table 3: UK Current Balance, Reserves and Liabilities (in \$m)

	UK current balance	UK reserves (gold + foreign exchange)	UK total liabilities	liabilities to the Sterling Area
1953	+526	2518	11211	7834
1954	+638	2762	11701	8187
1955	-221	2120	11326	8061
1956	+652	2133	11463	8008
1957	+678	2273	10970	7302
1958	+977	3069	11133	7053

Sources: UK Balance of Payments 1946-1956(2), Cmnd.122, HMSO, April 1957.

UK Balance of Payments 1956-1959, Cmnd.861, HMSO, October 1959.

(UK Balance of payments statistics were subject to numerous, considerable revisions. Since the argument is about the contemporary perception, I choose corresponding statistics.)

This huge amount of liabilities is linked with the role of sterling as a reserve currency for the Sterling Area. Most of the claims against Britain were resulted from the war and were held by Sterling Area Countries, as the table shows. The commitment towards the Sterling Area countries or the almost identical Commonwealth was directly linked to the commitment to preserving the value of Sterling. Devaluation would have been a blow for most Sterling Area countries and their reserves. It would have been a disaster not only for British prestige, but

probably also for its trade as a larger share of British trade was still directed to the Commonwealth than to Europe.<sup>43</sup>

Assigning to sterling policy highest importance also underlined the importance of relations with the United States, because of Britain's ultimate dependence on American monetary support. All through the postwar period, Britain had to earn substantive sums to pay back loans from the United States or international organizations, like IMF, EXIM Bank, or EPU. Those amounted to about \$168m a year in the mid-1950s, growing precipitously after the Suez crisis and its disastrous effect on Britain's external balance.<sup>44</sup> Since the famous 1946 loan Britain had not been able to rid itself of its dependence on American money; this dependence was partly necessity but expressed also a political choice.

Because of this close identity of British Sterling policy with the pursuit of harmonious relations with the Commonwealth and the United States it was very likely that in the case that British monetary policy necessitated choices which touched upon the interests of foreign countries Britain would rather accept conflicts with the Europe of the Six than with the USA or the Commonwealth. The conflicts regarding troop costs offer many instances for this observation.

Numerous explanations have been put forward to account for the chronic weakness of sterling, such as the backwardness of the British economy and its organisations, the stop-and-go cycles to cope with payment deficits, expansive government policies at home and abroad, speculation, etc.<sup>45</sup> There is still much more empirical work necessary to clarify the mutual influences of British monetary policy towards its general economic conditions and vice versa. Crucial for this study is the impact of Britain's policy of priority for sterling on its relations with Europe, and in particular Germany. The quarrel about troop costs assumed its great importance because the British government and parts of the public assigned to the

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<sup>43</sup> 'The Future of the UK in World Affairs', CAB 134/1315, PR(56)3, 1 June 1956; in: Goldsworthy(ed), *The Conservative Government and the End of Empire, 1951-57*, p.1, 1994.

<sup>44</sup> Peden, 'Economic Aspects of British Perceptions of Power', in: Di Nolfo(ed), *Power in Europe II, 1992*, p.150-51.

<sup>45</sup> For an assessment of this debate: Alford (1988), p.74-88.

neutralization of the foreign exchange cost of the BAOR an important role in correcting the monetary predicament.

However, from the analysis above and almost all accounts of British postwar monetary policy<sup>46</sup> it emerges clearly that the cost of the troops in Europe was not a major cause for British monetary difficulties, as the British government continuously claimed. Its absence would not have altered the basic components of the British monetary position and its monetary policy. As it will emerge more clearly in the following chapters, the problem was of a fundamentally political nature. The 1955 commitment had been made in a unique situation conferring a series of political advantages to the United Kingdom. Thereafter, however, British politicians did not have a consistent strategy with which to capitalize on this commitment. Instead, it was resented as liability. This sentiment increased and decreased in parallel to the Sterling situation. Britain continued initiating quarrels with its European partners on this problem instead of solving the deeper roots of its balance of payments problem. Troop reductions in Europe or support cost demands were a popular subject, they seemed to demonstrate activity but they were in the last analysis just window-dressing. The reason for creating the conflicts over support costs and troop reductions was not only the need to acquire foreign exchange and to relieve the British budget. The fundamental cause was a deep ambiguity towards the political role of the troops in Europe which is derived from an indecisiveness in Britain's whole approach towards Europe, as will be shown in the following chapters. Support cost and troop level questions became issues of highly symbolic and political value and were an expression of basic lines of British policy in this period.

The monetary problems of Britain can not explain the tense climate and the serious discords that were to prevail throughout all the support cost negotiations. One has to also take into account the psychological situation of the United Kingdom as a winner of the war, now having to beg financial assistance from their former enemies, whom the British forces moreover provided with military protection. This gave the support cost question a particularly hostile twist which should not be underestimated. A perusal of the extensive documentation on the support cost negotiations makes it impossible to ignore this sentiment. It formed the

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<sup>46</sup> An exception is, for example, Chalmers, *Paying for Defence*, 1985.

background of British frustration on the issue and expressed itself in acid statements against Germany's resistance to pay for its protection. *'The British people, who after all won the war, cannot accept that the Germans are treating the UK like dirt, while they have things their own way. They will not agree to keeping British soldiers in Germany, if the Germans do not play the game.'* Macmillan said to Dulles, and added somewhat prophetically: *'It may take a little longer for the US, but ultimately the US may feel that way, too!'*<sup>47</sup>

#### d) Foreign Troops and the German Balance of Payments

The British sentiment on the monetary consequences of their troop presence in Germany has been shown to be more politically motivated than to be underpinned by sound economic reasoning. A further claim, by all former occupation powers, was that the Federal Republic massively benefitted from the presence of foreign troops on its territory. This is the assertion that has to be tackled now.

From 1954 on, the German balance of payments showed a continuing surplus. This was especially due to a large surplus in Germany's trade balance. An almost equally important factor, however, has been mostly ignored by research: the increasing foreign-exchange receipts from foreign troops, notably the Americans. These receipts had a huge influence on the German balance of goods and services, particularly after the termination of occupation payments. At the end of 1959, when the increasing deficit of the American balance of payments focussed attention on the reasons for the German surplus, the *Bundesbank* prepared a report which investigated the influence of the foreign troops on the German balance of payments.<sup>48</sup>

Between 1950-1959, Germany acquired an amount of almost 16.5 billion marks (\$3926m) in foreign exchange from foreign troops on German soil, despite the occupation- and support

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<sup>47</sup> FRUS 1955-57, IV, Memo of conversation, 11 December 1956, p.127.

<sup>48</sup> Bundesbankarchiv, B330/Bd.10161: Vermerk: Die Bedeutung der Deviseneinnahmen von fremden Truppen für die Entwicklung der Zahlungsbilanz und der Währungsreserven, 4 December 1959.

costs paid to the stationing countries during this period.<sup>49</sup> 60% of these receipts accrued in 1957-59. Dollar-exchanges by American troops alone formed 87% of the amount. The British Army of Rhine (BAOR) exchanged Sterling to the tune of 1.3 billion marks (\$309m). Compared with the accumulated trade surplus of Germany over the period (\$5095m), the importance of these receipts for the German external financial position becomes very obvious.

Table 4:

Development of German Balance of Services and receipts from foreign troops (\$ million)

	Balance of Services	receipts from foreign troops	balance of services, excluding troop receipts	trade balance
1950	+123	+50	+73	-714
1951	+218	+87	+130	-24
1952	+388	+202	+185	+167
1953	+384	+271	+113	+595
1954	+306	+243	+62	+643
1955	+405	+292	+114	+286
1956	+619	+418	+201	+690
1957	+816	+633	+183	+976
1958	+705	+923	-218	+1190
1959	+401	+805	-404	+1286
1950-59	+4365	+3926	+439	+5095

Source: see fn.48. Table 5, Appendix I is from a similar, later document with slightly lower figures for receipts. For the trade balance: Bundesbank(ed), 40 Jahre DM. Monetäre Statistiken 1948-87, 1988, p.5.

The German balance of payments 1950-1959 had an overall surplus of about DM 40billion (\$9524m). Theoretically this amount would have been almost halved were it not for the presence of foreign troops in Germany. The receipts were booked in the German balance of services, which saw a surplus of about 18.3 billion marks (\$4365m) in this period. The Bundesbank also compared these foreign exchange receipts with the reserves in gold and foreign exchange the Federal Republic accumulated between 1950 and 1959 (DM21.8 bn;

<sup>49</sup> American sources put the figure for dollar exchanges above German payments, steeply rising after 1956, at DM 15392.7m (\$3665m) between 1945 and 1960; this corresponds roughly with the Bundesbank figure. See: Browder, *The GI and the Wirtschaftswunder*, in: *Journal of European Economic History* 22, 3/1993, p.610.

\$5190m). The Bundesbank concludes that '*a considerable part of the augmentation of German monetary reserves can be attributed to the stationing of foreign troops in the Federal Republic.*'<sup>50</sup> These figures are related only to the troops' impact on the German reserve position. Research on the overall economic consequences of foreign troop stationing in Germany is at a very preliminary stage. It is clear, however, that the impact was considerable, on the micro- as well as on the macro-level. For example, US forces counted among Germany's largest employers during the 1950s.<sup>51</sup> For many cities and regions, foreign garrisons remain an outstanding economic factor until today.

As in the case of comparing British troop costs to overall balance of payments statistics, certain reservations also have to be made in the case of German receipts before establishing too straightforward an interpretation of the monetary impact. It is impossible to calculate the exact extent of the commitment of German economic resources for services to foreign troops.<sup>52</sup> How did these claims impede the German ability to employ these resources elsewhere, for example in export-oriented industries? Many costs are not reflected in foreign exchange calculations, for example the use of huge areas for military training purposes, housing and facilities. Where would the German workforce, whose services made up the biggest part of the troop's foreign exchange cost<sup>53</sup>, have been employed? In this context one might recall that during the 1950s and 1960s serious labour shortages existed in Germany. Immigrant foreign workers solved the problem; however, money transfers to their home countries became a negative factor in the German balance of payments. Complicated side effects like these prevented any agreement between stationing and host country on the exact extent of the foreign exchange cost (for such an attempt, see ch.XI). Usually, however, the Federal Republic accepted the figure presented by its allies.

Despite these reservations, it is undeniable that allied troop maintenance played a considerable

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<sup>50</sup> BBA, B330/10161, Vermerk....., 4 December 1959.

<sup>51</sup> Browder (1993), p.601-612.

<sup>52</sup> Mendershausen, *Troop Stationing in Germany. Value and Cost*, 1968, p.85; Fried, in: Newhouse(ed), 1971, p.127-9.

<sup>53</sup> About half of the foreign-exchange cost was caused by civilian labour. Other services and exchange by soldiers amounted for the rest. See: PRO, CAB 134/1209, Committee on Services Cost in Germany, C.G.(56), 6.6.1956.

role in the accumulation of German balance-of-payments surpluses. It provided Germany, which had suffered from a critical dollar shortage until the early 1950's, with sufficient liquidity for debt repayments and vital imports, particularly from the dollar zone, without impeding domestic investment. This clear monetary gain would, however, rapidly become a political liability.

e) The Support Cost Negotiations 1955/56<sup>54</sup>

During 1955, the BAOR made provisions against the cessation of occupation costs. Considerable savings were achieved, facilitated by the fact that during the occupation regime, due to abundant German payments, British troops had lived on a 'somewhat more generous scale than elsewhere'.<sup>55</sup> Nonetheless, and despite warnings by the Foreign Office as to the potential of political conflict in the question, a majority in the British government pressed for German payments to continue. All through 1955, sterling had been under great pressure and the year-end balance showed a considerable deficit.<sup>56</sup> The prospect of having to assume from May 1956 on, when German payments ceased, an additional foreign exchange burden of perhaps up to \$200m seemed intolerable. A further inconvenience was the hardening of the EPU, effected in August 1955, which meant that debtors had to repay now 75% of their debt in gold or hard currency as opposed to the previous 50%. As troop costs were reflected in the EPU accounts this meant that any drain would have to be met mostly by hard currency.<sup>57</sup>

When the German reply to the 'NATO-questionnaire' 1955 on Germany's military build-up proved unsatisfactory, the time was deemed ready by the British government. It urged the United States to join in a common action asking for an extension of support payments by

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<sup>54</sup> Those and the following negotiations received a first treatment by W.Kaiser, 'Money, Money, Money', in: Schmidt G., *Zwischen Bündnissicherung und privilegierter Partnerschaft*, 1995, p.???. His account is useful regarding the details of the negotiating process.

<sup>55</sup> PRO, T225/424, Treasury Memorandum, 25 July 1955; CAB 134/1209, Committee on Services Cost in Germany, memorandum, May 1956; for the extent of the savings, see table 2.

<sup>56</sup> Dow (1970), pp.89-90, 255.

<sup>57</sup> PRO, T225/424, Treasury Memorandum, 25.7.1955.

Germany.<sup>58</sup> This proved to be more difficult than expected. The Americans adopted a very hesitant attitude based on a clear perception of the political difficulties new requests would cause for the German government. A certain unease at the prospect that the United States would have to settle the bill in the end by further aid to Germany also may have played a role.<sup>59</sup> However, the growing impression that the Federal Republic was not doing enough for rearmament finally led to an acquiescence of the United States to British demands. The NATO-meeting in December 1955 seemed a convenient moment but, as we have seen, the action proved abortive. The Germans, represented by their hard-nosed Finance Minister Schäffer, refused to concede any legal right for further support costs to the allies.

After the inconclusive meeting between Schäffer and the allied delegations, official requests were formulated by the Three Powers despite Germany's openly voiced opposition to negotiations. The British Aide-Memoire flatly rejected Schäffer's argument that Article IV/4 of NATO Finance Convention excluded any further cash payments.<sup>60</sup> It warned of rising domestic pressure in Britain towards reductions in the BAOR should Germany continue to resist payments; and it hinted explicitly at the low level of the German defence effort. A rapid start to negotiations on support costs was demanded.<sup>61</sup> The Aide-Memoire did nothing to alter the Federal Republic's opposition. The Germans rejected the contention that they spent less on defence than all the others and pointed to the fact that nobody requested payments from other countries with NATO troops on their soil.<sup>62</sup> This they felt to be utter discrimination.

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<sup>58</sup> An extensive account of the support-cost negotiations of 1955/56 and the events leading up to them is included in PRO, CAB 134/129, *An Account of the Negotiations leading up to the Agreements...on Support for the Forces in the Year 1956/57* (Hoyar Millar to Lloyd), 3.8.1956. The debate about the German response to the NATO-Questionnaire of 1955 already showed the difficulties German ministries had in projecting a reasonable plan for the military build-up. See: Greiner, in: MGFA III, pp.642-656.

<sup>59</sup> Kaiser (1995), p.4-6.

<sup>60</sup> PA-AA, MB 301, vol.62, *Aide-Memoire UK to German Government*, 26.1.56. Art. IV/4 of NATO Finance Convention contained a declaration of intent by Germany that, after the end of the occupation period, it would be ready to talk about further support '(e.g. goods and services)' with the stationing countries.

<sup>61</sup> *ibid.*

<sup>62</sup> BA, B126/34100, *Finance Ministry Memo on Stationing Costs*, 21.6.1956.



Mutual irritation mounted considerably during the first months of 1956 as both sides used the press to put pressure to back their arguments. The matter became an issue of wide public debate in Britain and Germany.<sup>63</sup> The United States increasingly feared over the prospect of a serious deterioration in British attitudes towards Germany which might have damaging effects on other policy areas: *'When their reserves decline, they become very sensitive about various policies. Their financial difficulties affect all of their policies and contribute to their position on such matters as Common Market.'*<sup>64</sup> The Americans decided to take a tougher stance and agreed on a common presentation of the three allied ambassadors at the *Auswärtiges Amt*, with their ambassador, Conant, taking the lead. He accused the Germans of leaving it to others to pay for its defence.<sup>65</sup> All three ambassadors demanded 'real' offers by Germany which until then had suggested only to permit a more liberal use of the occupation cost account and to increase its weapon purchases abroad (on the economic reasoning behind this offer, see ch.II).

Still the German position, represented by Schäffer, did not change. Dulles, Mollet, and Eden wrote to Adenauer expressing their concern about the Federal Republic's stance.<sup>66</sup> At this point, it became obvious to Adenauer that the issue might do lasting harm to British-German relations. Schäffer came under increasing attack from his colleagues for his stubbornness.<sup>67</sup> Adenauer ordered him to stop any further public comment on the issue.<sup>68</sup> He and Foreign Minister von Brentano came to the conclusion that a serious offer was unavoidable in this

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<sup>63</sup> BA NL Blankenhorn, 60, Letter Blankenhorn to Adenauer on conversation with Steel, 20.2.56; *ibid.*, 61/1, Letter Kirkpatrick to Adenauer, 13.4.56; FAZ, 7.2.1956.

<sup>64</sup> FRUS 1955-57, XXVI, Telegram from the North Atlantic Council Meeting, 17.12.55, p.62.

<sup>65</sup> PRO CAB 134/129, *An Account...*, 3.8.1956; BA, B126/34100, Finance Ministry on Representation made by Allied Ambassadors, 2.3.1956.

<sup>66</sup> BA, B136/3131, Mollet to Adenauer, 26.4.1956; Dulles to Adenauer, 26.4.1956; *Kurzprotokoll Kabinettsitzung*, 25.4.1956.

<sup>67</sup> *'I believe that the Finance Ministry's proposal about further US foreign aid was misplaced and therefore I have not been astonished by the reaction. Furthermore, the handling of the support cost question was, I think, not very skillful'*, von Brentano to Adenauer, March 1956, in: Baring(ed), *Sehr verehrter Herr Bundeskanzler*, 1974, p.188; see also: LES, Erhard-Adenauer correspondence, Erhard to Adenauer, 29.2.1956.

<sup>68</sup> BA, B136/3131, Adenauer to Schäffer, 2.3.1956.

situation.<sup>69</sup> Consequently, the Finance Ministry was relieved of its responsibility for the question and the Foreign Ministry took over. This did not, however, impede the Finance Minister from continuing with the strongest resistance. His position was motivated by electoral concerns and by the realistic expectation that in the run-up to the 1957 Federal elections, the reserves he had accumulated would be mercilessly plundered by domestic as well as foreign demands.<sup>70</sup>

At the end of April, von Brentano went to London for consultations. The support cost issue turned out to be the central point of discussion.<sup>71</sup> The Germans were now prepared to offer Britain \$83m cash and an advance payment of \$107m for arms purchases. They intimated that they preferred to continue the talks bilaterally so as to avoid another staging of the three allied ambassadors at the AA.<sup>72</sup> The British, exasperated by the slow progress of the talks which had been going on since February, agreed to bilateral talks. They rejected the cash offer and insisted upon \$143m. Forcefully, they made the Germans aware of the political importance of the subject. The AA minutes noted: *'Warning by the Chancellor of the Exchequer that we are heading towards a catastrophe -break-up of NATO, pullback of British troops- if solution is not found very rapidly. Very heavy strains in German-British relations due to this problem ... if the support cost question were solved, we could count upon a real intensification of economic and political relations between both countries'*.<sup>73</sup>

However, it soon became clear to the British that a sum larger than the year before was not attainable because of the results of Germany's parallel negotiations with the United States,

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<sup>69</sup> BA, NL 239 v.Brentano, 156/5, v.Brentano to Adenauer, 13.4.1956; *ibid.*, 156/6, v.Brentano to Adenauer, 20.4.1956. The attacks from abroad also centered increasingly on Schäffer: *'He [Dulles] knows how difficult these things were, particularly when a government had such a good finance minister'*; Conversation Adenauer - Dulles 12.6.56, in: FRUS 1955-57, XXVI, p.114. Schäffer even threatened to resign, but in the decisive cabinet meeting he and Strauß were overruled on the support cost question, see: BA, B 102/51520, Schäffer to Herwarth, 9.2.1956; BA, B102/51521, note on cabinet meeting, 8.6.1956.

<sup>70</sup> Henzler (1994), p.513-23.

<sup>71</sup> PRO, PREM 11/1366, WG 1051/1146: Record of Conversations Macmillan - v.Brentano, 30.4.1956; BA, NL Hallstein, 128, notes of conversations in London, April 1956.

<sup>72</sup> PRO, T234/30, Adenauer to Macmillan, 26.4.1956; PA AA, Ref.301/95, memorandum, 25.5.1956.

<sup>73</sup> PA-AA, Ref.200, Chancellor/Foreign Minister Visits, vol.4: memo on v.Brentano Trip to London, 5.6.1956.

France and other countries. The Americans, with their much larger force, had accepted an amount of only \$155m.<sup>74</sup> Even this had been approved by the German cabinet only after very strong pressure by the US government and against the continued resistance of Schäffer who spoke of an 'eternalization of the occupation statute'.<sup>75</sup> Finally, Britain settled for \$95m (£34m) cash payments and a secret declaration of intent by the German government to buy arms to the amount of \$524m in the year ahead.<sup>76</sup> Altogether Germany paid a total of \$357m (DM1.5bn) to the stationing countries. Their requests had been \$571m. Payments in the previous year had amounted to \$762m.

The agreement was criticized in both parliaments. British parliamentarians decried that the payments fell far short both of previous payments and the actual cost of the troops. Several speakers demanded a withdrawal of the BAOR.<sup>77</sup> In the Bundestag, von Brentano met the attacks of the opposition arguing that it had been a test case of Germany's international reliability. He stated that he had left the allies in no doubt that these would be the last payments.<sup>78</sup>

The monetary consequences were minor. The balance of payments problems remained. The troop cost problem, however, had entered the stage of British-German relations as an increasingly disturbing factor. The poisoning of mutual relations was therefore the most important consequence of the whole affair, *'which bid fair to do more damage to Anglo-*

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<sup>74</sup> PRO CAB 128/30, cm 45(56), 21.6.56. The US talks were concluded quickly to spare Adenauer at his US visit in June a discussion on this problem. For the results of these talks see Aide-Memoire US-Embassy to AA, 6.6.56, PA-AA Ref.301/95; France received \$66m after having to admit that 30,000 of its troops destined for NATO were engaged in Algeria: see PA AA, Ref.301/95, 28.5.56. This relatively generous treatment was criticised in the British press and parliament. Belgium received \$29m and Denmark, the Netherlands and Canada also secured small amounts. For details, see Appendix: Support Cost- and Offset Agreements.

<sup>75</sup> BA, B126/51521, Memorandum Finance Ministry, 8 June 1956; B126/34100, Excerpt of the 137th Cabinet Meeting, 6 June 1956.

<sup>76</sup> PA-AA, Ref.301/95, Aide-Memoire UK to Federal Government, 29.6.1956; PRO, FO 371/124616, v.Brentano to British Embassy Bonn, 29.6.1956.

<sup>77</sup> Hansard, House of Commons, 5th series, vol.555, p.866-70. The press echoed this criticism. The TIMES called the agreement 'deeply disappointing' (30.6.1956) and the ECONOMIST spoke of a 'sad effort' (7.7.1956, p.13-14).

<sup>78</sup> Verhandlungen des Deutschen Bundestags 2. Wahlperiode 1953-57; 155. Sitzung, p. 8416 B.

*German relations than any single issue for a long time.'*<sup>79</sup> It would have been tolerable if the problem had now ceased to exist. But it persisted, and the proposed weapon purchases proved to be a vain promise. The delay in German rearmament increased allied discontent with the agreement.

The Germans, on the other hand, felt that the agreements had done little to secure a stable troop presence, and rumours of renewed requests were reported during summer. When these proved to be true, the FRG had even more difficulties to resist than the year before. Germany felt obliged to continue payments which closely resembled occupation costs and as such were highly criticised by the public. The fact that the German government on the whole had been defeated over the issue, permits the highlighting of another characteristic of postwar policy for which the support cost negotiations are an excellent indicator. They became a continuing reminder of Germany's status of 'semi-sovereignty' after 1955. It was not only the restrictions of the Paris Accords but also the fact that Germany had voluntarily accepted dependence on a continued allied troop presence, which was to foster a strong compliance of Germany to the allies in other fields. Until the formulation of '*Ostpolitik*' in the late 1960s, Germany was to cope with the dilemma that, compared with its Cold War rhetorics, its actual contribution to defence remained relatively low, provoking financial requests from the countries which guaranteed its security.

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<sup>79</sup> PRO CAB 134/129, An Account, 3.8.1956.

## CHAPTER II

### THE GERMAN REARMAMENT CRISIS 1956

The support cost problem had been hardly solved, and in a manner that was unsatisfactory to all participants, when West Germany was put in the dock again: this time it was the delay in its rearmament program. It had to admit openly that its ambitious plans were unrealistic and that the build-up of a German army would proceed much slower than promised during the EDC negotiations. This failure became the basic argument for a continuation of German payments to support allied troops. This is an essential background to the burden-sharing discussion during the mid-1950s. What were the reasons for a development which surprised most observers? Which consequences followed for the sharing of the defence burden? In answering these questions I will concentrate less on the details of the rearmament process and the protracted practical problems which accompanied it;<sup>1</sup> indeed, my main intention is to outline the broader political and economic reasons for the delay and how they influenced the support cost debate. The chapter also points out some fundamental political and economic factors underlying West Germany's remilitarisation in the 1950s.

Initial rearmament plans had foreseen the build-up of a 500.000 man army within the period 1955-58. Despite deep doubts in the Finance and Defence Ministries as to the practical feasibility of this endeavour, Adenauer personally promised the Americans to keep to the schedule as agreed.<sup>2</sup> Already by the end of 1955 it had become quite clear to the German government that this was a very optimistic commitment. In public, however, it incessantly reaffirmed its intention to create the promised forces within three years.

Yet, there was never a coherent overall plan for the financing of the rearmament effort. The German government clung to the planned allocation of DM 9bn(\$2143m) a year which had been previously fixed during the early 1950s, despite great uncertainty about whether this sum

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<sup>1</sup> On these issues see the three volumes *'Anfänge Westdeutscher Sicherheitspolitik'* (ed.MGFA). The fourth volume by Abelshauser/Schwengler unfortunately appeared after completion of this thesis.

<sup>2</sup> BA, B136/2163, Schäffer to Adenauer, 31.8.1955; Conversation Schäffer-Tuthill, 23.7.55; Adenauer to Conant, 5.9.55.

was adequate. As regards the rest of the bill generous help by the Americans was hoped for. How big this 'rest' was remained secret to all participants. In any case, German hopes that US aid would cover much of the cost were wiped out by a sharp US Aide-Memoire in early 1956. It stipulated the end of grant aid to the Federal Republic on the grounds that the Germans were not doing enough for rearmament.<sup>3</sup>

Not surprisingly, the financial plans were revised continually during 1955/56. The projected cost shrank, for example, from January to June 1956 from DM 45bn (\$10.7bn) to DM 32bn (\$7.6bn).<sup>4</sup> Earlier, some estimates had predicted figures of DM60-80bn and more.<sup>5</sup> These downward revisions reflected the pessimistic view of the Finance Ministry about the available funds and the time schedule of the enterprise. At no time the allies were able to obtain a clear picture of German financial planning. No wonder, inside the German government itself nobody apparently had a real idea of how much rearmament would cost. It just became ever more obvious that there would be a certain delay.

This was not due to a lack of money. In 1954 the following funds were earmarked for the successive four years: the amount in the so-called *Juliusturm* (\$1.2bn)<sup>6</sup>, the US Nash-list grants(\$0.95bn), and the budgetary provision (\$8.57bn).<sup>7</sup> Of the \$4286m set aside for rearmament in 1955 and 1956, however, only \$194m were spent before the end of 1956. \$1267m were used for occupation costs and offset payments (see table 5). The rest was simply added to the *Juliusturm*. The German argument that the continuation of support cost payments would endanger rearmament or that rearmament would seriously damage the economic progress of Germany seemed, in view of these figures, quite exaggerated.

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<sup>3</sup> BA, NL Blankenhorn, 61b/1, US Aide-Memoire to Germany, 15.3.56.

<sup>4</sup> BA, B 126/51520, BMF Memo on Defence Planning, 25.1.1956; BA, B126/51521, Memo BMF: Verteidigungsfinanzierung, 28.6.1956.

<sup>5</sup> Abelshauser, 'The causes and consequences...', in: Heller/Gillingham(eds), 1992, p.317-18.

<sup>6</sup> The 'Juliusturm' was a large amount of unspent funds accumulated by the Federal government due to unexpectedly high tax revenues and the delay in rearmament. It was named after the tower in Berlin where the German Reich deposited French reparation payments after the 1870/71 war.

<sup>7</sup> Abelshauser, in: Heller/Gillingham(eds), 1992, p.316; Greiner, *Die militärische Eingliederung der Bundesrepublik Deutschland in die WEU und in die NATO, 1954-57*, in: MGFA III (1993), p.641-658.

Table 5:  
Allocation of German Defence Funds 1955 - 1956 (in million \$)<sup>a</sup>

	Defence budget allocation	Occupation and Support-costs	Research, damages	Purposes not related to defence	Balance (Budget minus expenditure)	Amount spent for rearmament
1955	2143	867 *	42	857	381	24
1956	2143	400	12	429	1286	170 *
1957	2143	n.a.	n.a.	n.a.	n.a.	n.a.

\* occupation costs until May 1955: \$152m; support costs until 31 March 1956: \$714m.

\* until 31 October 1956.

When the German government realized that it would soon have to admit the awkward truth about the delay, Adenauer looked for a scapegoat in the form of a political sacrifice. In the summer of 1956, the Minister of Defence, Blank, had promised NATO in writing that all force goals could be kept to. At the end of October, however, the Federal Government had to put its cards on the table. To 'spare' Blank embarrassment, a new defence minister was installed shortly before the Annual Review meeting of NATO. This was Franz-Josef Strauss who had been coveting the job for years.<sup>9</sup>

Finally, in autumn 1956, Germany's NATO partners were confronted openly with what they had already suspected. The first announcement was that the German conscription period would be reduced from 18 to 12 months. Publicly, the government justified this with allied troop reduction plans.<sup>10</sup> Internally, Adenauer stated his own purpose: he was well aware of the unpopularity of long military service in West Germany and undertook the move with a view to the next elections.<sup>11</sup> In his secret speech at the NATO Annual Review meeting in October, Strauss cited the difficult psychological situation of a demilitarised and defeated

<sup>9</sup> BA NL Blankenhorn 70/3/145-146, Memorandum of Finance ministry on Defence expenditure, 7.12.56.

<sup>9</sup> BA NL Blankenhorn 67/1/34, Letter Blankenhorn to Adenauer, 9.10.1956; Strauß, *Erinnerungen*, 1989, p.268-284; Schwarz, *Adenauer. Der Staatsmann 1953-67*, 1990, p.270-274; Greiner, in: *MGFA III* (1993), p.764-65.

<sup>10</sup> BA NL Blankenhorn 63/85, Federal government press-release, 27.9.56.

<sup>11</sup> Buchstab(ed), *Adenauer: Wir haben wirklich etwas geschaffen. Die Protokolle des CDU-Bundesvorstands 1953-57*, 1990, 20.9.1956, p.1031.

country which rendered military service unpopular.<sup>12</sup> The step, publicly announced without consulting Bonn's NATO allies, met with strong criticism from the Americans and British.<sup>13</sup>

Furthermore, Strauß informed his colleagues, procurement planning for the German forces would be stretched to take into account the requirements created by new strategic developments and the latest technological advances.<sup>14</sup> The most sensitive announcement was the admission that the build-up of the promised conventional army would be delayed; this delay would occur despite the well-known huge stockpile of unspent money Schäffer had accumulated. The Federal Government had informed the United States already before the NATO meeting that manpower targets were to be reduced to '80.000 instead of 96.000 by the end of 1956 and to between 175.000 and 200.000 by the end of 1957'.<sup>15</sup> Strauß, in his speech, gave an even smaller figure. The following table summarizes the numerous revisions of force goals in internal German estimates and compares them with the actual progress made.

Table 6: Revision of Force Goals For German Forces, 1955-56

Projected Force goals on:	Plan of October'55	December 1955	January 1956	March 1956	November 1956	Actual build-up
31.12.56	97.000	96.000	87.000	96.000	75.000	67.971
31.12.57	271.000	270.000	220.000	270.000	135.000	120.000
31.12.58	606.100	480.000	417.000	488.000	165.000	184.000
31.12.59	-	605.000	583.000	-	343.000(3/61)	248.000

Sources: Greiner, in: MGFA III, p.650,656,752-54,771,787; NHP, Defence Ministry note, January 1963.

<sup>12</sup> BA NL Blankenhorn 68/2/107, Draft of Speech at NATO Council, 22.10.56.

<sup>13</sup> *ibid.* 67/1/33, Letter Blankenhorn to Adenauer, 9.10.56; FRUS 1955-57, IV, Memo of Discussion at the 284th NSC Meeting, 10 May 1956, p.80. The Americans had tried in vain to warn the Germans of the consequences of a shorter military service; FRUS XXVI, 1955-57, p.93-98, conversation v. Brentano-Dulles, 4.5.1956 and conversation Strauß-Elbrick, 14.5.1956.

<sup>14</sup> as fn.12. Strauß meant the discussion about the 'New Look' in the Eisenhower administration and the massive equipment of US forces in Europe with tactical nuclear weapons.

<sup>15</sup> FRUS 55-57, XXVI, Amemb Bonn to DOS, 16 October 1956, p.168.



As to the reasons for these revisions, Strauß put particular emphasis on problems of accommodation as a result of the stream of refugees to Germany and on the generally antimilitaristic mood in the country.<sup>16</sup> The German defence minister reaffirmed his government's determination to attain the planned strength of its army; unfortunately, there would be an unspecified delay.

The rearmament crisis placed Germany in an awkward position. After all, rearmament had been the prize for the Federal Republic's sovereignty. It appeared that Germany, having achieved its political objectives, was now shirking its commitments. NATO-ambassador Blankenhorn wrote: *'At all events, we should avoid the impression that the delay in the build-up, which we cannot deny, is taking place only because we don't want to impede the extraordinary economic progress of the Federal Republic. It will be difficult, in any case, to counter the argument that in this and the next year we will make much less of a sacrifice for defence than other nations and that therefore the support cost question should be dealt with again.'*<sup>17</sup>

Blankenhorn was right. West Germany's NATO partners were very irritated. The official German arguments did not convince them, particularly after they had fought so long to make rearmament politically possible. They saw German rearmament not only as a gain for Western security and as a step towards integrating the Federal Republic in the Western Alliance, but also as an essential step in sharing the Cold War burden (see ch.I). Supplementing their own conventional troops partly with German forces had been a major aspect of the EDC debate. This prospect was, at least temporarily, delayed to a future date. Acheson's idea of utilizing the German economic potential seemed, once more, far from being fully implemented. Frustration understandably ran high, fueled by the very satisfying performance of the German economy while other NATO partners struggled with the defence burden.

An additional source of irritation was the delayed business for the armaments industries in

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<sup>16</sup> BA, NL Blankenhorn, 68/2, Draft of Strauss Speech at NATO Meeting, 22.10.56.

<sup>17</sup> BA NL Blankenhorn, 67/1, Letter Blankenhorn to Adenauer, 9.10.1956.

the US, France and Britain. Satisfying the presumed need for military equipment for the twelve planned German divisions had been a silent hope of all three governments. With the allocation of nine billion marks a year from 1955 onwards for the purpose of rearmament in the Federal budget a wave of orders for military equipment was expected to materialize soon (see ch.V). The most important aspect of this affluence was, however, that a fast build-up of the army was obviously not impeded by lack of money. Whereas the United States and Great Britain seemed more and more stuck with their troops in Europe, Germany appeared to be mainly concerned with accumulating foreign exchange reserves instead of creating a strong conventional army. It comes as no surprise that this situation had a decisive impact on the support cost debate.

What were the real reasons for the rearmament crisis? The causes for the failure were more complex than the official announcements suggested. One important factor was the delay in making a decision about the whole political organisation of the defence effort, caused by the defeat of the EDC project. As a result previous plans for the organisation of rearmament became obsolete.<sup>18</sup> Blueprints for the form of the German military contribution were extremely sketchy in 1955. Necessary legislative action by the Federal government had to be rushed through parliamentary procedures. This was not easily done. The whole rearmament process was strongly criticized by the Social Democrats, supported by a strong popular movement against rearmament.<sup>19</sup>

A second part of the problem was a 'practical' one. Although abundant funds were available for the years 1955-58, it was not easy to spend them in a reasonable way. Delays in building barracks, difficulties in acquiring land for them, the slow taking in of recruits, - all these were problems stated by the Germans as reasons for the unspent money.<sup>20</sup> Allied troops occupied much of what remained of prewar barracks and training areas. There was certainly also

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<sup>18</sup> Abelshauser, in: Heller/ Gillingham, 1992, p.312.

<sup>19</sup> On domestic opposition to German rearmament: Volkmann, 'Die innenpolitische Dimension Adenauer'scher Sicherheitspolitik in der EVG Phase, in: MGFA II, 1990, p.235-604; Ehlert, 'Innenpolitische Auseinandersetzungen um die Wehrverträge 1954-56', in: MGFA III, 1993, p.235-560.

<sup>20</sup> BA NL Blankenhorn, 68/2, Speech of Strauss at the NATO-Meeting, 22.10.56; see also: Greiner, in: MGFA III, 674-675.

considerable disorganisation within the German defence ministry and in the cooperation between the ministries. All these bottle-necks contributed to the delay; yet, in the end, they were not decisive. The major causes for the rearmament crisis were fundamental doubts about the economic and military conditions of a conventional buildup.

On closer view, it comes as no surprise that conventional rearmament was suddenly no longer a first-range priority for West Germany. Germany was now integrated into and protected by the Alliance. Thus, it had achieved its basic foreign policy goal. Conventional rearmament was neither popular with the people, nor did it fit into the general strategic trend of the Alliance which was stressing nuclear deterrence more and more. The German government adopted its own 'New Look' version, symbolized by the succession of Blank by Strauß.<sup>21</sup> Strauß, now in the position where he considered himself the ideal man, immediately set 'new priorities'. His plans to equip the Bundeswehr with nuclear delivery systems, and possibly also nuclear weapons<sup>22</sup>, incited violent public debate in Germany. 'Quality instead of quantity' became his often cited slogan, not only with respect to his nuclear plans but also regarding the conventional buildup.<sup>23</sup> He was unwilling to finance the application of outdated strategic concepts when, at the same time, Germany's allies put increasing emphasis on nuclear warfare on the battlefield, rocket technology, and sophisticated airpower.

The money saved because of the delay in rearmament was partly spent in politically more opportune ways, such as social expenditure.<sup>24</sup> A costly reform of the pension system was undertaken. Refugees, veterans and victims of the Nazi-regime received financial help. After all, 1957 was an election year. The rest was stockpiled to cover future burdens, as Finance Minister Schäffer tirelessly insisted on.<sup>25</sup> Blank, during his tenure, was not able to prevent

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<sup>21</sup> Greiner, in: MGFA III, p.733-737.

<sup>22</sup> The exact extent of Strauß' intentions is still hotly debated. For an assessment: Ahonen, 'Franz Josef Strauss and the German Nuclear Question, 1956-62', in: JOURNAL OF STRATEGIC STUDIES 18/1995, p.25-41.

<sup>23</sup> *ibid.*, p.822-25; Krieger, *Franz Josef Strauß*, 1996, p.34-42.

<sup>24</sup> Emminger, *D-Mark, Dollar, Währungskrisen*, 1987, p.78. On the expansion of welfare benefits: Hockerts, *Sozialpolitische Entscheidungen im Nachkriegsdeutschland*, 1980.

<sup>25</sup> Buchstab (ed), 1990, 12.7.1957, p.944; Köllner/Volkman, in: MGFA II, 1990, p.789-791.

funds not used for rearmament being diverted to these purposes, despite his protests against Schäffer's tight-fisted attitude.<sup>26</sup> The Finance Minister supplied the economic rationale behind the rearmament crisis. Schäffer felt that remilitarization could easily interfere with the phenomenal economic progress of the Federal Republic. He feared above all the inflationary impact of huge defence spending. To release the billions of the *Juliusturm* would foster this, for both German financial experts and public, equally distressing prospect.<sup>27</sup> The danger of inflation was aggravated by the fact that industrial production in Germany had almost no free capacity. That was one motivation behind Schäffer's promotion of arms purchases abroad.<sup>28</sup> Support cost payments were no substitute because was a waste of funds and he already foresaw a huge gap in the financial plans for the following years.<sup>29</sup> Arms purchases abroad, however, unburdened the booming economy and transferred surplus foreign exchange abroad (for a more detailed treatment of this question, see ch.V).

Industrial leaders and politicians agreed on these economic matters.<sup>30</sup> Domestic priorities rated higher than regard for alliance affairs. This applies also to the shortening of the conscription period. Labour shortages made this a reasonable step and, of course, this was a major aspect of the decision.<sup>31</sup> Thus, Schäffer and Strauß tried to extend rearmament over a longer period, although this meant major conflicts with the partners in the Alliance.

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<sup>26</sup> See for example the controversy in: BA, B126/34100, Blank to Chancellor's Office re Stationing Costs 1956, 13 July 1956; Schäffer to Chancellor's Office, 18 July 1956.

<sup>27</sup> The President of the Federal Bank, Vocke, supported Schäffer's arguments: '*Fact is that an acceleration of defence expenditures in combination with the release of billions for new Federal programs plus tax reductions, and all that in connection with continuing demands for higher wages...is enough to damage the strength of the currency*'; see: BA, B 136/3320, Vocke to Adenauer, 20.4.1956.

<sup>28</sup> BA, B 126/51520, Finance Ministry memo on defence planning, 25.1.1956.

<sup>29</sup> BA, B 126/51521, note Finance minister on cabinet meeting, 8.6.1956.

<sup>30</sup> BA, B 102/57514, BDI memo, 16.1.1956; *ibid.*, note on meeting Erhard, Strauß, BDI, 22.1.1957. It might also have been detrimental to the willingness of the industry to produce weapons that they were clearly told that arms production would remain under the tight control of politicians.

<sup>31</sup> Birtle, *Rearming the Phoenix, US Military Assistance to the FRG, 1950-60*, 1991, p.323-325.

Economic progress was the political priority for the Federal Republic after 1955.<sup>32</sup> It was the 'Wirtschaftswunder', and not 'Westintegration', which became the major factor of identification and rehabilitation in the eyes of the German public. This indicates a shift in basic policy aims from a search for security in the Western Alliance to an overriding emphasis on economic progress. The necessary security framework had been put in place. Now the policy of economic growth took priority, conflicting with the economic exigencies of rearmament.

The shift in policy priorities from the search for security in the Alliance to a promotion of economic growth in the European framework became a source of potential conflict with the British; whilst the search for security had tended to worry, above all, France. This was one background to the Anglo-German problems and to French-German harmony during the successive years. The delay in German rearmament was criticised mainly by Washington and London. Both exerted increasing pressure on Strauss and the German government. They succeeded in putting new steam into the stuttering effort.

When Strauß, under strong pressure from his NATO colleagues, tried to get more money released for rearmament, he met, like Blank, with the resistance of Schäffer. The Finance Minister was not willing to commit funds from the *Juliusturm* prematurely and fought stubbornly for his reserve.<sup>33</sup> Strauß identified him consequently as responsible for the slow progress of the Bundeswehr build-up.<sup>34</sup> He was not the only one to criticise the tight financial policy of Schäffer. Adenauer and von Brentano had already blamed his resistance in the question of support costs for strained relations with England.<sup>35</sup> Schäffer's insistence on restricted public spending and on holding reserves for future problems made his stance

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<sup>32</sup> For German economic policy in the Fifties see e.g. Ambrosius, *Europäische Integration und wirtschaftliche Entwicklung der BRD in den 50er Jahren*, in: Berding(ed), *Wirtschaftliche und politische Integration in Europa im 19. und 20. Jahrhundert*, 1984, p.271-294; Bühner/Schröder, *Germany's Economic revival in the 1950's: The Foreign Policy Perspective*, in: Di Nolfo(ed), *Power in Europe II*, 1992, 172-196.

<sup>33</sup> BA NL Schäffer, 34, memorandum by Schäffer, 18 September 1957.

<sup>34</sup> BA, NL Schäffer, 37, Schäffer memorandum on formation of the cabinet 1957, October 1957.

<sup>35</sup> Buchstab(ed), 1990, p.944; FAZ 15.6.1956; 17.6.1956.

within the cabinet increasingly unpopular and finally cost him his job in October 1957.<sup>36</sup> Although the most pronounced 'anti-spending' minister had disappeared it still took some time and much trouble before the Bundeswehr build-up gained momentum. The delay was overcome only at the end of the 1950s, probably not until after the Berlin Wall crisis in August 1961, and the strength of the German army remained for a long time below the level of allied expectations.

Not unexpectedly, the delay in German rearmament was seen as the incentive to pose new support cost demands towards the Federal Republic. Support costs were a palliative to justify continued troop maintenance by the US and the UK. Both felt trapped there by the immobility of the political situation and the foundering of their hopes that a German army could provide alternative conventional manpower. In this sense, support costs paralleled the discussion about the nuclearization of the alliance which started during these years. It was also sparked by a will to economize in military budgets and to alleviate the burden of Europe's defence on the British and American economy. If the Germans would not provide the necessary conventional forces, they had to pay for allied troops and to accept the defence of their territory by nuclear weapons over the use of which they had little control.

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<sup>36</sup> BA, NL Schäffer, 39, note on a cabinet meeting on 19.6.1957, 30 June 1956; Schwarz, *Adenauer*, 1990, p.354.

CHAPTER III  
THE SUPPORT COST NEGOTIATIONS OF 1957  
AND THE BRITISH 'NEW LOOK'

a) The Origins of the British Defence Review

During late summer 1956, indications of renewed British support cost demands multiplied. In addition, rumours circulated widely that the British government planned reductions in the forces it maintained in Europe. Overshadowed as those reports were by the Radford Plan debate, by German rearmament problems, and later by the Suez and Hungarian crises, they did not receive much attention. At the North Atlantic Council Ministerial Meeting in December 1956, however, the UK started a new round of support cost negotiations. They were burdened with an explicit threat of British troop-reductions in Europe. Macmillan, then Chancellor of the Exchequer, personally attended the meeting and gave a candid exposé of Britain's problems. He emphasized the foreign exchange problem the British were faced with, the enormous resources it employed for defence worldwide, and compared this with German deficiencies in their military effort. Macmillan urged NATO to undertake a strategic reappraisal which might lead to less reliance on conventional troops and to a stronger emphasis on nuclear weapons. He left no doubt as to the seriousness of his statements: *'...I must...make it quite clear that unless our overseas costs can be met, the future of our overseas contribution to NATO forces will be jeopardised'*<sup>1</sup>

This chapter will discuss the support cost negotiations 1956/57 against the backdrop of the British defence review initiated in 1956. The military and economic motives behind the review will be outlined. The defence review and the support cost negotiations showed the ambiguity of the British government about the continental commitment it had just taken on. London saw itself confronted with difficult choices regarding its relations with the rest of Europe if it wanted to bring its economic resources in a line with its security commitments. The decisions on these choices were to have a deep impact on British-European relations.

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<sup>1</sup> For the verbal text of Macmillan's statement see: BA, NL, Blankenhorn, 71/1, Record of NATO Council Meeting (C-VR(56)74), 13 December 1956. A telegram-style version is in FRUS 1955-57, IV, p.151-55.

Nobody, least of all the US government, was really taken by surprise by the Macmillan statement. In July 1956, at the same time as the American government discussed similar proposals (for the so-called Radford plan and its background, see ch.VI), Eden had written to Eisenhower proposing a reform in NATO strategy which might enable the UK to cut its troop deployments on the continent.<sup>2</sup> Using the argument of the increasing importance of nuclear weapons in modern warfare and citing the difficult balance of payments position of Britain, he urged a reappraisal of NATO's military policy, suggesting to supplement costly conventional forces with cheaper nuclear weapons. The United States, however, after a debate very much along the same lines, was impressed by the strong negative reaction within the alliance to US plans to reduce troops in Europe. They concluded that the political consequences of a military policy that relied solely on nuclear weapons would be dangerous.<sup>3</sup> Still, the American debate had left the British with the impression that the US was ambiguous over this issue and would not totally oppose a revision of the British defence posture. Even when the Americans became more outspoken against their blueprints for NATO reform, the British decided to continue with their initiative - particularly when the Suez Crisis turned out to be a major setback for English foreign policy.

In late 1956, Britain and France were forced by common superpower intervention to retreat from the Canal zone they had militarily occupied after Nasser had nationalized it. Not only Britain's military but also its economic vulnerability was clearly displayed during the crisis. The US had underlined its arguments against a continuation of the adventure with a temporary refusal to support the British currency.<sup>4</sup> Apart from the blow to British prestige, Suez had provoked a serious run on the pound and a tremendous loss of foreign-exchange. In the months of November and December, Britain had lost \$410m of its reserves, an enormous

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<sup>2</sup> FRUS 1955-1957, IV, p.92.

<sup>3</sup> *ibid.*, Memo Dulles to Eisenhower: US position on review of NATO strategy and force levels, 1 October 1956, p.96-98.

<sup>4</sup> Washington's use of financial pressure during the Suez Crisis is analysed in: Dobson, *The Politics of the Anglo-American Special Relationship*, 1988, p.166-73; Johnman, 'Defending the Pound: the economics of the Suez Crisis, 1956', in: Gorst/Johnman/Lucas, *Postwar Britain, 1945-64*, 1989, p.166-181; Kunz, *The Economic Diplomacy of the Suez Crisis*, 1991.



drain on the pre-Suez reserves of about \$2250m.<sup>5</sup> To stop the run the British government had to borrow \$1300m from the IMF and had to take up a loan of \$700m from the EXIM bank. Those loans had been approved by the Americans only after Britain had agreed to a cease-fire in the canal zone. The repayment of the debts incurred weighed heavily on Britain's external balance in the following years.

The monetary predicament was, already before it took these alarming proportions, one major cause for the British initiative. During 1955/56, apprehension had mounted in the British government that principal foreign policy objectives -to sustain Britain's role as third power in the world and to preserve sterling's role as reserve currency- were seriously prejudiced by the pressing burden of military expenditure. In March 1956, Macmillan and Defence Minister Monckton urged upon Eden '*a reappraisal at the highest level of the whole basis on which our defence policy should rest*'.<sup>6</sup> This reappraisal was to bring British resources and its defence posture in line. A 'Report on the Future of the United Kingdom in World Affairs', dated 1 June 1956 and prepared by Treasury, Foreign Office and Defence officials was the result.<sup>7</sup> The officials stated that the United Kingdom had an overloaded defence structure and this had placed the economy under constant strain. A concentration on essential political goals of defence policy was indispensable to avoid further damage. From these essentials -keeping the Americans in Europe, developing closer cooperation with North America, and maintaining the cohesion of the Commonwealth- Continental Europe was conspicuously absent.<sup>8</sup>

A reform of the traditional economic foundations of British military policy would have to take into account in particular the exigencies of the currency situation. Savings were to be achieved in places where foreign-exchange losses were high in proportion to political and military gains. The foreign exchange cost of the forces assigned to NATO was estimated now

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<sup>5</sup> The December losses were obscured in official announcements by adding the first tranche of the IMF loan to Britain's reserves; KCA 1956, p.15239; KCA 1957, p.15307.

<sup>6</sup> Defence Policy: memo by Macmillan and Monckton to Eden, 20.3.1956, in: Goldsworthy(ed), 1994, p.60.

<sup>7</sup> *ibid.*, p.61-81.

<sup>8</sup> *ibid.*, p.67.

to be \$190.4m a year for the BAOR and the 2nd TAF.<sup>9</sup> According to British government opinion as expressed in the report cited this was too high a price for the political gains of troop stationing in Europe. Accordingly reductions in defence expenditure '*must be found largely in our expenditure on our defence in Europe. It is there that the greatest scope exists for reducing demands on our engineering industry, our military manpower, our technical and scientific resources and our foreign exchange, in the interests of reestablishing our economic strength.*'<sup>10</sup>

The problem was how to achieve such a reform and the corresponding reduction without embarrassing the US or damaging British relations to third countries too heavily.<sup>11</sup> If NATO adopted a new strategic concept based mainly on nuclear weapons and requiring just a 'tripwire' force of conventional troops on the Cold War border the task would be much easier. This was the background of Eden's letter to Eisenhower. It soon became clear that the Americans were less than enthusiastic about the British proposals.<sup>12</sup> They argued that a strategic discussion in the alliance at this moment would endanger Congress legislation on foreign aid as well as the legislative procedures concerning rearmament in the German parliament.<sup>13</sup> They therefore urged London to delay presenting their plans for review in NATO committees. The tense international climate, marked by Suez and the Hungarian uprising, made a fast British move difficult anyway. A final consideration was that the British feared that premature announcements would seriously impair the further payment of support costs by Germany. There was no hope that reductions could be started before late 1957, and the previous agreement ended in May 1957. A follow-up agreement seemed therefore necessary in any case. These considerations suggested a slow pace for the British initiative.

Prior to the NATO meeting in December 1956 the British discussed their problem with the US delegation headed by Dulles. Foreign Minister Selwyn Lloyd stated that they '*could not*

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<sup>9</sup> CAB 129/84, CP(56)269, Memo by Minister of Defence: UK Forces in Germany, 28 November 1956.

<sup>10</sup> *ibid.*, p.69.

<sup>11</sup> CAB 134/1315, Cabinet Policy Review Committee minutes, 9 June 1956, in: Goldsworthy(ed) (1994), p.86.

<sup>12</sup> PRO, CAB 128/30, Cabinet Meeting Minutes, 19.6.1956.

<sup>13</sup> *ibid.*; FRUS 1955-57, IV, Memorandum US to UK, 29 June 1956, p.87-88.

keep troops in Germany unless a way was found to reimburse the British for this expense'. After Dulles asked: 'Unless the Germans pay for it?', Lloyd replied: 'Unless someone pays for it!'.<sup>14</sup> Ignoring this broad hint, Dulles acknowledged the gravity of the situation and agreed on the allegations that Germany was not doing enough for defence. However, he warned of the effect of reductions on the German electorate. He also declared himself against a reliance on the British version of the tripwire strategy which in US opinion was placing too much emphasis on nuclear deterrence.<sup>15</sup> This did not impress the British at all and they threatened openly to break the WEU-treaty, hinting that US help with respect to their nuclear capacity might be a solution.<sup>16</sup>

This plea was a further consequence of the defence review. If the UK, despite the envisaged cuts, was to retain a military capability compatible with its self-perception as third power in the world, recourse to increasing its nuclear potential seemed the only way.<sup>17</sup> However, US financial and technical help was necessary. Particularly, regarding rocket technology, the United Kingdom had fallen far behind. Mischievous jokes suggested that the next British rocket should be constructed in such a way as to allow highly trained athletes to carry it into enemy territory.<sup>18</sup> The US delegation was hesitant regarding help on this problem. However, soon afterwards the Americans started to expand nuclear cooperation with the British.<sup>19</sup> It is unlikely that this was coupled at that time to a British promise to limit their defence cuts in Europe. The quid-pro-quo were base rights for the Americans in Britain and the important objective was to repair Anglo-American relations after Suez. However, soon the troop connection would play an increasing role. At the end of the above mentioned meeting, both sides agreed that it would be better to wait first for the German reaction to the new support

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<sup>14</sup> FRUS 1955-57, IV, Anglo-American meeting, 11 December 1956, p.123, fn.2.

<sup>15</sup> *ibid.*, p.127.

<sup>16</sup> *ibid.*, p.130-31; see also: PRO, PREM 11/1270, American-British talks, 11 December 1956.

<sup>17</sup> Excellent on this subject: Clark, *Nuclear Diplomacy and the Special Relationship*, 1994.

<sup>18</sup> Quoted from: Porter, 'Downhill all the Way: 13 Tory Years', in: Coopcy/Tiratsoo/Fielding(eds), *The Wilson Governments, 1964-70*, 1993, p.21.

<sup>19</sup> An Anglo-American agreement on the proliferation of medium range missiles was signed in July 1958. See: Botti, *The Long Wait. The Forging of the Anglo-American Nuclear Alliance 1945-1958*, 1987, p.234; Bartlett, *The Special Relationship*, 1992, p.88; Clark (1994).

cost demands before the British committed themselves to a fixed position on reductions in Europe.<sup>20</sup>

b) The Support Cost Negotiations 1956/57

The British position on approaching the Germans was clear: the reform of their defence structure was not negotiable, but the willingness to compromise on particular points would be influenced by the German willingness to contribute to the foreign exchange cost. *'Decisions concerning withdrawal of our troops were therefore not primarily dependent on the outcome of the negotiations concerning stationing costs, although these negotiations would influence the extent to which we should wish to withdraw our troops.'*<sup>21</sup> Under these circumstances a favourable agreement seemed not very likely. Indeed, strong political arguments against a new round of negotiations had been raised in the Foreign Office after the embarrassing experience one year previously. But when the full extent of the delay in German rearmament became known in late 1956, those inhibitions were discarded.<sup>22</sup> The Germans were not surprised by the new request. Conscientious of their shortcomings in the military field and aware of the disastrous repercussions of the negotiations in 1955/56, they immediately accepted the initiation of a new round of negotiations.<sup>23</sup> Moreover, support cost payments were seen now explicitly as a means in the fight against suspected British troop reduction plans.<sup>24</sup>

Prior to Macmillan's speech at the NATO council meeting, the Germans met with the British on the subject of support costs.<sup>25</sup> Von Brentano and Schäffer already had come to an understanding with respect to the German position in the forthcoming negotiations. They

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<sup>20</sup> FRUS 1955-57, IV, p.134.

<sup>21</sup> PRO, CAB 134/2223, MAC(G)57, services cost in Germany, 1st meeting, 4.1.1957.

<sup>22</sup> An account of the 1957 negotiations is in PRO, CAB 134/2223, A Note on the Negotiations leading to the Local Defense Cost Agreement with the FRG, 1957. Memorandum by Gore-Booth (M 101/234), 15.10.1957.

<sup>23</sup> BA, B126/34103, Excerpt of Cabinet Meeting, 8.12.57; BA, NL Blankenborn 71/2, note, 17.12.56.

<sup>24</sup> PA-AA Ref.301/96, von Brentano to Adenauer, 6.12.56; von Brentano to Chancellor's Office, 4.1.1957.

<sup>25</sup> PA-AA, Ref.301/96, Meeting of UK-FRG delegations, 12 December 1956.

agreed on \$286m as an upper limit for all support cost requests - the rest of the stationing countries were expected to follow soon - and to a preferential treatment for Britain because of its special currency problems. One precondition in the negotiations would be that the allies would agree this time to terminate their demands once and for all.<sup>26</sup> The Federal Republic also, for the first time, proposed monetary measures during discussions in the English-German Economic Committee which was set up as the forum for the negotiations.<sup>27</sup> These comprised a premature repayment of postwar debts, investment in UK Treasury papers, and an enlargement of the hardly used account at the Bank of England destined for arms purchases (from £20 to £30m).<sup>28</sup> These offers were an expression of the increasingly strong reserve position of the Federal Republic which Bonn slowly began to use for political aims.

As direct support cost payments the German delegation offered \$120m. The British, however, demanded \$182m. The talks were complicated by requests which dribbled in from the rest of the stationing countries. Those requests were answered with a German offer of half the amount agreed upon in the previous year. France was excluded from this harsh treatment, but it was nevertheless offered considerably less on the argument that French forces in Germany were seriously under strength due to the Algerian war. Naturally, the affected nations protested, unsuccessfully, against the cuts.<sup>29</sup> The fast progress hoped-for in the British-German case proved illusive.

By far the greatest complication became the public announcement of British troop reduction intentions in February 1957, when the talks were almost concluded. Widespread speculation on the subject had affected the negotiations all the time.<sup>30</sup> The Germans were particularly disturbed by the British plans at a time when their own buildup had hardly started. This they

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<sup>26</sup> BA, B 126/51521, conversation v. Brentano-Schäffer, 14.12.1956 (also in: PA-AA, Ref.301/96).

<sup>27</sup> The Committee was headed by the Undersecretaries of Foreign Affairs. The first meeting took place on 14 January 1957; extensive documentation in PA-AA, Ref.301/96 and in PRO, CAB 134/2223, Mutual Aid Committee: Subcommittee on Germany 1957.

<sup>28</sup> PA-AA Ref 301, Bd.96, AA to NATO-Embassies, 28.1.57; BA, B126/34103, Cabinet Memo by Foreign Minister: German-English Financial Talks, 4 January 1957; PRO, CAB 134/2223, Note on Negotiations..., 15.10.1957.

<sup>29</sup> For documentation on these negotiations, see PA-AA, Ref.301, vols.97 and 100.

<sup>30</sup> see e.g. TIMES 11.12., 14.12.56; SZ 4.1.57.

saw as a grave military weakening of NATO front-lines. Furthermore, Bonn feared a combined move towards a nuclearisation of Western defence with Germany providing the 'foot-soldiers' as it had renounced the possession of own nuclear arms.<sup>31</sup>

The Germans added to their bargaining position in the support cost negotiations that '*German concessions [will] be made dependent on guarantees about the maintenance of previous force levels and combat capabilities*'.<sup>32</sup> They decided to request that a clause be inserted in the prospective agreement which coupled the result and any payments to a British guarantee for stable troop levels. This was exactly what the British wanted to prevent. They thought '*that nothing should be written in the agreement, which prevents us from making the reductions we have in mind*'.<sup>33</sup> The negotiations arrived at a deadlock. Macmillan, Prime Minister in January 1957, wrote an annoyed letter to Adenauer: '*...Your negotiators appear to be trying to bring financial pressure upon us to delay giving effect to reductions, which we regard as essential to our economy by leaving in doubt what contribution we could count on in 1957-58*'.<sup>34</sup> This was a foreboding of Macmillan's growing preoccupation with the issue. The support cost question was to acquire an important place in determining his attitude towards the Federal Republic. Adenauer, in his answer, expressed his contempt of the troop reduction plans.<sup>35</sup> Finally, a somewhat diluted version of the clause was accepted by the Germans. The negotiations were concluded in March. Germany agreed to pay \$140m cash, deposited £75m at the Bank of England as prepayment on postwar debts, and enlarged the account for military purchases to £30m.<sup>36</sup>

The final signature was once more delayed by the arrival of an official US support cost

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<sup>31</sup> For a German assessment of the British plans: BA, NL Blankenhorn, 75b/1, BMVg Memo: Militärische Beurteilung des britischen Weissbuchs, 25 April 1957.

<sup>32</sup> BA, B126/34103, von Brentano to Adenauer, 22.2.1957.

<sup>33</sup> PRO, PREM 11/1842, Macmillan to Lloyd, 8 February 1957.

<sup>34</sup> PA-AA Ref.301, vol.97, 22.2.57; also in: PRO, PREM 11/1842.

<sup>35</sup> *ibid.*, letter Adenauer to Macmillan, 23.2.57.

<sup>36</sup> BGBl 1959 II, Notenwechsel zwischen der Regierung der Bundesrepublik und der Regierung des Vereinigten Königreichs von Grossbritannien und Nordirland über gegenseitige Hilfe (Artikel 3 NATO Vertrag), p.414-417.

request for a sum much larger than expected. Arguing with the necessity of a preferential treatment for Britain and the need of the funds for its own rearmament effort, the Federal Republic, after some discussion, managed to get US acceptance of \$77.5m, half the amount of the year before. It had to accept a clause which granted the US the right to reopen the case within six months if the German rearmament effort still was behind schedule at that time.<sup>37</sup> After concluding with the USA, the British-German agreement finally was signed. Thus, the support cost problem was solved and discussions centred on the British troop reduction plans.

c) The British White Paper, April 1957

The new Prime Minister Macmillan and his Minister of Defence, Duncan Sandys, were deeply impressed by the constraints the financial position put on British foreign policy. One consequence of the Suez crisis, which had clearly exposed Britain's financial and military limits, was that it hardened the determination of the British government to continue with its controversial defence review, including the plans to trim the BAOR. This proved a thorny endeavour, given the obligations of the WEU treaty and the foreseeable resistance of the WEU member countries. Britain could not claim any overseas emergency as the first escape clause from the troop commitment. It had to base its plea on financial reasons. This required the consent of the WEU members.

The conflict would not remain an isolated issue, as the British realized beforehand. Defence Minister Anthony Head wrote to his colleagues when the December meeting of NATO was approaching: *'The problem facing us can, I think, be summarized as follows: How large a reduction should we propose to our Allies in the interests of our economic position, bearing in mind that if we go too far we may provoke a general reduction in military contributions to NATO, and indeed endanger the very stability of the alliance as well as damaging the prospects of the closer relationship with Europe which we have in mind in other fields'*.<sup>38</sup>

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<sup>37</sup> For the US-German discussion see: BA, B126/34104, US Aide-Memoire to Germany, 25.2.1956; DDRS 1987/149, Wilson to Eisenhower, 22.3.57; FRUS 55-57, XXVI, Adenauer to Eisenhower, 23.3.57; Krekeler Conversation with Dulles, 27.3.57; Dulles Memo to Eisenhower, 27.3.57; Memo of Conference with the President, 2.4.57; Eisenhower to Adenauer, 12.4.57, p.220-229. For the agreement on 7 June 1957: BGBL II, 1959, p.410-11.

<sup>38</sup> PRO CAB 129/84, CP (56), 269, Memorandum of Defence Ministry, 28.11.56.

During the NATO meeting it already became obvious that the other WEU members would not be pleased. When, in February 1957, the British officially presented their plans for a troop reduction in Europe at the WEU Council Meeting the dilemma became only worse, although meanwhile, the US had resigned itself to limited British reductions (for the ensuing debate, see ch.IV). The full extent of the British plans was finally made known in the famous Defence White Paper of April 1957, provoking further apprehensions on part of Britain's military allies.

The major changes the White Paper proposed were general reductions in manpower, the proposed end of national service in 1962, cuts in arms research and development and an increased emphasis on international cooperation in the development of new armament systems. These ideas were not entirely new, and the White Paper only summarized a discussion which had been going on throughout the 1950's.<sup>39</sup> The ultimate trigger for the implementation of these ideas may have been, as already said, the Suez Crisis at the end of 1956. The White Paper was no radical change in policies but an attempt to devise strategies limiting the obvious erosion of British prestige and freedom to act as a world power. It was a new strategy to pursue an old policy design.<sup>40</sup>

The causes and consequences of the 1957 White Paper have received much attention in the scientific literature.<sup>41</sup> The motives for initiating the defence review have already been shortly touched upon. The basic cause was the economic strain the military posture put on the British economy. This was summarized in the opening section of the White Paper: *'Britain's influence in the world depends first and foremost on the health of her internal economy and the success of her export trade. Without these, military power cannot in the long run be supported . . . Over the last five years, defence on average absorbed 10 per cent of Britain's gross national product. Some 7 per cent of the working population are either in the Services*

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<sup>39</sup> Navias, *Nuclear Weapons and British Strategic Planning, 1955-1958*, 1991, p.134.

<sup>40</sup> Dockrill, *The Defence of the Realm: Britain in the Nuclear Age*, in: Gourvish/O'Day(eds), *Britain since 1945*, 1991, p.144.

<sup>41</sup> The most recent account is Navias, (1991). Furthermore: Bartlett, *The Long Retreat*, 1972; Darby, *British Defence Policy East of Suez 1947-1968*, 1973; Rees, *The 1957 Sandys White Paper*, in: *Journal of Strategic Studies* 6(1989), p.215-29.



or supporting them. One-eighth of the output of the metal-using industries, upon which the export trade so largely depends, is devoted to defence. An undue proportion of qualified scientists and engineers are engaged on military work. In addition, the retention of such large forces abroad gives rise to heavy charges which place a severe strain upon the balance of payments.'<sup>42</sup> The section establishes a clear causal link between Britain's military expenditure and its overall economic problems. That this reasoning was the main driving force behind the defence review also is the tenor of the literature on the subject (see fn.39). It is useful to shortly recapitulate the main issues of the debate on military expenditure and British economic problems in which the issue of the foreign exchange losses of British troops in Europe was embedded.

The assertion of the White Paper that military spending was to a good part responsible for British economic problems was prevalent in the British government of that time and widely shared by contemporary commentators.<sup>43</sup> The argumentation is still influential and is sustained by critics of British policy in the 1950's such as Chalmers or Aaronovich.<sup>44</sup> It gained renewed force with the opening of archives since contemporary historians often tend to repeat the analyses in the papers of government officials. The argument usually goes that the high concentration of investment and labour force in defence industries diverted resources away from fast-growing industries such as consumer goods, which were the linchpin of the postwar boom in Europe, and such damaged British exports. Together with military expenditure abroad, this is seen as a central factor for British balance of payments problems. The fact that the crisis of British postwar recovery 1951 coincided with the 'Korea-rearmament' seems to underline the argument. '*Britain's incalculated act of sacrifice during the crisis at the start of the Korean War in embarking on a defence program which used up all the resources in sight and more, continued to exercise an unfavourable influence on economic development long after the event.*'<sup>45</sup>

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<sup>42</sup> HMSO, Cmnd.124, Defence: Outline of Future Policy, 1957, p.1.

<sup>43</sup> For a vigorous critic of British defence spending see: Shonfield, *British Economic Policy since the War*, 1958. See also: Bartlett (1972), p.105-06; *The Economist*, 5.1.1957.

<sup>44</sup> Chalmers, *Paying for Defence. Military Spending and British Decline*, 1985; Aaronovich(ed), *The Political Economy of British Capitalism*, 1981; for further references see: Geiger, in: Gorst/Johnmann/Lucas, 1991, p.96.

<sup>45</sup> Shonfield (1958), p.56.

It has, however, already been observed in the previous chapters that such a straightforward interpretation might be too simple. The foreign exchange cost of the troops has been put into perspective (see ch.I, where the financial consequences of troop maintenance were discussed). Chapter V will show that the failure of British arms export to Europe was mainly due to the fact that it was not consistent with the basic lines of British foreign policy. This argument can be extended to the whole sector of British exports. Complaints about the giving up of markets to the Europeans in the rearmament period often disregard the fact that Britain at that time was not necessarily willing to direct its trade towards Europe but rather towards the US and the Commonwealth.<sup>46</sup> The crucial interest in earning dollars and the unfavourable trade balance with the dollar area rendered exports there a priority. The second priority, Commonwealth trade, is not so obvious.<sup>47</sup> Although British trade with the Commonwealth was of a much higher value than with Europe, its level was stagnant compared to the breathtaking rise of inter European trade growth rates. The clinging to these imperial links can only be explained by political, or rather ideological, reasons. It would have been almost impossible to explain to the British public such a brusque revision of traditional foreign policy. The giving up or non-entering of European markets was a necessary consequence of these policies, not of the claims on resources by defence needs.

The military burden is only one of the many arguments in the great debate about British postwar 'decline'.<sup>48</sup> It is not surprising that the prevailing view on the effects of British defence costs on the economy was soon challenged, apart from the reservations already made. Snyder points out that '*the rearmament program strengthened (emph. in original) Britain's ability to earn reserves in the years thereafter*'.<sup>49</sup> He cites the receipts of US foreign aid (1952-1956: \$1 billion), the foreign exchange expense of US and Canadian troops in Britain (about \$182m a year in the 1950's), and military exports (\$577m until 1959). One might add US support for the pound which was not only motivated by economic motives but also intent

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<sup>46</sup> Burnham, *The Political Economy of Postwar Reconstruction*, 1990, p.150-176.

<sup>47</sup> For statistics about British trade in the 1950's see: UN, Statistical Office, *Yearbook of International Trade Statistics*, 1952, p.363; *ibid.*, 1955, p.689; *ibid.*, 1957, p.243, 589.

<sup>48</sup> Catterall, 'The state of literature on British postwar history', in: Gorst/Johnman/Lucas(eds), (1989), p.221-41; Kirby, *The Decline of British Economic Power since 1870*, 1981, p.119-125.

<sup>49</sup> Snyder (1964), p.214.

on enabling Britain to keep its military commitments. On the other hand, Snyder acknowledges the commonly presented bottlenecks of the rearmament program: the pressure on metal using industries, the concentration of research on defence, and the outlays for troops abroad.<sup>50</sup> Abelshauser, however, twists the traditional argument and maintains that the economic weakness was not produced by the effects of high defence costs, but, on the contrary, because of economic weaknesses deriving from other factors, Britain was no longer able to bear the expense.<sup>51</sup> A detailed analysis by Burnham confirms that the impact of rearmament was confined to a temporal check on exports whereas the commonly cited economic problems allegedly resulting from rearmament were already in place.<sup>52</sup>

This problem will hardly be solved until a detailed analysis for the British case is made. The difficult question whether military spending is a gain or a bottleneck for an economy has to be solved rather by comparably tedious sectoral studies than by sweeping statements.<sup>53</sup> Whatever the final result of this debate, it is clear that the straightforward assertion of the White Paper was too simplistic. This short review demonstrated that the monocausal linkage of high defence costs and economic decline is not as clear as the public discussion in Britain during the 1950's and parts of the literature suggest. Economic considerations in defence matters, as they were pushed forcefully in the support cost question and in the defence review 1957, were also shaped by underlying political choices with economic reasoning often following them. The remainder of this chapter will be concerned with these choices.

This chapter outlined the consequences of the British government's thinking that its economy and its military posture were no longer compatible. The political and economic shock of the Suez Crisis was the last straw and the Defence White Paper of 1957 the foremost expression of this thinking. The basic goals of British foreign policy remained the same. However, in order to continue with this policy Britain had to devise strategies which limited the constraints

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<sup>50</sup> *ibid.*, p.215.

<sup>51</sup> Abelshauser, 'Rüstung, Wirtschaft, Rüstungswirtschaft', in: Maier/Wiggershaus(eds), *Das Nordatlantische Bündnis*, 1993, p.103.

<sup>52</sup> Burnham (1990), p.176.

<sup>53</sup> One example is: Burnham, 'Rearming for the Korean War: The Impact of Government Policy on Leyland Motors and the British Car Industry', in: *Contemporary Record* vol.9/2, 1995, p.343-367.

imposed by the economic situation. Choices had to be made and these choices are significant within the scope of this research.

The emphasis Britain put on its nuclear potential as the most simple and least expensive way to sustain what remained of the beleaguered British power in the world was in many ways beyond its economic and technological resources.<sup>54</sup> A first choice was therefore necessary because the sustenance of a useful nuclear potential was not possible without cooperation from other countries. While the French, with similar problems, turned halfheartedly to Europe in the form of the FIG Agreement (see ch.V), the British accepted an increased reliance on the United States and valued the 'Special Relationship' higher than the European connection. In a paper of January 1957, entitled 'The Grand Design', Lloyd had proposed to his colleagues a pooling of the British nuclear program with European resources in the framework of WEU.<sup>55</sup> The paper was an attempt to escape a too pronounced dependence on the US as it became evident during the Suez Crisis. However, when it was discussed in the cabinet, a majority was against Lloyd's idea, citing in particular the importance of Anglo-American cooperation.<sup>56</sup> This result robbed Britain of the principal carrot it could have extended to the Europeans in exchange for cooperation in other policy fields. When Macmillan, in March 1957, went to meet the President on the Bermudas, his overriding concern was a broad intensification of Anglo-American cooperation.<sup>57</sup> Cooperation with the Europeans on nuclear arms matters was -for the time being- ruled out during Cabinet discussions on the White Paper.<sup>58</sup> This choice, subsequently reaffirmed on many occasions, would seriously impede the British realignment towards Europe.

The second choice, made in 1956, was very much in line with the first. It meant going ahead with a substantial reduction of forces in Europe. The exact figure, to which the army was to

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<sup>54</sup> The changes in British nuclear strategy are described in detail by Navias (1991).

<sup>55</sup> 'The Grand Design'(Co-operation with Western Europe). Cabinet memorandum CAB 129/84, 5 January 1957, in: Goldsworthy(ed), 1994, p.102-07.

<sup>56</sup> *ibid.*, p.107-110.

<sup>57</sup> For documentation on the meeting see: FRUS 1955-57, XXVII, p.704-67.

<sup>58</sup> PRO, CAB 128/31, Cabinet Meeting minutes, 22.2.1957.

be reduced, was 165.000 (from previously about 400.000 men). This figure was kept secret. The 77.000 men in the BAOR were targeted particularly. The result of the support cost negotiations seemed to make heavy cuts with regard to the sterling situation unavoidable. However, even a more acceptable result would not have deterred the British. The political risks of troop reductions were emphasized mainly in the Foreign Office. Apart from the foreseeable reaction of the allies, it was the shacking of confidence in Sterling, the inherent loss of British prestige, and the enlargement of Germany's role on the continent, which were the critical points<sup>99</sup>. Furthermore, the appearance of a reversal of policy so shortly after the WEU pledge was awkward. But these political risks were not regarded as high enough to justify the perceived economic strain. The British announcement at WEU in February 1957 to reduce the BAOR to 40.000 and to halve the 2nd.TAF until the end of 1958 triggered a long argument. It resulted in a two-year diplomatic battle, in which Britain was constantly on the defensive and which cast a long shadow over Britain's attempt to adjust itself to the evolving European integration process. The main problem was that the British government was not able to offer a politically acceptable alternative for troop maintenance or another kind of credible commitment to the Europeans.

Either one of the above mentioned choices alone might not have been interpreted as negatively in Europe. Both together, however, and the manner in which they were pushed through, exerted a blow with serious consequences on Britain's European policy. This will be the subject of chapter IV.

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<sup>99</sup> PRO, FO 371/124622, Brief for Committee on Service Costs in Germany, 14.5.1956; *ibid.*, undated FO note on troop reductions.



CHAPTER IV  
ADENAUER AND 'PERFIDIOUS ALBION'<sup>1</sup>:  
TROOP REDUCTIONS, SUPPORT COSTS, AND THE INTEGRATION OF  
EUROPE, 1957-59

a) Anglo-German Discords

In May 1959 the British Ambassador at NATO, Frank Roberts, reported an Adenauer quip he had picked up from his German colleague Blankenhorn. Allegedly, Adenauer had remarked that he now had two main enemies: England and his own Foreign Minister.<sup>2</sup> Whatever the authenticity of this quote, it was typical of the state of affairs between Britain and West Germany in 1959. It seemed as if the conflicts of the previous years and all the hardly concealed fundamental differences in basic policy views suddenly converged, culminating in a tense meeting between Macmillan and Adenauer at the end of year.<sup>3</sup> Numerous discords, whether they were about East-West relations, disarmament, the Free Trade Area (FTA) or support costs were inextricably linked and reinforced each other to produce a postwar low in British-German relations.

In retrospect, however, this seems quite surprising. The relationship between the United Kingdom and the Federal Republic after the war seemed to be under much better auspices than French-German relations. However, it should never attain the degree of close collaboration between Bonn and Paris which proved to be particularly harmful for Britain's attempts between 1957-63 to establish a form of European integration consistent with her basic foreign policy objectives. These attempts became indirectly dependent on German support. If Bonn had opposed as strongly as the Netherlands the French policy of excluding Britain, France at that time probably would not have taken the risk of antagonizing Germany with an uncompromising policy and thus driving it into the Anglo-American camp. It has to be kept in mind that the famous 'axe Franco-Allemand' emerged only slowly in the late

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<sup>1</sup> PRO, FO 371/145780, Balke to P.Tennant on an Adenauer-Remark, 29.10.1959.

<sup>2</sup> PRO, FO 371/145775, Roberts to Steel, 27.5.1959.

<sup>3</sup> For the continuous series of mutual recriminations during 1959 see the documents in PRO, FO 371/145777.

1950s. To assume tacitly that its formation was natural distorts reality and the fact that the situation was open, be it towards a looser or closer form of European integration, towards a 'Gaullist' or an 'Atlanticist' Europe. Insofar these few years have been decisive for the later shape of Europe.

The following chapter attempts to add some new viewpoints which make the critical choices of these years clearer. It will be argued that much of Germany's tacit support for French European policy originated from the German disappointment with Britain in the security field. Without the incessant arguments over support cost and troop-level questions from 1955 to 1959, Erhard and his strong partisanship in all parts of the German elites would have had a much stronger hand in the German debate with their more 'atlanticist' position. In the previous chapters I cited various instances which showed the conflicts dealt with in this thesis as closely linked to the European issue. This chapter aims at investigating the link between security questions (and their financial dimension) and the question of Britain's position in Europe. I will try to elaborate these links with particular attention to the support cost negotiations 1957/58 and to British troop reductions between 1957-1959.

A simple confrontation of dates suggests the supposed interrelation of British security policy and European integration. The Six had, soon after the EDC disaster, 'relaunched' Europe at the Messina conference in June 1955. At this time the feeling prevailed in Britain that the WEU pledge to maintain troops on the continent and a loose cooperation with other European institutions was enough involvement in Europe for the time being.<sup>4</sup> However, it rapidly became clear that troops could not substitute a consistent European policy. The fast progress towards the Rome Treaties surprised the British. Contrary to their expectations, the Spaak committee which worked out the Messina proposals for the Common Market overcame all the huge obstacles which laid in the way. Britain had withdrawn its representative already in

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<sup>4</sup> For Britain's European Policy as it evolved up to the ill-fated application in 1961-63, M. Camps', *Britain and the EC, 1955-1963*, 1964, is still indispensable. More recent works include: Young, *Britain and the European Community, 1945-92*, 1993; Greenwood, *Britain and European Cooperation since 1945*, 1992; Schmidt, *Großbritannien und Europa*, 1989; S.Ward, *Britain, France and the EC, 1958-1963*, (postgraduate thesis) 1992; Kaiser, 'Selbstisolierung in Europa: Die britische Regierung und die Gründung der EWG', in: Wurm(ed), *Wege nach Europa*, 1992, p.125-153; Schmidt, 'Großbritannien, die Gründung der EWG, und die Sicherheit des Westens', in: Salewski M.(ed), *Nationale Identität und Europäische Einigung*, 1991, p.169-231. For the FTA negotiations and EFTA see Camps (1964), and Griffiths(ed) EFTA (forthcoming).



November 1955 from the negotiations and saw itself completely excluded afterwards.<sup>5</sup> When the success of the Six became clear, Britain reacted and formulated its own alternative to the Common Market, the design of a wider Free Trade Area (FTA). The plan was presented to the OEEC on 13 February 1957. Only one day later, the British troop reduction plans were made public at the WEU Ministers Council.<sup>6</sup> This resulted in a long series of heated discussions between Britain and its WEU partners, which will be described in some detail below. The FTA plans of the British received less immediate scrutiny. Serious negotiations took place only when the Six finally had signed the Rome Treaties at the end of March 1957.<sup>7</sup> A new round of support cost negotiations began in mid-1957. It ended not until early 1958, accompanied by further British reductions, and placed the usual strains on German-British relations. The discussion about British troop levels lasted even longer, until well into 1959. The FTA negotiations had continued all along in the so-called Maudling Committee in a worsening climate, although differences on specific issues seemed to slowly converge. When suddenly the French declared in November 1958 that further talks on FTA were pointless, no decisive voice of opposition was heard from Germany. The subsequent foundation of EFTA only deepened the rift between the UK and Europe.

Throughout these events Britain followed a parallel policy of trying to achieve largest possible reductions of their Europe-based troops whilst on the other hand attempting to convince the Six of the benefits of their economic proposals. The outright denial or deliberate disregard for the awkward fact that both policies were inseparably linked, remained one of the most fundamental flaws in British policy until its unfortunate applications for EEC membership in the 1960s. Temporal coincidences are of course not enough to prove whether security conflicts spilled over to the process of European integration. The assumption is frequently made in the literature; but is hardly scrutinized in depth.<sup>8</sup> A closer look at the troop-reduction

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<sup>5</sup> Young, 'The Parting of the Ways?', in: Dockrill/Young(eds), *British Foreign Policy, 1945-56*, 1989, p.197-224; Griffiths, *The Creation of EFTA*(forthcoming); Milward, *The European Rescue of the Nation State*, 1992, p.426-27.

<sup>6</sup> Keesings Contemporary Archives, p.15723.

<sup>7</sup> On this condition France and Germany insisted; see FRUS 1955-57, XXVI, conversation Dulles-Adenauer, Bonn, 4.5.1957, p.240.

<sup>8</sup> Only Schmidt (1989) cites sources to this effect putting them in a larger context. Young (1993) and Greenwood (1992) almost completely blend out security and monetary considerations behind London's policy towards Europe.

debate, at the support cost negotiations in 1957-58, the failure of the FTA plan, and the British-German crisis of 1959 might provide some answers.

b) The Negotiations about British Troop Reductions 1957

When the British in February 1957 announced at the WEU meeting that they would reduce the BAOR from 77.000 to 50.000 men and halve the 2nd TAF (consisting of 466 aircraft and 15.000 men), they provoked a storm of criticism from their WEU partners.<sup>9</sup> The underlying motives for the British defence review have already been discussed. The White Paper of 1957 indicated a political choice for relations to the US and the Commonwealth as highest priorities to the detriment of British positions in Europe. That is exactly how the troop reductions and the White Paper were perceived. The Europeans, and partly also the US, refused to see the British problem merely as a financial issue. They strongly emphasized the political background and this shattered all British hopes that their goals would be accomplished without serious political irritations.

The French turned out to be particularly critical. British-French relations had suffered much because of the Suez Crisis and the British decision to intensify nuclear cooperation with the United States despite timid declarations to pool knowledge and resources with France. The WEU announcement was a further affront. France, which had accepted German rearmament only on condition of the British troop maintenance pledge, was shocked by the rapid erosion of this promise. When discussing the reductions with the British on 9 March 1957, French annoyance (and British intractability) '*led rapidly to a dramatic turn in a very friendly discussion*'.<sup>10</sup> Mollet denounced the breach of the WEU pledge which might lead to a recurrence of the situation in 1938. Macmillan pointed to his financial problems and to the fact that the French had long since moved big parts of their forces in Germany to Algeria without consulting anybody. The conversation ended on a depressing note: '*No agreement was reached, no compromise envisaged. Subsequently, it was indicated to the English ministers that, if they insisted on reaching a decision this week, it would be impossible to avoid*

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<sup>9</sup> Grewe, *Rückblenden 1976-51*, 1979, p.279-80.

<sup>10</sup> DDF, 1957, I, p.429.

*initialising at WEU an action contrary to their intentions.*<sup>11</sup> This sharp reaction was very inconvenient and surprising for the British. They had tended to neglect the impact their defence review would have on European political opinion and concentrated instead on getting approval by the US and NATO authorities.

Only very late the Americans had realized the real extent of the British plans, i.e. in early 1957. *'Sandys wanted to make it quite clear that HMG was not prepared to spend any foreign exchange on the maintenance of troops in Germany next year and therefore put us clearly on notice that the issue of whether any British forces would be maintained in Europe would arise in acute form in a years time.'*<sup>12</sup> The new British defence minister also provided the Americans with exact figures regarding the reduction plans which should be put into effect at the earliest time. Such precipitate action had been unacceptable above all for SACEUR Norstad who complained that these reductions made any forward strategy in Europe illusory. Washington shared this interpretation and made clear that though it understood the financial situation of the British it would oppose any rapid reduction. In this case, the Americans threatened, a US disengagement from Europe could not be ruled out.<sup>13</sup> Unison, Norstad and the US government demanded a phasing-out of the British plans. The British, which deemed US support crucial, had accepted this compromise to obtain American acquiescence to their plans. They agreed to start only at the end of 1957 with their first 13.500 men reduction of the BAOR (from 77.000 to 63.500) and to continue with a second tranche down to 50.000 in 1958/59.<sup>14</sup>

The eclat with the French endangered this compromise anew. A French-sponsored resolution against the British proposals was imminent, probably leading to a major diplomatic row. If the WEU members refused to approve the British case, an open breach of the WEU treaty would have been necessary in order to effect the cuts. The danger of antagonizing France and the others completely was obvious, particularly at that time. *'Moreover, the Paris Agreements*

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<sup>11</sup> *ibid.*, p.430.

<sup>12</sup> FRUS 1955-57, XXVII, Conversation US Sec.of Defense Wilson-Sandys, 29.1.1957, p.684.

<sup>13</sup> *ibid.*, p.685.

<sup>14</sup> BA, NL Blankenhorn, Letter to Adenauer, 11.3.1957; Mager (1990), p.180.

*and the current plans for the closer association of this country with Europe in a Free Trade Area had given great encouragement to our friends throughout Europe, and a faulty presentation of the withdrawal of British forces might do serious damage to our relations with European countries generally. We should therefore spare no effort to avoid a vote against us in WEU, which would leave us no alternative to breaking the WEU treaty....*<sup>15</sup> This quote from the Cabinet minutes illustrates that even if it came to a resolution the British government would not refrain from reductions on the continent. The serious considerations against such a confrontation, however, led the British to offer another minor concession: to wait with the discussion about the second tranche of reductions until October.<sup>16</sup>

Surprisingly, this proved to be enough. The French relented and refrained from a direct confrontation. This conciliatory mood might, however, not have been due to a reversal of their position but to relative weak support by the other Europeans, especially the Germans. The astonishing fact has its solution in a gentleman's agreement between the UK and the Federal Republic behind the scenes. After the Radford episode Germany had undertaken strenuous efforts to formulate a review of NATO which should promote closer consultation of the smaller nations by the Americans.<sup>17</sup> Looking for allies in this matter, the Germans had approached the UK. *'Mr.Lloyd said that the Germans attach great importance to their proposal for a review in NATO, and, although the British were unenthusiastic about it, they would support the Germans because the Germans had been so helpful to them in the WEU meeting.'*<sup>18</sup> Apart from that, the German government was convinced anyway of the inevitability of British reductions. It also was acquainted with the US position which had resigned itself to a certain number of reductions in view of Britain's economic problems.<sup>19</sup>

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<sup>15</sup> CAB 128/31, 17th meeting (5), 12.3.1957.

<sup>16</sup> *ibid.*

<sup>17</sup> Felken, *Dulles und Deutschland*, 1993, p.350-53.

<sup>18</sup> FRUS 1955-57, XXVII, memo of conversation Dulles-Lloyd, Bermuda, 22.3.1957, p.723. In the final result, the German efforts for more cooperation were not very successful. The US made clear that they reserved themselves the right to act without consultation if the situation demanded it. See: FRUS 1955-57, IV, Letter Adenauer to Dulles, 19.11.1957, p.187-190; conversations von Brentano - Dulles, 21.-24.11.1957, p.190-217.

<sup>19</sup> FRUS 1955-57, XXVI, memo on conversation v.Brentano-Dulles, Washington, 5.3.1957, p.216-217; *ibid.*, IV, Letter Dulles to Adenauer, 17.3.1957, 165-166.

Thus, the initial resistance of the WEU members had been overcome. On 18 March, the WEU council approved a reduction of the BAOR by 13,500 men and of the 2nd TAF by 50% of its aircraft and 25% of its personnel.<sup>20</sup>

However, for the UK this was only a first step. The central aim of the British reduction efforts in the following years was the manpower ceiling of 165,000 for the army, to be reached in 1962, in consistence with the abolishment of national service in this year. This long term perspective was known only to the US, SACEUR and Spaak as General Secretary of NATO.<sup>21</sup> It was evident that with such a manpower target further reductions in Germany were unavoidable, even below the figure of 50,000 which had been made known to the WEU partners.<sup>22</sup> The publication of the British White Paper on defence in April removed any doubts about British plans for the future of its forces in Europe. The basic purposes which were announced and the exclusive focus on nuclear weapons evoked mistrust and apprehension. The Germans in particular felt deceived because this kind of surprise was exactly what they had wanted to prevent with their reform proposals.<sup>23</sup> When Macmillan visited Bonn in May 1957 he was lectured about the German view of Western defence strategy, i.e. the importance of conventional forward defence.<sup>24</sup> The pronounced criticism compelled the UK to reassuring declarations about their intention to remain with troops in Europe. The British government thought it wise to wait until the financial situation at the end of 1957 as well as the outcome of new support cost negotiations were known, before starting the deliberations on a second tranche of reductions in WEU and NATO.<sup>25</sup>

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<sup>20</sup> Text of resolution in: Keesings Contemporary Archives 1957, 15724-725.

<sup>21</sup> PRO, T 225/1128, Report: Local Defense Cost Negotiations with Germany 1957-1958; prepared by Treasury, 16.10.1958.

<sup>22</sup> In January 1958 the British plans provided for a strength of 44,900 men in the BAOR by 1963 (and of 8,500 in the 2nd TAF by 1961), see: PRO CAB 129/91, Local Defence Costs in Germany: Report by Officials, 8.1.1958.

<sup>23</sup> BA, NL Blankenhorn, 75b/1, AA memo about British politics towards NATO, 29.4.1957; 75b/3, Diary Entry, 24.4.1957; NHP, Meeting with Chancellor Adenauer, 27.4.1957.

<sup>24</sup> BA, NL Blankenhorn 84/4, Summary Record on Adenauer-Macmillan conversations, 7.5.1957.

<sup>25</sup> Mager (1990), p.181-183.

c) A New Support Cost Row and Further Reductions

Although the Foreign Office raised objections against a new round of support cost negotiations, it became inevitable after heavy pressure was exerted by the Prime Minister and Treasury after a new balance of payments crisis.<sup>26</sup> Between July and September 1957, British reserves fell by £189m (\$529m) from a level of about £2400m.<sup>27</sup> Simultaneously, the repayment of the debts incurred during and prior to the Suez Crisis made the achievement of a positive balance of payments very difficult. The commitments of Britain included £80m a year repayments on US and Canadian loans, the repayment of the IMF drawing of £200m and of the EXIM bank loan of £180m.<sup>28</sup> The annual EPU deficits were an additional burden. To a certain extent, the 1957 payments crisis was a late legacy of the financial crisis accompanying the Suez adventure. The lasting debts incurred and, even more important, the profound shaking of confidence in the value of sterling would prove to be long lasting problems.

Markets got out of control in mid-1957. Suggested by the extreme surplus position of the Federal Republic and by the devaluation of the Franc in August, talk about a possible DM revaluation began and speculative money moved in huge amounts to Germany.<sup>29</sup> At the OEEC meeting in June, German and British interpretations of the imbalance had openly clashed. The British delegate called the German surplus '*very disturbing and depressing*' and accused the Germans of following an irresponsible monetary policy which took no account of the external situation.<sup>30</sup> According to the British, Germany had drained the system of reserves, accumulating them instead of re-investing them, as had been the enlightened practise

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<sup>26</sup> PRO, T225/1128, Report: Local Defense Cost Negotiations..., 16.10.1958.

<sup>27</sup> KCA 1957, 15770-71.

<sup>28</sup> PRO, CAB 134/2223, MAC(G)(57)29, 27.11.1957, UK Memo invoking NATO resolution of 26th July.

<sup>29</sup> Wippich, 'Die Rolle der Bundesrepublik Deutschland in der Krise des £-Sterling und des Sterling Gebiets, 1956/57', in: Schmidt(ed), *Zwischen Bündnissicherung und privilegierter Partnerschaft*, 1995, p.33-79.

<sup>30</sup> BA, B106/25878, Record of Working Party 19 Meeting of the OEEC Council 17-18 June, 3.7.1957.

of the Americans and the English after the war.<sup>31</sup> The Germans refuted this interpretation and saw the problem lying in different rates of inflation, thereby implying that the British should first fight against the sources of inflation in their own country.<sup>32</sup> They suspected that *'behind those...[British attacks]... obviously ... was the intention to prepare new requests on Germany in the framework of defence burden sharing (NATO)'*.<sup>33</sup> The differences between Anglo-American monetary policy, which accorded priority to the external account and to the stabilization of the currency on international markets, and the German policy which emphasized internal price stability<sup>34</sup> became clearly visible. Speculation against sterling calmed down only when German and English delegates came together at the IMF Meeting in September, and decided to make concerted announcements emphasizing their determination in maintaining existing parities.<sup>35</sup> They also decided to stop public accusations in these questions. However, the support cost question led to a fast termination of this uneasy truce. The monetary clash paralleled emerging conflicts in European and security matters.<sup>36</sup> From now on, international currency matters would become ever more strongly linked to these problems, and this would show itself immediately in the support cost negotiations.

In connection with the currency crisis, Britain had succeeded in obtaining a NATO resolution which said that a country with intolerable currency problems incurred by troop maintenance abroad could have the possibility of invoking examination of its problem by an independent team of NATO experts.<sup>37</sup> The United Kingdom, however, was at first reluctant to initialise such a multilateral NATO procedure, fearing that a public discussion would only heat on

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<sup>31</sup> FRUS 1955-57, IV, Dulles-Macmillan conversation, 14 December 1957.

<sup>32</sup> BA, B102/25878, Preparatory Meeting of German Officials on OEEC Conference, 3.6.57.

<sup>33</sup> BA, B102/25878, Excerpt of 248th ZBR Meeting, 26 June 1957.

<sup>34</sup> Germany had not to worry about deficits undermining their currency. Rather the contrary, foreign money moving in greatly complicated the Bundesbank's efforts to keep price rises under control despite the booming economy. See: Emminger, 'Deutsche Geld- und Währungspolitik 1948-75', in: Deutsche Bundesbank(ed), *Währung und Wirtschaft in Deutschland 1876-1975*, 1976, p.485-552.

<sup>35</sup> BA, B102/25817, Aide-Memoire UK to Germany, 18.9.1957; B102/12660, Emminger Report on IMF Annual Meeting, 30.10.1957.

<sup>36</sup> Unfortunately, a comparative study on the impact of monetary policy on European integration during the 1950s and 1960s does not exist.

<sup>37</sup> PA-AA, Ref.IIA7, vol.769, NATO Document C-M(57)112, 30 July 1957.

Sterling speculation and that Britain's own receipts by American and Canadian troops would be taken into account.<sup>38</sup> Therefore once more a bilateral approach to Germany was chosen and coupled with new discussions about troop levels which were to start in October 1957. *'The main point to make is that our decision as to whether any concession can be made over the 13,500 men will depend on what can be done to relieve us of the DM costs of troops in Germany. The whole question of what forces we can maintain and in particular whether we can make any concession to meet the point of view of our Allies depends on finance.'*<sup>39</sup> Any concessions, however, would at most apply to 5000 of the 13,500 men who were to be removed. Oddly enough, the British nevertheless expected a conciliatory mood from the Germans. This was based on incorrect reports from the embassy in Bonn: *'[There is now a] much better German understanding of our position and no inclination to have another knock-down drag-out row.'*<sup>40</sup>

Yet, German resistance to negotiations proved as strong as two years ago. The reaction to the British memorandum of 30 October was elusive.<sup>41</sup> All the Germans offered was an augmentation in the arms account at the Bank of England and in the £75m debt prepayment account, which had resulted from the last agreement. These offers were to underline that the Federal Republic was not prepared to extend any budgetary help and would confine its efforts exclusively to the monetary aspects of the problem.<sup>42</sup> Of course, the German proposals were unacceptable for the British as they would have only been a shortterm help for the balance of payments, but a longterm debt burden.

As the Germans refused to change their position, the British decided to invoke the NATO resolution of July, offering at the same time to limit their reductions to 8500 in the case of

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<sup>38</sup> PRO, T225/1128, report..., 16.10.1958.

<sup>39</sup> PRO, CAB 134/2223, MAC(G)(57)21, FO to UKdel Paris, 30.10.1957. See also: FRUS 1955-57, XXVII, memo of conversation Dulles-Lloyd, Bermuda, 22.3.1957, p.723.

<sup>40</sup> PRO, FO 371/130728, Steel to FO, 1.10.1957.

<sup>41</sup> PRO, T 225/1128, report..., 16.10.1958.

<sup>42</sup> BA, B126/34103, Finance Ministry Memo: Mutual Aid, Art.3 NATO Treaty, 28 November 1957; PA-AA, Ref.IIA7/769, von Brentano to Adenauer, 12 February 1958.



a satisfactory financial solution.<sup>43</sup> NATO appointed a panel of three experts to investigate the influence of the troops on the monetary problems of Britain. The German government made its disapproval of this procedure known immediately: '*A balance of payments problem resulting from troop maintenance in Germany does not exist...The British balance of payments position has general monetary and politico-economic reasons. It is out of place to link it with NATO defence questions*'.<sup>44</sup> Only late did the British government learn of the reasons for this intractability. They were bluntly told that Germany expected the British to pull back anyway and saw no point in paying anymore.<sup>45</sup> Furthermore, the Germans argued that their military build-up was in full steam now and that estimates for defence appropriations in the following years showed precipitous rises. Further support costs would only enlarge the gaps in future budgets.<sup>46</sup> They refused to accept the NATO procedure even when the experts approved the British case in their report, presented in January 1958.<sup>47</sup> With special regard to British efforts to strengthen their currency and to hold to this end their balance of payments in continuing surplus, the experts judged the British request for financial help legitimate. However, the Germans persisted in their argument that the British problem justified only monetary help, not budgetary payments, and made this position public.<sup>48</sup>

This led to a stalemate that even Spaak, who was at that time Secretary General of NATO and closely involved in the discussions, could not dissolve. His visit to Bonn proved as abortive as repeated personal messages of Macmillan to Adenauer.<sup>49</sup> Concerted pressure by the Western NATO members was futile.<sup>50</sup> Spaak was stunned by the atmosphere of suspicion

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<sup>43</sup> FRUS 1955-57, XVII, memcon Dulles-Lloyd, 22 October 1957, p.804.

<sup>44</sup> PA-AA, Ref.301, 98, AA Brief for NATO Council meeting, January 1958.

<sup>45</sup> PRO, FO 371/137374, Conversation Lloyd-v.Herwarth, 18.2.1958.

<sup>46</sup> BA, NL Blankenhorn 80/2, Memo prepared by German embassy at NATO: Financial Planning for Defence until March 1961, 9 November 1957.

<sup>47</sup> PRO, T 225/1128, Report..., p.7-8.

<sup>48</sup> KCA 1958, p.16239; PA-AA, Ref.301/98, AA memorandum for NATO-meeting, 17 January 1958.

<sup>49</sup> PRO, T225/1128, note on Spaak visit, 31.1.1958; PREM 11/2331, Record of Macmillan-Adenauer conversation in Paris, 15.12.1957; Adenauer to Macmillan, 4 January 1958; BA, NL Blankenhorn 85a/3, diary entry, 2.2.1958.

<sup>50</sup> BA, NL Blankenhorn 85b/2, Record of a Secret Meeting of NATO ambassadors, 21.1.1958; BA, B126/34103, Summary of NATO Council Meeting, 8 January Meeting.

towards England he had encountered in Bonn.<sup>51</sup> The FIG agreement (see ch.VI) had been signed in November 1957, and German willingness to co-operate with Britain was at its lowest.<sup>52</sup>

In late January 1958, the WEU council approved a reduction of 8500 men in the BAOR. The decision was doubtlessly eased by German resistance to accept the report of the NATO experts.<sup>53</sup> This passed the buck back to the British. Their plans to withdraw a further 5000 men, a strategic reserve of special importance, met concerted resistance.<sup>54</sup> Especially SACEUR Norstad was under no circumstances ready to accept this further weakening of his lines. The USA urged Britain to stop the reductions and accept a compromise in the support cost question, offering simultaneously American aid to cover the burden which was not met by a German-British agreement.<sup>55</sup> The Americans offered a further carrot: the intensification of Anglo-American cooperation in nuclear technology would proceed much smoother if the British were willing to maintain their military presence in Europe at roughly the same scale.<sup>56</sup>

The British government finally decided to take a step which was long overdue. It accepted a long-term solution for the problem, coupled with a new pledge for a minimum level of troops. Due to the increasing size of the German army, a continuation of support cost payments after the current year was doubtful.<sup>57</sup> Sticking to an uncompromising stance could have grave political consequences: '*(a) a weakening of NATO; (b) the frustration of our plans*

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<sup>51</sup> PRO, FO 371/137374, Roberts to FO, 3.2.1958.

<sup>52</sup> BA, B126/34102 contains a Finance ministry note reporting a striking re-orientation of German programs for military orders towards France and Italy, 18.2.1958.

<sup>53</sup> French resistance was this time less rigid. France agreed to the new reductions, yet not without signaling 'the very grave consequences which derive from the progressive weakening of the British presence on the continent, coming close to put into question the foundations of common defense'; DDF 1958 I, Pineau a Chauvel, 28.1.58, p.100-101.

<sup>54</sup> PRO, T 236/5099, UKdel Paris to FO, 8.4.1958; *ibid.*, Chancellor of Treasury minute on conversations in Paris, 28.4.1958; FRUS 1958-1960, VII, 1, Memo of Conversation Dulles-Norstad, 26.9.1958, p.358.

<sup>55</sup> PRO, T 225/1128, background notes: strength of BAOR, 30 October 1958.

<sup>56</sup> Clark, *Nuclear Diplomacy and the Special Relationship, 1957-62*, 1994, p.222-24.

<sup>57</sup> CAB 128/32, 16th cabinet meeting, 12.2.1958.

*under the heading of ... consultation, etc.; (c) more European Six Power activity...; (d) serious prejudice to the prospects for obtaining the free trade area; (e) an increase, especially in Germany, in the desire to make some sort of a settlement with Russia'.<sup>58</sup> Additionally, further large scale reductions became increasingly difficult to handle because of a lack of housing and facilities for the returning soldiers.<sup>59</sup>*

The British transmitted their new proposals based on these considerations to Spaak. These contained a declaration of intent to keep the BAOR at 45,000 men until 1962, if Germany covered one third of its foreign exchange cost during this period and supported sterling by prematurely repaying postwar debts as well as depositing a further advance amount for arms orders in the Bank of England.<sup>60</sup> For the first time Britain officially linked the FTA problem to the support costs. One of the conditions was that *'the organisation of Europe in the economic field develops in a manner consistent with the political and military organisation of NATO and enables the United Kingdom to participate with its Allies on equal terms.'*<sup>61</sup> The British informed the Germans that if their proposal was not accepted they would not hesitate to withdraw all their troops; the Germans replied that this only showed the British lack of interest in Europe.<sup>62</sup>

When the proposal reached the German government, however, a struggle broke out between the supporters of an uncompromising stance and more conciliatory advisers who grew more and more uneasy about British-German relations.<sup>63</sup> The lines of division were essentially the same as those later found between Gaullists and Atlanticists. The Germans even presented two different proposals at the same time. Soon after von Scherpenberg, Permanent Secretary of the *Auswärtiges Amt* and in charge of the negotiations, had communicated a plan close to the British position, another official memorandum, influenced by Strauß, arrived in London which

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<sup>58</sup> PRO, CAB 129/91, Local defence Costs in Germany. Report by Officials, 8.1.1958.

<sup>59</sup> CAB 128/32, CC 19(58), 27.2.1958.

<sup>60</sup> PRO, T 225/1128, report..., 16.10.1958; CAB 128/32, Cabinet Conclusions 19(58), 27.2.1958.

<sup>61</sup> *ibid.*

<sup>62</sup> PRO, PREM 11/2331, Lloyd-von Brentano discussion, 6 March 1958.

<sup>63</sup> BA, NL Blankenhorn, 85a/3, diary entry, 2 February 1958.

entirely rejected the British proposals.<sup>64</sup> It explicitly negated a connection between the organisation of Europe and monetary problems arising from the maintenance of British troops in Germany. An Adenauer visit to London, planned for April, however, gave new urgency. The Chancellor did not want to be bothered by the problem. Finally, the Germans gave up their resistance to cash payments. They wanted to secure the presence of a British force of at least some value, declaring that '*45.000 British soldiers were better than 50.000 French grandmothers.*'<sup>65</sup>

The UK, by agreeing to the Scherpenberg proposals, finally managed to achieve a solution after discussions lasting more than six months. The Germans paid \$33.6m (£12m) a year until March 1961, they maintained an interest free account for arms order at the Bank of England (\$140m), and they paid the 1962-1964 rates of the London debt agreement prematurely (£7.5m annually). The British government declared that it would keep its troops at 55.000 (i.e. including the strategic reserve) until the end of 1958 and at 45.000 until March 1961. 45.000 men was the highest number acceptable for Britain to remain in Germany under the manpower ceiling of 165.000 for the army, the figure which had been decided in the defence review. However, SACEUR and the US urged the British to postpone any further reductions to the latter figure.<sup>66</sup> This interest was used by the British to opt for additional dollar-aid.<sup>67</sup> Against an aid of \$25m destined for mutual weapon development, the British government agreed to keep the troop level stable in 1959.<sup>68</sup> This link was kept secret to spare the US government embarrassing questions in Congress. It displayed clearly the concern of the United States about the never-ending quarrel between its allies. The Americans also renounced once more to request support costs for themselves. The British told them in unequivocal terms that if the US persisted in demanding a share thereby limiting the funds available for them, their

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<sup>64</sup> This memorandum is in PA-AA, 301/98, Aide-Memoire, 27.3.1958.

<sup>65</sup> PRO, T 236/5099, Bonn tel.333 to FO, 12.4.58.

<sup>66</sup> For this and the following PRO, T225/1128, Background Notes: Strength of BAOR, 30.10.1958; UK Embassy Washington to Ministry of Defense on Sandys' talks in Washington, 27.9.1958.

<sup>67</sup> FRUS 1958-60, VII/2, conversation Dulles-Lloyd, 4.5.1958, p.327-328.

<sup>68</sup> FRUS 1958-60, VII/1, p.348, fn.1.

troops would leave Europe.<sup>69</sup> As compensation, the Americans agreed with the Germans on a pre-mature repayment of postwar debts to aid the weakening American balance of payments.<sup>70</sup>

The British-German agreement calmed down the support cost-front of British-German relations for three years. It did not prevent, however, the hidden tensions which made the problem such a hot issue from 1955 to 1958 from erupting in 1959 on the highest level.

#### d) The Organisation of Europe and the German-British Crisis 1959

In the previous chapters the deterioration of British-German relations due to fundamental political differences in monetary and security issues from 1955 on has been outlined. The British government was content with the status quo in Europe, judged the situation as essentially stable, and for this reason it saw no need to continue undermining one of the most fundamental objectives of its policy, the strengthening of sterling, by what it saw as a major reason for sterling's weakness, its troop maintenance in Europe. The Germans, on the other hand, still felt the need for direct protection and forward defence. They also expected Britain to express support for the long-term goal of German reunification. That they should pay for this with support for the British currency policy, which they saw as flawed due to domestic mismanagement, caused deep resentment. Problems such as support costs tended to expose these differences in full light and thus came to acquire a disproportionate potential for conflict. These conflicts had serious repercussions on other fields of British-German relations in general and on mutual policies towards the question of Britain's place in Europe in particular.

The British FTA proposal was an attempt to create an economic and political environment which would prevent the prolongation of the continual crisis that plagued Britain after World

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<sup>69</sup> *'The Foreign Secretary [Lloyd] said the question is simply this: Does the United States want to see Britain keep troops in Germany? They will not stay there unless their local costs are paid and a U.S. demand now for additional money would diminish this possibility'*; FRUS 1955-57, XXVII, memcon Dulles-Lloyd, 25 October 1957.

<sup>70</sup> see: Table 7, Appendix I; also: BA, B136/3132, von Brentano to Chancellor's Office, 10.3.59; PA-AA, Ref.IIA7/1201, AA memorandum on US support costs, 10 September 1958.

War II. After the Rome Treaty with its relatively strong integrative clauses and the common external tariff had been ratified, it was obvious that Britain would need strong support from within the Community in order to reconcile its proposal with the already existing arrangements. The success of the British proposals depended much on the German attitude, especially when the French position appeared more and more intransigent.<sup>71</sup> The prospects for a functioning German-British collaboration in this field did not seem bad.

In his famous Brussels speech in September 1956, Adenauer publicly emphasized his support for a close British alignment to the continent.<sup>72</sup> In 1957, he made plain his support for the FTA to Macmillan.<sup>73</sup> It was well known that the German Minister of Economics, Ludwig Erhard, was a fervent supporter of a larger economic cooperation than the limited Common Market. He was supported by the majority of industrial leaders and by the public opinion.<sup>74</sup> Additionally, the arrival of de Gaulle in power evoked deep apprehensions and mistrust in Germany, not least in Adenauer.<sup>75</sup> One of the first actions of de Gaulle, his proposal for a 'world directorate' composed of the US, Britain and France, infuriated the Germans and gave the British an opportunity to make easy points.<sup>76</sup> Equally irritating for Germany was the brusque revision of the FIG agreement by de Gaulle (see ch. VI). The British government had

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<sup>71</sup> PRO, FO 371/137387, Briefing Paper on Adenauer Visit, April 1958. Horne, *Macmillan, Vol. II*, pp. 34, 110-11; Young, 'Towards A New View of British Policy and Europe', in: Ahmann/Birke/Howard (eds), *The Quest For Stability*, 1993, p. 459.

<sup>72</sup> Schwarz (ed), *Adenauer. Reden 1917-1967*, 1975, p. 327-332. Adenauer, *Erinnerungen 1955-59*, 1967, p. 255-265; Adenauer: "....um den Frieden zu gewinnen". *Die Protokolle des CDU Bundesvorstands 1957-61*, 1994, p. 116.

<sup>73</sup> Macmillan Diary, 8.5.1957; quoted in: Horne (1989), p. 33.

<sup>74</sup> The last years have seen a rapid growth of archive-based research on German policy towards Europe after the Rome Treaties. See for example: Brenke, 'Europakonzeptionen im Widerstreit. Die Freihandelszonenverhandlungen 1956-58', in: VFZ 4/1994, p. 595-634; Schaad, *Anglo-German Relations during the Formative Years of the EC, 1955-61*, PhD thesis, Oxford 1995; Körfer, *Kampf ums Kanzleramt*, 1987; Küsters, 'Die Europapolitik der BRD im Spannungsfeld von EWG- und EFTA-Gründung 1956-58', in: Hudemann/Kälble/Schwabe (eds), *Europa im Blick der Historiker*, 1995, p. 203-240.

<sup>75</sup> BA, NL Blankenhorn, 19.5.1958, conference Adenauer, v. Brentano, Blankenhorn; *ibid.*, Blankenhorn to Adenauer, 23.5.1958.

<sup>76</sup> For de Gaulle's proposal see: FRUS 1958-60, VII/2, p. 81-83; PRO, FO 371/137378, Record of Adenauer-Macmillan conversations, 8.-9.10.1958; BA, NL Blankenhorn, note on German-English talks, 8.10.1958. The friendly but firm rejection of de Gaulle's memorandum by all NATO members marked the beginning of the long decline in France's relations to NATO, and the 'Anglosaxons' in particular, during de Gaulle's term. See: FRUS 1958-60, VII/2, Eisenhower to de Gaulle, 20.10.1958, p. 108-109.

every reason to hope that their supporters within the German government might overcome the advocates of a narrow European solution.<sup>77</sup> How was this possibility lost?

The neglect of the relations with Germany in the preceding years turned out to be a heavy burden. A decisive part of the German political establishment had come to regard British policy with deep mistrust. The failure to join the EDC, the subsequent military policy, the distance towards the Common Market and the hostile attitude of the British press were transmitted by Adenauer's aide von Eckardt to the British ambassador as German complaints. As for FTA, it was seen as a mere attempt by the British not to be excluded from the economic benefits of the EEC.<sup>78</sup> When the FTA was mentioned to Adenauer by the Australian Prime Minister Menzies, he elaborated on the British unreliability in the security field.<sup>79</sup> The feeling of suspicion peaked in early 1959 when Macmillan announced a trip to Moscow without consulting Adenauer.<sup>80</sup> The Chancellor feared that the British worked towards allied disengagement from Europe and deeply resented their disarmament plans.<sup>81</sup> The British embassy in Bonn stated woefully that the '*Chancellor's suspicions of us are not only still alive but more rampant than they have ever been...[He] is convinced that we are preparing to sell Germany down the river*'.<sup>82</sup> During the year 1959 the attitude of the British and German leaders towards each other went from bad to worse.<sup>83</sup> When the British warned the Germans of the dangers of a narrow European solution and urged them to use their influence against France, they mostly resorted to the threat of a British disengagement from Europe which, as it turned out, was a somewhat counter-productive move.<sup>84</sup>

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<sup>77</sup> Greenwood, *Britain and European Cooperation since 1945*, 1992, p.61-72.

<sup>78</sup> PRO, FO 371/137375, Steel to Lloyd: Minute on UK German relations, 10.4.1958.

<sup>79</sup> For example: BA, NL Brentano, 179, Scherpenberg to von Brentano on a conversation Adenauer-Menzies, 19.6.1959.

<sup>80</sup> PRO, FO 371/145773, Steel to FO, 3.2.1959; Adenauer, *Erinnerungen 1955-1959*, 1967, p.468-471.

<sup>81</sup> PRO, FO 371/145773, 3.2.1959, Steel to Foreign Office. See also: Siebenmorgen, *Gezeitenwechsel*, 1990, p.261. The attraction of disarmament for Britain at that time stemmed, of course, also from the prospect of some defence economies. See: DDF 1958 I, Chauvel to Pineau on conversation Moch-Lloyd, 3.3.1958, p.257.

<sup>82</sup> PRO, FO 371/145774, Bonn to Foreign Office, 31.3.1959.

<sup>83</sup> Horne, *Macmillan, Vol II*, 1989, p.133-136.

<sup>84</sup> See for example: BA, NL Blankenborn 87/5, Record of Adenauer-Macmillan conversation, 18.4.1958.

Even at that time, Adenauer's suspicious attitude was not shared unanimously in the German government. Repeatedly, Erhard had encouraged the British to pursue their FTA plans.<sup>85</sup> Prior to Adenauer's visit to England in November 1959 one of his own ministers, the Minister of Atomic Matters, Balke, had urged the British '*not to be so polite that he [Adenauer] comes back still believing that Britain is a negligible quantity*'. Balke criticised the Rome Treaty with astonishing frankness as '*a Catholic Alliance reviving the Carolingian empire in the form of a third force*.'<sup>86</sup> The same message was transmitted by the Bundesbank. Its representative at the BIS meeting in Basel, Blessing, had counselled the British to be tough with Adenauer in order to convince him of the dangers of an economic division of Europe.<sup>87</sup>

However, the British had not much in hand to be tough. Nuclear cooperation had been ruled out, a whole-hearted commitment to German reunification was very unpopular in England, and in the economic field both were more competitors than collaborators. The British capacity to influence German politics was therefore quite limited. At this point the function of the British troops in Germany as the guarantors of its security seemed the only means of pressure left. Internally, Macmillan had repeatedly made this link.<sup>88</sup> He even employed the troops to impress de Gaulle. '*If this negotiation [i.e. on the FTA; HZ] does not succeed, a very dangerous situation would result....I recall to your mind that we have made a big effort for Europe. For this reason we have four divisions in Germany. If, however, the issue of the [free trade] area does not progress in a satisfactory way, we would have to look for new friends*.'<sup>89</sup> Presumably de Gaulle was not very impressed by this intimidation. To him, Britain had already chosen its friends: they sat in Washington.

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<sup>85</sup> Erhard understood the Rome Treaties only as a first step towards a much larger economic framework. He did not share the predominantly political attitude of Adenauer towards the European institutions and supported therefore vehemently the British FTA proposals. See PRO, FO 371, 137388, Record of British-German meeting, 16.-19.4.1958. See also: Lappenklpper, 'Ich bin wirklich ein guter Europäer'. L.Erhard's Europapolitik 1949-1966', in: *FRANCIA* 18/3 (1991), p.85-100.

<sup>86</sup> PRO, FO 371/145780, Confidential Letter of P.Tennant (Overseas Director of the Federation of British Industries) to Maudling, Macmillan, and Lloyd, 29.10.1959. A remark on the letter says that the Prime Minister was 'impressed' by it.

<sup>87</sup> PRO, FO 371/145781, R.Makins to Foreign Office, 12.11.1959.

<sup>88</sup> PRO, PREM 11/2315, 24.6.1958, note Macmillan to Foreign Minister and Treasury, 24.6.1958. See also: Griffiths, 'The failure of the wider free trade area', in: *EFTA Bulletin* 3/4(1991), p.15-20.

<sup>89</sup> DDF 1958 I, Compte Rendu des Entretiens Franco-Britanniques, 29.-30.6.1958, p.870.



The Americans, who adopted a very hesitant attitude towards British demands to help them in the European question, were admonished with the same argument. Lloyd explained to them that *'the continued economic and political division of Europe would, for example, make it difficult for the U.K. to keep its troops in West Germany'*.<sup>90</sup> Nevertheless, the US indicated clearly to the Germans that they preferred the Common Market to a wider, possibly discriminating, free trade area.<sup>91</sup> This did not prevent Macmillan from repeating his threats even more explicitly in Washington: *'If exports fall, there will be a pressure on sterling of a sort which inexorably demands countering measures such as deliberalization and other backward steps. The British people would not be prepared under these circumstances to continue to spend across the exchanges, year after year, 50 or 60 million pounds to keep troops in Germany, as they would feel their economic distress was caused by German discrimination and would see no justification for continuing to help defend Germany.'*<sup>92</sup>

Directly and frequently the threat of disengagement was used with increasing intensity against the Germans.<sup>93</sup> In November 1959, it became an open means of pressure against Adenauer to induce West Germany to a more cooperative European policy. The relevant passage of the Adenauer - Macmillan talk is worth quoting at length for it makes the use of the troops for politico-economic aims extremely clear. After Adenauer had expressed his deep concerns over a British disarmament proposal for a denuclearized zone in Europe, Macmillan retorted harshly by putting into question the British WEU commitment: *'Frankly, had the British government of that day thought of the Six Powers of the European Economic Community forming an economic grouping from which Britain would be excluded, they would not have accepted such a commitment. Nor could it be expected that any British parliament would continue those obligations under such changed conditions. In this matter economics and politics run together. He hoped that Dr. Adenauer would realise that for an island people like the British, maintaining troops abroad for a long period was unprecedented<sup>94</sup> and would be*

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<sup>90</sup> FRUS 1958-1960, VII/1, conversation Lloyd-Dillon, 8.12.1959, p.176.

<sup>91</sup> *ibid.*, conversation Dillon - Adenauer, Erhard, et.al., 11.12.1959, p.196.

<sup>92</sup> *ibid.*, Memo of Conversation Macmillan - Herter, 28.3.1960, p.273.

<sup>93</sup> PRO, PREM 11/2707, Conversation Etzel-Lloyd, 17.6.1959.

<sup>94</sup> A puzzling interpretation of British 19th and 20th century involvement abroad.

*very difficult to continue if there were two economic groups in Europe engaged in a sort of economic war. The proposals for a common tariff for the Six meant a permanent discrimination against the UK. It would be almost impossible to honour the West European Union commitments while simultaneously conducting a tariff war. Therefore it was essential either to bring down discrimination to negligible proportions or to negotiate some other arrangements.'*<sup>95</sup> The meeting, which had started with mutual recriminations<sup>96</sup>, brought both sides nowhere closer to those 'other arrangements'.

What is especially striking in retrospect is the fact that the British did not realise that the worth of their security guarantee had been devalued by their own actions over previous years. The British troop commitment had been presented as a liability which Britain had no intention of carrying further if the cost was not offset. Whenever British politicians cited the danger of an economic division in Europe, they were confronted with the effects of their defence policy and whoever wanted to attack the British FTA plans was free to cite the defence policy as an evidence of Britain's shaky reliability. It was an additional irony that the reduction threat in 1959 was a mere bluff as the UK had quietly decided to stop the reductions.

Several circumstances worked together to induce the government to this step which stabilized the troop-level in Germany at about 55.000 men. Firstly, in November 1958, Khrushchev's Berlin ultimatum had greatly heated the climate of the Cold War. Secondly, the British were forced by a long-drawn guerilla war in Cyprus to give the country its independence and to reduce their garrison there by 20.000 men to a mere 5.000 men.<sup>97</sup> Upon their return, these troops and those coming from Europe encountered a serious lack of housing, training areas, and other facilities. This posed difficult administrative problems to the government and forced it to stop the reductions in Europe.<sup>98</sup> The arguments of the Foreign Office against reductions

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<sup>95</sup> PRO, FO 371/145780, Record of Conversation Adenauer - Macmillan, 19.11.1959.

<sup>96</sup> *ibid.*, Record of a conversation Adenauer-Macmillan, 18.11.1959.

<sup>97</sup> Keesing's Contemporary Archives, p.16833.

<sup>98</sup> 'Informed opinion in the Ministry of Defense is that in view of the Berlin Crisis and the rundown in Cyprus it is likely that this [i.e. the stop] is the line which will be recommended', PRO, T 225/1129, note, 29.4.1959. See also: PRO, PREM 11/2704, Record of a Meeting Strauss-Macmillan, 11.5.1959; T 225/1391, Treasury Brief for Etzel Visit, 10.6.1959; *ibid.*, Prime Minister to Chancellor of Exchequer, 9.7.1959.

also gained new weight. *'Nothing would suit Dr. Adenauer and Herr Strauss better than to see our troops in Germany reduced while theirs are being augmented. They want a larger share of the NATO commands...[and would be]...able to say...that we were of less use as allies and that there was less need to meet us over the FTA because we were pulling out of Europe anyway'*.<sup>99</sup> Finally, the Americans would have been certainly distressed by further reductions. To use the stabilization of the troop level now as a demonstration of European mindedness was therefore slightly anachronistic. Whatever the remaining value of this stick, it beat a donkey which was already on the wrong path.

Summing up all evidence, a powerful influence of security questions on Germany's attitude towards British European policy is visible in many ways.<sup>100</sup> This influence showed less on the level of the actual discussion of the British FTA proposals. Discussed were mostly economic problems. Britain's will to exclude agricultural products from the FTA, to sustain a preferential treatment for Commonwealth, and to resist a common external tariff was difficult for the Europeans to accept. They would have altered the character of the Rome Treaties. Recent research, however, has shown that these economic divergences might have been overcome or mitigated by certain compromise agreements.<sup>101</sup> Germany, for example, would have benefitted economically more from the FTA than from the Common Market. These compromise formulas might have been achieved by concerted pressure from the other Five on France. When, however, the moment was approaching for strong intervention to brush aside the obstacles, nothing occurred and the German government exerted very little if any pressure on France.

This unwillingness to search for a compromise or to support Britain more forcefully had much to do with the conflicts in the security and the monetary field. It was a clear misjudgement by the British government to employ their security guarantee in economic and monetary conflicts with Europe while simultaneously depriving this guarantee of much of its credibility; particularly, as Britain had not much else on offer for Europe. What spoiled the FTA for the

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<sup>99</sup> PRO, T 225/1391, Lloyd to Prime Minister, 8.7.1959.

<sup>100</sup> See also Schmidt (1989).

<sup>101</sup> Griffiths, *The Creation of EFTA* (forthcoming).

Germans was the lack of a political commitment. The proposal seemed more destined to contain than to cooperate with Germany. The support cost and troop level problem lent this impression much of its credibility. For long periods, support cost negotiations poisoned mutual relations and reduced them to a question of financial bargaining. Seen as a whole, these conflicts and British proposals for Europe did not fit together. Thus, British policy was seen as contradictory and confused at best, and as deliberately destructive at worst.

CHAPTER V  
CENTURION AND OTHER GADGETS:  
THE FAILURE OF BRITISH WEAPONS EXPORT TO  
THE FEDERAL REPUBLIC

Throughout the 1950s and 1960s, German arms purchases were seen by both the US and the UK as a principal way of balancing the foreign exchange cost of their troops in Germany. Therefore, they were a recurrent theme in all support cost- and -later- offset negotiations. The conspicuous failure of British efforts to conquer a large segment of the weapon market in the rearming Federal Republic had a significant impact on these negotiations as well as on many other bilateral issues. In order to trace these connections I will outline in the following chapter the causes and consequences of the British failure to sell a sizeable quantity of military hardware to Germany.

A considerable amount of time passed before German rearmament after 1955 would be able to relieve the NATO partners of some of their defence burden in Europe (ch.II). Neither did the build-up of the German army move as fast as desired nor the vast military orders which were expected to materialize. Impatience on the part of the British and the Americans rose fast. When the Germans somewhat impertinently asked the United States in early 1956 for more financial assistance to rearmament they received a blunt response. The Americans accused them of spending far less than the average of other NATO-countries on defence matters despite the excellent state of their economy. Therefore, any additional aid would be precluded.<sup>1</sup> Washington urged Bonn particularly to complete defence procurement plans and demanded that much higher orders be placed in European countries. This was a distinct hint on the support cost negotiations between Britain and Germany.

American grant aid to Germany was seen as increasingly anachronistic by the Eisenhower administration, given the economic situation in the Federal Republic. The last big item was the so-called Nash-list from 1953. It was worth about \$900m and it consisted mainly of loans

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<sup>1</sup> For the German memorandum: BA, B 126/51520, 10.1.1956; the answer: BA NL Blankenhorn 61b,1, Memorandum US to FRG, 15.3.56.

of military material, military training and exchange programs.<sup>2</sup> It was the only aid commitment of the United States to continue after the 1956 memorandum. This and earlier American military aid programs, however, had one important lasting consequence, because they provided the German forces with their basic equipment, for example tanks. The Bundeswehr developed in many respects a structural dependence on American material. This dependence tended to perpetuate itself because newly bought US arms were more compatible with existing stocks than material from any other source.

The Germans, in the period in which the US memorandum arrived, fully agreed with the request to buy the Bundeswehr equipment abroad. Firstly, they lacked their own armaments industry; advanced military material was only available abroad. Furthermore, as already outlined in chapter II, there were apprehensions of a macro-economic nature, brought forward by Finance Minister Schäffer and by Strauss. There was the danger of domestic inflation in case of too much government investment, the possible curtailment of German export capabilities<sup>3</sup>, and the disturbingly high balance of payments surplus. Strauß resumed: *'Apart from the advantage that arms and equipment from allied NATO countries originate from current production and have therefore -partly- considerable price advantages, ordering weapons abroad also effects trade policy. By buying abroad we correct payments imbalances caused by the German export surpluses in deficit countries. In particular, we are able to reduce our surplus in the EPU.'*<sup>4</sup> Most German industrial leaders shared the feelings of the government and argued that for the moment their total capacity was being employed.<sup>5</sup> To produce the equipment for the planned 12 divisions in such a short time was regarded impossible, damaging to export prospects, leading to tax rises and incalculable conversion costs. Furthermore, German industrialists still remembered vividly the demontation period

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<sup>2</sup> For US aid to Germany see: Birtle, *Rearming the Phenix*, 1991.

<sup>3</sup> FAZ, 6 March 1956. Precisely this was a hope of parts of the British government and industry.

<sup>4</sup> Strauß, in: BPl, 27.2.1958, p.330-331.

<sup>5</sup> Thus even industrial leaders at that time were in favour of arms purchases abroad, though this attitude diminished considerably later on. See: Brandt, *Rüstung und Wirtschaft in der Bundesrepublik*, 1966, p.148-151. See also: Abelshäuser, in: Heller/Gillingham, 1992, p.313, 327; Leaman, *The Political Economy of West Germany*, 1988, p.85; THE ECONOMIST, 11.2.1956, p.49.

after the war and the strong attacks on them for producing weapons for the Nazis.<sup>6</sup> Certainly, the competitive advantage by weapons industries in other countries also played a role in the initial reluctance of the German industry to fight for a share of the cake.<sup>7</sup> The industry's restraint in producing weapons was to change relatively quickly.

In 1955/56, however, German and allied objectives appeared in accordance. There was still the question from which sources Germany would get the equipment for its military forces. Would it cooperate mainly with the United States or with Western Europe? How strong was domestic production going to be? What role would the United Kingdom play? These decisions had not only economic consequences. They also were to be of considerable political importance.

Early on, France, the UK and the United States started to compete for German orders. During the EDC debate, a future European armaments cooperation along with the European army had been foreseen.<sup>8</sup> Such plans vanished together with the EDC. After Germany's accession to NATO, the three major Western weapon producing countries rushed to get their foot in a market with enormous potential. The US in October 1956 concluded an agreement stipulating the framework of defence procurement by Germany.<sup>9</sup> The US government would act as an agent for military sales and payments were to be transferred to a specific account maintained by the US Treasury. The French proposed shortly after the demise of EDC a European arms pool to the Federal Republic.<sup>10</sup> Despite these activities the Germans felt no urgent need to choose between the competitors. The rearmament crisis made the final form of the German army difficult to foresee. Therefore, procurement plans were at a rather preliminary stage. The strategic debate in the Alliance, undermining the importance of conventional weapons, added another factor of insecurity.

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<sup>6</sup> Brandt, 1966, p.86-87.

<sup>7</sup> *ibid.*, p.175-78.

<sup>8</sup> Abelshauser, 'Rüstung, Wirtschaft, Rüstungswirtschaft', in: Maier/Wiggershaus(eds), *Das Nordatlantische Bündnis*, 1993, p.97-98.

<sup>9</sup> TIAS 3660, Exchange of notes: Mutual Defence Assistance, 8 October 1956, p.2787-2802.

<sup>10</sup> Abelshauser, "Integration a la carte". The Primacy of Politics and the Economic Integration of Western Europe in the 1950s, in: Martin S.(ed), *The Construction of Europe*, 1994, p.13-15.

Political pressure from abroad, however, mounted, particularly in the context of the support cost negotiations. Soon after the US memorandum cited above had arrived, Blankenhorn, the German ambassador at NATO, was informed that the previously earmarked sum of \$619m for military purchases in Europe over the whole rearmament period would have to be increased as a consequence of the support cost negotiations to \$1430-1670m.<sup>11</sup> However, the authors of the memorandum added, that military experts did not expect orders of this size to be feasible. This was a sound judgement. When finally the first orders were placed their volume was disappointingly low. In the 'Questionnaire', the Federal Republic had to submit to the Annual Review Meeting of NATO in October 1956, the announced target figures for orders in Europe turned out to be considerably less than expected by the allies. Initially, Germany had planned to order weapons to the tune of about \$595m from European sources and \$2143m from the United States in the period 1957-1959. Defence Minister Strauss, however, explained that in the following two years, 1957-1958, \$286m could be expected for Europe and \$548m for the US, adding that even these figures were possibly too high.<sup>12</sup> Actual orders of \$238m in EPU-countries and \$286m in the United States had been placed until the end of 1956 by the Federal Republic.<sup>13</sup> This seemed to indicate a balance between European and American sources at this point.

The American lead, however, was to increase progressively. Various French efforts to get Germany to agree with their proposals of a bilateral arms cooperation scheme failed, most spectacularly in the famous Franco-Italian-German Trilateral agreement. Almost immediately after the EDC had been outvoted by the French parliament, the French had proposed a bilateral armaments organisation to Bonn which would work separately from the WEU armaments committee. For this reason, the Germans had initially stalled.<sup>14</sup> In late 1956, after the Radford plan crisis, Adenauer suddenly came out as a supporter of the French plans.<sup>15</sup>

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<sup>11</sup> BA, NL Blankenhorn, 61a/1/42-44, note Wirtschaftsministerium, 7 April 1956.

<sup>12</sup> *ibid.*, 68/1, NATO Review Meeting: Questionnaire on German military build-up, 29 October 1956.

<sup>13</sup> *ibid.*

<sup>14</sup> DDF 1956, II, Doc.188, Faure-Adenauer, von Brentano conversation, 17.9.1956, p.392-96.

<sup>15</sup> DDF 1956 III, Doc.104: Couve de Murville a Pineau, 3.11.1956, p.164-65; Doc.123: Notes pour visite du Chancelier: Cooperation franco-allemande, 3 November 1956; Abelshauser, in: Martin(ed), 1994, p.12-16; for some further details in a rather poor article on the issue: Bossuat, 'Les Armements dans les Relations Franco-Allemandes



Strauß, who was the major German driving source behind the idea of a European armaments cooperation, was also well disposed towards the French ideas. In 1957, the French extended their proposals even to the nuclear sphere.<sup>16</sup> A protocol was signed which stipulated French-German cooperation in the whole field of military production, including nuclear weapons.<sup>17</sup> Shortly afterwards Italy joined the agreement. France, however, in the last consequence was not ready to share its nuclear secrets and feared a violent Russian reaction if Germany was to acquire nuclear weapons. De Gaulle, on becoming head of state, cancelled the ominous third part of the agreement, concerning nuclear cooperation.<sup>18</sup>

Soon afterwards, the Germans decided to buy the American *Lockheed Starfighter* for their air force instead of the French *Mirage*, despite intense lobbying by the French.<sup>19</sup> The German decision rested upon many motives: Strauß' annoyance about the cancellation of FIG, the co-production component in the Starfighter programme which gave Germany access to high-tech know-how, the technical superiority and advanced stage of the US fighter, and high-pressure US lobbying combined with cautious hints about future help in upgrading the Starfighter to nuclear capability.<sup>20</sup> The French were furious. They considered the German decision a heavy blow to any future effort of European arms cooperation.<sup>21</sup> In fact, French-German cooperation in the field of armaments was to trail behind German-American cooperation for a long time.

Where did all this leave the British? As it turned out, they were left with the role of the odd

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(1945-63), in: *Revue d'Allemagne* 25/4, 1993, p.601-15..

<sup>16</sup> BA, NL Blankenhorn, 81b, conversation Faure-Adenauer, 16.11.1957; conversation Strauß - Chaban-Delmas, 20.11.1957.

<sup>17</sup> DDF 1957/II, Pineau to Bonn and Rome embassies, 20.11.57, p.717-718; protocol, 25.11.57, p.762-3.

<sup>18</sup> BA NL Blankenhorn, 92b/2, conversation Wormser/Laloy - Strauß, 19.11.1958; the episode is now quite well researched. For example: Fischer, 'Das Projekt einer trilateralen Nuklearkooperation. Französisch-deutsch-italienische Geheimverhandlungen 1957/58', in: *Historisches Jahrbuch* 112/1992, p.143-56; Barbier, Nuti, and Conze, in: *Revue d'histoire diplomatique* 104(1990), p.77-158.

<sup>19</sup> Kelleher, *Germany and the Politics of Nuclear Weapons*, 1975, p.103.

<sup>20</sup> BA, NL Blankenhorn, 92b/2, conversation Wormser/Laloy-Strauß, 19 November 1958; *ibid.*, 94/1, AA memo: German-French military cooperation, 26 November 1958; Kelleher (1975), p.103.

<sup>21</sup> DDF 58/II, Seydoux a Couve de Murville: Adenauer-Joxe Conversation, 28.10.1958.

man out, although they had to offer substantial know-how and a vast selection of military hardware. From the beginning, armaments trade as a means to reduce the imbalance in the bilateral payments account had been an issue in British-German support cost-negotiations. The British government, however, regarded arms trade as a rather ambiguous business. A big share of arms in exports was considered a mixed blessing. The Bank of England had noted this already in 1950. Dealing with the conversion of large parts of the British industry to arms production in the wake of the Korean War, it stated *'that if we concentrated wholly on armaments and made up the resulting shortages both at home and in the Sterling Area by buying civilian equipment from Germany, Germany at the end of the rearmament period would find herself with a firm foot in the markets which we had given up to her, and without the reconversion problem with which we ourselves would be faced'*<sup>22</sup>. This argument became common place in the British government.

Despite many reservations, Britain embarked during 1950-1952 on an ambitious rearmament program triggered by the Korean War and greatly expanded its arms production capacity.<sup>23</sup> The British metal producing industry, which accounted for about 40% of the country's exports, was especially affected.<sup>24</sup> Treasury observed in 1955 that the *'concentration of defence claims on the metal using industries has led to a direct conflict with exports and investments.'*<sup>25</sup> By this time the rearmament boom had long been over. Unlike the Federal Republic, however, Britain still had large parts of its capacity bound up in armament industries. Apparently, the foreboding of Bank of England had come true. *'The absence of any defence expenditure making claims on the economy, which compete with the claims of exports and investment, has been of great benefit to Germany during the period of reconstruction since the war and has given German economy a relative advantage over that of the UK, particularly in the export field.'*<sup>26</sup> This, as discussed briefly in chapter III, is a statement which is difficult to prove empirically. The major negative factor of the rearmament drive for

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<sup>22</sup> PRO, T 234/30, Letter Bank of England to Treasury, 25.9.1950.

<sup>23</sup> Burnham, 'Rearming for the Korean War', in: Contemporary Record 9/1995, p.343-67.

<sup>24</sup> Cairncross, *The British Economy since 1945*, 1992, p.100.

<sup>25</sup> PRO, T 234/24, Brief for a Meeting with German Ministers at NATO, December 1955.

<sup>26</sup> PRO, T 234/24, Treasury Memorandum, 13 December 1955.

Britain might have been the giving up of markets in Europe to Germany at a time when the latter's industry was still relatively weak. It should not, however, be disregarded that this was consistent with an overall trend of British policy, the concentration of economic policy on the Commonwealth and the United States.<sup>27</sup> In any case, in the mid-1950s the United Kingdom still had huge capacities bound in arms production. Its defence expenditure was falling. Therefore, the British either had to sell abroad or accelerate a costly reconversion of these industries.

When during the NATO meeting in 1955, Schäffer offered German arms orders to offset the foreign exchange drain resulting from British troop maintenance in Germany, his proposal was received with some indignation, particularly in the Treasury Department. *'We shall be tying up our manpower and industrial capacity on defence to the advantage of our strongest export competitor. The Germans do not conceal that they have no intention of disrupting their civilian industry and export potential. Dr Schäffer indeed offered that if it was the balance-of-payments that particularly worried us Germany would be prepared to buy arms from us. We shall have to consider in any case what advantages we can derive from the German policy of buying arms abroad. We shall however sell arms to Germany anyway. We have no spare materials or idle capacity to produce additional tank and aircraft whose export would be a pure gain to our balance of payments, offsetting our DM expenditure.'*<sup>28</sup> Great Britain concentrated its diplomatic efforts therefore on obtaining direct payments.

However, the Treasury's ambiguous stance on arms trade was not shared by other departments, notably the Foreign Office<sup>29</sup>, the Ministry of Supply<sup>30</sup>, and the embassy in Bonn which *'... had long considered that German purchases of British arms were the only long-term palliative to the balance-of-payments problems with which we are faced; not only*

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<sup>27</sup> Milward, *The European Rescue of the Nation State*, 1992, p.396-408.

<sup>28</sup> PRO, T 234/25, Treasury note, 2.1.1956.

<sup>29</sup> The FO, however, also cautioned *'that it is not necessarily in our interest to encourage the Germans to buy rather than to make arms, and thus encourage them knocking us for six in the export markets'*; see: PRO, FO371/124613, Warner to Bonn Embassy, 12 April 1956.

<sup>30</sup> PRO, T234/28, Rowan to Steel, 13 March 1956.

*in 1956, but for some years to come.*<sup>31</sup> This view was reinforced by the disappointing result of the first support cost negotiations. Apparently there was no alternative to arms trade. The ambiguity with which the government regarded this business would, however, prove to be of considerable disadvantage to its sales promotion efforts.

Estimates in the Ministry of Supply for German arms orders ran from £80m (\$224m) to £250m (\$700m) a year.<sup>32</sup> These hopes were confirmed by a letter of intent from the Federal government in June 1956 in the context of the support cost agreement, in which von Brentano promised German orders to the tune of \$524m in 1956/57.<sup>33</sup> However, no major new orders were received during that year. The German account in the Bank of England which was made up of prepayments for arms, as agreed in the support cost negotiations, remained almost untouched. Of the \$157m of arms orders, which were registered in March 1957, \$120.5m were for Hispano-Suiza armoured track vehicles, an order of dubious value, as it turned out later.<sup>34</sup> The British government grew more and more uneasy about the situation.

A particular blow for British expectations was the case of the Centurion tanks. The British government had high hopes of furnishing the German army with its model. The value of the prospective order was estimated at £50m (\$140m) which would have theoretically disposed of more than one tenth of Britain's accumulated EPU deficit.<sup>35</sup> Eden wrote twice to Eisenhower to obtain support for the British model against American competition.<sup>36</sup> The particular urgency in this case was caused by the highly critical economic situation of the Royal Ordnance Factories in Dalmeir where these tanks were produced. Of the four factories,

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<sup>31</sup> PRO, FO 371/124612, FO note to Treasury, 24.2.1956.

<sup>32</sup> PRO, CAB 134/1291, MAC(G)56, Memo Ministry of Supply, 10.1.1956; PRO, FO 371/124615, Bonn to FO, Tel.415, 30.5.1956; Bonn to FO, Tel.477, 13.8.1956.

<sup>33</sup> PRO, FO 371/124616, von Brentano to UK Embassy Bonn, 29 June 1956.

<sup>34</sup> PRO, FO 371/130727, FO Brief for Prime Minister, May 1957; see also PA-AA, Ref.301,96, Emminger to Auswärtiges Amt, 10.11.56: *'..English government is....embittered that none of these promises has been realised'*.

<sup>35</sup> EPU, Final Report 1959, p.36; PRO, CAB 134/1291, Ministry of Supply Memo, 26 January 1956.

<sup>36</sup> PRO, PREM 11/3344, Eden to Eisenhower, 18.2.1956; DDRS 94/1319, Memo McElroy for President: Tanks, April 1957.

three were kept working in the hope of German orders.<sup>37</sup> The German decision, however, was delayed more and more, and in September 1956 the case already seemed lost. Especially embarrassing for the British was that the Americans had given the German army 1000 M47 tanks free as part of the Nash-list. The new defence minister Strauß evoked renewed hopes that the rest could possibly be supplied by Britain. In May 1957 Macmillan, making a last desperate pitch, wrote once more to Eisenhower. *'Both for the sake of European cooperation, and in order to lessen the need for dollar end-item, it is most desirable that some of these requirements should be supplied by Britain.'*<sup>38</sup> But although Eisenhower promised support, the decision was taken in favour of the new American M48 tank. A final protest by Macmillan to Adenauer achieved nothing.<sup>39</sup>

This was a considerable fiasco. The Embassy in Bonn and the Foreign Office had wasted almost two years of strenuous efforts on the issue and now blamed the Americans. *'It is virtually useless for us to try to sell the Germans anything where we are in competition with the Americans. The reason is, of course, that the Americans have in the shape of MAAG some 200 American business men dressed up in uniform who have a great deal of time and money to be spent in nobbling the Germans who count . . . We have nothing comparable to offer.'*<sup>40</sup> The Pentagon had, in fact, contrary to Eisenhower's wishes, not hesitated to offer its good services in selling the M48 - particularly, as it was about to develop a successor model for which German funds were a welcome financial help.<sup>41</sup> Two other reasons were, however, decisive for the Germans. The first was the higher compatibility of the US tank with the already existing M 47 tanks, as Strauss emphasized later.<sup>42</sup> Moreover, the M48 appeared to be the newest model, whereas the British were about to replace the Centurion with a newer

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<sup>37</sup> PRO, FO 371/124612, Arms Working Party Meeting, 28.2.1956; CAB 128/30, CM 49(56), 12.7.56.

<sup>38</sup> PRO, PREM 11/3344, Macmillan to Eisenhower, 17.5.1957.

<sup>39</sup> PRO, PREM 11/3344, Adenauer to Macmillan, 29.6.1957; FO 371/130794, Macmillan to Adenauer, 28.7.1957.

<sup>40</sup> PRO, FO 371/130775, FO minute, 1.11.1957.

<sup>41</sup> FRUS 1955-57, XXVI, Memo of Conference with the President, 2 April 1957, p.227; *ibid.*, XVII, Eisenhower to Macmillan, 26 August 1957, p.782-83; DDRS 1994/1319, Memo McElroy to President, April 1957.

<sup>42</sup> PRO, PREM 11/2704, Record of a Meeting Macmillan - Strauß, 11.5.1959.

model not on offer.<sup>43</sup> The Germans were always ready to suspect, not without some justification, that they were being used to get rid of outdated material at a high price.<sup>44</sup>

Soon after the failure of the Centurion business a similar case happened with the British aircraft P 177. Again Britain kept facilities open only in the hope of selling the aircraft to Germany.<sup>45</sup> In the following up to the 1957 defence review, the RAF had been no longer interested in this expensive tool. Again the deal with Germany did not materialise due to French and American competition. Production had to be stopped at the end of 1957 when the German 'No' became known. This caused fierce protests from employees and management of the Saunders-Roe Company who had been dependent on this order and, moreover, was located in a region with a particularly weak economic structure.<sup>46</sup> As these examples show, balance of payments concerns and structural economic policy at home went hand in hand in the British government's promotion of arms sales.

Most damaging to the reputation of British weapons was the case of the Hispano-Suiza armoured track vehicles. The contract for the order, worth about \$120m, had been concluded under Strauss' predecessor Blank. The main partner, the dubious Swiss firm Hispano Suiza, had subcontracted the largest part of it to British Leyland without any involvement of the British government.<sup>47</sup> Unfortunately the vehicle proved to be of a dreadfully poor quality and, moreover, there had been cases of bribery in the Federal Defence ministry when the order was made.<sup>48</sup> When Strauss realised this, he cancelled 1800 of the 2800 ordered vehicles, thereby reducing Britain's far biggest arms export success in Germany to a third of

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<sup>43</sup> PRO, FO 371/124632, Embassy Bonn to FO, tel.49, 26.1.1956.

<sup>44</sup> PRO, FO 371/130727, FO Brief for Prime Ministers Visit to Germany, May 1957; PRO, FO 371/137471, Gore-Booth to FO, 29.1.1958.

<sup>45</sup> *'HMG have continued to finance development only in order to give the Germans time to make up their minds'*, PRO, FO 371/130773, Brief on Arms Sales for Adenauers Visit to London, 17.12.1957; FO 371/130727, FO Brief for Prime Ministers Visit to Germany, 5/1957.

<sup>46</sup> PRO, FO 371/137471, FO Brief for Mr. Harvey's visit to Bonn, 15.1.1958; PA-AA Ref.301, vol.37, Embassy London to Auswärtiges Amt, 24.12.57; KCA 1957, p.16020.

<sup>47</sup> PRO, FO 371/137476, Embassy Bonn to FO, 29.8.1958.

<sup>48</sup> A series of articles with essentially correct information on the affair can be found in: FRANKFURTER RUNDSCHAU, 6.-16.12.1958.

its original size.<sup>49</sup> Although the British government was aware of the shady circumstances of the deal, the loss of such a tremendous amount of foreign exchange (about \$84m) was a considerable shock.<sup>50</sup> The UK therefore urged the German defence ministry to review its decision. Eventually, the Germans were willing to reinstate parts of the order because of their disillusionment with the Franco-Italian-German agreement and because of the need to use the arms account at the Bank of England.<sup>51</sup> However, the affair left a very bad impression.

The series of failures caused considerable annoyance in the British government. *'The Germans must realize that these disappointments and the way in which they have come about are having an adverse political effect in the United Kingdom and are seriously disturbing Anglo-German relations. In particular they strengthen the hands of those . . . who do not wish the United Kingdom to cooperate with Germany or, indeed, with Europe; . . . the view is gaining ground in some quarters that the Germans have been leading us up the garden path.'*<sup>52</sup>

Compared to the estimates of 1955, the result of the British efforts was miserable. In July 1957 the preliminary level of orders was \$168m, March 1958 \$213m and in 1961, after the Hispano-Suiza deal had been slashed, it was as low as \$138m.<sup>53</sup>

Frustrated, British civil servants contemplated the reasons for these failures. They produced a tremendous variety of explanations: the anti-British attitude of Strauß; the possibility that British weapons were outdated and too expensive; the Franco-Italian-German Tripartite Agreement; Britain's reluctance to cooperate in arms production and its independent strategic policy; the secretiveness and absence of cooperation from British services; the reluctance of Britain to make government-government deals and, of course, US competition.<sup>54</sup> Although

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<sup>49</sup> PA-AA, IIA7/1202, BMV to AA, 6 November 1958; Interministerial Meeting, 6 November 1958.

<sup>50</sup> PRO CAB 129/86, C(58)236, 15.11.58, FO 371/137476, Steel to Ministry of Supply, 28.8.1958.

<sup>51</sup> PRO, FO371/137477, Embassy Bonn to Ministry of Supply on McFarlane-Hopf conversation, 19 April 1958.

<sup>52</sup> PRO, FO 371/137471, FO Tel.144 to Bonn, 21.1.1958.

<sup>53</sup> Data derived from: FO 371/130774, 15.7.1957; PREM 11/3344, 31.3.1958; BA, NL Etzel, note Referat Fp2, 18.3.1961.

<sup>54</sup> PRO, PREM 11/3344, Ministry of Supply to Prime Minister on Export of Arms, 12.3.1958; FO 371/124613, Bonn to FO, 17.4.1956; FO 371/137374, conversation Lloyd-v.Herwarth, 18.2.1958; FO 371/145946, McFarlane (Bonn) to Ministry of Supply, 29.1.1959; FO 371/124616, Anglo-German Economic Committee: Arms Supply to

the last reason was grave, the political explanations are more important. All evidence points to British hesitation in becoming involved in a cooperative arms development scheme on the continent.<sup>55</sup> When it seemed to go ahead without Britain as in the case of FIG, there was great indignation. As long as British policy, however, seemed to be that of maintaining political, economic and military<sup>56</sup> distance from the continent, it was not surprising that the Germans felt it to be more convenient politically to cooperate with the United States and France. A business such as armaments trade made more political sense when pursued with these countries. British arms export policy to Germany was not consistent with the overall tendency of British foreign policy. This was the main bottleneck. The consequence was that the level of British sales remained disappointing throughout the 1950s and 1960s.

Although a more cooperative attitude came up in the British government after 1958, American competition would become the decisive factor for high-tech weapons in the 1960's. Regarding less sophisticated types of armaments, German industry caught up rapidly and expanded its share greatly. Failures like the Hispano-Suiza contributed to this trend.<sup>57</sup> The change of British policy came too late. The UK continued to trail far behind American and French sales, reaching about the level of Italian sales to the Bundeswehr.<sup>58</sup> In the 1960s, arms sales became again an integral part of German-British offset agreements. Even this did not change much. The continuing distance between Germany and the UK, underlined by quarrels about support costs, monetary policy, and troop-levels, impeded closer military cooperation between the two countries. In a way, European integration in the economic field without Great Britain was paralleled by a similarly exclusive continental cooperation in strategic-military matters.

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Germany, 22.11.1956.

<sup>55</sup> For example: from the start of their rearmament the Germans had expressed their priority for government-government deals instead of negotiating directly with the foreign firm in which case they suspected to be charged a higher prize. Whereas the US had immediately agreed to such a scheme, the UK government, mainly because of the industry's and the services' resistance, steadily refused. See: Pro, FO 371/137474, Brief on Adenauer visit, 29 April 1958; FO Brief for Defence Minister's visit to Germany, 20 March 1958.

<sup>56</sup> The German military thought until the late 1960s that British weapons were not suitable for warfare on the continent; Interview of the author with former German defence minister, von Hassel, 17 August 1994.

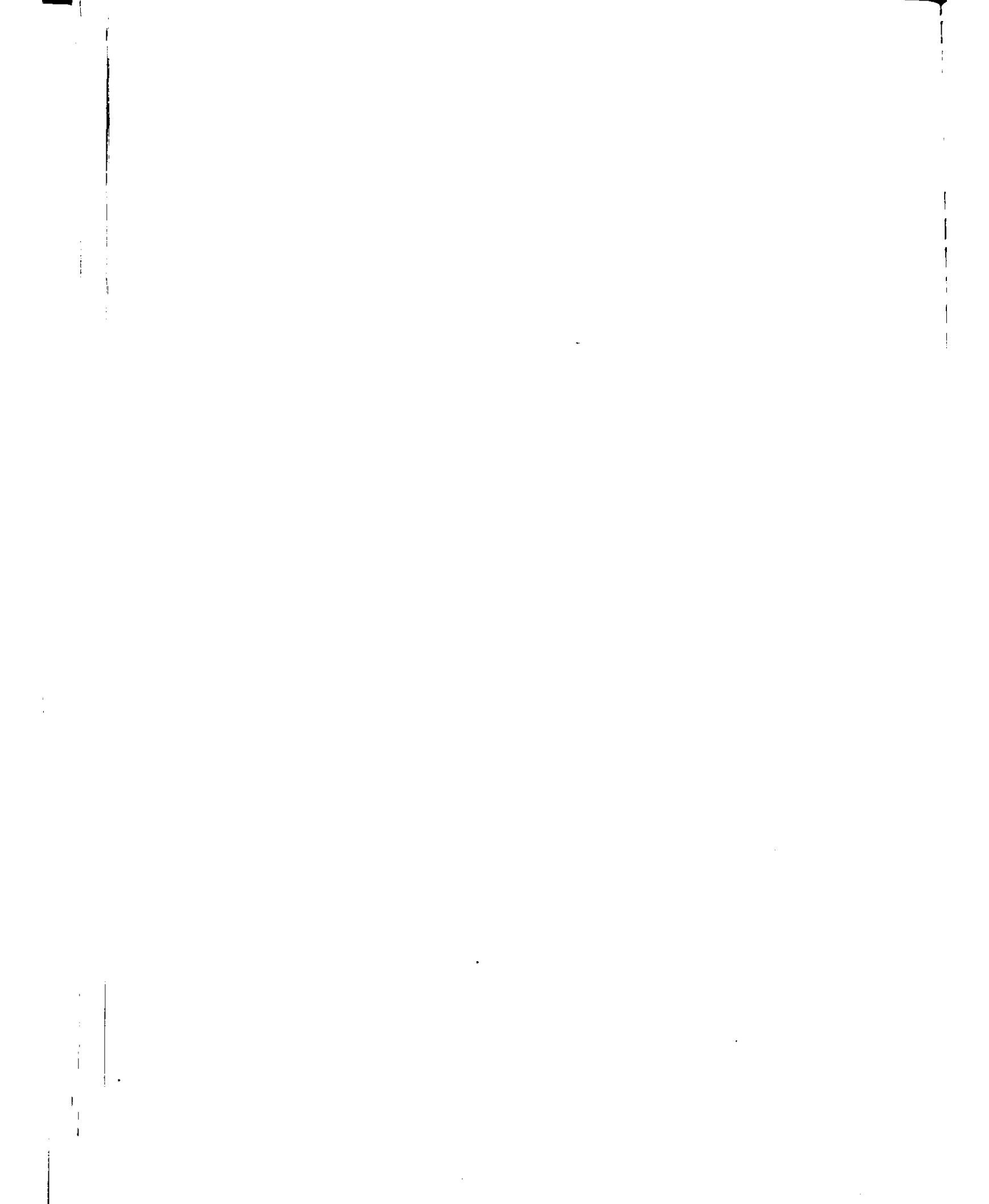
<sup>57</sup> BA, B136/3105, Summary of Strauß' remarks at Meeting of Budget Committee, 27 February 1959.

<sup>58</sup> BA NL Etzel, vol.17, BMF memo, March 1961; Snyder (1964), p.223; Appendix, table 6.



**PART II**

**TROOPS AND DOLLARS  
IN GERMAN-AMERICAN RELATIONS,  
1955-67**



CHAPTER VI  
THE RADFORD PLAN:  
AMERICAN POLICY TOWARDS ITS TROOPS IN GERMANY, 1955-58

The American GI's in Germany were, in sharp contrast to the controversies surrounding the British troop commitment from 1955 onward, no source of serious conflict between sending and host country - apart from one significant episode which is the subject of this chapter. The American military presence became an integral feature of the European postwar settlement within a few years. Divergences on their military and political role were mainly played out in strategic debates which affected the troop level insignificantly. This relative calm and stability, however, should not lead one to conclude that preoccupations, similar to the British ones, did not exist in US government circles. On the contrary, the principle of a seemingly unlimited presence of their troops in Europe was never accepted by the American government as a whole nor by Congress and the public. In the absence of powerful financial counter-arguments (balance of payments problems), however, the political arguments for a stable troop level carried the day by and large. This changed only in 1959/1960 when the American dollar came under pressure similar to that affecting the English pound. In the following chapter I will retrace US government discussions regarding the rationales for troop stationing in Europe, concentrating on the Radford plan episode. This will be preceded by a short discussion of the strategic debate in whose terms the troop level question was couched during the 1950s. The motivations behind the German insistence on a stable troop level will be outlined in more detail as in chapter I.

Allied force levels in Europe were influenced by changes in strategic thinking and revised war plans. However, this influence was felt mainly at the planning level. When the plans were to be implemented, financial and political considerations proved to be stronger than strategic doctrines. To understand the debate about force reductions, it is nevertheless necessary to recapitulate briefly the basic lines of the strategic discussion within the Alliance during the 1950's. The debate about force levels in Europe was couched in strategic terms and those arguments were among the principal ones brought forward to justify a lower or higher American force level.

The strategic debate in the Western Alliance was mainly about the most appropriate balance between conventional and nuclear weapons.<sup>1</sup> The basic lines of NATO's military strategy were set by the United States which also retained, due to its exclusive possession of a huge nuclear potential, the ultimate decision about the nuclearisation of an eventual war. However, the established concepts of deterrence were challenged consistently, not only by the Europeans, but also from within the US administration and from many semi-official strategic thinkers. Technological progress, political considerations, revised estimates of Soviet military power and, above all, economic limitations led to frequent doubts about the wisdom of the strategic doctrine of the day.

A stable factor in strategic thinking after the war was the feeling that NATO's troops were conventionally inferior to the Warsaw Pact forces. In the first years of the Cold War it was therefore tacitly accepted by American and British military planners that in case of a full-scale attack, the Soviet Union would conquer large parts of continental Europe.<sup>2</sup> With the help of airpower and nuclear strikes the occupied territory was then, following closely allied strategy in World War II, to be liberated. However, the experience of the Korean War 1950-51 clearly showed the uselessness of atomic weapons in liberating occupied territory.<sup>3</sup> In addition, the prospect of Soviet occupation was completely unacceptable for the Europeans. The implementation of a forward strategy became politically imperative. Its expression was the huge conventional build-up program which was decided at the NATO Council Meeting in Lisbon, February 1952. It provided for 96 divisions as force goals, and it was clear that without German resources and manpower these goals were impossible to achieve.<sup>4</sup> To close the gap until the new forces were available was one of the reasons for the United States to

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<sup>1</sup> For an excellent review of the American strategic debate see: Trachtenberg, *History & Strategy*, 1991.

<sup>2</sup> Krieger, 'Die Ursprünge der langfristigen Stationierung amerikanischer Streitkräfte in Europa', in: Herbst/Bühner/Sowade(ed), *Vom Marshall-Plan zur EWG*, 1990, p.373-399; Greiner, 'Zur Rolle Kontinentaleuropas in den alliierten strategischen Planungen', in: Maier/Wiggershaus(ed), *Das Nordatlantische Bündnis 1949-56*, 1993, 147-50.

<sup>3</sup> Freedman, *The Evolution of Nuclear Strategy*, 1981, p.71-72; Greiner, in: Maier/Wiggershaus(eds), 1993, p.150-152.

<sup>4</sup> Steinhoff/Pommerin, *Strategiewechsel*, 1993, p.13-15; Wampler, 'Conventional Goals and Nuclear Promises: The Truman Administration and the Roots of the NATO New Look', in: Heller/Gillingham (1992), p.53-58.

formally approve the stationing of a large number of American troops in Europe.<sup>5</sup>

However, even given the existence of a German army it was soon realized that the Lisbon plans were utopian, especially from a financial point of view. A way out of this dilemma was provided by the development of tactical nuclear weapons for use on the battlefield. The Eisenhower-administration adopted a corresponding military policy from 1953 onwards, termed 'New Look', which was based on an almost complete reliance on nuclear deterrence to decisively reduce the cost of defence. With tactical nuclear weapons and by keeping the advantage of the US in nuclear technology it seemed possible to entrust deterrence mainly to nuclear weapons, avoiding the expensive maintenance of large conventional forces. Consequently the nuclear stockpile was increased to gigantic dimensions (from 50 nuclear warheads in 1948 to 18500 in 1960) and tactical nuclear weapons were stationed in Europe.<sup>6</sup> During the 1953 NATO Council meeting the allies were informed of the new strategy.<sup>7</sup> They were assured by the US that an attack on them would be answered immediately by atomic weapons. This was made credible by the presence of American troops on the front line which would force the Americans from the first day to take part in any hostilities.

The military value of conventional troops themselves, however, was put into question when seen in those strictly strategic terms. The so-called sword (strategic ballistic weapons) and shield (conventional troops supported by tactical nuclear weapons) strategy, which was the result of the New Look and was approved by NATO with document MC 48, assigned the troops the role of a tripwire.<sup>8</sup> How strong this tripwire should be, however, was never established and was subject to heated debates. Consistent pressure increased during the 1950's to save as much as possible on military budgets in various countries, notably the US and Britain. The Eisenhower-administration and the Macmillan government in Britain never abandoned the hope of soon being able to reduce their commitment decisively. The

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<sup>5</sup> See ch.1; see also Trevorton, *America, Germany, and the Future of Europe*, 1992, p.64-91.

<sup>6</sup> Rosenberg, 'The Origins of Nuclear Strategy, 1945-1960', in: *International Security* 7(1983), p.3-71.

<sup>7</sup> Maier, *Amerikanische Nuklearstrategie unter Truman und Eisenhower*, in: Maier/Wiggershaus(ed), (1993), p.234-240.

<sup>8</sup> Cioc, *Pax Atomica*, 1988, p.7.

Europeans, however, saw these commitments as essential in political and military terms for the postwar European security architecture. After all, a real forward strategy was established by NATO only in the early 1960s.

Thus, the political implications of conventional troops turned out to be essential obstacles to reductions. Even when reliance on nuclear deterrence was paramount, troop reductions (or reduced force goals) became highly contested issues. It became clear that whatever strategical thinking was predominant at the time, its practical implementation would be mainly dependent on political and economic circumstances. This is demonstrated by the first German-American dispute on troop levels in 1956/57, which created diplomatic discords to a considerable extent. German and American strategic and political concepts of the troops were diverging increasingly and these differences were intensified by economic considerations. The crisis concerning the so-called Radford plan made this abundantly clear.

On 13 July 1956, the New York Times published an article reporting that the Chairman of the US Joint Chiefs of Staff, Admiral Radford, planned a reduction of American conventional manpower by 800.000 men, almost one-third of the total strength of the US army.<sup>9</sup> Evidently the European theatre would be affected by reductions of this size. Adenauer was highly alarmed by the report and he initiated a major diplomatic effort to counter what he considered as a dangerous development with disastrous consequences. The German ambassadors in Washington, London, Paris and at NATO were called in to the *Bundeskanzleramt* for consultations, emissaries went to Washington, to NATO and WEU, and Adenauer himself wrote a pathetic letter to his "dear friend" John Foster Dulles.<sup>10</sup> In this letter he painted an apocalyptic picture of the future world situation should the American disengagement plans prove true. Apparently the report came as a real shock to him. The strong reaction of the German government raises many questions. What reasons lay behind this extraordinary reaction to an unconfirmed report? What was the real background of the article? And what were the consequences of the affair on mutual relations? Above all: what were the roots of

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<sup>9</sup> NYT, 13.7.1956.

<sup>10</sup> Interview de Maiziere in the European Historical Archives, Florence; IFZ, NL Krekeler 39, Adenauer to Dulles, 22.7.1956; *ibid.*, 47, Hallstein to Krekeler, 20.7.1956; FRUS 55-57, XXVI, Conversation Murphy-Ambassador Krekeler, 17.7.1956, p.131-133.

one of the most consistent policy positions of the Federal Republic during the Fifties and Sixties, i.e. the insistence on a stable level of US troops in Germany?

Adenauer's reaction clearly underlined the importance he attached to the US troops in Germany. For him these troops were the fundamental symbol of the American commitment to Europe. They were not only the principal condition under which the other Europeans accepted German sovereignty, they also guaranteed protection against a Soviet Union which at that time most Germans held to be extremely expansionist. The principal deterrent, the American nuclear umbrella, was effective and credible for Germany only in combination with the strong conventional troop presence of the NATO members. Without this 'hostage function' of a force that could pursue forward defence, Germany would have been confronted with two very inconvenient situations in the event of war: either occupation or nuclear war on German soil. Thus, a strong and credible conventional force-level was essential. This was one of the main reasons for the German government to accept the establishment of a large conventional army so shortly after the war, in opposition to a large part of the West German population. As Adenauer well understood, the presence of US troops represented US control which made this buildup acceptable to the rest of Europe.

Apart from these strategic and political reasons, domestic reasons were responsible for Adenauer's (and his successors') uncompromising stance towards stable troop levels. Any sign of American disengagement might have revived the bitter debate about rearmament and *Westintegration* which had dominated German politics in the early Fifties.<sup>11</sup> The opposition movement had ardently criticized Adenauer's policy which aimed at achieving sovereignty within the Western framework by rearming Germany and silently delaying the prospects of reunification in the future.<sup>12</sup> If the Federal Republic was to be rearmed, any chance of an understanding with the Soviet Union over Germany as a whole seemed impossible. Another argument of the antimilitaristic movement, led by the SPD, was the fear that German soldiers would, in the case of war, serve only as cannon fodder, having to fight the battle on the ground. The implementation of the 'New Look' strategy in the United States with its reliance

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<sup>11</sup> Adenauer, *Erinnerungen 1955-59*, 1967, p.197-214; Pötering, *Adenauers Sicherheitspolitik 1955-1963*, 1975, p.62-90.

<sup>12</sup> See ch.II, fn.19.

on nuclear weapons, also for tactical purposes on the battlefield, gave this interpretation some plausibility. Redeployment or reduction of American troops therefore touched upon Adenauer's worst fears, possibly driving the Germans towards neutralism by undermining the credibility of 'Westintegration.'<sup>13</sup> He had placed all his credit on this policy. His 'Grand Design' was threatened by the possibility of an American disengagement. The Chancellor complained that the Radford plan '*would destroy my whole policy*'.<sup>14</sup> An additional galling detail of the whole affair was that it came just after the Chancellor had returned from a visit to Washington without having been informed of the American plans.

The US government was well aware of these circumstances; and even if one assumed that it did not know until the NYT story, it knew perfectly well afterwards thanks to Adenauer's tireless efforts to communicate his disapproval. What lay behind the NYT report?

That Eisenhower basically supported the view that the American commitment of manpower in Europe was only of a temporary nature is well-known and he mentioned this conviction frequently.<sup>15</sup> Indeed, a reduction of expensive conventional manpower would have been an essential point in putting the economizing aspects of the 'New Look' strategy into force. Out of fear of negative repercussions on the EDC debate, Eisenhower and Dulles never seriously planned such a risky move during the first half of the 1950s.<sup>16</sup> On the contrary, the Paris Accords were supplemented by a solemn declaration by the President that US troops would remain in Europe as long as needed.<sup>17</sup> Soon, however, the economic consequences of this commitment became an issue in the Eisenhower administration, particularly after German

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<sup>13</sup> These arguments are all summarized in a speech Foreign Minister von Brentano gave to the hastily invoked WEU-Council at 15 September 1956; see BA NL Blankenhorn 67/3.

<sup>14</sup> *ibid.* 63/3/194, Adenauer conversation with Quarles, 10.9.1956.

<sup>15</sup> 'The President said he had always insisted that the Europeans should develop ground forces to replace ours...'; FRUS 1955-57, IV, Memorandum of Conference with the President, 2.10.1956, p.100. See also: Trachtenberg, 'The Nuclearization of NATO', in: Trachtenberg (1991), p.163-68.

<sup>16</sup> Thoss, 'The Presence of American Troops in Germany, 1949-56', in: Diefendorf/Frohn/Rupieper(eds), 1993, p.417-420.

<sup>17</sup> The pledge stated the US government's intention to '*continue to maintain in Europe, including Germany, such units of its armed forces as may be necessary and appropriate to contribute its fair share of the forces needed for the joint defense of the North Atlantic area while the threat to that area exists, and will continue to deploy such forces in accordance with agreed North Atlantic strategy for the defense of this area*'; FRUS 1952-54, V,2, p.1345.



contributions petered out.

The US Treasury warned frequently of the foreign exchange loss implicit in long-term troop maintenance abroad.<sup>18</sup> However, prior to 1958 these warnings did not have the force to overcome the political counter-arguments by the State Department. The focus of the administration's efforts to reduce the cost was therefore on budgetary savings. Cost saving studies were a common exercise for US military services in these years. It seems that the Radford plan was part of such a cost-saving study which had leaked out.<sup>19</sup> These studies were also an expression of the deep dissatisfaction large parts of the administration felt by the slow progress the allies were making towards achieving more self reliance in defence matters, thus failing to relieve the United States of the heavy burden of its expensive worldwide commitments. While apparently proposals in the size of the Radford plan survived only the lower levels of the government, a lively discussion was nevertheless going on in the higher ranks about the possibility of 'streamlining' the forces, fed by the need to economize and suggested by new strategic priorities. These discussions were reinforced by British intentions to reduce the British Army of the Rhine (BAOR) in Germany. There were also considerable internal struggles going on between different branches of the US forces over the question of the most appropriate strategy in employing conventional and atomic weapons. The Radford plan indicated a certain prevalence of the Air Force opinion to the detriment of the position of the army, whose influence shrank with the diminishing importance of the large troop contingents in Europe. It is well possible that army officials were responsible for the leak to the NYT.<sup>20</sup>

During August and September 1956, the American government discussed different approaches to the problem.<sup>21</sup> There was an overall agreement on the desirability of cuts in troop deployments abroad. *'It should be our purpose to seek to establish a situation that would*

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<sup>18</sup> FRUS 1955-57, XIX, Memo of Discussion at the 280th NSC Meeting, 22.3.56, p.272-73.

<sup>19</sup> FRUS 1955-57, XIX, 249th NSC Meeting, 17 August 1956, p.349.

<sup>20</sup> Rosenberg, in: *International Security* 7(1983), p.42-43; Felken, *Dulles und Deutschland. Die amerikanische Deutschlandpolitik 1953-1959*, 1993, p.366.

<sup>21</sup> FRUS 55-57, IV, Memorandum of Conversation, p.93.

*permit the withdrawal of a considerable amount of U.S. ground forces from Europe as soon as this can be done without undue risk. The creation of the German divisions and the imaginative use of military manpower may afford that opportunity. The sole question presented is whether circumstances at this time permit us either to withdraw forces, or even publicly to disclose a trend in that direction.*<sup>22</sup> According to the State Department, such a political situation did not yet exist. German pressure apparently worked. The prospect of a SPD victory in the German elections alarmed the Americans more than necessary. For the time being the principal goal was *'to avoid undercutting Adenauer'*.<sup>23</sup> Eisenhower agreed to that. He *'felt very definitely that we cannot take divisions out of Europe at this time. The effect on Adenauer would be unacceptably damaging'*.<sup>24</sup>

Moreover, the German position was supported by France. The French Premier Mollet informed Dulles that France still insisted on the absolute necessity of American troop-presence: *'Mr.Mollet explained to Mr.Dulles that the French understanding of the European defence problem is founded on three principles: 1. Necessity of an American presence in Europe . . . It is indispensable . . . that [the US] should be represented physically: the problem of the force levels arises from that. 2. Impossibility to rely solely on atomic weapons . . . 3. Necessity that nuclear weapons are kept . . . at the place . . . where defence is organized'*.<sup>25</sup> Considerations regarding the effects of reductions on German rearmament also weighed heavily on the decision to pursue them, if at all, very quietly.<sup>26</sup> US-Senator George was sent on a goodwill-tour to Europe to calm emotions. He assured Adenauer that there would be no withdrawal or reduction as long as the US presence was welcome to the allies.<sup>27</sup> This firm position would also deter the United Kingdom from bringing forward proposals for a reduction of their forces in Europe during the forthcoming NATO-council

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<sup>22</sup> NSA, NHP, Wampler OH sources, Box 5, Elbrick/MacArthur II to Dulles, 27 September 1956.

<sup>23</sup> FRUS 55-57, XIX, 249th NSC Meeting, 17 August 1956, p.349.

<sup>24</sup> *ibid.* Memo of Conference with the President, 2 October 1956, p.99.

<sup>25</sup> DDF 1957, II, Entretien Dulles Mollet, 6.5.1957, p.740.

<sup>26</sup> NA, RG 59, 711.5, 9-1657, Paris POLTO 600: Parkins to Secretary of State, 16 September 1957.

<sup>27</sup> FRUS 55-57, XXVI, Conversation George - Adenauer, 28.9.56, p.161-63.

meeting in December 1956.<sup>28</sup> The convenient moment for large-scale US troop-reductions was expected to lie somewhere in the near future -an assumption that proved to be wrong. 'A *job of changing the German psychology from the present feeling that if we did make any reduction whatever, we are abandoning them*', would have to be sustained, as Dulles put it.<sup>29</sup>

The Americans tried a more subtle method to reduce the troops which was suggested by the President. '*The President asked why we cannot streamline divisions and cut down backup troops without public announcement. It could be done on a worldwide basis, avoiding the connotation of pulling out of Europe*'.<sup>30</sup> So it happened. The available data shows that manpower in Germany fell from 262.000 in 1956 to 235.000 in 1958.<sup>31</sup> The departing troops were mostly airforce units whose functions were made obsolete by tactical nuclear weapons arriving in Europe.<sup>32</sup> Large-scale reductions were ruled out for the time being. During discussions on the military budget the subject was regularly brought up,<sup>33</sup> but only at times of a sharply deteriorating balance of payments, 1958-60 did serious debate start anew.

However, these events were enough to influence Adenauer's policy to a considerable extent. He was by no means reassured. In every conversation with American politicians in late 1956 he returned to the subject and complained about US policy, demanding incessantly more consultation.<sup>34</sup> When Germany's failure in its own rearmament became clear these continuing complaints naturally caused a great deal of annoyance in Washington.<sup>35</sup> The US suspected that the turmoil was used by Adenauer to counteract American criticism regarding

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<sup>28</sup> The UK had already informed the US of its intention to review its defense policy with the intention to lower their troop level in Europe; see ch.III.

<sup>29</sup> *ibid.*, p.94, fn.1.

<sup>30</sup> FRUS 1955-57, XXVI, Memo of Conference with the President, 2.4.1957, p.226.

<sup>31</sup> see Appendix I, table 3.

<sup>32</sup> FRUS 1955-57, IV, Memcon President - Norstad, 28 October 1957, p.184-85; DDRS 1992, NSC Memo: US Security Effort Overseas, 19 December 1957.

<sup>33</sup> For example: FRUS 1955-57, XIX, Memo Cutler for the President, 1 July 1957, p.533-35; 332d NSC meeting, 25 July 1957, p.556-65; 345th NSC meeting, 14 November 1957, p.681.

<sup>34</sup> BA NL Blankenhorn 63/3, Adenauer conversation with Quarles, 10.9.56; FRUS 1955-57, XXVI, Message from SACEUR (Gruenther) to Goodpaster, 19.11.1956, p.174-175; Schwarz, *Adenauer*, 1990, p.320.

<sup>35</sup> BA NL Blankenhorn 73/5, Conversation Adenauer with Globke and Blankenhorn, 17.1.1957.

the planned reduction of the German conscription period from 18 to 12 months.<sup>36</sup> This motive cannot be ruled out completely, considering Adenauer's style of policy-making. But his grievances had a very real background, as we have seen. That the cuts undermined seriously the fighting ability of the troops was presumably not even Adenauer's opinion. However, German mistrust about the US commitment to Europe remained. Adenauer saw it from now on as a high probability that the United States would redeploy their troops in due course and he wanted to be prepared for this situation.<sup>37</sup> Frequently in the following years he cited the Radford plan as evidence of the unreliability of the United States presence. Any new sign of shrinking US troop levels would revive this mistrust.

The Radford plan also had immediate repercussions on German foreign policy. In a speech in Brussels in September 1956 Adenauer emphasized as strongly as ever before the importance of the European integration process.<sup>38</sup> Implicitly criticizing the United States, he gave strong approval to the *relance* of European Integration, initiated by the Conference of Venice in May 1956. It is quite evident that the Radford plan played a prominent role in making Adenauer an outspoken European at this time.<sup>39</sup> Frankly, he spoke to the French about his misgivings. *'At present, the Chancellor regards the American policy with strong reservations and this also applies to statesmen and diplomats of the United States . . . To counteract he considers it absolutely necessary that the European countries are united. From there derives his will to revive European policy in a situation which he thinks is the last opportunity'*.<sup>40</sup> During a famous meeting with Mollet at the height of the Suez Crisis (Mollet and Pineau left the room twice during the conversation to call London) he appeared to be almost hysterical about the danger of a Soviet-American co-dominium over the world.<sup>41</sup>

It is also highly probable that the Radford plan led Adenauer and parts of the German

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<sup>36</sup> FRUS 1955-57, XXVI, Telegram from Embassy Bonn to Sec. of State, 16.10.1956, p.167.

<sup>37</sup> See Buchstab (ed.), *Protokolle*, (1990), p.1028-30; Schwarz (1990), p.302.

<sup>38</sup> Adenauer, *Reden 1917-1967*, (ed. Schwarz), 1975, p.329.

<sup>39</sup> Kilsters, 'The FRG and the EEC-Treaty', in Serra(ed.), *Il Relancio dell' Europa e i Trattati di Roma*, (Brussels 1989), p.495-506.

<sup>40</sup> DDF 1956, III, 1990, Couve de Murville to Pineau, 10.10.56, Doc.261, p.553.

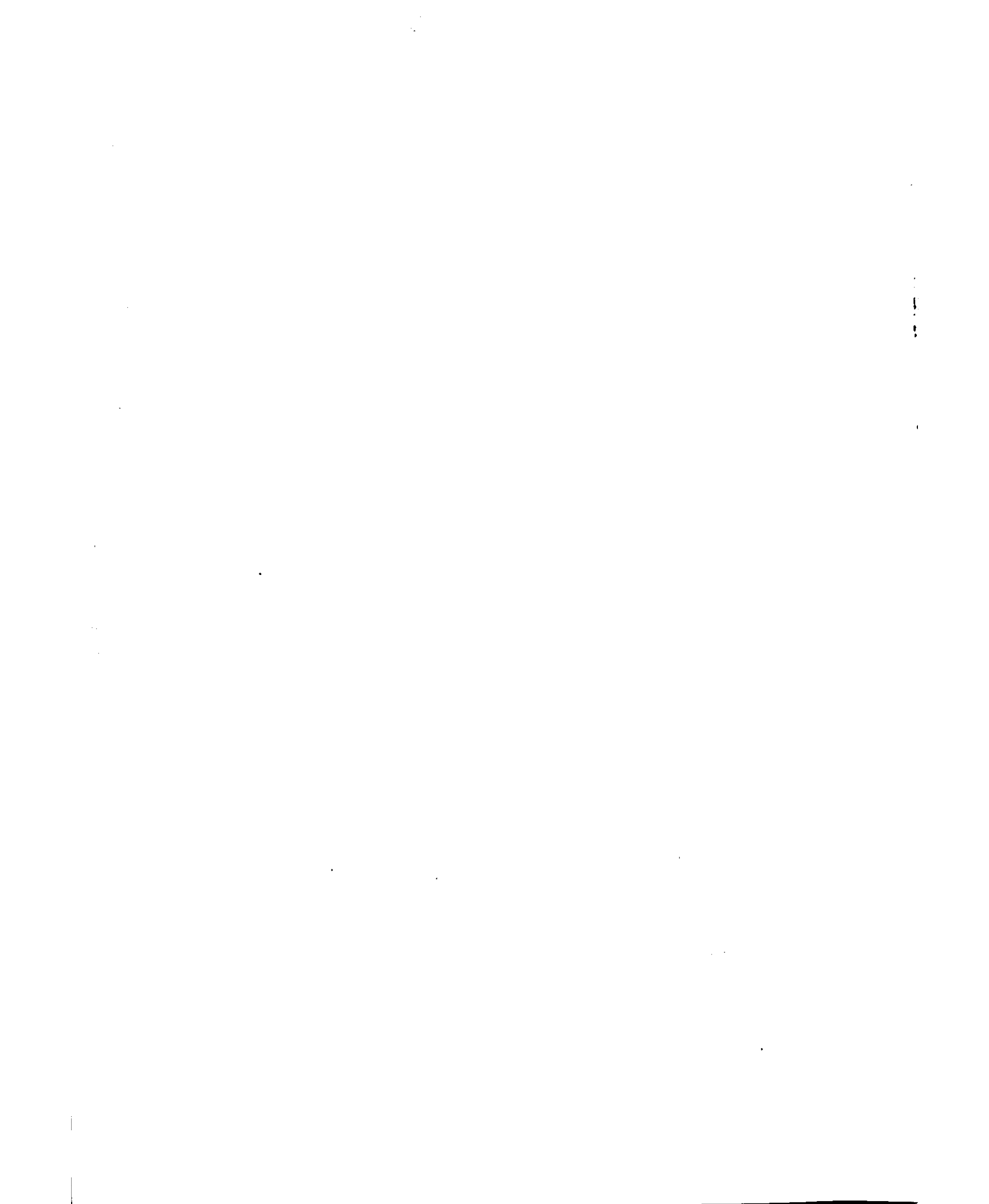
<sup>41</sup> DDF 1956, III, 1990, Compte Rendu des Conversations Adenauer/Mollet a Paris, 6.11.56, Doc.138, p.237.

political establishment to question the abstinence of Germany in the nuclear field. *'On military side, I gather, he [Adenauer] has the impression that while risking his reputation in pressing for rearmament, those who dispose of nuclear power will alone make decision [sic] affecting his countrys fate and that he will playing with marbles'*.<sup>42</sup> Defence Minister Strauss got a free hand for talks about nuclear cooperation with France and Italy.<sup>43</sup> The Radford plan thus had a considerable impact in forcing West Germany to see the limitations and problems of too strong a reliance on the United States. It made abundantly clear that the US presence and its role of a pacifier was not to be taken for granted. It was, however, only a foretaste of the debate during the 1960s.

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<sup>42</sup> FRUS 1955-57, XXVI, Memo of Acting Director of CIA, Cabell, to Sec. of State, 28.8.1956, p.148; see also: Greiner, 'Die militärische Eingliederung der BRD in die WEU und die NATO 1954-57', in: MGFA III, p.731-736.

<sup>43</sup> See ch.V.



CHAPTER VII  
THE AMERICAN BALANCE OF PAYMENTS AND THE SECURITY  
COMMITMENT IN EUROPE: THE RESPONSE OF THE EISENHOWER  
ADMINISTRATION

a) A Turning Point in European-American Relations?

In November 1960, the US Secretary of Treasury, Anderson, and the Undersecretary of State, Dillon, paid a visit to Bonn which has been termed 'a striking symbol' for the changing nature of European-American relations.<sup>1</sup> Whereas in the first postwar decade European delegations used to cross the Atlantic in order to negotiate economic help with their American counterparts, the mission of Anderson and Dillon aimed at rallying the Europeans to the defence of the American currency which had been under pressure since 1958. Germany was the main target and the negotiator's agenda included a request for a direct contribution towards the cost of maintaining US troops in Germany. Press commentators on both sides rushed at the event. The German press commented on the visit with particular malice. Anderson and Dillon were portrayed as begging for money and, to underline this characterisation, DER SPIEGEL printed a photo showing the stout German minister of economics, Erhard, lecturing the skinny Anderson.<sup>2</sup>

The visit appeared to signal a new framework in which European-American relations were to evolve: the limits of American economic power and the success of the European recovery made themselves felt, particularly in the monetary field. This had vast political consequences. Monetary problems were to affect American-German relations (and American-European relations in general) during the 1960s deeply. A closer look into the causes and consequences of the visit may give us an understanding of the nature of the changes going on. Throughout the rest of the thesis, these fundamental changes will be evaluated through an analysis of the troop cost question.

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<sup>1</sup> Solomon, *The International Monetary System, 1945-81*, 1982, p.33.

<sup>2</sup> SPIEGEL 49/1960, p.27-29.

First, I will briefly portray the developments in the international monetary system prior to 1960, in particular the emergence of large American balance of payments deficits. These were widely seen as the most conspicuous sign of a fundamental change in US-European relations. Later on, commentators usually referred to the decline of the dollar when speaking of a supposed 'decline of US hegemony'.<sup>3</sup> I will then concentrate on the specific question of how the US security effort in Europe was linked with the dollar problem. The Anderson-Dillon mission as one important response to the balance of payments deficit will serve to underline - as in other examples in this thesis- the interrelation of security and monetary problems in German-American relations. An analysis of the issues at stake during the negotiations and of the German response will provide the necessary empirical base to address those questions.

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<sup>3</sup> This, in my opinion problematic, notion dominates the writings by political scientists on the events in the international monetary system. Yet, there is agreement neither on whether US hegemony was actually declining or not, nor on whether this hegemony was benign or repressive. This ambiguity illustrates the problem of using the concept as a given analytical tool in historical research. Another drawback is that an emphasis on US hegemony fosters a tendency to portray European policies as essentially reactive to American policies. Historians of US-European relations during the 1950s have seriously questioned the extent of American influence in shaping European affairs. See for example the debate on the Marshall plan. For a summary of the debate see Maier, 'Introduction', to: Maier/Bischof(eds), *The Marshall Plan and Germany*, 1991. The use of the concept of hegemony in analysing transatlantic relations is critically assessed by Gadzey, *The Political Economy of Power: Hegemony and Economic Liberalism*, 1994.



b) The International Monetary System until 1958 and the Causes of the Dollar Problem

The Anderson-Dillon mission was an indirect consequence of the emergence of a huge deficit in the American balance of payments and of the parallel shrinking of the American gold reserves.

Table 7:  
US Liquidity Deficit<sup>4</sup> and Gold Reserve Position, 1952-1961 (in \$ billion)

	1952	1953	1954	1955	1956	1957	1958	1959	1960	1961
Liquidity Balance	-1.21	-2.18	-1.54	-1.24	-0.92	0.62	-3.35	-3.65	-3.71	-2.43
Gold Reserves	23.25	22.09	21.79	21.75	22.06	22.86	20.58	19.51	17.80	16.95

Sources: Liquidity Balance: Survey of Current Business, October 1972.  
Gold Reserves: UN Statistical Yearbook 1962

From 1958 onward these figures moved increasingly to the centre of public and official attention. In order to understand why this development occurred and why it caused such enormous alarm in the United States and in financial circles all over the world, it is necessary to outline briefly the basic features of the international monetary system as it evolved during the postwar period.

Already during World War II, various blueprints for a postwar monetary system had been drawn up in Great Britain and the United States. The common ground in these plans was the conviction, especially strong on the American side, that the chaos in international financial markets during the 1930s had had a decisive influence on the catastrophic events that followed.<sup>5</sup> The lesson drawn was that a stable exchange rate system of convertible currencies

<sup>4</sup> Again, as in the British case, we encounter the difficulty of evaluating balance of payments statistics. How to measure the balance of payments correctly has always been a point of contention among economists. Every country has its own accounting method. Moreover, governments have numerous possibilities to manipulate the statistics, by changing the method of accounting, etc. The present study has no intention to participate in this debate. The officially announced figures, used in diplomatic dealings and in major financial statistics, are accepted as the base on which decision makers founded their policy. The so-called *liquidity balance*, equalling liquid liabilities to foreign governments and private holders as well as changes in official reserve assets, was regarded until 1966 by the US government as the overall measure for the balance of payments position.

<sup>5</sup> Bergsten, *The Dilemmas of the Dollar*, 1975, p.329; the classic study on the creation of the postwar monetary system is Gardner, *Dollar-Sterling Diplomacy*, new rev.ed 1969. A recent assessment is: James, 'The IMF and the Creation of the Bretton Woods System', in: Eichengreen(ed), *Europe's Postwar Recovery*, 1995, p.93-126.

had to be established to curb disruptive tendencies in the world economy and to allow an undisturbed flow of multilateral trade. This reading was a fundamental driving force of US postwar economic policy towards Europe. The central role accorded to monetary policy in the stabilization of postwar Europe and in creating an economically liberal Atlantic system, protected by an American dominated security system, provides an important rationale for understanding the US reluctance regarding changes in the system. The monetary system and the security system were two sides of the same coin and changes in one sphere invariably affected the other, as we shall see later.

To avoid the unilateral currency devaluations and the massive trade restrictions which had characterized the 'beggar thy neighbour' policies of so many interwar governments, American and British officials devised, at the 1944 Bretton Woods Conference, a system of fixed exchange rates for the major world currencies, based on the dollar as the center of the system. The value of these currencies was pegged to the dollar. Exchange rate changes were to be limited to the extreme circumstances of a 'fundamental disequilibrium'. This turned out to be a very vague definition. The value of the dollar was expressed by a fixed rate to gold (\$35/ounce). Dollar holders were guaranteed by the US government that they could exchange their dollars for gold at any time at this rate. The US gold stock thus provided the essential foundation stone of exchange rate stability in this system. The objective was to make all major currencies convertible with each other and with the dollar, thus guaranteeing an undisturbed flow of goods and capital in the world economy. In case a country experienced balance of payments difficulties, it would draw on the resources of a newly created body, the International Monetary Fund (IMF).

This system, negotiated between Britain and the United States, but perforce also accepted by the rest of the industrial countries (apart from the communist bloc), had another important consequence which made it different from prewar practices. The participating governments *'formally committed themselves to the principle of collective responsibility for the management of the international monetary order.'*<sup>6</sup> In international organisations like IMF, OEEC, EPU, the Bank of International Settlements (BIS), etc., monetary policy was discussed

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<sup>6</sup> Cohen, *Organizing the World's Money*, 1977, p.93.

and common solutions were sought.

This was particularly important when the strict rules of the Bretton Woods system regarding monetary policy turned out to be out of tune with the severe realities of the postwar world and the rapidly changing economic circumstances. The major problem was the immense need for capital and goods to reconstruct the war-ravaged European economies. Only the US was able to provide such capital and essential commodities. Thus, they became by far the biggest supplier of goods on world markets, and the need for dollars to pay for these goods soon made the dollar a rare asset. The resources of the IMF were not large enough to provide enough liquidity. Most governments had to impose strong restrictions to prevent runs out of their currency into the dollar. The ill-fated attempt by the United Kingdom to return to convertibility in 1947, for example, resulted in such a run. It made it clear that a longer transitory period than expected would be necessary before full convertibility was to be achieved. Meanwhile, US economic programs and military aid fuelled the European economies with liquidity in the form of dollars. This provided governments with the possibility to build up their reserves and kept the European market open for US business. What emerged was a dollar-gold standard differing in many aspects from the plans envisaged in Bretton Woods. However, the system proved to work very well for most of the 1950s.

How important the provision of dollars for the recovery of Europe actually was is still an issue of debate among historians. It suffices here to say that at the end of 1958 most European countries had achieved the goal of closing the dollar gap and had built up respectable monetary reserves, mainly held in dollars. De-facto convertibility was introduced. However, the sudden emergence of huge US balance of payments deficits threw the system almost immediately into crisis.

### c) The Debate on the Balance of Payments Deficit

The debate on the causes and consequences of the American deficit produced innumerable pages by governments, journalists, and scientists.<sup>7</sup> Not surprisingly, the debate was started by economists. The most influential contribution has been the early study by the Belgian-American economist R. Triffin, 'Gold and the Dollar Crisis', published in 1960. In his book Triffin pointed to an inherent paradox in the dollar-gold system which later became known as the Triffin Dilemma. His analysis focused on the international monetary system's dependence on dollars as main source of liquidity. This was a consequence of the liquidity gap after the war which had put countries in reconstruction on a de facto dollar standard. Dollars came to make up a huge part of their reserves, and the American currency became the main transaction currency. The role of the dollar as reserve currency and transaction unit implied, according to Triffin, that the United States necessarily had annual balance of payments deficits caused by the outflow of dollars to the growing world economy. However, as the amounts of dollars in the reserves of the major industrial countries and those accumulating in the system mounted, the US gold reserves, which guaranteed the value of the dollar, were no longer able to cover all the claims on the US government. Consequently, confidence in the value of the dollar waned and dollar-holders exchanged the dollar for gold, causing a drain on the US gold stock. The necessary measure to restore confidence, would have been to restrict the outflow of dollars. This, however, would have resulted in a shortage of liquidity for world trade (gold as a rare raw material was not able to cover the expansion of world trade). Thus, the system was undermining itself. The solution Triffin devised for this

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<sup>7</sup> The contributors to the extensive literature on monetary problems in the 1960's can be roughly divided in four categories with many works crossing the borderlines: Economists, Political Scientists, Historians, and Participants in International Monetary Diplomacy. Examples for accounts by economists: Triffin, *Gold and the Dollar Crisis*, 1961. Bordo/Eichengreen(eds), *A Retrospective on the Bretton Woods System*, 1993; Horsefield(ed), *The IMF 1945-65: 20 Years of International Monetary Cooperation*, 1969; Yeager, *International Monetary Relations: Theory, History and Policy*, 1976. Political scientists tackled the problem mostly by scrutinizing the power structure behind international monetary relations. See for example: Block, *The Origins of International Economic Disorder*, 1977; Bergsten (1975); Cohen B., *Organizing the World's Money: The Political Economy of International Monetary Relations*, 1977; Odell, *US International Monetary Relations*, 1982; Cohen, *International Monetary Reform, 1964-1969*, 1970; Strange, *International Economic Relations of the Western World 1959-71*, 1976. Historical accounts based on archival research are rare: Borden, in: Paterson(ed), *Kennedy's Quest for Victory*, 1989, p.57-85; Kunz, in: Kunz(ed), *The Diplomacy of the Crucial Decade*, 1994, and, recently, James, *International Monetary Cooperation since Bretton Woods*, 1996. Policy-makers concerned with monetary problems also produced many volumes. Amongst the best known are: Gilbert, *Quest For World Monetary Order*, 1980; Solomon (1982); Roosa, *The Dollar Problem and World Liquidity*, 1967; Coombs, *The Arena of International Finance*, 1976.

problem was a kind of a world bank where the rich industrial countries were to pool their reserves and which would become the source of liquidity. However, like most of the ingenious mechanisms economists contrived, this proposal was out of tune with political realities. The surrender of sovereignty to such a body was hardly acceptable to any nation.

As usual, governments looked not for the possibly most rational solution to the monetary problems but for the politically most opportune.<sup>1</sup> Corrective actions in the monetary field entailed -as they do still- very unpopular measures. This was a strong incentive to continue the system by curing the symptoms and neglecting the causes. After all, the Triffin dilemma had been there since the end of the war, and the system had nevertheless worked to mutual advantage.<sup>8</sup>

The different elements of the American deficit were easily identifiable. Apart from temporary factors, four causes of a structural nature were mainly responsible:

1. US military expenditure abroad (including foreign aid). The maintenance of military facilities on a worldwide base and the expansion of foreign aid to stabilize friendly governments were essential parts of American Cold War foreign policy. In the case of Europe, the implicit outflow of capital coincided positively with the European need for dollar liquidity during the 1950's. This need vanished, as we have seen. The US military posture, however, remained essentially the same, as did the dollar drain associated with it. As in the British case, it is hardly possible to establish the exact impact of troop maintenance abroad on bilateral payments balances. The only concerted effort during the Trilateral negotiations of 1966/67 failed (see ch.XI).
2. US investments abroad and long-term capital outflow. As the European recovery proceeded, investment in the European market became very attractive for American businesses. Factors like low labour costs, the lowering of tariffs within the Common Market, the proximity of markets, etc., made this an obvious strategy for US investors.<sup>9</sup>
3. The shrinking American trade surplus, closely connected with re-emerging European

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<sup>8</sup> This inertia was one of the major reasons that flexible exchange rates were ruled out for such a long time; see: Milward, 'The Origins of the Fixed Rate Dollar System', in: Reis(ed), *International Monetary Systems in Historical Perspective*, 1995, p.135-51.

<sup>9</sup> Ilgen, *Autonomy and Interdependence*, 1985, p.27.

competitiveness and output.

**4. Short-term capital movements.** The pegged exchange rate system made speculation against currencies under pressure good business without many risks. Sterling, and subsequently the dollar, became repeatedly the target of speculative attacks, requiring costly rescue actions.

Table 8:  
Selected US balance of payments figures, 1955-1961 (\$ billion)

	Liquidity Balance	Trade Balance, incl. government financed exports	Direct Investment Abroad	Direct Military Expenditures Abroad
1955	-1.24	2.90	-0.82	-2.90
1956	-0.92	4.75	-1.95	-2.95
1957	0.62	6.27	-2.44	-3.22
1958	-3.35	3.46	-1.18	-3.43
1959	-3.65	1.15	-1.37	-3.11
1960	-3.71	4.89	-1.67	-3.09
1961	-2.43	5.57	-1.60	-3.00

Source: Survey of Current Business, October 1972; June 1975.

A rapid correction of these factors would have required revolutionary changes in US foreign and domestic policies, such as an 'agonizing reappraisal' of its security policy, the introduction of currency controls, direct controls over American investment abroad, or curbing the domestic economy to keep prices down. This last option was hardly considered in the United States, contrary to the British case. To balance its external account Britain resorted, as we have seen, repeatedly to restrictive domestic policies (see ch.I). There were hardly any other options available apart from devaluation and large-scale borrowing abroad. The United States, on the other side, were able to exert enough influence to get other countries to hold large parts of their reserves in dollars and not exchange them for gold. As we shall see later, they were also able to induce other countries, including Britain, to a monetary policy which actively supported the reserve currency role of the dollar.<sup>10</sup>

<sup>10</sup> Britain lacked this bargaining power. Everybody, except the Sterling Area countries, was free to cash in surplus sterling for dollar and thus add to the rampant speculation against the pound.

Devaluation, the most logical way of adjustment for a country with a persistent deficit, was ruled out as long as the dollar was not seen as fundamentally overvalued. Without the acceptance of such a view by Washington's major trading partners, those would follow the US move and neutralize it by devaluing themselves. It was also very likely that a change of the dollar gold parity would have ended an international monetary system which hold considerable advantages for the United States. It had been instrumental in building up a 'free world' economically and militarily compatible with American policies, it had helped to finance long-term military commitments abroad without balance of payments constraints or domestic inflation<sup>11</sup>, and it made the United States the issuer of the world's principal vehicle and reserve currency. Further reasons against devaluation were notions of prestige and national pride. Until the early 1970's US presidents saw devaluation as humiliating for the nation and disastrous for themselves on the domestic scene. It is not by accident that militarist language like 'the battle for the dollar' or 'war against the deficits' was used so often by the US government.

Thus, radical solutions were ruled out. Other, less grave, measures were sought. These measures often implied active cooperation by other countries. US governments did not see the deficits as their sole responsibility. The view became prominent in Washington that American policies which had helped to rebuild and protect Europe were the main cause of the deficits, and that the beneficiaries should take over part of the burden of adjustment. This basic underlying conviction is fundamental for an understanding of American international monetary policy in the 1960s. It also partly explains the emphasis many American politicians put on the foreign exchange cost of their troops, though they were only a limited part of the problem.

A structural omission in the working of the international monetary system was responsible for much of the political argument between Europeans and Americans on the payments deficit. Nowhere was it stipulated whether surplus or deficit countries would have to take the

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<sup>11</sup> This argument was brought forward forcefully by European critics of US monetary policy. '...the United States had used its exorbitant privilege as the centre-country of a gold-exchange system to run a perpetual balance of payments deficit and to finance a distant and expensive war in Vietnam by inflationary credit creation rather than by a transfer of resources from the civilians to the military by means of taxation'; Strange, 'Interpretations of a Decade', in: Tsoukalis(ed), *The Political Economy of International Money*, 1985, p.11.

necessary steps in case of a persistent imbalance.<sup>12</sup> On a worldwide level there were no formal procedures to settle such imbalances. The conflict had to be decided by interstate bargaining and a basically economic problem became a highly politicized issue. Monetary adjustment usually has strong repercussions on the domestic economy and politics of the adjusting country, and is risky for every government. It is much safer to get other countries to adjust. The result are various political and economic pressures leading to the kind of linkages of which offset is a prime example.

The disagreements about the responsibility for adjustment found their expression in profoundly different views of European and US governments about the reasons for the monetary problems and its possible cures. This fundamental divergence is well summarized in an exchange of letters between J.Holtrop, president of the Dutch central bank, and E.Bernstein, a high American IMF official.<sup>13</sup> Both made overtly clear whom they thought should take the principal steps to solve the problem. Holtrop concluded his letter by stating that *'the solution of the American balance of payments problem has fundamentally to be found in the internal economic policies of the United States. This conclusion is not different from the one we have arrived at when balance of payments troubles, after the period of reconstruction was over, still harassed many European countries'*. Bernstein retorted: *'If the United States continues to bear an excessive share of the expense of defense within Europe ... and relieves the European countries of meeting an adequate part of the cost of their own defense, it is inevitable that these wealthy countries will save too much...this is the central part of the US payments problem ... the US cannot solve its payments problems through its own financial policies.'* These key positions were to be repeated over and over during the 1960s. They formed the background of a debate which became increasingly acrimonious.<sup>14</sup>

In the late 1950s, however, both sides agreed that they had better to find some common

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<sup>12</sup> Hoffmeyer, *The International Monetary System. An Essay in Interpretation*, 1992, p.70.

<sup>13</sup> The letters are in the Archive of the Dutch Foreign Ministry: MF/GT/891/EEG/E/Algemeen/4: Holtrop to Bernstein, 26 July 1960; Bernstein to Holtrop, 17 August 1960. I thank Y.Alkema for making these documents available to me.

<sup>14</sup> A concise summary of European-American differences in monetary matters is provided by Cleveland, *The Atlantic Idea and its European Rivals*, 1966, p.75-95.



ground and coordinate their monetary policies to a greater extent than previously. The introduction of convertibility for European currencies in 1958 had vastly increased the amount of capital movements, and the negative American balance of payments caused speculation on a large scale. The Europeans first pointed out the dangers of this development. They had rebuilt their reserves now, yet dollars were still accumulating on their accounts. The temptation to transfer them back via exchange to gold was strong, but, as we have seen, a two-edged strategy given the dangers for the international monetary system this implied. There was widespread transatlantic agreement on the desirability to continue with a system which had served the participants well since the end of the war and whose breakup would have unforeseeable consequences. The only question was which action was to be taken and, above all, who would have to take it.

**d) The Eisenhower-Administration and its Response to the Balance of Payments Problem**

It is difficult to trace the exact point at which the balance of payments began to seriously trouble the American administration and public. There had always been deficits during the 1950s, apart from an exceptional 1957 when the Suez Crisis pushed raw material prices up and produced a small surplus.<sup>15</sup> Shortly afterwards, the American economy slumped into a brief recession, characterized by low investment rates and rising unemployment. When it recovered, parallel to a period of stagnation in European economies, the trade balance of the United States was unsettled by an import boom in the US and a slowing down of exports to Europe. The traditionally high American trade surplus with Europe, which had balanced capital export and government expenditure abroad, shrank considerably. Suddenly a yawning balance of payments deficit emerged. At the same time, the drain on the US gold stock grew to record levels. The recession obviously also had led to a loss of confidence in the dollar. Additionally, Britain and France refilled their depleted reserves.

The combination of these temporary and the structural factors outlined above caused the high 1958-1960 deficits. The government registered the gold outflow with particular concern. In November 1958, Eisenhower and Anderson informed the Senate Majority Leader about

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<sup>15</sup> For the following paragraph, see: NA, RG 59, Lot Files: BEA, OGA, Box 5, Background Paper: US Balance of Payments Position, 16.11.1960.

warning voices from abroad concerning dollar stability. Eisenhower struck the key of the later debate, stating that *'the stability of our currency is an absolute necessity to our security and our economic development.'*<sup>16</sup> However, serious preoccupation and discussion started only in mid-1959. From the outset, the solution of raising the price of gold, which meant a devaluation of the dollar, was ruled out as contradicting basic US postwar policy.<sup>17</sup> Foreign economic policy was still much a prerogative of the State Department, and in a short paper of July 1959 it laid out its proposed course. The authors acknowledged that the present trend in the balance of payments could not be allowed to continue. The sharp decline of the trade balance and large military expenditures abroad were identified as the fundamental problems.<sup>18</sup> Rejecting explicitly restrictive measures in the domestic economy, the paper proposed the removal of trade restrictions of all kinds, the substitution of US foreign aid by European aid, and a reduction of military expenditure. The cabinet approved a program of action along those three lines in August 1959.<sup>19</sup> Subsequently Washington intensified its efforts towards trade liberalization, in particular vis-a-vis Europe, and towards a better sharing of the foreign aid burden.<sup>20</sup>

Divergences within the administration emerged on the third issue. It had been a recurrent theme in European-American relations in the 1950s that Washington felt it bore a disproportionate share of the cost of common defence. Time and again, Eisenhower criticized the European reticence in taking up more of the burden: *'We should ask when the hell these other people are going to do their duty. We have got to get tougher with them ... These other NATO powers cannot go on forever riding on our coat-tails ... All of these nations seem to be trying to figure out how little they themselves can do and how best to leave us do the rest*

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<sup>16</sup> NSA, NHP (Fred Kaplan Donation), Box 1, folder 61, 18.11.1958.

<sup>17</sup> FRUS 1958-60, IV, US-British Meeting, 10.6.1958, p.27-28; *ibid.*, Minutes of Cabinet Meeting, 13.3.1959, p.103.

<sup>18</sup> *ibid.*, Paper prep. by DoS: Internat. Payments Position of the US, 24.7.1959, p.115-120.

<sup>19</sup> *ibid.*, Record of Actions on Items presented at Cabinet Meeting, 19 August 1959, p.53-54.

<sup>20</sup> A US initiative at the GATT session in 1958 led to the lifting of many quotas in European-American trade. The so-called Dillon Round, negotiating mutual tariff reductions started only in 1961. See: Alkema, *Regionalism in A Multilateral Framework*, Ph.D., EUI 1996. For the American effort to get their allies to share the foreign aid burden, see Kaufman, *Trade and Aid*, 1982.

*of the job.*<sup>21</sup> The gold outflow and the deficits added to this feeling. *The President said he would have no objection to new measures in Berlin and Germany. He commented that, for example, it is time to pull out some of our forces now located in Europe. He cited the balance of payments difficulties the U.S. is experiencing at the present time.*<sup>22</sup> The foreign exchange cost of American forces in Germany had risen sharply throughout the 1950s, in particular after the termination of occupation and support cost payments. From FY 1953-1955 it had been \$250m, in 1956 \$316m, in 1957 \$425m, in 1958 \$545m, and in 1959 \$686m; a level which was expected to remain stable.<sup>23</sup> Compared with the liquidity deficit, it seemed as if troop stationing in Germany contributed to about 20% of the deficit. As we have seen in ch.I, when discussing the cost of British troops, it is very difficult to establish the real impact of troop stationing abroad on the balance of payments of the sending country. There is, however, little doubt that American troops contributed considerably to the accumulation of reserves by the Federal Republic. This factor and the growing dissatisfaction with the immobility in the political and military situation in Europe sparked a vivid debate within the US government, which centred on the question whether monetary and military developments required a reduction of the US military commitment in Europe. The arguments used during this debate will be outlined in some detail; they were to come up again and again in subsequent discussions within US governments.

In late 1959, during the budget discussions, a series of high-level meetings was devoted to the problem. The initiative seems to have originated -like the Radford plan- in the Department of Defense. The Secretary of Defense, McElroy, thought that troop cuts in Europe were now possible and desirable for military reasons. These were first the diminished importance of conventional troops due to the gigantic nuclear capability the US had built up during the 1950s, both in the strategic and tactical range, and second the improved mobility of combat

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<sup>21</sup> FRUS 1958-60, VII, Memo of Discussion at the 390th NSC Meeting, 11.12.1958, p.368-69.

<sup>22</sup> *ibid.*, IX, Memo of Conference with President, 16.10.59, p.70.

<sup>23</sup> NA, RG 59, BEA, OGA, Box 14, Briefing Paper for the Anderson-Dillon mission: Support Costs, November 1960. To give an illustration of how this foreign exchange was used: The 1959 figure (\$686m) was divided up in \$295.5 for contractual services, \$243m for military pay, and \$109m for materials and supply.

forces.<sup>24</sup> He was supported by the Secretary of Treasury, Anderson, who argued that the balance of payments problem was as vital as defence matters. In his opinion, it could not be solved by conventional means and it urgently required action on military expenditure abroad.

Against this, Gates, the Deputy Secretary of Defense, pointed out that *'he did not see how we could balance our budget unless we completely revolutionized our military strategy'*.<sup>25</sup> His position was supported by the State Department: *'There seems to me to be no greater problem facing this Government than whether or not to warp our military doctrine and stunt our military establishment to meet temporary economic pressures. We face the alternative whether to run an uncertain risk of some loss of confidence in the dollar or the certain risk of a loss of confidence in America's determination to make common cause with its allies and maintain a rational and credible deterrent to communist aggression. If this happens, the standing of the American dollar and a great deal more besides will inevitably be prejudiced'*.<sup>26</sup> The President took an intermediary position. Though he was increasingly frustrated with the fact that the US with its troops seemed to be stuck in Europe and deeply worried about the gold drain, he was also highly sensitive to any action which could unsettle NATO. At the beginning of November he met SACEUR Norstad, who argued strongly against force cuts in view of the uncertain situation regarding Khrushchev's Berlin ultimatum. After once more denouncing the Europeans for 'making a sucker out of Uncle Sam', the President agreed in the end *'that we cannot take ruthless actions simply for financial reasons.'*<sup>27</sup>

Soon afterwards he convoked a NSC meeting in which the opponents in the debate presented their arguments again.<sup>28</sup> The Director of the Budget, Stans, pointed out that the commitment

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<sup>24</sup> *'The U.S. is going to have to begin withdrawing...in FY 1961...it would give us a great deal more flexibility to have the principal body of our troop strength in the U.S. where they could be dispatched quickly to any trouble spot...it seemed likely that West Germany would soon be in a position to take over the U.S. role as chief defender of Western Europe'*, excerpt from a memcon Burden-McElroy, attached to a Memo Merchant to Herter, 25.9.59, NSA, The Berlin Crisis, Doc.nr.1666.

<sup>25</sup> FRUS 1958-60, VII,1, Conversation Herter, Anderson, McElroy et.al., 24.10.59, p.488-94.

<sup>26</sup> *ibid.*, Memo from Acting SecState, Smith, to Herter, 29.10.1959, p.496.

<sup>27</sup> *ibid.*, Memo of Conversation Norstad-Eisenhower, 4.11.1959, p.497-500.

<sup>28</sup> *ibid.*, Memo of Discussion at the 424th NSC Meeting, 12.11.59, p.504-15.

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in Europe cost the US \$2.5 billion (plus \$900 million military aid) in budgetary terms, of which \$1.2 billion were relevant for the balance of payments. He doubted whether the budget could stay in balance with this burden. State Department and CIA representatives, on the other side, warned of political destabilization in Europe in case of troop cuts. They thought that reductions should only be effected if there was a corresponding move by the Soviet Union. The President apparently had already made his mind up against reductions beforehand. Grudgingly, he stated that the time was not yet ripe for reductions. The final decision was *'that there would be no significant cuts in Calendar Year 1960 in the forces committed to NATO for that year, unless agreed to through negotiations [with the SU; HZ].'*<sup>29</sup> Eisenhower's rather timid disarmament proposals, however, never came close to mutual force reductions. This was partly due to Adenauer's resistance to any such a scheme. The idea, however, that mutual balanced force reductions were a solution to the problem was to surface again, particularly during the Johnson administration.

The outcome of the debate signified that the balance of payments problem would remain for the moment separated from the issue of troop levels in Europe. After all, the dollar problem was widely seen as temporary, manageable and even self-correcting because costs and prices were rising faster in Europe than in the United States. The political rationale behind the troop commitment was still perceived as strong enough to overcome a short-term economic difficulty. Washington's activism therefore centred on trade liberalization and foreign aid. Germany was asked to establish a foreign aid program of its own.<sup>30</sup> The Germans, relieved at the absence of troop cut threats or support cost demands, promised vigorous efforts. However, the results were poor. One year later, during the annual meeting of the IMF and the World Bank, the Germans were the targets of strong criticism directed at their failure to initiate a foreign aid program to correct their high surplus.<sup>31</sup>

At the same meeting, the Americans were confronted with the wide-spread anxiety in

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<sup>29</sup> *ibid.*, p.515.

<sup>30</sup> FRUS 1958-60, IV, Anderson Memo to President, 2.12.59, p.357; FRUS 1958-60, VII, 1, Conversation Dillon - German Government, 11.12.59, p.196-201.

<sup>31</sup> NYT, 27.9.1960, p.5; Financial Times, 28.9.1960.

international financial circles about the future of the international monetary system if the deficits continued. This was no surprise. Despite a remarkable recovery in the trade balance, another high balance of payments deficit was expected for 1960. It was clear that the first efforts had not yielded the expected results. The gold outflow continued with irritating regularity. US liabilities came perilously close to the point where they were no more covered by US gold reserves.

Increasingly, the American government became also aware of a possible spillover into other policy fields. This was true, above all, for relations with the allies who were the main recipients of out-flowing dollars or gold. In case of serious conflict -and de Gaulle's actions since his ascendancy to power were ominous- this factor could possibly be used as a tool against the United States. *'Mr Herter said that a report, almost a rumour, had come to him that, during the conversations of de Gaulle and Adenauer, they talked about shifting the currency base from dollars to gold, in part as a means of putting pressure on the United States to accede to some of their ideas affecting NATO. The President said that if this were to happen, our immediate and necessary action would be to pull our forces out of Europe and that this would destroy at their very heart the security arrangements in Europe.'*<sup>32</sup> The exchange shows clearly the hidden political conflict in the balance of payments question, and also its emerging linkage to the context of security policy in the alliance.

As the gold losses continued, despite the recovery in the trade balance, more drastic action than the export promotion program advocated by the State Department was obviously necessary. The options seemed limited. Restrictive action in the domestic economy was hardly considered, given its unpopularity in the middle of Nixon's election campaign against Kennedy and the fact that the economy had just surmounted a recession. Interest rates remained low for this reason, and what was decisive, they remained lower than in Europe.<sup>33</sup> Thus, when in autumn the budget planning began, attention focused again on US military

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<sup>32</sup> FRUS 1958-60, IV, Memo of Conversation, 12.8.1960, p.127.

<sup>33</sup> From June to August 1960, the US discount rate was lowered from 4% to 3%. The Germans, fighting with an booming economy, put their rate up from 4% to 5%, and thus attracted massively speculative capital. See: Emminger, 'Deutsche Wahrungspolitik im Spannungsfeld zwischen innerem und auerem Gleichgewicht', in: Deutsche Bundesbank(ed), *Wahrung und Wirtschaft in Deutschland, 1876-1975*, 1976, p.502.

commitments. This time, the feeling that the monetary problem would be of a temporary nature had been shattered.

Anderson informed his colleagues that *'this large outflow and accumulation by financially strong Western European countries and Japan was more likely to create a crisis both for the US and the Free World than any other set of existing circumstances.'*<sup>34</sup> He accused the State Department and the Pentagon of having blocked all burden-sharing initiatives by citing various political obstacles. According to Anderson, it was time *'to negotiate on a bilateral basis with the European countries, and especially Germany, for the payment of the cost of maintaining US forces abroad'*<sup>35</sup>. The President agreed on the need for firm measures, and an action program for further study was formulated, which included the removal of the troop's dependents from Europe, support cost negotiations with Germany, force reductions, further trade liberalization, etc. Simultaneously, Eisenhower wrote a letter to Adenauer in which he pointed to the need of German action in the field of international monetary policy and announced that Anderson and Dillon would visit Bonn to pursue corresponding negotiations.<sup>36</sup>

The alarm in the US government grew close to panic when an unforeseen event in October 1960 rocked the foundations of the international monetary system. Within a few days a wave of speculative gold acquisitions drove the price on the London gold market from the official \$35 an ounce up to \$40.<sup>37</sup> The danger of a run on the US gold stock was obvious. In view of the absence of sufficient gold sales by the producing countries it was up to the United States to furnish gold to fulfill the demand. The US authorities supplied the Bank of England

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<sup>34</sup> DDRS 92 (408), Memo of Meeting with the President, 4.10.1960.

<sup>35</sup> *ibid.*

<sup>36</sup> FRUS 1958-60, IX, Eisenhower to Adenauer, 7 October 1960, p.692-94. Adenauer's response ostentatiously welcomed the prospect of a visit. However, he urged Eisenhower not to request anything like support costs, citing the well known argument of an impending election campaign; *ibid.*, Adenauer to Eisenhower, 20.10.1960, p.694-696.

<sup>37</sup> The London gold market was the place where 85% of all newly mined gold was handled, either by central banks or by private dealers. The Bank of England had assumed responsibility for controlling the market price. Yet, under the pressure in October 1960 its reserves were soon exhausted.

with gold from its reserves to enable it to keep the price down.<sup>38</sup>

The alarming signal of the London Gold Crisis was that it showed the thin ground on which the international monetary system was built. The whole system rested upon the certainty that the United States would guarantee the exchange value of the dollar with its reserves, and around 1960 it became clear that the reserves in Fort Knox were not adequate to cover the foreign liabilities. The slightest hint that the United States in these circumstances would increase the official price of gold met with an immediate run out of dollars into gold. The election race in 1960 provoked such a slide of confidence centring on the intentions of Kennedy in case were he to be elected. Huge amounts of short-term capital moved to European accounts in anticipation of a change in monetary policies. Only after Kennedy on 31 October pledged firmly to defend the dollar gold exchange rate, did markets slowly calm down. For the Eisenhower administration the London Gold Crisis was the last straw and any impediments against drastic action were thrown over board. *'We can't afford to let our monetary system break down before Mr Kennedy is even sworn in'*<sup>39</sup>, Eisenhower remarked and added in a telephone conversation with Herter that *'... when you are going into a war - and this is in effect a kind of war- you take lesser objectives and put them aside.'*<sup>40</sup> Anderson struck an equally apocalyptic note: *'... we had not been faced by a problem as serious as the one facing us now. Moreover, this was a unique experience; it had never happened to the United States before.'*<sup>41</sup>

Hastily, the government put together an emergency program. Two weeks later, Eisenhower issued a directive outlining steps with respect to the US balance of payments.<sup>42</sup> It was the first in a long series of presidential action programs dealing with the balance of payments threat. Eisenhower's directive contained no analysis of the deeper causes of the deficits. Nor

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<sup>38</sup> Strange (1976), p.76.

<sup>39</sup> FRUS 1958-60, IV, Memo of Conference with the President, 15.11.1960; p.138.

<sup>40</sup> Kesaris(ed), Minutes of Telephone Conversations of the Secretaries of State, 1953-61 (microfilmed), Reel 10, 15.11.1960.

<sup>41</sup> FRUS 1958-60, VII/1, Memo of Discussion at the 465th NSC Meeting, 31.10.1960, p.529.

<sup>42</sup> American Foreign Policy. Current Documents 1960, p.786-92.



was there an attempt to evaluate its implications for future policies. The only new step, apart from restating well-known remedies -trade liberalization, domestic economic stabilization, tying of foreign aid programs to purchases in the US- was an extensive reduction in the number of dependents of US military personnel abroad. There were, in fact, not many actions by which the outgoing Eisenhower administration could show its determination to resolve the problem. During another tense discussion of the problem, Anderson ruled out restrictive trade measures as inimical to US interests and monetary remedies as setting off speculation. The only field where the government could act rapidly unilaterally was in the field of military commitments abroad. That was the background of the dependents decision.<sup>43</sup> Regarding military expenditures abroad in general, the directive identified them as a major cause but limited the related paragraph to the wish *'that our friends and allies accept their full share of the costs of maintaining the security of the free world.'*<sup>44</sup>

e) The Anderson-Dillon mission, November 1960

That concrete action would follow was announced one day later. Anderson informed the press of the US government's intention to pursue with the German government talks regarding ways to relieve the monetary pressure. In the aftermath of the London Gold Crisis, the announced Anderson-Dillon visit had changed its scope. What had originated as a proposal to discuss bilaterally various measures to resolve the balance of payments problem, narrowed now to an outright demand for funds to balance the foreign exchange cost of US troops. The question whether the US delegation should demand support costs, that is straight budgetary help, or some kind of transaction which would offset the dollar drain was decided in favour of Anderson's position. *'Mr. Anderson said ... he would ask Adenauer for \$650.000.000 a year as payment for keeping our troops on their soil. Drastic action is necessary here.'*<sup>45</sup> Throwing over board all political arguments, Anderson pressed his position, against resistance in the State Department and to the surprise of most participants, including the US embassy in Bonn and the German government.

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<sup>43</sup> FRUS 1958-60, IV, Memo of Conference with the President, 9.11.1960, p.130; Kesaris(ed), Telephone Conversations, Reel 11, telcon Anderson-Herter, 11.11.1960.

<sup>44</sup> American Foreign Policy, Current Documents, 1960, p.789.

<sup>45</sup> FRUS 1958-60, IV, Memo of Conference with the President, 15.11.1960, p.138; see also: Donfried, *The Political Economy of Alliance: Issue Linkage in the West-German American Relationship*, Ph.D.thesis, 1991, p.61-65.

In the midst of the preparations for the visit, Kennedy won the presidential elections. This deprived the delegation of much of its bargaining power. Anderson and Dillon therefore tried to enlist the support of Kennedy for the initiative and requested a meeting with the newly elected President. All they achieved, however, was an explanatory meeting with one of Kennedy's advisers.<sup>46</sup> Kennedy was clearly unwilling to be committed to a step which might produce far-reaching political consequences.<sup>47</sup> This reflected the judgment of the State Department which increasingly had moved to the sidelines of the discussion. Herter was present in almost none of the above-mentioned meetings on the balance of payments. It very soon became known that Dillon himself was less than enthusiastic about the mission.<sup>48</sup> As a possible candidate for a post in Kennedy's cabinet he was in a precarious position, anyway. All in all, the signs did not bode well for a successful mission.

Meanwhile, the Germans tried to prepare themselves, assuming that they would be asked mainly for more foreign aid<sup>49</sup> and not for support costs. If the latter was to happen, the demand would be rejected outright as a revival of occupation costs.<sup>50</sup> In a cabinet meeting on 15 November, the big foreign aid program was finally approved. It amounted to about one billion dollars of which more than a quarter would be supplied by German industry.<sup>51</sup> This large capital export program has to be seen not only as an attempt to take the wind out of the American sails but also in the context of Germany's efforts to get rid of the surplus capital streaming into the country. Additionally, the Germans planned to accept a larger share in

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<sup>46</sup> JFKL, PPP, Transition Files: Task Force Reports, Box 1073, Conversation Nitze-Anderson, 16.11.1960.

<sup>47</sup> One indication that the Kennedy people did not approve of the mission is a memo by an unidentified official on this subject, addressed to Vice President elect, Johnson. It complained that Anderson had become 'almost obsessed' with the gold outflow and that 'gold outflow, troop reductions, and NATO atomic arms plans are moves which really ought to await the transfer of powers'; LBJL, VPSF, Box 9. After the American delegation had returned from Germany, the German ambassador in Washington, Grewe, reported that Acheson had ridiculed their effort and that Kennedy had felt insufficiently informed; PA-AA, Büro STS, 79, Grewe to AA, tel.2447, 30 November 1960.

<sup>48</sup> NA, RG59, DF 1960-3, 762a.5/11-460, Leddy to Dillon transmitting an Anderson memo on the troop cost issue, 4.11.1960; NYT, 27.11.1960, p.3.

<sup>49</sup> In August, Dillon had written to Adenauer on this subject. The U.S.embassy was advised to tell German authorities that '*their first financial and moral obligation was to establish a significant longterm lending program*'; see: NA, RG 59, 862a.0000, 8-260, Dillon to Adenauer; 862a.10, 8-160, Dillon to Bonn embassy, 1.8.1960.

<sup>50</sup> BA, B126/34104, Preparatory Meeting of Officials prior to US delegation visit, 7.11.1960.

<sup>51</sup> BA B126/34104, Excerpt of 129th Cabinet Meeting, 15.11.1960.

NATO infrastructure costs and possibly the prepayment of postwar debts.

The records of the actual conversations are not yet completely available. However, detailed accounts exist from both sides and this permits an accurate reconstruction of the issues. At the outset, Anderson and Dillon met with Adenauer. According to Dillon the meeting only served to underline that the Chancellor did not understand the problem 'at all well' and just kept on repeating, *'that there is only one thing that worries him, and that is the possibility that we might redeploy some of our troops.'* On this point Anderson remarked that Eisenhower was resolved to take any measure necessary to protect the dollar.<sup>52</sup>

After this short encounter the delegations met and the Germans presented their proposals.<sup>53</sup> These included the foreign aid program, the NATO infrastructure costs, and the proposal of a prepayment of postwar debts, provided the Americans released German assets, vested during World War II. There was also some talk about larger military purchases in the United States, and the Germans promised 100% prepayment to the already existing Treasury account, on which Germany transferred the payments for its military orders. As a last concession, they also offered to negotiate about the assumption of some U.S. military aid to Turkey and Greece. The Americans, however, considered the foreign aid program as self-evident and possibly just self-serving, and the other measures as too small. *'The US Secretary of Treasury, Anderson, outlined in very drastic words the US situation and its needs, and he hinted very outspokenly to German moral obligations in this respect .... it became clear that, in the end, a German budgetary contribution was expected.'*<sup>54</sup>

In a meeting of officials, the US delegation presented the details of its proposal. It foresaw that Germany would pay an amount of \$600m to a fund at the US Treasury which was to be used for direct payments to the US and for additional purchases of military equipment to be

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<sup>52</sup> FRUS IV, 1958-60, p.142-43.

<sup>53</sup> This account is based on: FRUS 1958-60, IV, Memo of Conference with the President, 28.11.1960, p.142-47; DDRS 87(2061), Anderson to Eisenhower, 23.11.1960; BBA, ZBR, Extract from the records of the 83.ZBR meeting: Emminger reports on US-German financial discussions, 1.12.1960.

<sup>54</sup> BBA, ZBR, 83d meeting, Emminger report, 1 December 1960.

delivered to poorer NATO allies.<sup>55</sup> State Secretary Hopf from the Federal Defence Ministry responded that it was impossible to add such a large amount to the German defence budget. He also rejected the notion that the foreign exchange losses in Germany were responsible for the US deficits. The Americans suggested *'that an increased contribution to the United States defense effort could be explained to the German public as a contribution towards Germany's own defense'*. At this point, the representative of the Federal Finance ministry delivered a fierce rejection of the American demands. He could *'not see what practical significance there could be in having a joint fund if all the money was to come from German sources and if the main purpose was to distribute these funds to ease the US balance of payments ... any payment of support costs was out of question. Those times are gone forever.'*<sup>56</sup>

The differences were irreconcilable. Subsequent negotiations on separate items of the agenda brought no result. As in earlier conflicts with the British, the Germans denied the existence of a linkage between military commitments and foreign exchange problems. Instead, they pointed to the large outflow of American private capital to Europe. A welcome example was the recent decision by the Ford Company to purchase the shares of its British subsidiary, thus transferring \$358m abroad, much to the annoyance of the US government. Later, Dillon commented angrily *'that General Norstad had said it would be a long time before the GIs buy a Ford again.'*<sup>57</sup> The suspicion was voiced in US circles *'that they [Ford] are doing this to get their money out of the United States in anticipation of real trouble here ... the Europeans, who have a large experience in this kind of thing, certainly recognize it as just that.'*<sup>58</sup>

The Germans, of course, welcomed the additional argument, which later should become part of de Gaulle's repertoire against US hegemony. After some more bickering about the causes of the balance of payments deficit the Americans broke off the negotiations, to the surprise of the Germans. Anderson, in somewhat tormented language summarized the results in a

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<sup>55</sup> NA, RG 59, Lot File, BEA, OGA, Box 5, memcon US-German officials, 22.11.1960.

<sup>56</sup> *ibid.*

<sup>57</sup> FRUS 1958-60, IV, Memo of Conference with the President, 28.11.1960, p.144

<sup>58</sup> *ibid.*, p.145.

telegram to the President: *'For practical purposes there is very little relief either to our budget or balance of payments position that will result from our discussions...We made clear to the Chancellor and his associates that in view of these circumstances and in view of the key position which the U.S. dollar occupies in the international financial system we will be required by irresistible logic to make whatever decisions we deem appropriate both in our domestic and foreign policies, including both military and economic matters as are necessary and appropriate to our firm resolve that we will not allow the dollar to deteriorate.'*<sup>59</sup> After going to Bonn, Anderson and Dillon went to France, where they got a noncommittal statement of support for their monetary policies, and to London. The British consoled the American delegation with their own dismal experiences over the issue. Lloyd called the German proposals 'chicken food' and expressed his difficulties in understanding the German psychology.<sup>60</sup>

Yet, it is difficult to see, even without knowing all details, how Anderson could have expected that the Germans would take such far-reaching steps as required by the US deficit when dealing with a lame-duck administration. It even seems that the Germans were informed beforehand that the newly elected President did not approve of the line taken during the talks.<sup>61</sup> Thus, they quietly leaned back and waited for the position of the new administration. On top of that came heavy US press criticism of the American delegation and its clumsy negotiating tactics.<sup>62</sup> When the Eisenhower administration took stock of the mission, it had to acknowledge that the results had been poor and that *'anything the Germans really do they will want to do for the new administration, so as to get maximum credit with them.'*<sup>63</sup> Nevertheless, Eisenhower did not want to leave his post with such a failure and the Atlantic Alliance in disarray. In his last two months in office he tried to leave his mark on three major issues related to US-European relations: balance of payments talks, troop reductions, and the problem of NATO nuclear sharing.

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<sup>59</sup> DDRS 87/2061, Bonn to SecState (Anderson to President), 23.11.1960.

<sup>60</sup> NA, RG 59, Lot Files, BEA/OGA, Box 5, memcon Lloyd-Anderson, 25.11.1960.

<sup>61</sup> BA, B126/34104, Embassy Washington to AA, 22.11.1960.

<sup>62</sup> See for example NYT, 24 and 25 November 1960.

<sup>63</sup> FRUS 58-60, IV, p.144.

Regarding the talks with the Germans, those were continued at a lower official level almost immediately after Anderson and Dillon went home. The demand for outright support costs was, due to the reaction of the Germans, quietly dropped.<sup>64</sup> The talks concentrated on the German offer. Shortly after the US delegation had returned, a group of participants met to discuss the prospect for a huge increase in the German defence budget, which promised to result in much higher procurement abroad. The officials agreed that, because France and Britain were eager to obtain part of these orders, the main question was '*where the prospective business goes*'.<sup>65</sup> The Americans lost no time. From 29 November to 12 December, Pentagon officials pursued in collaboration with the US embassy negotiations about military purchases in Bonn.<sup>66</sup> The Germans remained non-committal, citing budgetary problems as well as possible protests by third countries and the German industry in case of increased procurement from US sources.<sup>67</sup> Little progress was also made on the question of debt prepayment as linked to the vested German assets, on infrastructure costs, and the assumption of military aid.<sup>68</sup> All these issues found a conclusion soon after Kennedy took over. The outgoing administration would get no concessions.<sup>69</sup> Eisenhower and Anderson, in turn, spared no effort to impress upon the new President the importance of the issue.<sup>70</sup>

Discussions also continued within the administration on the issue of troop levels. The supporters of reductions argued in favour of immediate reductions.<sup>71</sup> There was much debate on whether the US should announce such a reduction at the North Atlantic Council Ministerial Meeting in December. Finally the following sentence was introduced into Herter's statement:

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<sup>64</sup> On 28 November, Press Secretary Hagerty said that the issue of support costs would not be taken up again since 'the Germans are not prepared to discuss it'; KCA 1960, p.17955.

<sup>65</sup> NA, RG 59, DF 1960-63, 811.10/11-2960, Memo: German Assistance to US B/P problem, 29.11.1960.

<sup>66</sup> Documentation in NA, RG 59, 811.10, Box 2286, Bonn 824, 2.12.1960; Bonn 825, 2.12.1960; Bonn 848, 6.12.1960; Bonn 870, 8.12.1960; Bonn 891, 13.12.1960; see also: Donfried (1991), p.83-84.

<sup>67</sup> NA, RG 59, DF 1960-63, 811.10/12-1360, Bonn 891, 13.12.1960.

<sup>68</sup> DDRS 92(1330), Paris to SecState 2508: Meeting Anderson/Dillon-Erhard, 15.12.1960.

<sup>69</sup> PA-AA, Büro STS, 79, Carstens memo on German-American financial talks, 11 January 1961.

<sup>70</sup> FRUS 58-60, IV, Anderson Memo: Meeting with Kennedy, 6.12.1960, p.147-51; FRUS 1961-63, IX, Memorandum for the Record, 19.1.1961, p.1-2; Eisenhower, *Waging Peace*, p.715.

<sup>71</sup> FRUS, IV, Memorandum of Conference with the President, 30.11.1960, p.543-47.

*'Some redeployment may become a necessity unless our balance of payments can be brought into a more reasonable equilibrium.'*<sup>72</sup> More was not possible given Kennedy's and the State Department's opposition.

Herter's speech also saw the emergence of another project which would, like the troop cost talks, long outlive the administration which initiated it: the plan of a multi-laterally manned NATO atomic force. The scheme was intended to give the Europeans a say in nuclear matters, prevent the development of national atomic capabilities, and solve the credibility dilemma of NATO, which lay in the question whether the United States would really go to nuclear war for Europe, in particular after the Soviets had demonstrated that they were able to reach US territory with nuclear weapons. Herter offered as a first contribution to this multilateral force (MLF) five submarines equipped with POLARIS missiles.<sup>73</sup> The plan was to fulfill the European demand for more participation, leaving, however, the last decision to the Americans. This ambiguity was to plague the project, apart from the protracted practical problems, until its hardly glorious finish in the mid-Sixties.

When Eisenhower handed over the office to his successor he had just made some tentative steps concerning American monetary problems and Europe's demands for equality, particularly in the nuclear field. Transatlantic relations in the 1960s were to be dominated by these issues. The balance of payments was to play a central role in the game, and consequently, so too did the troop cost problem.

The deeper cause of the problems outlined in this chapter, however, lay in the simple fundamental fact that the monetary system and the Atlantic security system, which had been to a large degree two sides of the same coin, showed increasing signs of incompatibility. The monetary system, in itself irrational as critics like Triffin and others pointed out, had

*die beiden sind verbunden, kann man sie nicht  
nein, die beiden waren aus demselben*

<sup>72</sup> FRUS 1958-60, VII, 1, p.681; for the debate on this phrase and the German reaction to it see: NA, RG 59, DF 1960-63, 811.10/12-1460, Herter to Eisenhower, 14.12.1960; *ibid*, 12-2360, White to Merchant, 23.12.1960.

<sup>73</sup> For the discussion and the proposal see: FRUS 58-60, VII/1, p.611-82; a recent analysis of the MLF story is Haftendorf, *Kernwaffen und die Glaubwürdigkeit der Allianz: Die NATO Krise 1966/67*, 1994, p.107-48, with references to the extensive literature on the subject.

functioned well during a period of unprecedented American commitments abroad.<sup>74</sup> It had allowed this expansive policy without disrupting the domestic economy and thus leading to an erosion of domestic support for American foreign policies. It also had been of considerable advantage to America's principal allies. Thus, the monetary system had fostered (or not impeded) economic growth at home and had made the financing of the Cold War possible.

This advantageous situation slowly but inexorably changed. The strains American commitments abroad put on the monetary system became increasingly evident. The principal ways out were to reform either the security system to relieve the strain on the monetary system (and this would have amounted to a fundamental change in Cold War policies) or the other way round. If both these ways were not taken, a third possibility was to find temporary expedients in the hope that the situation would change back to an equilibrium. This is what happened. The next chapter will deal with the coming about of one of the most important of these expedients.

Trade  
agreement

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<sup>74</sup> These US commitments abroad included not only direct military commitments, military interventions, foreign aid, military aid, and other material help, but also the enormous expansion of American 'cultural' activities abroad.



CHAPTER VIII  
 OFFSET AND MONETARY POLICY  
 DURING KENNEDY'S PRESIDENCY, 1961-1962

a) The International Monetary Policy of the Kennedy Administration

Since the first accounts of Kennedy's presidency were published it has become a commonplace that the President took a keen interest in monetary matters and that he considered the dollar-gold problem one of his most serious challenges, up to the point of comparing it with the nuclear threat.<sup>1</sup> Contrary to the far-flung initial expectations of the Kennedy team, balance of payments matters became an ongoing preoccupation which turned up with irritating regularity on the agenda. Research has interpreted these monetary problems as an expression of the decline of American hegemony and Kennedy's policy as a fight against this decline.<sup>2</sup> Unfortunately, those sweeping interpretations lack serious empirical underpinning. A thorough historical account of how Kennedy managed his international monetary policy, how it evolved and changed over time, where exactly the points of debate lay, and what strategy towards the surplus countries was pursued, is still wanted. Such an endeavour is, of course, far beyond the scope of this research. I will try to sum up and supplement previous research, caution against oversimplifying arguments, and outline briefly the rationales behind US monetary policy towards Europe, and in particular towards Germany.

This will lead to the question of how American security policy towards Europe became increasingly linked to the monetary problem. One significant result of this problem was the first offset agreement. The genesis of this crucial agreement for German American relations in the 1960s will be outlined -for the first time- in detail. An analysis of the motives of the participants and of the significance of the agreement concludes the chapter.

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<sup>1</sup> Schlesinger, *A 1000 Days*, 1964, p.654; Sorensen, *Kennedy*, 1965, p.405; Rostow, *The Diffusion of Power*, 1972, p.136; Roosa, *The Dollar and World Liquidity*, 1967, p.3.

<sup>2</sup> See, for example, Borden, 'Defending Hegemony: American Foreign Economic Policy', in: Paterson, *Kennedy's Quest for Victory*, 1989, p.57-85; Calleo, *The Imperious Economy*, 1985; Matusow, 'Kennedy, the World Economy, and the Decline of America', in: Snyder(ed), *JFK. Person, Policy, Presidency*, 1988, p.111-22.

It emerged clearly from Kennedy's first balance of payments message to Congress, shortly after his inauguration, that he intended no radical departures from existing policies towards solving the dollar problem. After the appointment of Douglas Dillon as Secretary of Treasury this came as no surprise. The central passage of Kennedy's talk went as follows: *'The United States official dollar price of gold can and will be maintained at \$35 an ounce. Exchange controls over trade and investments will not be invoked. Our national security and economic assistance programs will be carried forward.'*<sup>3</sup> The President declared himself also against any far-reaching reform of the international monetary system. The Kennedy administration saw the balance of payments deficit as a manageable problem and was confident of solving it within a relatively short period. Policies required would include a more sophisticated use of available monetary instruments, further removal of trade barriers, and strong efforts at home to improve the competitiveness of American goods.<sup>4</sup>

Proposals from within the administration for more radical solutions, like a change in the gold price, capital controls, or restrictions on tourism, never prevailed.<sup>5</sup> The Treasury Department clung to its leadership on monetary issues. The two main elements of its policy were a more vigorous domestic economic policy than Eisenhower's had been, and increased participation by other industrialized powers in the management of the international monetary system. This second element was based on the optimistic assumption that these countries, mostly affluent members of the Atlantic Alliance, were actually willing to cooperate on the required large scale.

*Europe had to help*  
 The idea that the European countries had an obligation to help the United States was rooted in the thinking of the Kennedy administration as deeply as it had been in Eisenhower's. It

<sup>3</sup> The Balance of Payments and Gold Outflow from the US: Message of President Kennedy to the Congress, 6.2.1961; in: DAFR 1961, p.30.

<sup>4</sup> This approach had been suggested by a special Task Force on the balance of payments, which produced a comprehensive report on the problem for Kennedy in December 1960; see: JFKL, PPP, Transition Files: Task Force Reports, Box 1073. One of the ongoing conflicts within the administration was, whether economic policy was to be pursued with little regard to balance of payments objectives, as the CEA demanded, or whether economic policy, in particular short-term rates, were to be dominated by monetary considerations, as the Treasury maintained. On these debates, see the forthcoming Ph.D. by F.J.Gavin, University of Pennsylvania.

<sup>5</sup> Dillon and Roosa warned that plans for radical changes would create additional large-scale speculation as long as the position of the dollar was not safe. This argument was accepted by Kennedy; see: Roosa, 1967, p.6-13; Odell, *US International Monetary Relations*, 1982, p.106-108.

stemmed from Kennedy's and his advisers' conviction that the surplus countries bore an at least equal part of the responsibility for the crisis of the monetary system and that it had been generous American policies which had enabled the Europeans to acquire their huge currency reserves. The interpretation that the US problems were a result of inadequate policies by the Europeans was widespread in the new government. The pre-presidential Task Force on 'Foreign Economic Policy' stated in its report's section on the balance of payments deficit that it *'resulted principally from the failure of other major industrialized powers to pursue adequate policies of growth'*.<sup>6</sup> The reproach of building up its economy with American help and then shirking its obligation to help the US in its monetary policy, was mainly directed at Germany. *'To some significant degree...Germany's ability to maintain its export volume can be attributed to liberal U.S. policies on trade, aid, and investment'*, Ball wrote in early 1961, and Secretary of State Rusk echoed him: the *'Germans have an obligation to make a contribution to the solution of this problem without need for any compensatory action on our part'*.<sup>7</sup> *Ball's 1st paper (Germany's need to help)*

From many of his remarks, it appears that Kennedy himself fully shared this opinion.<sup>8</sup> When de Gaulle vetoed the British accession to the Common Market in January 1963, an event which blatantly exposed the weaknesses of US foreign policy towards Europe, this factor became a dominant theme in the ensuing discussions. Kennedy voiced his frustration in a series of remarks which were typical for the German-American burden-sharing debate in the 1960s. *'We have been very generous to Europe and it is now time to look out for ourselves, knowing full well that the Europeans will not do anything for us simply because we have in the past helped them. No longer dependent on the U.S. for economic assistance, the European states are less subject to our influence. If the French and other European powers acquire a nuclear capability they would be in a position to be entirely independent and we might be on the outside looking in. We must exploit our military and political position to ensure that our*

<sup>6</sup> Report, 31.12.1960, JFKL, PPP, Transition Files, Box 1073; for a similar statement: NSA, The Berlin Crises Collection, Doc.2054, Gregh-Nitze discussion on NATO strategy, 25.5.61.

<sup>7</sup> JFKL, POF, Countries: Germany, Box 116a, Ball to JFK, n.d.(February 61?); NA, RG 59, DF 1960-63, 811.10, Box 2287, Rusk to Dillon, 1.2.1961. For a similar statement see: JFKL, POF, Departments & Agencies:CEA, Box 73, Heller to JFK: The Future of the Dollar, 15.9.1961.

<sup>8</sup> See for example his discussion with the French Minister for Cultural Affairs, Malraux, on 11 May 1962, in: FRUS 1961-63, XIII, 695-701.

*economic interests are protected.*<sup>9</sup> Similar statements multiplied during the 1960s in media comments, in Congress, and, last but not least, in the U.S. government. At the highest levels, monetary and security problems were seen as inseparably linked.

In this matter, the governments of the United States and the United Kingdom saw eye to eye. In his first meeting with Kennedy, Macmillan put the blame for the American and British payments problems on the Europeans (in particular the Germans) who had failed to reinvest the foreign exchange they had acquired via Anglo-American aid and military expenditure in Europe after the war.<sup>10</sup> Both heads of government strongly emphasized the need for adequate compensation for their foreign exchange losses. Thus, a clear split emerged in monetary policy between the European surplus countries and the deficit countries, Britain and the USA. This split was to some extent paralleled by divergences in security matters (nuclear and non-nuclear members of the Alliance) and in trade policy (EEC and non-EEC countries). Though these lines of conflict were, of course, often blurred when it came down to specific issues and Germany found itself frequently caught in the middle, it very much dominated relations in the Western Alliance during the 1960s, and the different issues linked up with and reinforced each other.

The American activism in international monetary policy centred on two fields:

- 1) the intensification of monetary cooperation between the major monetary powers by a series of multilateral agreements, vigorously pursued by Dillon and his Undersecretary Roosa (they will be dealt with only parenthetically in this thesis).
- 2) the reduction and sharing of the defense and foreign aid burden, with an offset of military expenditure in Europe as the most important component, strongly pushed by Secretary of Defense McNamara. Though these policies were pursued by different ministries and in a different institutional setting, they have to be seen as a whole.

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<sup>9</sup> FRUS XIII, 1961-63, Remarks of President Kennedy to the NSC Meeting, 22.1.1963, p.486.

<sup>10</sup> NSA, The Berlin Crisis Collection, Doc.2024: CAB 133/244: Record of a Meeting Macmillan-Kennedy, 5.4.61.

b) Military Strategy and the Balance of Payments

Kennedy made it from the outset clear to all concerned that he assigned to military burden-sharing a very high importance.<sup>11</sup> This derived not only from his determination to defend the dollar and his conviction that America's allies had to carry a larger share of the defence burden. Changes in military strategic thinking also led to a more assertive burden-sharing policy. The new administration had started immediately with a revision of American military-strategic policy which led to a stronger emphasis on conventional forces. The strong inclination by the preceding administration to reappraise the military commitment in Europe because of balance of payments reasons was not shared by the Kennedy administration, at least not during its first year. Eisenhower's directive to curtail drastically the number of the dependents of the American overseas forces was renounced due to heavy criticism by the military and the supposedly strong impact on the morale of the GI's.<sup>12</sup>

Simultaneously, the Americans sought to educate the Europeans on their new strategic ideas. These, subsumed under the heading of 'Flexible Response', expanded on ideas formulated during the closing stage of Eisenhower's presidency, notably by people like Robert Bowie and Maxwell Taylor.<sup>13</sup> Appalled by what they saw as an irresponsible reliance on the immediate use of nuclear weapons in case of an even limited conflict and based on a more balanced estimate of Warsaw Pact Forces, strategic planners in the Kennedy administration tried to switch the emphasis of military strategy away from nuclear weapons towards a better conventional capability in order to have an increased range of options. The situation in Berlin underlined this need. A corresponding commitment by the Europeans to conventional troops in order to make 'Flexible Response' credible became a top priority of US security policy towards Europe.<sup>14</sup> A study group, headed by Dean Acheson, summarized these ideas in a policy paper, and the so-called Acheson report became a policy guideline approved by

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<sup>11</sup> JFKL, NSF, Meetings & Memoranda, Box 328, NSAM 22, JFK to Rusk, 20.2.61.

<sup>12</sup> JFKL, NSF, Clifton-Kaysen Memos: Memo of Meeting JCS with the President, 27.1.61; JFKL, POF, Departments and Agencies: Defense, Box 77, McNamara to JFK, 1.2.1961; JFKL, OH Interview Gilpatric, p.80.

<sup>13</sup> For the Bowie Report see: FRUS 1958-60, VII,1, doc.266; Taylor, *The Uncertain Trumpet*, 1960. For the development of Flexible Response see: Stromseth, *The Origins of Flexible Response*, 1988.

<sup>14</sup> DDRS 1995/1414, Briefing Book for Adenauer Visit: Position Paper NATO, April 1961.

Kennedy.<sup>15</sup> In April, Acheson went to Europe and told Adenauer (and de Gaulle) that *'the new administration wished to correct some harmful impressions created toward the end of the old one ... American troops were not to be withdrawn from Europe, nor would there be any threat to do so'*.<sup>16</sup>

However, as Acheson recalled later, he *'was never quite sure how completely [Kennedy's] mind was sold on this-----the thing that continually seemed to bother the President about this was the continuation of so large a body of American troops in Europe without any plan that they should come home at a specific date ... Surely we do hope to bring them home, but the point was to bring the Europeans in such a state of confidence and growing capabilities that this time would come. It would never come if you keep saying, "if you don't do exactly what we want, we'll go home". This was the wrong way to act. I don't think he was ever quite with me on this.'*<sup>17</sup> Kennedy's ambiguity is not surprising, given that 'Flexible Response' with the inherent continuation or even augmentation of American troop presence in Europe conflicted with balance of payments objectives. What made sense in military-political terms, did not at all coincide with perceived economic necessities, contrary to the situation in the 1950s. One way to square the circle was to get the Europeans to assume more of the burden of conventional defense. Another possibility was to negotiate a financial compensation for the American foreign exchange losses wherever possible. To achieve this, however, the threat of American disengagement would be the obvious means of pressure. Such threats, on the other side, undermined the credibility of US military policy. There are few doubts that Kennedy acutely felt this dilemma.

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<sup>15</sup> FRUS 1961-63, XIII, p.285-91.

<sup>16</sup> FRUS 1961-63, XIII, Telegram Embassy Bonn to DOS: Adenauer-Acheson conversation, 10.4.61, p.270; *ibid.*, Conversation Gavin-de Gaulle, 20.4.61, p.244. This reassurance was repeated by Kennedy during Adenauer's first meeting with the new President, *ibid.*, p.273.

<sup>17</sup> JFKL, OHI Acheson, p.12-13.

c) Towards the First Offset Agreement

The Kennedy administration wasted no time to preserve the momentum of the financial talks which had been initiated by Anderson and Dillon. Even before inauguration, Dillon sent Secretary of State-Designate Rusk a memorandum urging immediate action by the new government.<sup>18</sup> The offset of American foreign exchange losses in Germany became the first of many German-American disagreements during Kennedy's tenure. The German government, in order to get a good start with the new administration, had decided to table new proposals without delay. However, counting upon a more relaxed attitude of the new team, the Germans made almost no changes as compared to the offer they had already presented to Anderson and Dillon. The main points -the foreign aid program, the debt prepayment (linked to the vested assets question), NATO infrastructure costs, advance payments on military orders, etc.-remained the same. The Germans also pointed out that the program was devised for one year to ease a *temporary* strain in the US balance of payments.<sup>19</sup>

The American reaction was indignation at the impertinence of trying to sell the same offer twice. Kennedy, in a press conference, said that the proposals did 'not meet the problem or the opportunity.'<sup>20</sup> The first high-level visit from Germany, Foreign Minister von Brentano, scheduled to take place in mid-February, provided him with the chance to communicate directly his disappointment.<sup>21</sup> The Americans wanted to use the opportunity to impress upon the Germans *their* understanding of the balance of payments problem. The approach was based on the assumption '*that a general condition of economic imbalance exists in the Western world which can only be rectified by continuing and concerted measures which members of the Alliance should take....and which calls for sustained action by the Germans*

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<sup>18</sup> FRUS 1961-63, IX, Dillon to Rusk, 13 January 1961, p.105.

<sup>19</sup> NA, RG59, DF 1960-63, 811.10, 2-2/61, Bonn 1174 + 1175 to Secstate, 2.2.1961; see also: BPI, 10.2.1961, p.258.

<sup>20</sup> KPPC, 8.2.61, p.29; for a similar critique by the embassy see: NA, RG 59, DF 1960-3, 811.10/2-361, Bonn 1186, 3.2.61.

<sup>21</sup> '*As the Chancellor is interested in power it would seem to me that I should give Mr.Bretano [sic] a sense of our disappointment with their progress*'; NA, RG 59, DF 1960-63, 033.619-62A11, Box 77, Kennedy to Rusk, 8.2.61.

*as the major surplus country of the West.*<sup>22</sup> Obviously, the United States aimed at a long-term commitment of Germany towards relieving the American balance of payments. This expectation derived from America's long-term commitment to Europe's security. Presumably, the Germans would resist such an approach which would have deprived them of much of their autonomy in monetary policy making. A fundamental conflict emerged between the American interest to enlist German monetary powers for the defence of the dollar and the German attempt to retain as much freedom of manoeuvre as possible. The outcome of the offset negotiations would reflect a first answer to this conflict.

The von Brentano visit brought no solution to these large questions. The US government handed the visitor an aide-memoire which set out its basic position on the balance of payments problem. It stated that the deficit existed mainly because of the American commitment to the defense of the Free World, and that this burden as well as the foreign aid burden had to be shared equally among the members of the Alliance. The proposed German measures were deemed inadequate because they did not meet the condition of a sustained program.<sup>23</sup> The aide memoire suggested a multilateral solution to the burden-sharing problem. W.Rostow maintained that after the von Brentano visit *'Kennedy considered and tentatively supported a multilateral approach in the Alliance to the offset problem.'*<sup>24</sup> He added that concerted pressure by the Department of Defense and the Department of Treasury had killed that proposal. It would have taken in any case a long and protracted negotiating process to get all of NATO into a comprehensive burden sharing system. The Kennedy administration, looking for fast solutions, was hardly prepared for such a major diplomatic effort. The idea was appear again from time to time; however, it never came close to implementation.

On some of the lesser German proposals, agreement was achieved very soon after the von Brentano visit. The German share of the NATO infrastructure cost was augmented to 20%.

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<sup>22</sup> JFKL, POF, Countries: Germany General, Box 117, Rusk memo for the President, 15 February 1961; PA-AA, Büro STS, 79, Record of Dillon - von Scherpenberg talk, 17 February 1961.

<sup>23</sup> BPI, 23.2.61, p.322.

<sup>24</sup> Rostow, *The Diffusion of Power*, 1972, p.236, 395.



Table 9: Distribution of NATO Infrastructure Cost 1956-64 (in %)

	1956-60	1961-64
USA	36.98	30.85
Germany	13.72	20.00
United Kingdom	9.88	10.15
France	11.87	12.00

Source: BPI, 17.2.1961, p.294. The total cost of NATO infrastructure programs was \$676m a year (1957-60), resp. \$733m (1961-64).

The foreign aid problem was separated from the offset discussions and referred to the OECD. The major reason for this was that the Americans wanted to avoid that uncertain foreign aid efforts would be played off against other burden sharing issues, causing lower results in both areas.<sup>25</sup> The Anderson-Dillon mission had signalled the beginning of a regular German foreign aid program. That did not prevent the issue from becoming time and again a controversial topic in German-American discussions during the 1960's. The issue of trade liberalization was allayed by some smaller measures of Germany and for the time being lost its relevance in the context of offset. However, it was clear that the US government regarded all these matters as relatively unimportant. The real issues were extended monetary cooperation and full offset of the US troops' foreign exchange cost. It is not intended here to reconstruct the history of German-American monetary cooperation during the 1960s in detail as it evolved in a multilateral (OECD, IMF, BIS) and bilateral context, involving governments, central banks, and other players in the monetary field. This monetary collaboration expanded greatly during the Kennedy years and it will blend into our story at various moments. I will concentrate on probably the most important component of this cooperation: military offset.

The main part of the talks during 1961 was held on a lower official level than during the Anderson-Dillon mission. Officials of the Federal Defense Ministry (BMVg), the Federal Finance Ministry (BMF), the US Treasury and Defense Departments, and the US embassy in Bonn had met almost immediately after the mission to work out alternatives to a direct contribution. The large agenda was split up into several issues which were assigned to three

<sup>25</sup> NA, RG 84, Post Files: Embassy Bonn 1959-61, Box 17, 320: US Policy, DOS Circular Telegram, 18.3.1961.

working groups. The first group included the representatives of the BMF and dealt with the debt prepayment question. Contrary to the Eisenhower administration, the new government categorically declined to link the issue with German assets seized by the US government during the war, fearing that such a deal might require a long and uncertain ratification debate in Congress.<sup>26</sup> The Germans were bluntly told that the new administration would take no action whatsoever on the problem. This was a painful defeat for the German government which had hoped to score a great popular success on an issue which was highly sensitive in Germany. Endless bilateral discussions had been going on during the 1950s.<sup>27</sup> Finally, after the Dillon-Anderson mission the US seemed ready to compensate the former owners of the assets linking that with premature debt prepayment by the Federal Republic. The German government prepared already draft treaties.<sup>28</sup> Disappointment ran high when this chance was lost. At that point, the Germans probably began to suspect that they had fallen in the offset question from the frying-pan of Eisenhower into the fire of Kennedy. Despite the lost opportunity, Germany agreed, after some more discussions to prepay, as an offset measure, DM587m of its postwar debts, without conditions attached.<sup>29</sup>

In any case, this was a convenient way to transfer back the surplus dollars which had streamed to German accounts during speculative waves in 1960 and 1961. Short-term capital had continued to move into the country as again and again rumours of a DM revaluation made their way to the public. Doubtlessly, these rumours were intensified by the fierce struggle within the German government on the question. Adenauer and Erhard repeatedly clashed on the issue; industry, consumer organisations, and financial experts bombarded the government with recommendations for and against; even within the *Bundesbank's* highest levels opinions were divided.<sup>30</sup> Though there is no doubt that the United States was in favour of a revaluation, they apparently put no direct pressure on the German government and

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<sup>26</sup> BA, NL Etzel, vol.18, memo: prepayment of US postwar aid, 20 March 1961; NA, RG 59, DF 1960-63, 811.10, Box 2287, Ball to Rusk, 30 January 1961; Rusk to Dillon, 1 February 1961; RG 59, Lot Files, BEA, Office of German Affairs, Box 12, memcon Dillon/Ball-Scherpenberg, 19 February 1961.

<sup>27</sup> Kreikamp, *Deutsches Vermögen in den Vereinigten Staaten*, 1979.

<sup>28</sup> BA, B136/2125, Referat 6: note for Cabinet meeting, 10 January 1961.

<sup>29</sup> BPI, 13.4.61, p.657; see table 6, Appendix.

<sup>30</sup> The best account of this conflict is: Körfer, *Kampf ums Kanzleramt*, 1988, p.464-518.

stayed clear of the wasps' nest. When the British urged them to press the Germans towards revaluation, Dillon answered that the US accorded to this question a lower priority than to bilateral payments negotiations.<sup>31</sup> Only when finally, in March 1961, the DM was revalued from DM4.20/dollar to DM4.00/dollar, the US treasury committed a minor blunder by calling the revaluation a 'modest but useful step'. Nothing illustrates the nervousness of monetary markets during the 1960s better than the deluge of funds moving to Germany after this statement which seemed to hold the possibility of a further revaluation. The German ambassador protested personally to Kennedy.<sup>32</sup> The markets calmed down only in mid-1961, after combined intervention by all major central banks. It was the pound which, once more, came under pressure during these weeks and was saved only by one of the many multilateral monetary rescue actions of the 1960s.<sup>33</sup>

The offset negotiations had continued during the monetary turmoil. After the debt prepayment question was settled, they concentrated on weapons procurement and sharing of military facilities. The Ministries of Defense assumed the responsibility for the talks which increasingly promised to be the only way to come anywhere close to the great aims the Americans envisaged. Accordingly, when Adenauer was scheduled for his first state visit in April 1961, the American interest had switched towards a pure bilateral military offset scheme. In a forceful memorandum Dillon pressed upon the President the importance of pursuing the issue in his talks with the Chancellor. *'I hope you will talk with the Chancellor about the importance of prompt action by Germany to step up its military procurement in the United States for at least the present year. Less urgent; but also important, is our desire for a reduction in the cost of contractual services for our military establishment for which we now pay Germany...without active Federal Republic cooperation there is no way of bringing our expenditure in Germany down to a tolerable level short of troop withdrawal which we do not want to contemplate.'*<sup>34</sup> Dillon estimated the amount of prospective German orders

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<sup>31</sup> FRUS 1961-63, IX, US-UK bilateral talks, 15-16 December 1961, p.111-12.

<sup>32</sup> FRUS 1961-63, XIV, p.21-5.

<sup>33</sup> Strange (1976), p.82-89.

<sup>34</sup> JFKL, POF, Countries: France/Germany, Box 116a, Dillon to President: Discussion with Chancellor Adenauer on balance of payments, 7.4.61. For the actual talks see FRUS 1961-63, IX, 13.4.61, p.114-6.

at about \$430m/year which would bring down the foreign exchange cost of the troops (inflated to \$650m because of the DM-revaluation) to \$220m. Strauss had informed Dillon that only an increase to \$200m was reasonable, but State Secretary van Scherpenberg during the von Brentano visit had quoted a figure of \$400m a year for 1961; this had met opposition in the German government, notably from Erhard.<sup>35</sup>

Progress in the bilateral working groups on procurement and sharing of military facilities was slow. The first disagreement arose not on the level of orders but on the US insistence that the Federal Republic was to commit itself for an extended period to a certain level of purchases. This was unacceptable for the Germans. The proposed level of \$450m of arms orders in 1961 -in addition to \$125m already made - was dismissed in the same vein as completely 'unrealistic.'<sup>36</sup> The Americans suspected that this intransigence was due to French and British competition for German orders.<sup>37</sup> This was not a major reason, as we shall see later. Both sides tried, however, to keep the talks confidential. *'The FRG would be subjected to difficult pressure, not only from other governments, but from German domestic industry as well.'*<sup>38</sup> The sensitivity of the subject makes it even today difficult to get a consistent record of the talks, particularly from the German side. Many questions will remain open, probably until the archive of the Federal Defense Ministry at Freiburg finally opens its post-1955 holdings to the general public.

The main objective of the US during the talks was simple: to get a commitment to increased military procurement as extended and voluminous as possible. This was promoted at the highest levels, in particular the Secretaries of Treasury and Defense. The potential of the vague proposals for sharing military facilities and contractual services was unclear. It seems, however, that the US government soon realized that this issue could provide additional

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<sup>35</sup> *ibid.*

<sup>36</sup> NA, RG 59, DF 1960-63, 762a.5, Box 1903, memcon FRG officials-US embassy officials, 16.3.61.

<sup>37</sup> NA, RG 59, 762a.56, Bonn 1487, 18.3.61: 'British are applying extensive pressure to increase level of German procurement and Selwyn Lloyd will arrive next week to discuss matter with Strauss. Federal Republic also peculiarly dependent on France because of basic need for training areas and French tendency to relate procurement to rights for facilities creates fundamental political problem.'

<sup>38</sup> *ibid.*, 762a.5, Box 1903, memcon US embassy/MAAG-BMVg, 6.6.61.

leverage, and, in case of a satisfactory agreement, also political advantages. The Americans proposed, and the Germans agreed, to undertake long-range studies on a large number of questions, including, for example, sharing of logistic services, training facilities, reserve stocks, and developing standardized military equipment.<sup>39</sup> Detailed talks on these issues started in May 1961.

However, during the first seven months of 1961 the Germans dragged their feet on any longterm commitment towards military purchases. This might well have been an expression of Strauss' continuing insistence on buying the most modern material. In a long and animated discussion with Kissinger in mid-1961, Strauss complained about the outdated equipment of the US army: *'...he would be willing to approve a huge increase in German procurement of military items in the U.S. but was reluctant to do so when the Germans could produce better weapons here ... If the U.S. would modernize her weapons to match qualitatively the German weapons, then the German orders would soon erase the American balance of payments problem.'*<sup>40</sup> Apart from the slight exaggeration concerning the quality of weaponry made in Germany, there was a barely hidden quid pro quo. If the US was ready to sell the most recent developments of its weapons industry, inclination and money to buy American would increase immediately. Strauß still had lingering suspicions that Germany would be sold second-rate material, as it had happened sometimes in the 1950s. He also was conscious of German technological backwardness and hoped for some spill-over.<sup>41</sup> He and his officials clearly realized the leverage the offset issue provided to them in two issues: equality in the equipment of German forces and access to advanced military technology which at that time was considered the spearhead of technological progress.

Furthermore, Strauß expected a clarification of the future course of American military policy

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<sup>39</sup> NA, RG 84, Bonn Embassy 1959-61, Box 25, 322.3 Logistic Support, Morris to van Scherpenberg, 14.4.61; Van Scherpenberg to Morris, 18.4.1961.

<sup>40</sup> NA, RG 59, DF 1960-63, 762a.5, Bx 1903, 5/1961. Apparently, Kennedy got hold of the conversation and ordered an investigation of Strauss' allegation. The charged officials expressed surprise about Strauss' remarks as the German army was almost exclusively equipped with U.S. weapons. see: NSA, The Berlin Crisis, Doc.2121, memorandum, 3.7.1961.

<sup>41</sup> Kelleher, *Germany & the Politics of Nuclear Weapons*, 1975, p.90-91, 96-97.

before embarking upon a large procurement program.<sup>42</sup> The strategic reorientation of the Kennedy administration had met with strong resistance in the Federal Republic. The Germans feared that increasing reliance on limited conventional response would invite Soviet adventurism, lead to the loss of Germany in the event of war and make the country a nuclear battlefield.<sup>43</sup> By getting a larger voice in nuclear questions, and particularly by getting access to the 'hardware', Germany would acquire much more influence over the formulation of military policy in NATO. This would have brought the Federal Republic a big step closer towards pursuing a forward defence for its own territory, and thus reduced its dependence on other countries for this task. During the final stages of the Eisenhower administration, American intentions for nuclear sharing had gone very far, up to the point of considering the equipment of German forces with tactical nuclear weapons.<sup>44</sup> Kennedy, however, took a strong position against nuclear proliferation. Under those circumstances, acquiring nuclear delivery systems was the closest the Federal Republic could come towards more direct influence over the use of nuclear weapons on its territory. What Strauß' intentions amounted to was in the last consequence the use of the strong reserve position of the Federal Republic to enhance its military and political influence on vital defence questions. As we shall see, Strauß succeeded.

The available records of the Working Group meetings give further indications of German objectives.<sup>45</sup> First: the request that the US government act as purchasing agent in weapons procurement, because of lack of qualified German personnel for negotiating directly with US firms (a procedure similar to the one agreed in the MSMS agreement of October 1956; see ch.V). Second: the Germans emphasized the importance of a joint use of logistic facilities,

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<sup>42</sup> 'Basic decision increase level of procurement in US dependent on Strauss' acceptance of new strategic viewpoints and agreement on precise balance between nuclear and conventional forces; NA, RG 59, DF 1960-63, 033.62A11, 6-2461, Bonn 2170, 24.6.61.

<sup>43</sup> Schwartz, *NATO's Nuclear Dilemmas*, 1985, p.154-55; 167-170. On the strategic disagreements between West Germany and the US in the early 1960s see: Kelleher (1975); Mahneke, *Nukleare Mitwirkung. Die BRD in der atlantischen Allianz 1954-70*, 1972; Stromseth (1988); Steinhoff/Pommerin, *Strategiewechsel. Bundesrepublik und Nuklearstrategie in der Ära Adenauer-Kennedy*, 1992; Hoppe, *Zwischen Teilhabe und Mitsprache, Die Nuklearfrage in der Allianzpolitik Deutschlands 1959-66*, 1993; Haftendorn (1994).

<sup>44</sup> Trachtenberg, *History & Strategy*, 1991, p.180-91.

<sup>45</sup> NA, RG 84, Bonn Embassy 1959-61, Box 25, Bonn 1711: Studies on Procurement, Joint Use and Contractual Services, incl. memcon US-FRG officials (15 May), 24.5.61.

training areas, airfields, barracks, etc. In these areas the German defense ministry faced particular difficulties. The German rearmament effort had been hampered from the beginning by various shortages due to the densely populated country and the occupation of the most convenient training-, stationing-, and storage locations by allied forces (see ch.II). When the build-up accelerated in the early 1960s these problems became even more pressing. The unfortunate 1961 attempt by the German government to negotiate with Franco training areas in Spain derived from these problems. Bonn's NATO allies were not very cooperative in this respect. According to Strauß *'arrangements for depots in France was [sic] completely dependent on German procurement in France.'*<sup>46</sup> Third: The Germans insisted during the talks that the negotiations should be kept out of the public and that an eventual agreement should be concluded in a form not requiring Bundestag approval.<sup>47</sup> A public debate on the issue had to be avoided at every price.

In July, the amount of proposed German orders was still far from forming a full offset.<sup>48</sup> The US military stalled at the idea of having to share its facilities in Europe with another army. The gap between American and German expectations was large until an event happened which should play the decisive accelerator function for the offset talks: the erection of the Berlin wall in August 1961.<sup>49</sup>

The consequences were manifold. The Americans augmented their forces in Europe despite misgivings about the gold drain such an action implied. The administration soon backed away from the initial idea to send up to six divisions.<sup>50</sup> After long discussions, however, it was decided to augment the American forces in Germany by 45.000 men, with the option for

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<sup>46</sup> NA, RG 84, Bonn Embassy 1959-61, Box 26, memcon Gilpatric-Hopf/Strauß, 24.10.1961.

<sup>47</sup> NA, RG 84, Bonn 1959-1961, Box 25, 322.3 Logistic Support, Bonn 1711, 24 May 1961.

<sup>48</sup> For the following paragraph see: NA, RG 59, DF 1960-63, 811.10/7-1561, memcon Dillon-Strauss, 15.7.61; RG 84, Bonn Embassy 1959-61, Box 26, Bonn 211, 29.7.1961.

<sup>49</sup> For a concise analysis of the Berlin Crisis see: Trachtenberg, *History and Strategy*, 1991, p.169-234.

<sup>50</sup> For the discussions see: JFKL, POF, Countries: Germany general, Box 117, Memo of Meeting on Berlin, 17.7.61; *ibid.*, McNamara to JFK: Status of Berlin Build-up, 7.9.1961; LBJL, VPSF, Box 4, notes on NSC meeting, 19.7.61.

further reinforcements if the situation required that.<sup>51</sup> The additional gold drain was expected to be offset by the German government. Because of tactical reasons, the US embassy in Bonn advised that the exploration of this subject should start only after the ongoing offset talks were concluded.<sup>52</sup>

The wall also stirred up a feeling of vulnerability on the part of the West Germans and demonstrated how much the Federal Republic depended on the Western Alliance for its security. The Western response, deemed as lukewarm by a large part of the German population, sparked renewed doubts about the Western security guarantee. In this situation, funds suddenly flowed abundantly for the further build-up and modernization of the Bundeswehr. The German defence budget was increased by about DM 3bn to DM16.6bn (\$4.15bn).<sup>53</sup>

The US leverage in the offset talks increased considerably. The Americans decided to meet some of the German requests to capitalize on the situation. *'We are approaching the strongest bargaining position since the negotiations began. Our negotiating leverage is increased by the possibility of major deployments to assist in the defense of Berlin and Germany, and also by the fact that the Department of Defense is prepared to provide the German forces with a cooperative logistics system for which the Federal Republic has been pressing.'*<sup>54</sup> This system included, for example, the provision of US government procurement services, sharing in selected areas of common items and US war reserves, on-call support for German forces (tying in the Bundeswehr as a customer to the US logistical system for providing spare parts), and maintenance services.<sup>55</sup> Equally important was that the Americans indicated they were willing to continue selling their most advanced weapon systems. They stepped up the pace

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<sup>51</sup> US troop strength rose from 233,000 to 277,600. For details of this build-up see: NSA, *The Berlin Crisis*, Doc.1942, US Army Europe Headquarters, *The Replacement and Augmentation Systems in Europe, 1945-63*, ch.6, March 1964.

<sup>52</sup> NA, RG 59, DF 1960-63, 811.10/9-1261, Ball to Dowling, 12.9.61; *ibid.*, 9-2261, Bonn 700, 22.9.61.

<sup>53</sup> Table 1, appendix.

<sup>54</sup> JFKL, POF, D&A: Treasury, Box 89, Dillon to JFK, 14 September 1961

<sup>55</sup> NA, RG 59, DF 1960-63, 811.10/9-2161, Bonn 694, 21.9.1961; *ibid.*, Tyler to Ball: US/FRG military offset negotiations, 9.10.61; RG 84, Bonn Embassy 1959-61, Box 26, Bonn A-403 to DOS, 30.9.1961.



in the negotiations.<sup>56</sup>

At an October meeting of the Procurement Working Group, the Germans informed a delighted US delegation that the level of procurement would rise substantially above previous estimates.<sup>57</sup> The circumstances seemed to be propitious for a comprehensive understanding. The negotiations moved to a higher level. Kennedy informed Adenauer that he would send Undersecretary of Defense, Gilpatric, for talks with the Federal Defense Ministry. He expected the Germans to *'work out with us arrangements to insure that U.S. military expenditures in Germany do not drain foreign exchange reserves from the U.S. to Germany.'*<sup>58</sup> The Gilpatric trip was given very low key public treatment to avoid drawing attention to the wide-ranging issues discussed. The Undersecretary of Defense brought along with him an outline of the logistics assistance actions which the Department of Defense was prepared to offer to the Germans.<sup>59</sup> He also assured Strauß that the US would continue to furnish the Bundeswehr with modern missile systems.<sup>60</sup> The condition the US set for these offers was straightforward: a formal commitment by the Federal Republic to offset the entire foreign exchange cost of US troops in Germany.

Strauß certainly understood that the consequence was a far-reaching commitment to the United States in the military-economic field at the expense of other allies. He remarked to Gilpatric *'that if he signed the agreement as presently drafted the British ambassador would be in his office the following morning to demand equal treatment.'*<sup>61</sup> This, however, did not prevent an eventual signature. The German defence minister, however, insisted upon limiting the agreement to two years and he demanded renewed, preferably multilateral, negotiations

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<sup>56</sup> For example, the soon to be ousted von Brentano was -once more- confronted with the problem, this time by Rusk: NA, RG 59, DF 1960-63, 811.10/8-14.61, memcon, 14.9.61; see also: *ibid.*, 862a.10/9-1461, Martin to Ball: Treasury, Defense and State Meeting on US/German Financial Negotiations, 14.9.61.

<sup>57</sup> NA, RG 59, DF 1960-63, 762a.5/10-1261, MAAG Germany to Secstate, 13.10.61; *ibid.*, 862a.10, 12-2261, discussion Embassy-BMVg officials, 18.12.61.

<sup>58</sup> JFKL, POF: Countries: Germany general, Box 117, Kennedy to Adenauer, 16.10.1961.

<sup>59</sup> NA, RG 84, Box 26, Bonn to DOS: Summary Statement by Gilpatric, 2.11.1961.

<sup>60</sup> FAZ, 27 October 1961; FR, 29 October 1961.

<sup>61</sup> *ibid.*, memcon Gilpatric-Hopf/Strauß, 24.10.1961.

in case of a substantial augmentation of US forces due to the completely unclear Berlin situation. After some discussion, Gilpatric accepted these conditions and a brief memorandum of understanding was signed on 24 October 1961. The following paragraph established the working principle of offset: *'It is anticipated that under the proposed cooperative logistics system, payments by the Federal Republic of Germany to the United States for materiel and for research, development, procurement supply, maintenance and other logistics services, including the Federal Republic of Germany's share of the system's capital and operating expenses, will be sufficient to insure that military transactions of direct benefit to the U.S. balance of payments are large enough to offset the transactions of U.S. forces in Germany of benefit to the FRG balance of payments, on the basis of such forces presently stationed in Germany or heretofore announced for movement to Germany. In the event of further deployment of U.S. forces to Germany, the two governments will consider methods whereby the balance of payments effect of such movements can be adjusted to their mutual benefit.'*<sup>62</sup>

The memorandum would be in effect for a period of two years during which the accumulated foreign exchange cost of US troops in Germany was estimated at about \$1450m. This signified that procurement in the US was to make up roughly one-sixth of the German defence budget. Strauß supplemented the memorandum with a letter of comments. In this letter he set forth: 1. that a firm commitment beyond US FY 1962 was not possible, 2. the mentioned condition in case of an increase in US manpower, 3. the impossibility of concluding a similar agreement with any other country, 4. the necessity to maintain existing military-economic relations with other NATO countries, 5. a demand for US political support if the agreement was to create problems with other NATO allies.<sup>63</sup> As it turned out soon, Strauß' apprehensions were well-founded.

The immediate problem was, however, how to place the broad understanding into a more precise framework. This led in the following weeks to hectic discussions on financial,

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<sup>62</sup> For a full version of the memorandum, see: NA, RG 84, Bonn Embassy 1959-61, Box 25, Bonn to DOS, Treasury, Defense and White House, 24.10.1961. The German version is in an attachment of a letter by Kennedy to Adenauer: JFKL, Correspondence Adenauer-Kennedy, Kennedy to Adenauer, 25.11.62, with note on German obligations and payments to the US pursuant to the military offset agreement. See also, FRUS 1961-63, IX, p.132-3.

<sup>63</sup> *ibid.*, Strauss to Gilpatric, 30.10.1961.

organisational and procedural details, as well as on the elements of the cooperative logistics system. Talks commenced on a large number of items which the FRG would eventually buy.<sup>64</sup> The financial framework posed a particular problem. The Federal Ministry of Finance objected to its implementation at the last minute. The ministry had been almost completely excluded from the talks. Its intervention, however, came too late to change the outcome. An agreement was concluded based on the example of the MSMS agreement of October 1956. The period for order and payments targets were split. Orders to the tune of \$1450m were to be made in US CY 1961 and 1962, the equivalent payments were to be placed in FY 1961/62 and 1962/63 (ending June 1963). A formal exchange of letters between Strauß and Gilpatric recorded the details.<sup>65</sup> The payments level was made contingent upon the working of the logistics agreement. Once more, the Germans requested that the letter exchange be held in strictest confidence in order to avoid difficulties with the UK.

Nevertheless, the ticklish problem of informing the British and the French became now urgent. The Federal Republic was particularly afraid that the UK, pursuing then its own offset talks with the BMF, without much success, would react furiously and demand equal treatment. Another delicate question was the need to inform the French. First, the political scope of the agreement was certain to displease the French government; second, the provisions of the logistics arrangements on war reserves and on-call support entailed the presence of German materiel in France, because the bulk of US war stocks in Europe was deposited there. This, and the possible presence of the German military for control and inspection purposes, was very likely to incense the French, who were known to display little humour on issues regarding their sovereignty.<sup>66</sup> Already in August 1961, the US embassy in Paris had warned of difficulties because an US-German logistics agreement might undermine a French-German agreement, thus robbing the French of an important lever in their dealings with the Federal Republic. The embassy also expressed doubts about whether the Franco-American agreements regarding the use of French facilities by US forces and the lines of communication through

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<sup>64</sup> NA, RG 59, DF 1960-63, 762a.5/12-1661, MAAG to OSD(Washington), 16.11.1961.

<sup>65</sup> NA, RG 59, DF 1960-63, 762.0221/1-3162, Bonn 1774 (Section I+II), 31 January 1962; *ibid*, Bonn 1789, 1 February 1962; Bonn 1796, 2 February 1962.

<sup>66</sup> *ibid*, 762.0221/1-962, Ball to Tyler, 9 January 1962.

France allowed the sharing of these facilities with other countries.<sup>67</sup> The State Department cautioned against entering the agreements without informing the French, even if this entailed the risk that the French would veto an important part of the agreements. *'The core of the problem is that the US Line of Communication in France will under the proposed agreements be used to supply and store materiel for FRG forces.'*<sup>68</sup> Finally, rather vague information was conveyed, painfully avoiding the mention of the crucial payments arrangements.<sup>69</sup> It took the French some time to figure out the scope of the deal.

#### d) Military, Political and Monetary Aspects of the Agreement

The foregoing has been the first detailed account of the genesis of the offset agreement. However, to really evaluate its significance, it is necessary to place it in the military, political and monetary context of overall German-American relations. In the following paragraphs these consequences are, for the sake of clarity, discussed separately, but it is self-evident that all these factors were inextricably intertwined.

The *military* importance of the agreement lay primarily in linking the American and German military efforts in Europe on many levels to a hitherto unknown extent. The immense amount of procurement made the Bundeswehr for a long time a mostly American equipped army. The Federal Republic gained access to some of the most modern weapon systems which existed, and to instructions on how to use them.<sup>70</sup> The Americans guaranteed the delivery of this high-tech procurement which the FRG was not able and/or not allowed to produce. This was an important step towards the modern posture for German forces Strauß fought for so fervently. That the agreement gave the Germans the possibility to buy weapons capable of

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<sup>67</sup> NA, RG 84, Bonn Embassy 1959-61, Box 26, Paris 69, 5 August 1961.

<sup>68</sup> NA, RG 59, DF 1960-63, 762.0221/1-962, Tyler to Ball, 9 January 1962.

<sup>69</sup> NA, RG 59, DF 1960-63, 762a.5/2-1062, DOS to Paris/Bonn, 13 February 1962.

<sup>70</sup> Some items already agreed upon included for example tanks (\$104m), 2 PERSHING battalions (\$126m), a NIKE and a SERGEANT missile system (\$69m), etc. For a lump sum payment of \$75m Germany acquired the remaining items on loan from the NASH list. See also: NHP, Talking Points for Visit of Minister to the US, 13.11.61.

delivering nuclear warheads might have been even an unwritten condition for Strauß' consent.<sup>71</sup>

Cooperation between the American and the German forces was intensified probably even more by the logistics arrangement. A joint State/Defense/Treasury memorandum to Erhard in July 1963 listed the following areas: '*Co-Production of common military equipment by German and US sources, re supply and maintenance support for FRG forces through US military logistics systems, training of FRG troops in US military schools, joint usage of military facilities, and joint research and development projects*'<sup>72</sup>. The Federal Republic thus gained storage space in the *Hinterland* and badly needed training areas, for example the huge Grafenwöhr area, a place well known by every German recruit for its more than average amount of dust and mud, and still jointly used by US and German forces. Eventually, German military personnel would go in large numbers to the United States for training purposes. Certainly, US-German cooperation along these lines had existed before. But there are few doubts that these arrangements, which saw a vast extension over the next years, 'americanized' the German forces, coming close to outright dependence. This danger was realized by the Germans but, at that time, accepted due to the benefits.<sup>73</sup> Anyway, a large part of the procurement budget of the Bundeswehr in the next years was to be reserved for purchases in the US, to the detriment of other weapon producing countries and probably even the German industry.<sup>74</sup>

This leads directly to the political aspects of the agreement. With regard to the massive amount of procurement and the close cooperation of the West German and American forces, European armaments cooperation was pushed far into the future. The Strauß-Gilpatric understanding was a clear option for the US, even if that was not so obvious at the time. The much-debated military provisions of the Franco-German Treaty of 1963 were insignificant compared to the effects of the offset agreement. It fostered a closer alignment of West

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<sup>71</sup> Kelleher (1985), p.162.

<sup>72</sup> NA, RG 59, SF 1963, FN 12, Box 3451, DOS 147, 17 July 1963.

<sup>73</sup> NHP, Talking Papers for Meeting with Gilpatric, 6 February 1963.

<sup>74</sup> PA-AA, Ref.IIA7, 835, Memo II7: German-French Military Cooperation, 8 January 1965.

Germany on the United States in the monetary and security spheres at a time when serious doubts arose whether Germany would not gang up with de Gaulle. In this sense it was a direct continuation of American policy towards Germany after the war which had aimed at incorporating Germany economically as well as militarily into the Western Alliance as tightly as possible. The continuation of the offset agreement became for these reasons a top priority of American foreign policy (see ch.IX). There were few American-German high level meetings in the 1960s during which the Germans were not reminded of the essential importance of continuing the agreements.

For the German government the agreement was of similar political importance: it virtually bought itself the continuation of the security structure of the 1950s, i.e. the continuation of a large US troop presence in Germany. Eisenhower's policy had cast deep doubts on the US commitment. At the end of 1961 the military planning of NATO still foresaw the fall back of its forces to the Augsburg-Weser line in case of a war, which meant giving up half of Germany.<sup>75</sup> The Berlin Wall crisis appeared to the Germans as initiating a new intensified phase of the Cold War, making American protection more valuable than ever. The offset agreement became a means to stifle US inclinations to redeploy their forces. Later, when Erhard replaced Adenauer, abandoning the latter's policy to look for a closer cooperation with the France of de Gaulle to reduce Bonn's dependence on the US, a stable US troop level became essential for him to ward off his Gaullist adversaries on the domestic front.

Probably the most important consequences of the offset agreement lay in the financial field. By considerably augmenting the production numbers of military items, the Pentagon was able to reduce unit costs for their own procurement. Its weapon industries derived a huge profit.<sup>76</sup> Planning figures for 1964 indicate that military exports to Germany made up roughly a third of all American weapon sales abroad.<sup>77</sup>

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<sup>75</sup> NA, RG 59, DF 1960-63, 762.0221/12-1161, Paris 3035: Norstad Briefing of NATO Military Committee, 11.12.61.

<sup>76</sup> It has not been possible to get precise information as to the US industry's influence on offset. However, it seems that relations between the sales agencies at the Pentagon and US industry were cordial, to say the least. See: Medick, *Waffenexporte und Auswärtige Politik der US*, 1976.

<sup>77</sup> NA, RG 59, Box 3753, DEF 19-3 US, Summary of Military Sales: FY 64 Order Goals, 8 July 1963.

Time and again the US government referred to the offset agreement as the most important success of its monetary policy. By counting these military sales as balance-of-payments relevant gains, the Kennedy administration achieved a large part of the reduction in the US deficit from \$3.9bn in 1960 to \$2.67bn in 1963. Kennedy himself made it clear that *'it should be understood that under present circumstances military offset agreements enjoyed a clear priority over increased development assistance because of the immediate and direct benefits which this objective can bring to our balance of payments'*<sup>78</sup>. This view of the importance of the offset agreement was based on an overwhelming consensus between departments in Washington, with particularly strong proponents in Defense and Treasury. The agreement provided Treasury with a breathing space in which it was able to pursue its policy of surrounding the dollar with 'peripheral defenses'. Without the offset deal higher deficits would have made this strategy much more difficult to justify and the dollar gold standard might have come down earlier than 1971.

One might ask - and critics of the agreements did so ceaselessly- how many of these sales were really additional sales which would not have been made anyway. This is, of course, not easy to answer. Very probably, the Federal Republic would have augmented its purchases anyway, though probably not to the same extent. What counts, however, is that this augmentation was directly linked to the principle of offset, that is, balancing the foreign exchange cost of US troops in Germany. This was a manifestation of the Federal Republic's policy to support the dollar. It was used as such by the American government and perceived as such by other governments. As a high placed collaborator of de Gaulle recalls: *'Every time there was a meeting of Europeans to coordinate their policies, the State Department announced, as if by chance, that in order to reduce the US deficit, a possible reduction of US forces in Germany was under consideration. Thus, the Germans told us: "We have no chance, we have to support the American position".'*<sup>79</sup> It would take a long time before this link between the defense of the dollar and the maintenance of the US commitment in Europe was to be dissolved.

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<sup>78</sup> NA, RG 59, DF 1960-63, 811.10/8-862, DOS Circular Telegram, 8 August 1962. Accordingly, the US made strong efforts to achieve similar agreements with other stationing countries. They succeeded, for example, in the case of Italy which agreed to purchase a \$100m of equipment a year from the US.

<sup>79</sup> Institut de Gaulle(ed), *De Gaulle et son Siècle III*, 1992, p.157.

All in all, offset allowed the Kennedy administration to bring the two contradictory objectives mentioned at the outset of the chapter into accord: the continuation of the American military presence in Europe to deter the Soviets and preserve American influence in European affairs, and the continuation of the dollar-gold system in a period when the Atlantic security system and the world's monetary system became increasingly incompatible. The German government managed to combine a number of advances towards the goal of military equality with the avoidance of large scale US reductions which would have signified a drastic change in the Atlantic security structure. The price was support for the dollar.

In hindsight, it is easy to see that the agreement was possible only because a set of favourable circumstances coincided: the impact of Berlin; the availability of funds and the German need for advanced weapon systems; the US willingness to provide the advanced military material; the German forces' requirement for logistic help; the incessant pressure by McNamara and his associates; the absence of sizeable German and European competition; the almost complete exclusion of the Federal Finance and Foreign Ministries from the talks. The offset agreement was a bargain which may have made sense only for a short period; nevertheless it soon became an institutionalized factor of German-American relations. Both sides showed very early signs of disenchantment with their part of the bargain. The question was when it would come unstuck.



## CHAPTER IX

**THE BARGAIN SLOWLY COMES UNSTUCK:  
TROOP REDUCTIONS, OFFSET, AND THE BALANCE OF PAYMENTS, 1962-65**

## a) The Handling of the Offset Agreements

The agreement whose genesis is described in the previous chapter had been formulated, with the exception of the target figure, in a rather vague form. The question arises as to how the agreement was actually executed and how the 'Offset' was managed? This question has received almost no attention in the literature. However, only after describing the working of Offset is it possible to understand the peculiar course the history of the offset agreements took in the succeeding years.

The German and American ministries of defence were charged with putting the provisions of the Strauss-Gilpatric agreement into practice. Their officials kept the subject in their hands until 1966. Given the far-reaching political content of the agreement, this is important. Particularly conspicuous is the relative absence of the State Department and the *Auswärtiges Amt* in this context.

In the US, offset was managed by the Pentagon with some participation by the Treasury Department; only when problems transported the issue to a politically sensitive level, did the State Department belatedly try to get in anew. A team of highly motivated Pentagon officials, supplemented by some Treasury and embassy people, had undertaken the detailed negotiations with the German defence ministry. The same officials began now to travel regularly to Germany to discuss projects and orders. These frequent shuttle missions to Bonn by Kuss and Sullivan, the Pentagon and Treasury officials in charge, soon stirred up considerable irritation in the US embassy in Bonn which felt bypassed and warned of the absence of political considerations in the multi-million-dollar deals concluded between the *BMVg* and the Pentagon salesmen.<sup>1</sup> Already in August 1962, officers in the American embassy concluded, somewhat resigned, that *'State is no longer trying to keep fully abreast of the machinations*

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<sup>1</sup> McGhee Papers, 1988 add., Box 1, Tyler to McGhee, 16 April 1964; McGhee to Tyler, 18 April 1964.

*of Messrs. Kuss and Sullivan. We have neither the manpower nor the money.*<sup>2</sup>

Very soon, a kind of military-industrial complex, dealing with offset, emerged in the Pentagon. Its existence was closely linked to the rise in German military purchases and it expanded its activities soon on a worldwide scale. For McNamara's Defense Department, the sale of military hardware became a major source of revenue. During the Kennedy administration, the Pentagon initiated a professionally organized sales campaign which quickly multiplied American military exports. From 1961 to 1966 American military sales abroad rose from \$630m to \$1.937m.<sup>3</sup> The Federal Republic alone took about one third of all those exports.<sup>4</sup> A special sales agency, headed by Henry J. Kuss, was established in the Pentagon which was called, somewhat euphemistically, 'Office for International Logistics Negotiations'. This agency expanded their activities with the blessing of McNamara on an unprecedented scale, in close cooperation with the about twenty major weapon producing firms. Industry representatives accompanied Kuss on his sales missions to Germany.<sup>5</sup> In Germany, the MAAG, counting over one-hundred employees, established day-to-day contacts with procurements officers in the German defence ministry.<sup>6</sup> German military personnel was trained on US weapons, German supplies were processed and placed in the US supply system, maintenance of damaged weapons was provided, procurement services were extended, etc. - all, of course, against dollars.<sup>7</sup>

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<sup>2</sup> NA, RG 59, DF 1960-63, 862a.10/8-862, Box 2658, Freshman to Dowling: Your Meeting with Dillon, 8 August 1962.

<sup>3</sup> Armed Forces Management, January 1967, p.36. Journals like AFM and Defense Industry Bulletin, partly financed by the Pentagon, served as show-case for the US industry's weapon production. They clearly show the close cooperation between the DOD and the major arms exporting firms. Most of these exports went via the Pentagon and as such they were registered as gains in the account of the Defense Department. On this subject, see also: Medick, *Waffenexporte und Auswärtige Politik der Vereinigten Staaten*, 1976 and Louscher, 'The Rise of Military Sales as a U.S Foreign Assistance Instrument', in: ORBIS 20/1977, p.933-64. Only at the end of the 1960s, Congress became aware of the major foreign policy implications of McNamara's sales offensive; see ch XI.

<sup>4</sup> NA, RG 59, SF 1963, Box 3753, DEF 19-3US, Kuss Memorandum: Summary of Military Sales FY 64 Order Goals, 8 July 1963.

<sup>5</sup> McGhee Papers, 1988add., Box 1, DOD/FMOD Conference in Bonn: List of Participants, 22 May 1963.

<sup>6</sup> NA, RG59, SF 1963, Box 3760, DEF19-2 US-WGER, Bonn 3161, 22 May 1963.

<sup>7</sup> 'U.S. Foreign Sales Carry a Guarantee of Continued Logistics Support' AFM, January 1967, p.71-72.

Thus, the Pentagon was able to reap some revenue and, in particular, curtail the tremendous balance of payments impact the intensification of the Vietnam War had on its activities. The continuation of German orders became a core element in McNamara's management of his department. His strong insistence on offset by military purchases even when the Federal Republic claimed to have no further need is derived from that.

Dillon and McNamara were mainly interested in a constant flow of offset funds and did not care very much what was sold and how this was done, as long as it did not concern sensitive material. Once the agreement was concluded it quickly became an institutionalised factor on which McNamara counted in his military-economic policy, particularly regarding the foreign exchange component of military expenditures, and on which Dillon relied in his efforts to stabilize the American balance of payments. Few thoughts were given to the longterm aspects of the agreements.

A similar pattern emerged in Germany. As reported, the negotiations were conducted and concluded by *BMVg* officials, apart from a last minute intervention by the Finance Ministry which achieved only a short delay. It seemed a deliberate policy by the German defence ministry to keep other ministries out of the offset process. As long as the offset funds were covered by the defence budget, the Finance Ministry would see no reason to take up the troublesome issue. Its officials had their hands full coping with British demands for offset; a task which they had assumed very reluctantly and after all other concerned ministries had declined to manage it (see ch.X).

The involvement of the *Auswärtiges Amt* in the offset process was also conspicuously low. At the end of 1962, when Foreign Minister Schröder was questioned by Dillon about indications that the agreement would not be fully honoured, he displayed an almost awkward lack of knowledge on the subject.<sup>8</sup> This is particularly striking if one remembers the important role the AA played in the support cost negotiations with the British after 1955. Even if we account for Schröder's unwillingness to discuss the complicated problem at this level, it might well have been true that he knew very little about the details, as he claimed.

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<sup>8</sup> FRUS 1961-63, IX, conversation Schröder-Dillon, 15.11.1962, p.157-9.

Relations between him and Strauß were not particularly cordial. Furthermore, offset was in line with Schröder's policy of close alignment to the US. His interest was that the BMVg took care of the issue, so that it might not interfere with the general conduct of German-American relations. What the AA was worrying about was the maintenance of the US troop level. However, it refused to accept its linkage to the level of offset, even when it became increasingly obvious that this link took the form of official US government policy.<sup>9</sup>

Chancellor Adenauer also was unwilling to concern himself with such a technical matter. When McNamara tried to obtain Adenauer's comments on the issue, the Chancellor just responded that the Pentagon chief should discuss offset with Blessing, the president of the *Bundesbank*, and with Abs, one of Adenauer's principal advisers in monetary affairs; both of them were at that time hardly experts on offset.<sup>10</sup> In his memoirs there is no reference to the offset agreement.<sup>11</sup>

Thus, the Defence Ministry was left with a politically highly sensitive issue. This situation was not particularly harmful as long as the Defence Minister was Franz-Josef Strauß, a powerful figure in the cabinet and on the domestic political scene. He also was not the man to be susceptible to American pressure. However, his dubious role in the SPIEGEL affair put an unexpected stop to his career in late 1962. He was replaced by Kai-Uwe von Hassel, who distanced himself from the impetuous and energetic style of Strauß and had much less standing in the German cabinet. Von Hassel failed to initiate a change of policy on the offset issue which was vigorously pushed by the Americans, in particular by McNamara, every time he met them. It is unclear when the defence minister realized the limited rationality of continuing with offset by military purchases and why he then did not put on the brakes. It might have been loyalty to Erhard which prompted him to adhere to the principle of offset until it was too late.

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<sup>9</sup> PA-AA, B150/27/4, Memorandum Ref.11(116): Frage eines Junktims zwischen...Truppenstationierung...und Rüstungskäufen, 24 April 1964.

<sup>10</sup> AAPD 1963, McNamara-Adenauer Talks, 31 July 1963, p.864-65.

<sup>11</sup> With the result that the Adenauer-centred research on German-American relations until 1963 ignored the issue, like many fundamental economic problems, completely. See, for example, the almost complete absence of economic issues in Schwabe(ed), *Adenauer und die USA (Rhöndorfer Gespräche, Bd.14)*, 1994.

When Erhard became Chancellor in 1963, the alliance with the US became his and his Foreign Minister's, Schröder, all-important objective. This objective they had to defend against powerful critics at home. They expected the management of offset to occur in such a way as not to interfere with their coveted German-American relationship. Von Hassel himself was very Atlanticist and thus had every intention of assuring continued American support for the Erhard government. Dahlgrün, the Finance Minister, was no Schäffer. As a member of the smallest coalition party, the FDP, he developed no particular profile and was not the man to challenge the Chancellor and the Foreign Minister on policies they considered essential. As a result, nobody in the government took up the issue vigorously and initiated a re-negotiating process with the Americans. This neglect was particularly blatant in the case of Erhard who by this very carelessness dug part of his own political grave. Numerous high-level interventions by US officials should have warned him that some kind of a political time-bomb was ticking, or, at least, that the American side placed more importance on the 'hardware' of mutual relations than on declarations of friendship.

Summing up, it appears that the management of offset was pursued on both sides with insufficient consideration to future political problems, in the interest of short-term political and economic objectives. Officials in the BMVg and McNamara's salesmen had considerable autonomy in pursuing their multi-billion dollar deals in a highly sensitive area of mutual relations, and of transatlantic relations in general.

Probably even more conspicuous than this was the absence of democratic control, due to the secrecy surrounding the agreements. Only very few members of Congress or of the *Bundestag* were aware of the deals and had a vague knowledge of what was going on. When the problem surfaced in 1966, most parliamentarians and the public were caught by surprise regarding the scope of the agreements. There had hardly been any discussion of the agreements in the press until signs of trouble became overtly clear in early 1966.

b) The second offset agreement and the institutionalization of offset

Shortly after the Gilpatric Strauß letter exchange of February 1962 was consummated, the Americans had directed their thoughts towards a successive agreement, providing for orders in CY 1963-64, and payments in FY 1964 and 1965. Somewhat to their surprise the negotiations proved short and not very complicated. The Americans, again headed by Gilpatric, had offered to extend their logistics cooperation to the Navy and the Air Force, including the U.S. mainland, which involved mainly the training of German soldiers in American facilities.

Additionally, the Germans sought a commitment by the US to extend the logistics cooperation to comprehensive wartime support. This was to assure a supply for German forces from bases abroad in the case of an attack which was thought to result in a substantial initial loss of German territory.<sup>12</sup> Studies on this question were initiated.<sup>13</sup> The US embassy saw several advantages in such a scheme. First, it would result in forging a stronger dependence of Germany on US material and shield American sales against competition from foreign or German weapon producers. Second, it would probably allow the US to sell some of its warstocks in Europe which were to be reduced anyway due to McNamara's cost saving campaign. Finally, it would enhance US influence on German military policy. *'United States influence could also be exercised indirectly on significant FRG policy decisions, e.g. as counterweight to such remote, but nevertheless conceivable, factors as a Franco-German "third force" approach to European defense or any future tendency of the FRG to pursue an independent (be it neutralistic or adventurous) military policy vis-a-vis the Soviet bloc.'*<sup>14</sup> The offset agreement also served as tool to bind West Germany closer to the Atlantic Alliance.

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<sup>12</sup> NA, RG 59, DF 1960-63, Box 1276. 611.62a/6-1262, Bonn A-1493: US/FRG Wartime Logistics Support Agreement, 12.6.1962.

<sup>13</sup> McGhee Papers, 1988add., Box1, MAAG to Ambassador:DOD/FMOD Conference, 22 May 1963; PA-AA, B 150/9, Memo of Understanding on the creation of a logistic system for wartime support, 1 August 1963.

<sup>14</sup> NA, RG 59, DF 1960-63, Box 1276. 611.62a/6-1262, Bonn A-1493: US/FRG Wartime Logistics Support Agreement, 12 June 1962.

The new features were embodied in a second memorandum of understanding, signed on 14 September 1962, again with very little public repercussions. The German side, however, already began to have second thoughts on the continuation of offset. Strauß had insisted on inserting an additional clause which stipulated that offset payments would be made '*subject to the availability of funds*'.<sup>15</sup> This proved to be a bad omen.

Already in August, reports had arrived in Washington that the German defence budget might be affected by growing German uneasiness about future strategic trends in NATO and about the country's economic prospects.<sup>16</sup> In October, it became clear that the Federal defence budget in 1963 would be much lower than both the US government and the BMVg expected, and lower than necessary in order to fulfill the goals agreed to in NATO defence planning. Adding a further blow, the BMVg specified that under these circumstances all new procurement orders would be stopped by January 1963 at least and payments for orders already made would be delayed.<sup>17</sup> The uncertainty regarding the defence budget was part of a protracted political situation in Bonn.

Adenauer, against the opposition of part of his cabinet, occupied himself in achieving closer cooperation with the France of de Gaulle. France had always been particularly interested in arms cooperation and sales by its industry, and it was only prudent for the German government to wait with new orders until the outcome of Adenauer's plans took concrete forms. Furthermore, the German Finance Ministry was insistent on limiting a further growth of the defence budget on which the Ministry of Defence had counted in their offset deals. Strauß was immobilized by the SPIEGEL affair and not able to put up a fight for more money. It is quite likely that the BMVg officials who informed the Americans of the problem, painted an exaggerated negative picture to get the US government to exert pressure on Adenauer and the Finance ministry.<sup>18</sup>

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<sup>15</sup> McGhee Papers, 1988 add., Box 2, Memorandum of Understanding, 14 September 1962.

<sup>16</sup> NA, RG 59, DF 1960-63, Box 2658, 762a.5/8-2362, Bonn 556, 23.8.1962; *ibid.*, Bonn 597, 28.8.1962.

<sup>17</sup> NA, RG 59, DF 1960-63, Box 1903, 762a.5/11-3062, Bonn A-1193, 30 November 1962.

<sup>18</sup> *ibid.*

If this was the reasoning, it worked perfectly well. The Americans reacted fast and vigorously. The embassy in Bonn urged an approach to Adenauer by the President himself during the Chancellor's forthcoming visit in November.<sup>19</sup> Dillon and McNamara fully concurred with this idea. They pointed out that the German decision to delay the payment of \$225m, which were expected to arrive before the end of 1962, would swell the US payments deficit by this very amount. Both advised Kennedy to hit Adenauer strongly on this point.<sup>20</sup> The President did not need much persuasion. Alluding to the Cuba Crisis, he told the Chancellor: *'Since our difficulties in October we had had to draw on our dollar resources even more and had since then heard the disquieting rumor that for budgetary reasons the Federal Republic was expecting not to fulfill this agreement ... This would have a very bad psychological effect.'*<sup>21</sup> One day later, a strong-worded memorandum covered the points more specifically. As the United States was maintaining its full force in Europe, it felt it should *'have the right to expect Germany, in turn, to do its full share.'*<sup>22</sup> Therefore, the US requested an augmentation of the German defence budget. Another memorandum, ten days later, listed up German obligations under the offset agreement and warned of *'disastrous consequences'* in case payments would be deferred as announced.<sup>23</sup>

Apparently, this broadside convinced Adenauer and provided enough ammunition to overcome the resistance of the Finance Minister. Two weeks later, the Chancellor informed Kennedy that the projected defence budget would be augmented by an additional DM 1.1bn (\$275m) and that the Strauß-Gilpatric agreement would be fully honoured. He added that German defence expenditures now had reached their upper limit.<sup>24</sup> The US government expressed its satisfaction with the steps taken. However, the peace did not last very long. With his famous press conference on 14 January 1963, de Gaulle effectively rocked the boat of Kennedy's

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<sup>19</sup> *ibid.*, 11-862, Box 1903, Bonn 1299: memcon Schiffers-Morris, 8 November 1962; 862a.10/11-1062, Box 2658, Schiffers-Sullivan talks, 10 November 1962.

<sup>20</sup> *ibid.*, Box 2658, 862a.10/11-1362, Dillon/McNamara to Kenndy, 9.11.1962.

<sup>21</sup> FRUS 1961-63, XV, Adenauer-Kennedy talks, 14 November 1962, p.435-6.

<sup>22</sup> *ibid.*, Memorandum Kennedy to Adenauer, 15.11.1962, p.444-5.

<sup>23</sup> Kennedy-Adenauer Correspondence, compiled in the JFK Library, Boston: Kennedy to Adenauer, 25.11.1962.

<sup>24</sup> *ibid.*, Adenauer to Kennedy, 12.12.1962.



European policy. The solemn signing of a Franco-German Treaty of friendship and cooperation only one week later appeared to the Americans like an act of utter provocation by Adenauer.

The Kennedy administration, in the follow-up, undertook a reappraisal of its European policy. I will later analyse the effects of this reappraisal on the issue of troop levels in Europe (see paragraph c). On the continuation of offset, the crisis of trust in German-American relations had no direct impact. Initially, the US was deeply worried about a possible nuclear deal between France and Germany, and in addition a diversion of German military procurement to French sources. The Germans hastened to reassure the Americans on these points.<sup>25</sup>

Internally, however, the Germans were extremely sceptical as to whether they would be able to fulfill the agreement. French pressure was only one aspect in these apprehensions. Not only the difficult budgetary situation, but also the uncertainty regarding the future of NATO policy and Franco-German cooperation in the wake of the treaty, as well as the danger of increasing dependence from American sources were some of the reasons.<sup>26</sup> Therefore, the *BMVg* declined stubbornly to commit itself to more than \$1000m of payments during the term of the second agreement, using the safeguard clause in agreement.

The Americans, on the other hand, tried to extract from the Germans an unambiguous, loophole-free commitment to full offset payments. The Treasury and Defense departments were particularly active. In mid-1962, the continuation of offset became, in the absence of other major successes against the balance of payments deficit, the highest priority in the Treasury. Dillon noted that a large part of the improvement in the balance of payments had been due to offset.<sup>27</sup> With presidential approval, military offset agreements took uncontested precedence over previously equally valued efforts by the US to convince its allies to share

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<sup>25</sup> NHP, note on von Hassel-Gilpatric talks, 13.2.1963; BA, NL Blankenhorn 152/1, Bonn Circular Telegram re von Hassel-Gilpatric talks, 20.2.1963.

<sup>26</sup> NHP, Brief for von Hassel re Conversation with Gilpatric, 6.2.1963; NA, RG 59, SF 63, DEF19 WGER, Bonn 2176, 22.2.1963.

<sup>27</sup> FRUS 1961-63, IX, Dillon to Kennedy, 14.11.62, p.155.

the foreign aid burden.<sup>28</sup> The Americans undertook initiatives to conclude military offset agreements with numerous other countries, including France, Italy, and Japan.<sup>29</sup>

Foremost in the considerations behind this policy was, of course, the balance of payments objective. On the occasion of the President's trip to Bonn and Rome, Dillon urged the emphasizing of the importance of military offset agreements, *'which contribute so significantly to meeting our balance of payments goals and which constitute from the balance of payments point of view our top priority financial objectives in these countries.'*<sup>30</sup> In the absence of other major breakthroughs in the fight against the deficit and in the absence of a political decision for large-scale reforms in the international monetary system, the offset mechanism had taken on the role of a palliative for coping with a fundamental monetary imbalance.

The sale of military hardware was considered, apart from these monetary reasons as advantageous from a business point of view and also with regard to political objectives. Elaborating on the desirability of American-German co-production of a new tank, the US embassy in Bonn wrote that *'the co-production technique ... offers [the] only realistic method for [the] future not only to get our share [of] German armaments orders but also, and more importantly, to keep [the] Fed[eral] Rep[ublic] closely tied to U.S. in conventional weapons.'*<sup>31</sup> A similar argument was used by Dillon: *'...we should move promptly to make sure that European countries place orders now for U.S. manufactured equipment, rather than make plans to meet their needs from their own production or from other foreign sources.'*<sup>32</sup>

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<sup>28</sup> NA, RG 59, DF 1960-63, 862a.10, 8-862, Box 2658, Freshman to Dowling, 8.8.1962.

<sup>29</sup> France refused to buy more US weapons as long as the Americans refused to sell nuclear technology. Italy agreed on 19 September 1962 to buy a yearly \$100m of military equipment in the US; however, this was coupled with US credits to Italy. See: JFKL, POF, Departments&Agencies: Treasury, Box 90, Dillon to JFK, 9 October 1962. In connection with the Vietnam War, numerous Asian countries also assumed offset obligations; see: LBJL, NSF, NSC Histories: The 1968 Balance of Payments Program, doc.9e, Military Account, 25 December 1968.

<sup>30</sup> NA, RG 59, SF 1963, Box 3455, FN 12 WGER, Dillon to Ball, 31.5.1963.

<sup>31</sup> NA, RG 59, SF 1963, Box 3769, DEF12 Armaments, Bonn 2817, 20.4.1963.

<sup>32</sup> JFKL, POF, D&A: Treasury, Box 90, Dillon to President, 13.5.1963; see also: NA, RG 59, SF 1963, Box 3753, DEF 19-3US, Kuss: Summary of Military Sales FY 64 Order Goals, 8.7.1963.

In 1962-65, the Germans continued to buy heavily in the United States, due to the reasons cited in ch.VIII and also because of increasing US pressure. Among the largest items were again modern missile systems like PERSHING or SERGEANT. This led to a certain uneasiness in the State Department about the spread of these weapons. *'If the Chancellor (or von Hassel) suggests that Germany could meet its offset obligations by purchasing more Pershing missiles beyond the four battalions now contemplated, it would be advisable not to make any commitment but simply to agree to consider the request in the light of other Allied strategic interests [i.e. a continued conventional build-up].'*<sup>33</sup> In the end, those considerations were overcome by the need to meet the foreign exchange cost of the troops, estimated at about \$1350m in FY 1963-1965.<sup>34</sup>

Despite the purchase of such expensive tools, the Germans lagged consistently behind schedule with their offset payments.<sup>35</sup> They refused to commit themselves to more than \$1bn of offset in the two years covered by the second agreement.<sup>36</sup> In July 1963, the US sent a long memorandum to the German government listing the advantages of the cooperative logistics system and requesting a firm commitment to a payment target of \$1300m<sup>37</sup>. The same point was made by McNamara to Adenauer when the two met on 31 July. Von Hassel, who was present, said that because of increasing domestic production, Germany had to limit purchases abroad. He mentioned that the US had abandoned a scheme already agreed upon in April which would have allowed Germany to make up the gap by investment in US treasury bonds. McNamara denied that such an agreement had existed and threatened that, in case the offset target was not fulfilled, the US would have to reconsider its troop commitment. At that point, Adenauer cut the quarrel short by referring this subject to

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<sup>33</sup> DDRS 1979, 305B, Presidents European Trip, June 1963: Scope Paper Germany, 14.6.1963; see also: McGhee Papers, 1988add, Box 1, Gilpatric to von Hassel, 8.5.1963.

<sup>34</sup> NA, RG59, SF 1963, DEF13 US-WGER, Tyler to Rusk: Sale of Pershings/Sergeants to the FRG, 21.5.1963.

<sup>35</sup> NA, RG 59, Box 3451, FN12US, Bonn 5, 1 July 1963.

<sup>36</sup> NA, RG 59, SF 63, FN 12US, Box 3451, Bonn 374, 27.7.1963; see also: McGhee (1989), p.75-6.

<sup>37</sup> NA, RG 59, SF 1963, FN12US, State/Treasury/Defense message, 16.7.1963.

discussions of financial experts.<sup>38</sup>

Nevertheless, McNamara's veiled threat was taken very seriously by the German government. Apart from budgetary considerations and the apprehension regarding one-sided dependence, the German reluctance to commit themselves to a fixed level of payments was fed by disturbing signs emanating from Washington. Increasing rumours threw doubt on the continuity of the US troop presence. In fact, the years 1962/63 saw a major debate within the American government regarding the future of its troop commitment to European defence.

#### c) The Troop Reduction Debate in the Kennedy Administration

The Strauß-Gilpatric agreement did not stop discussions in the US government about the adequate level of American forces in Europe. This had many reasons. Doubts about the continuation of offset were nurtured by delays in German payments. The balance of payments remained highly in deficit. After the erection of the Berlin Wall and the Cuban Crisis, fears of direct Soviet aggressive acts subsided. A gradual acceptance of the Status Quo and the pursuit of some kind of detente in Europe became open objectives of US foreign policy. Apprehensions of irresponsible acts by the Germans diminished as the Federal Republic became politically, economically, and militarily increasingly accepted and stronger linked to the West. All those trends, which touched upon the rationales which once had led to the stationing of US troops (see ch.I and VI) surfaced in the troop reduction debate of 1962/63, whose outcome was to be of great importance to European-American relations in general and the offset story in particular.

As soon as the Berlin crisis subsided, the ratio behind the Acheson report lost logical force and the day-to-day concern of the balance of payments came to carry more and more weight.

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<sup>38</sup> AAPD 1963, McNamara-Adenauer Talks, 31.7.1963, p.864-65; see also: McGhee Papers, 1988add., Box 1, Bonn to Department of State on Adenauer-McNamara Talks, 2.8.1963. During the same meeting, McNamara came up with a proposal that the Germans should acquire US logistic facilities in France which the Americans were about to close. A corresponding memorandum was signed on 1 August (NA, RG 59, SF 1963, Box 3766, DEF13 US-WGER, Bonn 971, 14.9.1963). This set the stage for a major German-French row. The French explained that '*since Franco-US LOC [Line of Communications] arrangements are on completely different basis from Franco-German arrangements (German used facilities being under French command) France did not see how US facilities could be transferred to Germans* (ibid., Paris 1337, 19.9.1963).

It has been already mentioned, that Kennedy himself was deeply sceptical about the wisdom of keeping so many troops in Europe. His frustration had mounted when reports showed that the ambitious goal of eliminating the balance of payments deficit at the end of 1963 would not be accomplished. Attacks against the Europeans which were not ready to increase their conventional force level multiplied, most bluntly perhaps during a tense discussion with the French Minister for Cultural Affairs, André Malraux, on 11 May 1962. An ill-tempered Kennedy repeated several times that the US would be happy to leave Europe if that was what the Europeans wanted. *'If it is desired that we should cease to carry the load in Europe, nothing would be better from our point of view - it has now cost us about \$1.300.000.000 to maintain our forces in Europe and the savings on these forces would just about meet our balance of payments deficit ... We feel like a man carrying a 200-pound sack of potatoes, and other people not carrying a similar load, at least in potatoes, keep telling us how to carry our burden.'*<sup>39</sup>

The expression of such sentiments by the President encouraged those sections in the administration which saw the forces in Europe as a wasting asset. They had their champions in McNamara and Dillon. Opposed to reductions was the State Department (although Rusk was somewhat ambiguous), which still saw the European theatre as of paramount importance to US foreign policy objectives and therefore accorded to the 7th army a political importance which went much further than military and financial considerations. The consequence of this conflict was a long drawn-out controversy in the administration.

Very rapidly after the Berlin Wall had been erected and US troops had been augmented by about 40.000 men, the DOD tabled first plans to bring the costly reenforcement back. The army and the State Department thought this much too early and weighed in successfully against such precipitate action.<sup>40</sup> No reductions were effected in early 1962, but the planning in the Defense Department went ahead - not only regarding the reenforcement but also the

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<sup>39</sup> FRUS 1961-63, XIII, p.695-701.

<sup>40</sup> *'While the messages received here do not expressly state so it is believed that gold drain from the US was central among considerations behind the orders to USAREUR'* USAREUR to Dowling, 11.1.1962, McGhee Papers, 1988 add., Box 1. See also: JFKL, NSF, Depts & Agencies: DOD, Box 275, Taylor to President, 9.12.1961; FRUS 1961-63, XIV, telcon Rusk-Kohler, 15.1.1962, p.760; FRUS 1961-63, XIII, Rusk to McNamara, 20.1.1962, p.356-7.

regular forces. Nobody in the administration took the President's orders to reduce the foreign exchange component in the expenses of their departments more seriously than McNamara. In mid-July, he had compiled an impressive list of saving measures, called Revised Project 8, which were to reduce the balance of payments impact of defence expenditures by about \$1bn.<sup>41</sup> McNamara considered in his project large-scale reductions in the regular 7th army, at a magnitude of about 44,000 men in a long-term perspective. He made no secret of his opinion that he considered the bulk of these forces as unnecessary expense. Based on new assessments of the Soviet threat which set Warsaw Pact military capabilities much lower than previously estimated,<sup>42</sup> he thought large reductions possible with regard to the military situation and, anyhow, necessary from a balance of payments point of view.

The Department of State reacted alarmed. In its view the Berlin crisis was not yet over and advance consultation with the allies was necessary even before reducing the Berlin roundout forces.<sup>43</sup> However, one factor was undeniable: gold losses in the first half of 1962 reached alarming degrees.<sup>44</sup> Faced with this predicament the State Department was fighting a continuous rearguard campaign in the troop level issue. During 1962, as long as the studies on Project List VIII went on, State managed to fend off DOD and Treasury pressure for large-scale reductions. In the meantime, the Americans continued with their concerted effort to get the Europeans to build up their conventional forces. Much has been written on other places about the basic disagreement on strategy between the US and Germany in these years.<sup>45</sup> Whereas the Americans pointed to the necessity of avoiding immediate recurren to nuclear warfare the Germans talked about the inferiority of their forces which had no tactical nuclear weapons at their disposal.<sup>46</sup> Behind the German arguments were further considerations.

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<sup>41</sup> Total annual defence outlays entering the American balance of payments were about \$3bn/year in 1961; JFKL, NSF, Meetings&Memoranda, NSAM 171, Box 337, Revised Project Eight, 10 July 1962.

<sup>42</sup> Enthoven/Smith, *How much is enough? Shaping the Defense Program, 1961-69*, 1971.

<sup>43</sup> NA, RG 59, DF 1960-63, 740.56311/5-1762, Fessenden to Johnson, 17.5.1962; FRUS 1961-63, XIII, Johnson to Nitze, 23.5.1962, p.394-5.

<sup>44</sup> FRUS 1961-63, IX, Report by Cabinet Committee on Balance of Payments to President, 27.7.1962.

<sup>45</sup> see ch.VIII, fn.43.

<sup>46</sup> The disagreement is well summarized in an exchange between Adenauer and Kennedy on 14 November 1962; see: FRUS 1961-3, XIII, p.452-3.

Firstly, the nuclear dilemma of the Federal Republic which had to insist on forward defence and an immediate use of all available weapons to deter any attack on its territory. Any doubts about the American willingness to use all its firepower for the defence of Germany limited the credibility of deterrence and impinged directly on the German security. For this reason, the Germans tried in the late 1950s and 1960s consistently to get a stronger voice in the planning for the use of nuclear weapons.<sup>47</sup> Secondly, once again, economic reasons played an important role. Accordingly, Strauss informed Adenauer that the conventional program the US wished was financially impossible and strategically undesirable.<sup>48</sup> A fundamental dilemma of German foreign policy throughout the 1960s appears in this context. Having renounced the possession of nuclear weapons, the Federal Republic was effectively unable to live up to its own Cold War rethorics by conventional means. As long as it did not change its rigid stance in the East West conflict and achieved some kind of accommodation with the Eastern bloc, it would remain necessarily dependent on the US and its troops. It would be unable to get rid of its dependence by conventional means, and even if it effected a large buildup, the danger of American withdrawals mounted. This created the political and military necessity to assure the American troop presence by all means, including offset.

Whereas in 1962, Kennedy, despite McNamara's efforts, shied away from provoking a crisis with Europe over troop reductions, his thinking changed strongly in 1963. The major event responsible for this change might have been the mentioned crisis in German-American relations provoked by the Franco-German treaty of January 1963. However, already some weeks before the General's press conference, the President had clearly indicated his impatience with European defence efforts. In a discussion with the military leadership in December 1962, the President, referring to the gold outflow and the limited military rationality of forward-basing so many troops, questioned strongly the necessity of the US

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<sup>47</sup> Whether German politicians actually strove for ownership of nuclear arms is still debated; see: Ahonen, 'F.J.Strauss and the German Nuclear Question, 1956-62', in: *Journal of Strategic Studies* 18/1995, p.25-41. For an argument which explains the Berlin crisis convincingly with Soviet fear of German nuclear ambitions see: Trachtenberg, 'The Berlin Crisis', in: Trachtenberg (1991), p.170-73.

<sup>48</sup> NHP, Strauss to Adenauer, 21.12.1962; for the strategic dilemma and economic reasoning, see: NHP, Talking Paper for Meeting with the President, 18.11.1961; *ibid.*, Results of Talks between AA and BMVg in Münstereifel, June 1962; BA, NL Carstens, 620, Draft protocoll on BMVg - AA colloquium, February 1963..

effort.<sup>49</sup> McNamara immediately promised a plan to withdraw 50-70.000 men from Europe. The President's frustration was heightened by de Gaulle's veto over the UK entry to the EC and the signing of the Franco-German treaty in January 1963. All this came on top of an already manifest unease in the administration about the handling of the Skybolt affair with the British.<sup>50</sup> Altogether, these events blatantly exposed the contradictions and conflicts governing the relations in the Western Alliance.

Kennedy's reaction was impetuous. He requested a sweeping reappraisal of US policy towards Europe, including the American troop presence, based on a 'cold, hard' attitude in order to preserve US interests. *'As soon as the French have a nuclear capability, the President continued, we have much less to offer Europe and the Europeans may conclude that continuing their ties with us will create a risk that we will drag them into a war in which they do not wish to be involved. If we are not vital to Germany, then our NATO strategy makes no sense. The President said that we must not permit a situation to develop in which we would have to seek economic favors from Europe. He thought we should think now about how we can use our existing position to put pressure on the Europeans if the situation so demands ... He thought we should be prepared to reduce quickly, if we so decided, our military forces in Germany.'*<sup>51</sup>

Bad news from the monetary front were strongly on the President's mind during these

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<sup>49</sup> DDRS 1995/1787, memcon JFK, McNamara, JCS, 27 December 1962.

<sup>50</sup> In mid-1962, McNamara had cancelled, to the shock of the British government, the further development of the Skybolt rocket, due to technical deficiencies. This rocket had been promised to the British as delivery system and was essential for maintaining an independent British deterrent. When Macmillan shortly afterwards met Kennedy in Nassau, he categorically asked the Americans to provide a substitute. Despite heavy misgivings -the Kennedy administration pursued a policy of non-proliferation and would have liked to see a phase-out of the independent British nuclear force-, Kennedy acceded to the British demands. Later on, Kennedy felt that Macmillan had pushed him into the corner and even LBJ was still haunted by the fear that the British Prime Minister, Wilson, would 'do the Macmillan' on him. Opponents of the concessions to Britain thought that de Gaulle might take the implicit snub badly and retaliate with an assault on Britain's application for EEC membership. This actually happened, though other reasons played a more important role in de Gaulle's veto. For the very interesting Kennedy-Macmillan talks, see FRUS 1961-63, XIII, p.1088-1115. Kennedy afterwards commissioned a long study on the mistakes made in the Skybolt-affair (JFKL, NSF, Meetings & Memoranda, Box 322, Neustadt Report to the President: Skybolt and Nassau, 15 November 1963). It was later transformed into a book by the author (Neustadt R., *Alliance Politics*, 1970). An excellent study on the issue is Clark, *Nuclear Diplomacy and the Special Relationship*, 1994. On the British EEC application and related aspects, see the articles in Griffiths/Ward(ed), *Courting the Common Market*, 1996.

<sup>51</sup> FRUS 1961-63, XIII, Summary record of NSC Executive Committee Meeting 38 (pt.II), 25.1.1963, p.488-89. See also his remarks to the NSC, *ibid.*, 22.1.1963, p.484-87.



remarks. The situation at the beginning of 1963 seemed bleak. Treasury expected further substantial gold losses during the succeeding months and reaching the revered goal of a balance of payments equilibrium seemed highly unlikely before 1965.<sup>52</sup> French policy with regard to its huge dollar reserves was incalculable. De Gaulle might cash in his dollar reserves at any time and thus provoked a major currency crisis. Kennedy felt that the American monetary weakness provided the Europeans with much of their leverage against the US and he ordered Treasury to assess the relative monetary strengths of France and the US.<sup>53</sup>

In the weeks after the Franco-German treaty the Americans undertook a vigorous effort to get the Federal Republic to an unambiguous declaration of adherence to the principles of the Atlantic Alliance and US-American postwar relations.<sup>54</sup> The Americans succeeded with the famous Bundestag resolution, accompanying the ratification of the Franco-German treaty. A carrot in form of a renewed US initiative concerning the MLF was extended to the German government. Overshadowed by these diplomatic ramifications, the question of the future of the US troop commitment in Europe remained open. The issue showed up consistently on the agenda during the discussions of these weeks and formed one of the questions Kennedy put before the NSC Executive Committee which was to coordinate the reappraisal.<sup>55</sup> During the discussion, the principal differences emerged. Whereas Dillon urged a reduction arguing with the balance of payments impact, Rusk remarked *'that we are in Europe not because the Europeans want us there but because we believe our presence there is essential to the defense of the U.S.'*<sup>56</sup>

This was a basic point, and on this point Kennedy, supported by McNamara and Dillon, had serious doubts. To them, the US troop presence in Europe increasingly represented more a favour extended to the Europeans than a policy dictated by US interests, particularly from a

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<sup>52</sup> FRUS 1961-63, IX, Kaysen to Kennedy, 21.1.1963, p.43-44; Dillon to Kennedy, 16.1.1963, p.159-60.

<sup>53</sup> JFKL, POF, D&A: Treasury, Box 90, JFK to Treasury, 19.1.1963; for Dillons answer, stressing the need to get the non-French countries to a cooperative policy regarding their dollar reserves, see *ibid.*, Dillon to President, 24 January 1963.

<sup>54</sup> Schwarz, *Adenauer. Der Staatsmann*, 1991, p.810-26.

<sup>55</sup> FRUS 1961-63, XIII, p.156-7.

<sup>56</sup> *ibid.*, p.161.

monetary perspective. Typical of this is the letter Kennedy wrote to Adenauer the day after this discussion. He mentioned the '\$45bn and 16 years of American economic and military assistance' which had brought nothing but hostility, and warned of a new isolationism in the United States.<sup>57</sup> There was a considerable amount of self-deception in these statements which were to become so common during the 1960's. The Europeans, for the most part, saw US postwar policy not just as dictated by altruism but also by what one might call euphemistically enlightened self interest. If the continued presence of the US troops was consistently being presented as a favour and a burden for the US it was clear that the hard-nosed Macchiavellians Adenauer and de Gaulle were easily able to put the sincerity of the commitment in doubt.

The President was not convinced by the State Department claim as to the continuing importance of having troops in Europe. He raised his doubts about the stalemate situation in Europe soon after the January debacle in a meeting with the JCS. Kennedy urged the military to come up with plans '*as to how much we can reduce our forces in Europe in the next 12 months*'. He denounced the insufficient defence efforts of the allies, cited the reduced military threat in Europe (calling it 'about the eighth on the list of trouble spots'), and proclaimed it as '*absolutely essential for us to protect our monetary position...Eventually we will have to confront them [the Europeans] with the fact that either they must pay or we will have to cut back*'.<sup>58</sup> His remarks summarized the arguments of the reduction proponents: the unlikelihood of a crisis in Europe, based on an implicit recognition of the status quo (which was at variance with the German reunification postulate); the vulnerability of the dollar, interpreted as a sign of political weakness of the United States; the frustration regarding the unwillingness of the Europeans to accept American strategic views and to live up to an equitable sharing of the defence burden. Similar concerns were summarized in a memorandum by McGeorge Bundy of March 1963. '*One might conclude from a general perusal of these papers [i.e. the results of the reappraisal of American policy towards Europe; HZ] that the twenty year involvement of U.S. forces in Europe may well be extended another twenty years or even more. In spite of U.S. difficulties with the political, social and economic problems of*

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<sup>57</sup> *ibid.*, Kennedy to Adenauer, 1.2.1963, p.164-65.

<sup>58</sup> FRUS 1961-63, XIII, Memorandum for the Record, 28.2.1963, p.516-18.

*Western Europe, its crushing burden of expenditures on armaments, and the potentially destructive erosion of the U.S monetary position, little consideration is ever given to ways of reducing the impact or effects of these issues*<sup>59</sup>. Bundy conceded, however, that reductions without compensatory moves by the Soviet Union were dangerous, and that thorough advance consultation with the allies was necessary.

The State Department complemented those counter-arguments with a long list of its own against reductions. Reductions might heighten the present uncertainty in NATO regarding future military strategy, they might signify the abandonment of 'flexible response', play into de Gaulle's hands, weaken American political influence in Europe and particularly in Germany, and, finally, according to the DOS, the balance of payments gain would be relatively small compared to other corrective measures.<sup>60</sup> An additional reason for avoiding precipitate moves in early 1963 was the forthcoming Kennedy visit to Germany in June.<sup>61</sup>

This point carried the day and Kennedy was careful not to commit himself to any specific action during his visit, which was a spectacular success.<sup>62</sup> Kennedy also avoided a clear statement on foreign military expenditure during his second balance of payment message to Congress in July 1963.<sup>63</sup> He emphasized particularly the need to improve the competitiveness of American trade and proposed an 'Interest Equalization Tax' to increase the cost of borrowing in the United States for foreigners.

The emphatic reaffirmation of German-American friendship during Kennedy's trip did not stop the planning for reductions in the DOD. It continued along several tracks. There was first the slow reduction of the Berlin reenforcement (from a peak level of 273.377 in June 1962,

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<sup>59</sup> LBJL, VPSF, Box 4, Burris to LBJ: McBundy re European Policy, 13.3.63.

<sup>60</sup> NA, RG 59, SF 1963, DEF 6 US/NATO, Johnson to Rusk: Political Effects of Troop Withdrawals from Europe, 17.5.1963; Bruce to Rusk, 21.5.1963; FRUS 1961-63, IX, Rusk to McNamara, 7.6.1963, p.66.67.

<sup>61</sup> NA, RG 59, SF 1963, US 6-8NATO, Box 3749, Johnson to Rusk, 9.5.1963.

<sup>62</sup> See his speeches in the Paulskirche/Frankfurt, 25.6.63, and in Naples, 2.7.1963, in: DAFR 1963, p.203-211; AAPD 1963, Kennedy-Adenauer talk, 24.6.1963, p.670. The President, however, warned Adenauer that recent events in Europe had evoked doubts in the US as to the wisdom of keeping the troops there; *ibid*.

<sup>63</sup> PP Kennedy:1963, p.574-84.

the troop strength in Germany fell to 241.222 in September 1963<sup>64</sup>), second the cut-down in non-combat troops, and finally, highly sensitive, plans to reduce a considerable portion of combat troops over the long range. Those plans had received a new boost when in the first half of 1963 the administration began to review its previous balance of payments policies. In April, Kennedy had a long meeting with his principal advisers to discuss new ways of solving the balance of payments problem.<sup>65</sup> Asked about possible actions by Defense, McNamara replied that he expected a net adverse balance of \$1.6-1.7bn a year in the military account over the next years, provided the offset agreement is continued at the present rate. McNamara doubted this and thought the only way for large savings was by effecting troop reductions, mainly by thinning out units.<sup>66</sup> Asked by the President about the deficit in the military account he stated that the *'only way to improve our position was to reduce troop deployments...this can be done without reducing our effective military strength.'*<sup>67</sup>

Following this meeting, Kennedy charged the Secretary of Defense with presenting a program in July which would achieve foreign exchange savings of \$300-400m in the Defence account.<sup>68</sup> The proposals McNamara presented in July were coordinated with the State Department and contained only minor reductions in Europe.<sup>69</sup> However, as soon as the major part of McNamara's proposals was approved, the President requested the next program. This time savings without actual reductions in effectives were no more possible.<sup>70</sup> In September, the new program was on the President's desk. In the European theatre, it proposed the removal of about 50% of US combat aircraft (according to the plans made possible by a greatly increased missile force), the reduction of the army by 30.000 to about 205.000 men,

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<sup>64</sup> NSA, The Berlin Crisis, Doc 1924, The Replacement and Augmentation Systems in Europe, March 1964, p.63.

<sup>65</sup> FRUS 1961-63, IX, Memo for the Record: Meeting with the President, April 18, 24 April 1963, p.51-62.

<sup>66</sup> *ibid.*, p.60.

<sup>67</sup> *ibid.*

<sup>68</sup> *ibid.*, Memo Kennedy to Cabinet Committee on Balance of Payments, 20.4.63, p.62.

<sup>69</sup> *ibid.*, McNamara to Kennedy, 16.7.1963, p.68-73.

<sup>70</sup> NA, RG 59, SF 1963, DEF6-8US/NATO, Box 3749, Schaetzel to Kitchen, 24.7.1963; *ibid.*, DEF6 US, Box 3747, Popper to Schaetzel, 19.9.1963; *ibid.*, FN12US, Dept.of State to Harriman, 19.7.1963.

as well as other streamlining measures.<sup>71</sup> The plans were to be implemented until FY 1966 and would produce estimated foreign exchange savings of \$339m. Owing to the increased mobility of US forces, the Pentagon expected no significant weakening of US military effectiveness.

The State Department protested strongly and eloquently against such far-reaching cuts, arguing that they *'would be the gravest sort of mistake, fraught with adverse political and psychological consequences, perhaps out of all proportion to the intrinsic military significance, but, nevertheless, carrying a real danger of jeopardizing our entire existing national security posture.'*<sup>72</sup> These measures would evoke fears of US disengagement from Europe, upset NATO, reduce significantly the military capabilities of NATO, and lead to political turmoil. The State Department recommended that studies in other balance of payments related fields with much larger saving potentials should be urgently pushed forward. The strong counter-attack proved successful. Kennedy accepted the State Department's arguments and effected only limited reductions, particularly in Britain and France. Germany was spared. Presumably, the offset agreement together with loud German protest against minor reductions in summer 1963 played the central role in this decision.<sup>73</sup> The President accompanied his decision, however, with the wish that a political base should be established from where they could proceed towards implementation of the steps not accepted.<sup>74</sup>

This result was formulated as policy guidance in a National Security Action Memorandum (NSAM 270).<sup>75</sup> Rusk was charged with publicly announcing the government's intention to effect at the moment no combat force reductions in the European theatre. At the end of October, the Secretary of State traveled to Europe and visited Germany. In a programmatic speech at the Paulskirche in Frankfurt, he outlined the government's position on troops in

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<sup>71</sup> FRUS 1961-63, IX, p.94-96.

<sup>72</sup> FRUS 1961-63, IX, Rusk to Kennedy, 18.9.1963; this memo was based on NA, RG 59, SF 1963, DEF 1US, Box 3746, Johnson to Rusk, 16.9.1963. See also: *ibid.*, Kitchen to Rusk, 19.9.1963.

<sup>73</sup> FRUS 1961-63, IX, Dillon to LBJ, 2 December 1963.

<sup>74</sup> FRUS 1961-63, IX, Bundy Memorandum for the Record, 23.9.1963, p.97-98.

<sup>75</sup> *ibid.*, NSAM 270, 29.10.1963, p.98-100.

Europe in a phrase which should from then on become the official line on the subject for the succeeding years: *'We have six divisions in Germany. We intend to maintain these divisions here as long as there is need for them -and under present circumstances there is no doubt that they will continue to be needed.'*<sup>76</sup> The same statement was repeated by Kennedy in a press conference a few days later. The President reaffirmed that apart from some streamlining of non-combat personnel, the US would keep its six divisions in Europe 'as long as they are required.'<sup>77</sup> No specific definition of this 'need' was given, and, likewise, no specific conditions were attached to the pledge. The discussion within the government had, however, stopped just short of linking the pledge directly with the continuation of offset. It was only a very small step towards the establishment of such a link as official policy; a majority in the US government probably already adhered to this view. Large-scale plans to reduce the troops in Europe were blocked for the following years; the 'streamlining', however, continued. At some moment during 1965, the official line changed: 'six' was supplemented by 'five'.<sup>78</sup>

#### d) The Offset/Troop-Level Link becomes Official Policy

It came as a surprise to the Americans when, in summer 1963, on the occasion of a 600 men thinout in the Berlin garrison, the German government protested at the highest level. Adenauer personally intervened with Rusk. He argued that during the present negotiations on the nuclear testban treaty those reductions seemed a compliment for Khrushchev.<sup>79</sup> The negotiations had renewed Adenauer's suspicions about an impending deal between the Soviet Union and the United States. He was particularly vexed about a possible inclusion of East Germany as a contracting party.<sup>80</sup> This might have constituted an implicit recognition of the East German state and thus undermined the 'Hallstein doctrine', a center piece of German foreign policy which held that West Germany alone represented the whole of Germany. Adenauer thought any detente moves potentially dangerous as they all moved towards some

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<sup>76</sup> DAFR 1963, Adress by Secretary of State Rusk in the Paulskirche, Frankfurt, 27.10.1963, p.220.

<sup>77</sup> *ibid.*, p.222-3.

<sup>78</sup> PSSD, reel XIII, p.781.

<sup>79</sup> AAPD 1963, Rusk-Adenauer Conversation, 10.8.1963, p.973-75; *ibid.*; Knappstein to Carstens, 9.8.1963, p.965-67.

<sup>80</sup> Schwarz (1991), p.846-51.

recognition of the Status Quo. For the US government, however, the Cuban crisis had marked the climax of the Cold War and any new conflict on European issues would have been extremely inconvenient due to the increasing American involvement in Vietnam.

When the German Foreign Minister Schröder visited Washington in September, Kennedy tried to reassure the Germans and indicated that the US had decided against troop cuts at the present moment. Schröder repeatedly stated that the German government was not against any reductions as long as there was consultation well in advance and time to prepare the public opinion.<sup>81</sup> The President agreed with Schröder on this point. It may, however, well be that both men had a different idea of consultation. Schröder would have hardly accepted the definition of 'consultation' outlined in NSAM 270: *'Possible redeployments of US forces under consideration within the government should not be discussed publicly nor with our allies until a decision has been made and a politico-military plan for action approved. Following these steps, we should consult as appropriate with our allies before any public announcement is made, and then proceed with our intended actions. Wherever possible, action of low visibility should be taken without public announcement.'*<sup>82</sup>

Whatever reassurance the Germans had taken from the Kennedy-Schröder talk, it was badly shaken by a series of official and unofficial public statements in the US soon afterwards. First, Eisenhower gave a widely reported interview where he recommended drawing down forces in Europe to one division.<sup>83</sup> Then, on 19 October, Gilpatric delivered a speech which seemed to indicate reductions in connection with military exercise BIG LIFT in which the US trained the moving of large forces from the US to Europe and back. *'By employing such a multi-base capability the U.S. should be able to make useful reductions in its heavy overseas military expenditures without diminishing its effective military strength or its capacity to apply that strength swiftly in support of its world-wide policy commitments.'*<sup>84</sup> These remarks were accompanied by similar statements from Senators and other leading personalities, producing

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<sup>81</sup> FRUS 1961-63, IX, Kennedy-Schroeder Conversation, p.86-87.

<sup>82</sup> FRUS 1961-63, IX, NSAM 270, p.99.

<sup>83</sup> Williams (1985), p.137-38.

<sup>84</sup> AAPD 1963, p.1365, fn.3.

headlines in German newspapers.<sup>85</sup>

The timing of these announcements was particularly unfortunate from a German point of view. The remarks occurred in the first weeks of Erhard's chancellorship. The former Economics Minister had assumed the post only after long and bitter resistance by Adenauer who had humiliated his rival consistently.<sup>86</sup> Erhard's arrival was linked with a distinct reorientation of German foreign policy towards repairing the damaged relationship with the United States and taking a more independent stance towards de Gaulle. Discontent with Adenauer's one-sided inclination towards France had been a major factor in increasing inner-party criticism directed against the aging Chancellor. However, Adenauer was not so easily put off. He kept the chairmanship of the CDU, and thus retained a major voice in German politics. Together with other heavy-weights, like Franz-Josef Strauß, he made no secret about his dislike for the 'atlanticist' orientation of his successor's foreign policy. Domestic debates on foreign policy were for the following years to be shaped mainly by this conflict between 'Atlanticists' and 'Gaullists'. News of impending US troop reductions therefore undercut the new Chancellor's policy which was founded upon the steadfastness of the US commitment in Europe.<sup>87</sup> They looked like a vote of no-confidence for the new government and reinforced the arguments of de Gaulle and his supporters in Germany. The US troop presence had always been a major domestic issue in Germany; now it became directly linked with the fate of the Chancellor.

Erhard and Schröder immediately voiced their concern about the statements of Eisenhower and Gilpatric to the American ambassador, McGhee.<sup>88</sup> The Germans repeated their apprehensions to Rusk on his visit in October. The Secretary of State showed them the draft of his Frankfurt speech and repeated the assurances of the ambassador, not without saying that

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<sup>85</sup> For example: FR, 21.10.1963, 'Gilpatric Announces Troop Cut'.

<sup>86</sup> Körfer, *Kampf ums Kanzleramt*, 1988.

<sup>87</sup> This point was brought to the President's attention by McGhee; see: McGhee-Kennedy conversation, 19 September 1963, McGhee Papers, 1988 add., Box 1.

<sup>88</sup> AAPD 1963, Erhard-McGhee Conversation, 22.10.1963; Schroeder-McGhee, 22.10.63, p.1359-71.



the Federal Republic should take a broader look at the worldwide responsibilities of the US.<sup>89</sup> In his meeting with Defence Minister von Hassel, the Secretary of State stated that the US position was influenced by two aspects. *'(1) If NATO does not meet its force goals - and most member countries have not- how can we explain it to our people and justify our continuing to meet our goals? (2) The offset. If our gold flow is not brought under control, the question could become an issue in next year's elections. The continuation of Germany's payments under the offset agreement is vital in this respect.'*<sup>90</sup> There was hardly any doubt left what the condition for the continued US troop presence was. The German government did not feel reassured by Rusk's speech. Talks with other countries affected by reductions reaffirmed their apprehensions.<sup>91</sup> The assassination of Kennedy in November 1963 evoked new uncertainty concerning the future course of American foreign policy. It therefore became a major objective of Erhard to obtain a commitment of the new President to the assurances Rusk had given in his Frankfurt speech.

Lyndon B. Johnson sought to follow the policies of his predecessor. However, on the troop level issue the situation was still in flux. Despite the public assurances, the planning for further reductions had continued. Kennedy himself seemed eager to continue with the reappraisal.<sup>92</sup> He had given orders to develop plans for implementing the elements of the McNamara proposals which had not been approved in October.<sup>93</sup> However, firm decisions were still pending.<sup>94</sup> This was the situation when Erhard went to Washington, shortly after the inauguration of Johnson as successor of Kennedy.

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<sup>89</sup> *ibid.*, Erhard-Rusk, 25.10.1963; Schröder-Rusk, 26.10.1963, p.1384-97.

<sup>90</sup> McGhee Papers, 1988 add, Box 1, Memorandum on von Hassel Rusk talks, 25.10.1963.

<sup>91</sup> The Japanese Foreign Minister, Ohira, reported US plans for deep cuts in US forces in Japan, and the British Labour Deputy, Brown, claimed during a conversation with Schröder that Kennedy in person had given him the impression that the US would withdraw soon. See: AAPD 1963, Ohira-Schröder, 7/8.11.1963, p.1421-22; Carstens-Brown, 27.11.1963, p.1507-09.

<sup>92</sup> JFKL, OHI R.G.Gilpatric, p.83-84.

<sup>93</sup> DDRS 1992/3513, Background Paper for Erhard Visit: US Force Levels in Europe, 19.11.1963; NA, RG 59, SF 63, Box 3749, DEF6-8US/NATO, Johnson to Rusk, 21.10.63.

<sup>94</sup> McGhee Papers, 1988add., Box 1, MAAG to Ambassador, 18.12.1963.

Dillon had furnished the new president with several memoranda for the meeting emphasizing the importance of the balance of payments problem. He termed the deficit and the gold drain the most serious present threat to American political and military leadership. According to Dillon, it had been caused in large part by military spending overseas and he felt the Germans should be made to realize their crucial role in this matter. *'If Germany wants the United States to continue its commitments in support of the Alliance, Germany must be as helpful as possible in correcting pressures on our balance of payments.'*<sup>95</sup> He urged the President to press for lower German interest rates, for a continuation of the policy of not exchanging dollars to gold, and, above all, for a firm offset commitment. *'In view of our recent public assurances of our intention to maintain the present level of our combat forces in Germany "as long as they are required", it would seem appropriate and important to obtain Erhard's assurance that the FRG will continue to fully offset U.S. dollar expenditures in Germany both in new orders and in actual payments for "as long as may be required". It would seem to me that failure of the FRG...to fully offset our defense expenditures in Germany would be as clear evidence as we could have that the current level of U.S. forces in Germany was no longer required.'*<sup>96</sup>

Johnson followed this advice though he did not explicitly link offset with the troop level. In his talks with Erhard, however, he repeatedly underlined the importance he attached to the continuation of offset.<sup>97</sup> During a car trip on the grounds of the Johnson Ranch with the President personally behind the wheel, he pointed to the mounting criticism in his country because US troops remained now in Europe for such a long time despite modern airlift capabilities and the unfair division of burdens. Erhard insisted on the absolute necessity of maintaining existing troop levels and underlined this with the remark that in his opinion the GI's felt very happy in Germany. Johnson quipped that he was sure they would feel even

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<sup>95</sup> LBJL, NSF, Country file: Germany, Box 190, Dillon to LBJ, 13.12.1963; see also: *ibid.*, Dillon to President: Late Report on Germany and our Payments Deficit, 20.12.1963; DDRS 1980/435A, Dillon to President, 18.12.1963.

<sup>96</sup> LBJL, NSF, Country File: Germany, Box 190, Dillon to President: German Offset Agreement, 13.12.1963; see also: DDRS 1995/199, Bator to Bromley Smith outlining the President's position on offset, 6.5.1964: *'1. The U.S. prefers the status quo. 2. The status quo, however, has two components: offset purchases in the previousl agreed amounts and force levels. 3. If the Germans unilaterally alter the status quo by not living up to their offset commitments, we shall certainly be forced to reconsider the question of force levels'*.

<sup>97</sup> For the talks on 28/29 December, see: AAPD 1963, p.1672-1713; specifically p.1673-74, 1696.

better at home.<sup>98</sup> The communique of the meeting contained a repetition of Rusk's assurance in Frankfurt as well as a principal commitment of Erhard to the continuation of offset.<sup>99</sup>

The meeting made clear that pressure in the US on the issue of troop levels would continue. The only change was one of emphasis: whereas Kennedy was haunted by the fear of gold losses, Johnson was more receptive to congressional criticism. The most important factor in the communique was the offset-troop level link which was implicit in it. With the onset of the Johnson administration, this became official policy for a majority in the US government. During the months to come, the Americans sought to put Erhard's principal promise into an agreed payments scheme for the 1962 agreement as well as to prepare the ground for a new agreement. There would be several opportunities to get the new policy across.

In April 1964, McNamara sent a draft memorandum for a new agreement covering the years 1965/66. He intended to sign this memorandum on his visit to Germany in May. The German officials felt unease at the prospect of formalizing their Chancellor's promise of December 1963.<sup>100</sup> The Finance and the Economics Ministries expressed doubts whether the defence budgets of the succeeding years would be high enough to continue the practice of offset by military procurement. State Secretary Hopf from the BMVg agreed with these doubts, citing additionally the pressure from domestic armaments industries and increasing European co-production. However, as AA and Chancellory officials explained, the political importance of continuing with the agreement had priority over these concerns. There were no illusions about the American insistence on a continuation of offset, though the Germans hoped they would be able to avoid a direct link between troop levels and offset.<sup>101</sup> A formula pointing to the uncertainty of future military procurement levels was to be inserted to any new memorandum of understanding.<sup>102</sup>

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<sup>98</sup> *ibid.*, Erhard-Johnson Conversation in Stonewall/Texas, 28.12.1963, p.1699-1701.

<sup>99</sup> EA 19/1963, p.D33-34.

<sup>100</sup> AAPD 1964, Interdepartmental Meeting of German Ministries, 4.5.1964, p.504-06; BA, B136/3133, memo for cabinet meeting, 5.5.1964.

<sup>101</sup> PA-AA, B150/27/4, Memorandum Ref.II(II6): Frage eines Junktims zwischen...Truppenstationierung...und Rüstungskäufen, 24 April 1964.

<sup>102</sup> AAPD 1964, Interdepartmental Meeting, 4 May 1964, p.504-06.

In May 1964, McNamara arrived in Bonn with two major objectives: to consummate the third offset agreement and to urge the Federal Government to come forward with tangible help in Vietnam. Erhard was non-committal as regards Vietnam. He added that it would be problematic to continue offset on previous levels due to budgetary problems and the increasing competition from German domestic industry for arms orders.<sup>103</sup> McNamara remarked that Germany would do better to manufacture for its exports than shifting to the production of military equipment. He concluded the exchange emphasizing the US *'just cannot continue to maintain [its] forces in Germany without full offset payments.'*<sup>104</sup> In his conversation with von Hassel the Secretary of Defense was even more outspoken: *'He wished to make clear that he was making no threats, but it would be absolutely impossible for the United States to accept the gold drain caused by the U.S. forces in Germany, if Germany did not assist through continuation of the Offset Agreement.'*<sup>105</sup> Von Hassel responded only *'yes, yes'* and reminded McNamara that the German cabinet would not like such a link. The Secretary agreed that the link should not be made public, but *'privately there must be an association'*.<sup>106</sup>

This was the bluntest reminder of the offset-troop link the German government had ever received and thereafter that the German government could have had no illusions regarding the condition for the maintenance of the US troop level. Whether this threat was decisive for the signing of a further memorandum of understanding on the same day is difficult to determine, given the scarcity of German documents. The Erhard government, in any case, accepted the commitment in order to preserve its overriding foreign policy priority: undisturbed relations with the United States. That this was an uncertain bet on the future was clear to all informed and there were many signs of misgivings within the government, not least in the memorandum itself which has been published in parts recently.<sup>107</sup> The yearly rate of payments for 1965/66 was fixed at \$1.35bn. The protocol contained a proviso that the

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<sup>103</sup> McGhee (1989), p.143-45; McGhee Papers, Bonn 1514: Offset Agreement, 11.5.1964.

<sup>104</sup> *ibid.*

<sup>105</sup> DDRS 1995/3179, McNamara - von Hassel Talk, 11 May 1964.

<sup>106</sup> *ibid.*

<sup>107</sup> AAPD, 1964, p.125, fn.2.

contracting parties were aware of the difficulties regarding fulfilment of offset by military payments. This would only be possible if a corresponding need for weapons existed for the German forces and if satisfying this need from US sources made economic sense. In case a full military offset was not possible, negotiations should take place to determine other methods of offset.<sup>108</sup> This wording is open to quite a degree of interpretation. Thereafter, the US left no doubts regarding its insistence on full military offset. However, it would seem that the Germans rightly felt that they were not obliged to meet this goal under all circumstances. We will refer back to this when dealing with the big crisis of offset in autumn 1966 (see ch.XI, fn.4).

The US administration tried to get the commitment reaffirmed on the occasion of Erhard's visit in June 1964. Only the State Department still put up some resistance against the rapid erosion of the rationales which had once led the US government to station more than 300.000 men in Europe. In a memorandum for the President, McGeorge Bundy expressed the new logic bluntly: *'I myself agree with Dillon and McNamara, who argue that we should closely link the offset agreements and our ability to maintain troop levels. The Secretary of State --or his advisers-- say that this linkage would be "short-sighted and untrue". I doubt if he is right, since our troop levels in Germany are justified, finally, more by the psychological needs of the Germans than by strategic necessity. If the Germans will not pay for psychological comfort, why should we?'*<sup>109</sup> When the President mentioned the problem in his talk with Erhard and expressed his expectation for full offset, Erhard reassured the President in this point.<sup>110</sup> Again he emphasized the preeminence of the German-American alliance in all his considerations. He had few choices left between an unbending Cold War policy, punctuated by a few timid steps of Ostpolitik, and an equally unflinching repudiation of Gaullist policies.

Internally, however, the German government was increasingly preoccupied. Very soon it became all too obvious that Erhard's promise was far from easy to fulfil. It was clear that a

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<sup>108</sup> *ibid.*

<sup>109</sup> LBJL, Country File: Germany, Box 191, 11 June 1964.

<sup>110</sup> AAPD 1964, Conversation Johnson-Erhard, 12 June 1964, p.656-659.

new offset pattern would require an initiative at the highest level.<sup>111</sup> This did not happen, neither in 1964 nor in 1965.

e) Offset and German Defence Budget, 1965

During 1965, German payments were falling more and more behind the schedule. When the Americans received first reports about the lag in meeting the offset-commitment, they interpreted it as the recurrence of problems with previous agreements which in the end, despite many complaints by the Germans, had always been fulfilled. This was a mistaken assumption. It was precisely the fulfillment of the previous agreement which had heavily mortgaged the 1965/67 offset. To meet the payment goal of the second memorandum of understanding in time, the German defence ministry had advanced huge payments to the US Treasury account destined for purchases of weapons. Much of these advanced payments were on orders which would be delivered much later, and even on orders not yet placed.<sup>112</sup> The BMVg thus had reinitiated the policy of advance payments on armaments orders which had been so common in the 1950s. The problem was that this time a major build-up phase was nowhere in sight. Both military and economic reasons meditated against a further increase in the Bundeswehr equipment. The American embassy was advised of these problems during several briefings by BMVg officials. According to them, the German forces had reached their 'consolidation phase' after the rapid build-up during the Berlin Wall crisis.<sup>113</sup> They were fully equipped with modern material, up to the point that they lacked trained personnel to use their weapons as well as storage sites to protect them. Numerous indications show that the saturation point might have been reached already in 1963/64 when Germany, on a large scale, began to give away military surplus material. Countries 'benefitting' were Israel, Greece,

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<sup>111</sup> *ibid.*, AA memorandum, 28 December 1964, p.1565-7.

<sup>112</sup> McGhee Papers, 1988 add., Box 1, Bonn A-341: Review of Recent Trends and Future Prospects of the German Defense Program and the Offset Agreement, 30 August 1965.

<sup>113</sup> *ibid.*; see also: *ibid.*, Blaser to McGhee: Outlook for the Offset Agreement as revealed by the Attitude of the Germans during Mr.Kuss' visit, 8 October 1965.

Turkey as well as numerous developing countries.<sup>114</sup>

Another structural problem accompanying the 'consolidation' of the German forces was the rapid increase in operating costs, such as wages, social benefits, repair of equipment, etc. This was intensified by strong competition for manpower by the German industry in a labour market which was close to full employment, leading to a general rise in German wages during these years. Consequently, the share of funds earmarked for procurement declined in case of a stagnating defence budget.

According to the BMVg officials, it was also the unclear military strategic situation in the Alliance which suggested the discontinuation of the immense procurement program of the early 1960s. The debate evoked by the new strategic ideas of the Kennedy administration was still unresolved. The intricate discussion about future NATO strategy almost paralysed NATO military planning; the French completely refused to go along, and the British pursued their own agenda, largely dictated by economic objectives. The MLF was in a state of agony since the end of 1964, and only the German government still stood firmly behind the idea. Force planning exercises for the late 1960s were of course volatile and superficial in this situation, and nobody knew exactly on which kind of forces and on how many the NATO alliance would agree in the end.<sup>115</sup> This was not the ideal situation for continuing with major investment in new weapons systems. Nor did the trend towards detente with the Eastern bloc add incentives to invest in new arms. The absence of a crisis situation in Europe made neither rapid agreement on strategic concepts nor heightened military preparations seem very likely.

Even if the circumstances described above had been more conducive towards a continuation of offset, the German government would still have faced another major problem: where to get the money from to pay for new purchases. The years 1965/66 saw the Erhard government desperately struggling to balance its budget. During the election year 1965 the government

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<sup>114</sup> The old M48 tanks, for example, were transferred via Italy to Israel, based on an understanding between Erhard and LBJ; see: DDRS 95/924, Department of State to Bonn embassy, 18 June 1964; AAPD 1964, Memo Ministerialdirektor Dr.Sachs, 22 December 1964, p.1559; AAPD 1965, Memo Carstens: Appendix IV: Conversation Schröder, von Hassel, Carstens, 29 July 1963, p.11. Thiel, *Dollar-Dominanz, Lastenteilung und Amerikanische Truppenpräsenz in Europa*, 1979, p.46.

<sup>115</sup> Haftendorn, *Kernwaffen und die Glaubwürdigkeit der Allianz. Die NATO-Krise von 1966/67*, 1994.

had greatly expanded social programs for veterans, families, farmers and elderly people; it had lowered taxes, and introduced a broad array of subventions amounting to over DM 6bn.<sup>116</sup> Already before the elections the Finance Minister warned Erhard of the imminent unsettling of the budget and the government tried to put on some breaks.<sup>117</sup> The elections in October 1965 were a big triumph for Erhard. The investment had paid off; however, the bill was presented immediately. Required by the constitution to present a balanced budget, the government had to cut back government programs on all levels and to go back on some of the election promises. The damage for Erhard was considerable. Even in its reduced form, the budget still rested on the assumption of greatly increased tax revenues in 1966. The defence budget had been particularly affected by the cutbacks. It stagnated at DM17.5bn (in comparison: 1962, DM14.9bn; 1963, DM 18.3bn; 1964, 19.1bn; 1965, DM17.3bn).<sup>118</sup> Because of the inevitable rise of fixed costs this particularly curtailed the available funds for procurement.

From mid-1965 onwards, almost no new orders and payments were made. The American government realised that intervention on the highest level was needed. Erhard's visit in December 1965 presented the obvious opportunity. State disagreed again with Treasury and Defense as to how strongly offset was to be linked to troop levels; all agreed, however, that the President should press the Chancellor strongly to fulfill the agreement.<sup>119</sup> According to McGhee, Johnson spared no effort. 'Towering' over the Chancellor, 'gesticulating and speaking in a strong strident voice', he lectured Erhard like a school boy.<sup>120</sup> The President was incensed at the lack of German support in the Vietnam theatre. On top of that, they would not even honour their offset commitments.<sup>121</sup> Johnson said that the quarterly balance

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<sup>116</sup> SPIEGEL 43/1966, 17.10.1966; Hildebrand, *Von Erhard zur Grossen Koalition*, 1983, p.123-126.

<sup>117</sup> *ibid.*, p.135.

<sup>118</sup> McGhee Papers, 1988 add, Box 1, memcon Dahlgrün-McGhee, 9 November 1965; Blaser to McGhee, 8 October 1965. This figures should not be confounded with the actual expenditure detailed in table 1, App.I.

<sup>119</sup> DDRS 1995/200, Position Paper on Offset for Erhard visit, 15 December 1965.

<sup>120</sup> McGhee, *Present at the Creation*, 1988, p.183-5; see also: McGhee Papers, 1988 add, Box 1, memcon Erhard-LBJ, III of III, 20 December 1965; McGhee to Leddy, 13 January 1966.

<sup>121</sup> AAPD 1965, Erhard-Johnson conversation, 20 December 1965, p.1938-42.



of payments figures would soon be published and demanded an immediate lump sum payment of \$100m. Erhard emphasized his own difficulties and promised to do what he could. In their last meeting, after the communique had already been formulated, the President came back again on these points. He *'asked the Chancellor if he understood correctly that the FRG would honour the (offset) agreement. The Chancellor nodded agreement'*.<sup>122</sup> The communique stated that the offset *'agreements were of great value to both governments and should be fully executed and continued.'*<sup>123</sup> This rather unenthusiastic approval of Erhard's was interpreted by the Americans as a new fixed commitment.

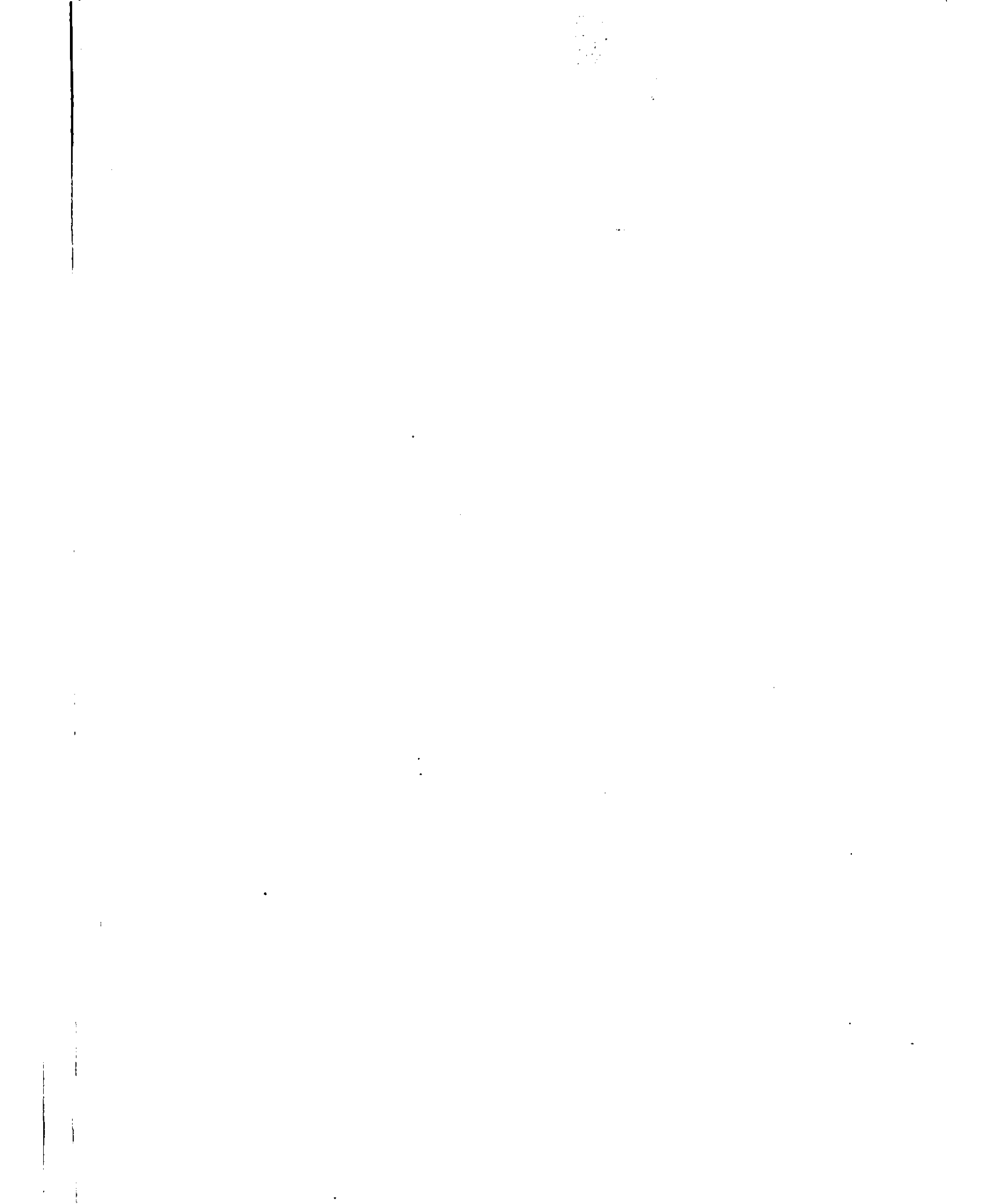
This raises the question as to why the German government did not try to renegotiate the agreement instead of committing itself to new payments which it knew it would hardly be able to make. Certainly, the Germans were up for heavy weather if they approached the US with such proposals but it would seem an alternative preferable to the certain risk of a major embarrassment when the cards had to be put on the table. The scarcity of German sources allows only hypothetical answers to this question. Preparatory efforts for renegotiations were apparently made. Already by the end of 1964, the AA planned to approach the *BMVg*, formally responsible for offset, with such an initiative. However, the project was repeatedly delayed and nothing happened.<sup>124</sup> A major reason for this was probably the prospect of a major row with the Americans during the election year 1965. Erhard would not open this Pandora box. After his triumph in October, he might have entertained some hopes that he could get some concessions without a major crisis; the treatment during his December visit in Washington dispersed those quickly. Instead of taking an initiative, the German government hoped that the situation might resolve itself by muddling through. However, it could hardly foresee that during the year of 1966 a series of unforeseen circumstances would propel offset to a central place in German-American relations and in the domestic discussion of both countries.

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<sup>122</sup> McGhee Papers, 1988 add., Box 1, memcon LBJ-Erhard, 21.12.1965.

<sup>123</sup> PP Johnson 1965, pt.II, p.1165-7.

<sup>124</sup> AAPD 1964, note Ministerialdirektor Sachs, 28.12.1964, p.1565-67, esp. fn.13.



## CHAPTER X

**THE CULMINATION OF THE BURDEN-SHARING CONFLICT: CHANCELLOR ERHARD'S VISIT TO WASHINGTON, SEPTEMBER 1966**

## a) The McNamara - Von Hassel Meeting, May 1966

This chapter resumes all the threads laid out in the previous ones in order to give a comprehensive picture of the crisis in which many of these developments culminated. During Chancellor Erhard's visit to Washington in September 1966, and the months that preceded it, all the problems inherent in the offset conflict emerged to the surface, interrelating and reinforcing each other, resulting in a postwar low in German-American and German-British relations.<sup>1</sup>

Most German experts concerned with the execution of the offset agreements became quickly aware that a continuation of full offset by purchases of weapons after 1967 was practically impossible. It also became apparent that the targets agreed upon in the von Hassel-McNamara protocol of 1964 would be reached -if at all- only by counting non-military purchases or other substitutes. During a cabinet meeting in March 1966, the Ministers of Defence and Finance as well as the Bundesbank, which began to take part in the deliberations concerning offset, noted furthermore that without a supplementary budget later in the year it would be impossible to honour the agreement.<sup>2</sup> The ministers foresaw a prospective gap of about \$700m in orders at the end of 1966 and of \$1130m in payments in June 1967. The decision to proceed with a supplementary budget, however, was postponed because it would have required difficult compromises among the parties (CDU/CSU/FDP) of the strained coalition government in Bonn. It was decided to sound out first the Americans as to their acceptance of alternatives to arms purchases.

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<sup>1</sup> German-British Offset, which during the early 1960s had been marginalized compared with the scope of the US-FRG agreements, plays an important role in this context. A short account of German-British offset, 1960-66, will be inserted as necessary background.

<sup>2</sup> Military Diary von Hassel, entry of 25 March 1966; BA, B136/3135, Excerpt from the 20th Cabinet Meeting, 25 March 1966; Osterheld, *Aussenpolitik unter Bundeskanzler Erhard*, 1992, p.304.

On 14 May, von Hassel and McNamara met in Washington. The German Defence Minister disclosed publicly that he expected a payment gap of \$600m in 1967 when the term of the agreement ended, and that the German government wanted to abolish the strict formula of offset by military orders. Von Hassel's appeal failed. McNamara retorted that in this case the U.S. would reduce its forces in proportion to the payment gap.<sup>3</sup> These statements provoked a strong public reaction, and angry comments in Germany.<sup>4</sup> The spokesman of the German government denied the existence of any linkage between troop levels and offset payments.<sup>5</sup> Erhard complained to Secretary of State Rusk that announcements such as McNamara's were highly embarrassing for his government.<sup>6</sup> On the otherhand, however, von Hassel reasserted once more in public that the German government had every intention of fulfilling the offset agreement.<sup>7</sup> Subsequently, the Americans tried to calm the debate and denied any plan to withdraw any significant number of troops from Europe.<sup>8</sup>

After the row, the public increasingly took note of the problem and speculations regarding troop-levels and offset continued all through summer 1966. Offset which until then had played only a marginal role in public debates suddenly became a big issue. The press and parliaments in both countries regularly brought the matter up. This came at a moment when both the offset and the troop level problem were approaching a critical point where top-level intervention and difficult compromises would be required to get out of the deadlock. The circumstances for such an effort turned out to be extremely unfavourable. A series of domestic and international developments exacerbated the prospects for a smooth solution and seriously limited the bargaining space of both the German and the American governments (not

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<sup>3</sup> 'The Secretary stated further that he must point out, as he has in the past, that unless a full offset agreement is attained with the Federal Republic, the U.S. would be required to reduce its forces to the level of the offset goals' LBJL, NSF, NSC Histories: Trilaterals, Box 51, Background Paper: US/German Military Offset Relationship, November 1966; see also: NHP, von Hassel note on talks with McNamara and Acheson, 15 May 1966; SZ, 16 May 1966; FAZ, 16 May 1966; NYT, 6 June 1966, p.40; Raj, *American Military in Europe*, 1983, p.220-23.

<sup>4</sup> Grabbe, *Unionsparteien, Sozialdemokratie und Vereinigte Staaten von Amerika, 1945-66*, 1983, p.531.

<sup>5</sup> FAZ, 17 May 1966.

<sup>6</sup> McGhee Papers, 1988 add., Box 2, Rusk-Erhard conversation, 9 June 1966.

<sup>7</sup> Von Hassel in parliament, 1 July 1966, in: VdB, 5th period, 54.sess., p.2609-2613.

<sup>8</sup> Press Conference Johnson, McNamara, Rusk, 11 June 1966, in: PSSD, pt 3, reel IV, 0007; Press Conference Rusk, 27 May, in: DOS Bulletin, 13 June 1966.

to speak of the British). These developments exposed all the contradictions inherent in the traditional offset approach. The issue became a focus for the multi-faceted crisis of the Western Alliance in the mid-1960s, combining political, economic, and military aspects.

In this chapter, I will first outline the developments in the international field which made the offset problem so difficult to solve (the NATO crisis, Vietnam, the British offset picture, developments in the monetary field). Then I will analyze the increasing domestic pressure which built up against the German and American governments. Finally, Erhard's abortive and fatal attempt to renegotiate the offset agreement during his September 1966 visit in Washington will be described in detail. The chapter aims to place the offset conflict in a variety of contexts in order to give a comprehensive picture of the issues involved in the offset problem during the 1960s.

#### b) NATO Crisis and International Monetary Problems in the Mid-Sixties

McNamara's public troop reduction threat came at a particularly inconvenient moment for the Erhard-government. In March, the withdrawal of 30000 combat personnel from the 7th army, the American forces in Germany, had become known. The German government had not been consulted, and the news that those forces would be substituted to the last man by recruits failed to reassure the Germans. Actually, a thinning-out process had been going on for quite some time. The State Department had told its missions abroad to remain silent on the issue and to '*avoid to extent possible further categoric statements on the maintenance of present composition and number of our forces*'.<sup>9</sup> However, the changes could not go unnoticed, particularly as the reductions concerned mainly highly trained personnel.<sup>10</sup> The logical conclusion to which most observers came was that the moves had something to do with

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<sup>9</sup> FRUS 1964-68, XIII, DOS to US Mission at NATO, 9 December 1965. For the German reaction: NHP, Talking Paper for Meeting with General Wheeler, 9 April 1966; Rühl, Neue Ziele im Atlantischen Bündnis, in: Kaiser/Mende(eds), *Die Internationale Politik 1968/69*, 1974, p.322-323; Haftendorn, *Kernwaffen und die Glaubwürdigkeit der Allianz*, 1994, p.227-28.

<sup>10</sup> DDRS 1995/2652, Cleveland to Rusk and McNamara, 19 May 1966.

Vietnam. With increasing irritation, the US government denied those charges.<sup>11</sup> Persistent questioning in Senate Hearings, however, evoked a comment by McNamara that the reductions would 'probably not' have been effected without Vietnam.<sup>12</sup>

Such contradictions hardly calmed down the suspicions on part of the German government. The substantial thinning out -in both quality and quantity- became the subject of extensive discussion in the media. Particularly galling for the German government was that, against their promises, the Americans had not consulted Erhard. Only after repeated requests they disclosed details of the operation. Internally, the German government resigned itself from then on to the unavailability of large-scale reductions in the near future.<sup>13</sup> Due to its beleaguered position in foreign policy issues in the domestic debate, however, it felt unable to abandon a stance which had been a dogma of German policy since 1955. Those critics who saw the US on their way towards a concentration on Asia and an accommodation with Soviet Russia in the European theatre would have taken US reductions as a confirmation of their analysis. The Erhard government therefore tried to postpone the inevitable withdrawal as long as possible, and to avoid offset becoming the excuse for the Americans.

The unquestionable weakening of American combat power in Germany was aggravated by another event which rocked the foundations of NATO: the French withdrawal from the military organisation of NATO, and de Gaulle's announcement that all foreign forces and installations would have to leave French territory by 1 April 1967.<sup>14</sup> The events and the

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<sup>11</sup> See McNamara's reaction at a press conference on 2 March 1966: 'Let me answer your question. Where are you from?' Questioner: 'From Germany.' McN.: 'It is absolutely not true and you are the first that ought to know it. I am sick and tired of having implications made that we have drawn down the forces in Western Europe when we haven't. The 7th Army...will not be affected...by our operations in South East Asia', in: PSSD, XIV, p.1396.

<sup>12</sup> *ibid.*, Hearing before the Senate Committee on Foreign Relations, 20 April 1966, p.2127.

<sup>13</sup> 'In the long run, US troop reductions will be inevitable. It is, however, essential to maintain during the negotiations with the U.S.A. that troop reductions should take place only when the strategic, operational, and military-political preconditions are more favourable than at the moment'; NHP, Talking Papers for Chancellor-Minister talks in Washington, 20 September 1966; Personal Diary von Hassel, Entries of 23 July and 3 August 1966.

<sup>14</sup> For pertinent documentation, see: FRUS 1964-68, XIII; EA 21/1966, D228-240.

political-military consequences of this move have been discussed extensively elsewhere.<sup>15</sup> I will concentrate on the impact of de Gaulle's move on the offset conflict.

The United States had long been expecting a French action. Earlier on, it started with contingency planning in case its troops had to leave French territory.<sup>16</sup> This allowed for a relatively calm reaction, memorably summarized by Johnson with the words: 'If a man asks you to leave his house, you don't argue; you take your hat and go.'<sup>17</sup> Walking out had even some advantages: a part of the 75000 US personnel in France was redeployed inconspicuously to the US.<sup>18</sup> Air force units were relocated to UK bases and helped the British to some additional foreign exchange earnings.<sup>19</sup> These economic 'gains', however, were offset by the interruption of the US logistics system concentrated in France and the removal of the NATO headquarters, both of which involved heavy expenses. Estimated at between \$175-\$275m, this cost was a major element of the US government's discussions on the consequences of the French move.<sup>20</sup> The German-American payments balance also was affected. Certain military installations, such as the US army headquarters, were moved to Germany, and provision and supplies had to be re-routed to German and Benelux ports.<sup>21</sup> The Bundesbank estimated that this reorganization would increase the US forces' foreign exchange need from DM5.4bn(\$1.35bn) envisaged in the offset agreement to DM6.3bn(\$1.575bn). This precipitate rise in the cost, which was exacerbated by pay and wage rises, obliterated all savings the Pentagon had achieved in the last years. Naturally, this lessened the American willingness to compromise on offset.

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<sup>15</sup> Haftendorn (1994), p.209-227; Harrison M., *The Reluctant Ally*, 1981; Costigliola, *France and the United States. The Cold Alliance since World War II*, 1992; Gardner, in: Paxton, *De Gaulle and the United States. A Centennial Reappraisal*, 1994, p.257-278; Institut de Gaulle(ed), *De Gaulle et son Siecle*, vol.4, 1992; Vaisse/Mélandri/Bozo(eds), *La France et l'OTAN 1949-96*, 1996.

<sup>16</sup> LBJL, NSF: Memos to the President: McG.Bundy, Box 3, Bohlen to Rusk, 4 May 1965; Bator Papers, Box 3, Memo for the President: de Gaulle and NATO, 3 March 1966.

<sup>17</sup> Johnson, *The Vantage Point*, 1971, p.305.

<sup>18</sup> 18.000 military personnel and 21000 dependents were reduced. Prospective foreign exchange savings were estimated at about \$110m/year; FRUS 1964-68, XIII, Talking Paper prepared by Dept. of Defense, July 1968, p.729.

<sup>19</sup> LBJL, NSF, Bator Papers, Box 3, Fowler to President: Sterling Crisis, 18 July 1966.

<sup>20</sup> FRUS 1964-68, XIII, Summary Notes of 566th NSC Meeting, 13 December 1966.

<sup>21</sup> Rühl, in: Kaiser/Mende et.al.(eds), *Die Internationale Politik 1968/69*, 1974, p.323-325.

De Gaulle's move had not only financial and logistic consequences, it also cast grave doubts upon the continuing rationality of the Western security structure. Because NATO troops stationed along the 'Iron Curtain' had lost their *hinterland*, the military sense of their mission was put into question. The reaction in the United States and Great Britain was that the already undermined political and military rationale of conventional troop maintenance was further damaged. In West Germany, the effect was the reverse: the dependence on conventional protection offered by the Anglo-Saxons grew. The status of the French forces in Germany (about 71000 men), which were withdrawn from SACEUR command from 1 July on, was in a limbo until the end of 1966. Initially the German reaction, mainly advocated by Foreign Minister Schröder, was to insist on a clear NATO commitment for these troops, particularly in war-time operations. The French refused, and, in the end, a more conciliatory attitude was pursued by Erhard, tacitly supported by the Americans.<sup>22</sup> This was a major political defeat for Schröder, who was to play a rather passive role in the final months of the Erhard-government.<sup>23</sup> In all, the French action deepened the feeling of insecurity on side of the Germans and like many of de Gaulle's policies, served to underline German dependence on US protection. On the other hand, it heightened American frustration with the situation in Europe. It was a major point for those who argued that Europe did not only not need, but actually did not want a direct commitment from the US any more.<sup>24</sup>

The main reason for the growth of this sentiment was, however, the escalation of the war in Vietnam. During 1965 American military involvement in South East Asia multiplied. The war absorbed public attention increasingly, and dominated all activities of the government. Europe became a distant theatre with no major crisis expected.<sup>25</sup> This had a deep influence on US

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<sup>22</sup> Ample documentation on this issue and the whole France-NATO crisis is in FRUS 1964-68, XIII. For a German view, see: NHP, Talking Papers for Chancellor/Minister visit to Washington, September 1966: Status of Negotiations regarding Cooperation of French Forces with NATO.

<sup>23</sup> Grabbe (1983), p.528-29.

<sup>24</sup> Williams, *The Senate and U.S. Troops in Europe*, 1985, p.140-141.

<sup>25</sup> For the impact of the Vietnam War on US-European relations: Knapp, *Vietnam als Belastung des Verhältnisses zwischen den Vereinigten Staaten und ihren Verbündeten*, in: Carstens/Mende(eds), *Die internationale Politik 1966/67*, 1971, p.70-73; Grosser, *The Western Alliance*, 1980, p.237-43. The recent study of Arenth, *Johnson, Vietnam und der Westen*, 1994, -descriptive, tiresomely repetitive, and full of confounded platitudes,- is useful only in so far as it shows how not to write diplomatic history.



policy towards Europe. The progressive thin-out of US forces in Europe has been already mentioned. A parallel development was the precipitate fall in the quality of the troops.<sup>26</sup> Vietnam also played a major role in American efforts to formulate a detente policy towards the Soviet Union, summed up in Johnson's bridge-building speech in October 1966.<sup>27</sup> Speculation about a reorientation of American policy towards the Pacific became a preferred issue of political commentators on both sides of the Atlantic. As the struggle in Asia intensified, the US government became increasingly interested in some sort of accommodation with the Soviet Union in Europe, whereas Bonn still clinged to the reunification postulate, opposing most steps by the Americans to reduce tensions in Europe.

The American willingness to support the German viewpoint was not increased by the European response to the new core problem of the American containment strategy, the Vietnam War. In the US, frustration about Europe's lukewarm response towards the American effort in Vietnam ran high. Angry memoranda by the American government did nothing to change this stance, and a perception of European ingratitude permeated comments in the government, Congress, and the press.<sup>28</sup> Why should the United States continue to make sacrifices for the defence of Europe, if the Europeans would not lend a helping hand to their partners in an emergency?

Vietnam also had a heavy impact on the US balance of payments; in what manner and to what extent exactly is a question still to be answered by economic historians. Some basic observations, however, can be made. The rise of the foreign exchange cost directly related to the escalation is impressive: from 1964 to 1967, outlays in South East Asia rose from \$847m to \$2318m.<sup>29</sup> Parts of this loss was offset by various agreements similar to the ones concluded in Europe. Nonetheless, the burden remained immense. The Administrative History

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<sup>26</sup> There was a serious lack of officers and specialists. Criminal incidents abounded, drug use and racial conflicts became major problems. See: Nelson, *A History of U.S. Forces in Germany*, 1987, p.83-84.

<sup>27</sup> PP Johnson 1966, p.1125-30; Hanrieder, *Germany, America, Europe*, 1989, p.90.

<sup>28</sup> For an aide-memoire to the FRG requesting a whole list of possible German aid projects for South Vietnam, see: McGhee Papers, 1988 add., Box 1, 6 July 1964.

<sup>29</sup> Shepler/Campbell, *US Defense Expenditure Abroad*, in: SCB 12/1969, p.44. Countries with the biggest increases between 1964-67 were Vietnam (\$64m to \$564m); Japan (\$321m to \$538m); Thailand (\$34m to \$286m); Korea (\$91m to \$237m). The liquidity deficit in 1967 was \$4.89bn.

of the Treasury during the Johnson-Administration summed up: *'There was tacit recognition during 1966 that the efforts to achieve equilibrium in our balance of payments would not be successful as long as the hostilities in Vietnam continued on such a large scale'*.<sup>30</sup> This statement also takes into account indirect effects of the war. The rapid rise of government spending in defence, supplemented by the effects of the parallel 'Great Society' program, led to an economic expansion which, in the absence of tax rises, put increasing pressure on prices. The trade balance was unsettled by the related augmentation of domestic demand.<sup>31</sup> These developments produced increasing apprehensions in the Department of Treasury that the balance of payments might have got out of control. Estimates of the year-end deficit went to about \$2bn, despite 'cosmetic' operations to the tune of \$1.5bn.<sup>32</sup> Additionally, there was the incalculable risk of a run on Sterling. All this came on top of heavy gold losses, particularly in 1965.

The main reason for this was another de Gaulle challenge. During a press conference in February 1965 the General denounced the dollar-gold system as an instrument of American hegemony, enabling the United States to buy up with cheap money foreign industries.<sup>33</sup> Therefore, he urged all dollar holding countries to present their dollars at the US Treasury so as to undermine the dollar-gold standard. In the first quarter of 1965, the US Treasury lost \$3.244bn of gold (\$1.928bn of it to France), from April to June another \$1.198bn (French quota: \$0.592bn).<sup>34</sup> The only reason why the United States were able to withstand the challenge was that all major gold-holding countries reacted with disapproval to de Gaulle's

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<sup>30</sup> LBJL, *Administrative History Treasury*, vol.1, pt.II, ch.IX: Balance of payments.

<sup>31</sup> Solomon, *The International Monetary System, 1945-76*, 1977, p.100-102; on the economic policy of the Johnson-administration: Kettl and Kaufman, in: Divine R.A., *The Johnson Years, Vol.II*, 1987, p.54-109.

<sup>32</sup> The 'cosmetic' operations consisted mainly in switches by Foreign Central Banks from liquid dollar holdings to longer-term securities; LBJL, NSF, Memos to the President: W.Rostow, Box 9, Bator to President: Balance of Payments, 6 July 1966. It was enough to prolong 12-month bonds to 13 months to make them disappear from the statistics of liquid liabilities, which formed part of the liquidity balance (the overall measure for the US balance of payments until the late 1960s); Gilbert, *Quest for World Monetary Order*, 1980, p.140.

<sup>33</sup> De Gaulle, *Discours et Messages, 1962-65*, 1969, p.330-34. For de Gaulle's attack on the gold standard, see: Calleo, 'De Gaulle and the Monetary System: The Golden Rule', in: Paxton/Wahl(eds), *De Gaulle and the United States*, 1994, p.239-255; Institut de Gaulle(ed), *De Gaulle et son Siècle, Vol.III: Moderniser la France*, 1992; Bordo/Simard/White, 'France and the Bretton Woods International Monetary System, 1960-68', in: Reis(ed), *International Monetary Systems in Historical Perspective*, 1995, p.153-80.

<sup>34</sup> Odell, (1982), p.119. At the end of 1964, US gold reserves stood at \$15.47bn.

suggestion. If they had followed the example, the monetary system would have collapsed. Its preservation, however, was still in the interest of most countries, not least because the decisive countries were almost all linked in a security partnership with the US. This was especially the case of the Federal Republic, which due to its large reserves played a pivotal role.<sup>35</sup> To refrain from gold conversions was not particularly difficult for the Germans at that time. From 1963 to 1965 they had balance of payments deficits which they financed by reducing their dollar reserves.<sup>36</sup>

The US government immediately issued a new statement after the de Gaulle challenge committing itself unswervingly to the \$35/ounce ratio. This stifled internal voices for parity changes.<sup>37</sup> However, the new Treasury Secretary, Fowler, knew that determination and piecemeal measures à la Dillon/Roosa would not do anymore. The US therefore took the lead in proposing a new reserve unit, initiating years of discussions with the Europeans, which eventually led to the establishment of the so-called Special Drawing Rights.<sup>38</sup> The complicated negotiating process was continuously disturbed by the developments outlined above. It was clear that the dollar-gold system was on the brink. The accumulation of these dangerous signals made the short-term balance of payments the prevalent consideration of US officials in dealing with the issues posed by Erhard's visit in September.

Both in the monetary and the security field, the situation reached a critical point in 1966. The fundamental bases of the transatlantic relations thus entered into a crisis at the same time

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<sup>35</sup> De Gaulle elaborated on his main argument, namely that the reserve role of the dollar liberated the United States from monetary discipline and allowed US firms to buy up foreign industries with cheap credit, already in January 1965 at the occasion of Erhard's visit in Paris. He did not inform his visitor of the spectacular step he was to take only two weeks later; AAPD 1965, Conversation Erhard-De Gaulle, 20 January 1965, p.150. The German government immediately disassociated itself from the move. It expressed, however, to the Americans similar concerns about the high level of US investment abroad which forced Germany to balance the monetary consequences by way of Offset; AAPD 1965, Erhard-McGhee conversation, 8 February 1965; p.270-73; Knappstein to Schröder on talk with the President, 9 February 1965, p.282.

<sup>36</sup> The Bundesbank President, Blessing, informed Erhard that following de Gaulle's example, as some economists had proposed, made no economic sense under these circumstances. He assured Erhard that the Bundesbank had ways of converting foreign exchange surpluses to gold without drawing directly on US reserves; see: BA, B136/3322, Blessing to Erhard, 22 February 1965. See also Appendix I, table 1.

<sup>37</sup> Gilbert (1983), p.136-37.

<sup>38</sup> The most comprehensive analysis of the creation of SDRs remains Cohen, *International Monetary Reform, 1964-69*, 1970.

when the offset practice was running into almost insurmountable practical difficulties, in the German-American as well as in the Anglo-German context.

### c) British Offset During the 1960s

The final spark which forced the US to tackle the mass of problems which had accumulated in Europe in 1966, was a crisis in Anglo-German offset dealings. Compared with the amounts of money and the serious implications for Western financial and security policy involved in US-German offset, the parallelly pursued British-German offset was but a sideshow - a very noisy one, however. The British took the issue as serious as they had done during the 1950s.<sup>39</sup> A great many of complicated questions were raised during the negotiations and a complete detailed account would go beyond the scope of this thesis. I will give a brief survey of story and issues, concentrating on the aspects which are important to the main argument of the thesis.

We left the British-German offset quarrel at the end of 1958 when, after tiresome complications, an agreement was reached covering the three years until March 1961 (see ch.IV). This had removed the issue for some time from the mutual agenda. The basic causes for the conflict, however, had not disappeared. The British government still regarded their continental commitment with ambiguity and the pound remained weak, betraying the illusions HMG might have entertained during a period of calm in the foreign exchange markets. In 1960 it seemed as if the British currency had finally reached a stable level. The British government was able to pay back large parts of the debts it had amassed during and after the Suez-Crisis.

This was warmly welcomed by the Americans as they struggled with their emerging and persistent payments problem. One result of their efforts drew particular attention in London:

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<sup>39</sup> Historical research has been less impressed by its importance. British-German offset in the 1960s is a virtually uncultivated field, despite the abundance of material available in German and British archives. Whightman (1988) gives a brief, coherent account, p.38-40. Further details in Schmidt, *Die Labour-Regierung, die Bundesrepublik und Europa, 1964-67*, in: Schmidt (1989), p.253-314, Mendershausen (1968), and Haftendorf (1994), p.227-241.

the Anderson-Dillon mission. As their three-year agreement was about to expire, the British were afraid -not without reason- to be left out in the cold by a massive German-American deal.<sup>40</sup> More importantly, the London gold crisis in October 1960 and the speculation following the revaluation of the German DM in March 1961 vividly demonstrated the continuing weakness of Sterling. A new agreement seemed therefore imperative, particularly because the government ruled out the possibility of further troop cuts. First, the Berlin Crisis was still in full swing, second, the BAOR was already under strength drawing increasing criticism from NATO authorities, and third, a reduction *'could not fail to wreck such hopes as exist for a settlement of our European problems and it must bedevil our relations with the new American administration from the start.'*<sup>41</sup> These remarks hinted at Kennedy's requests on the British to live up to their conventional troop commitments to NATO, and at the need to get German political support regarding the British EEC-membership application of July 1961.<sup>42</sup>

However, the British were not prepared to absorb the foreign exchange burden of their troops just for the sake of these political gains. In March 1961, Selwyn Lloyd, now Chancellor of the Exchequer, arrived in Bonn for a new round of talks.<sup>43</sup> As during the Anderson-Dillon visit, the Germans resisted any attempt to renew direct payments. The British accepted that the support-cost concept was out of date. The negotiations took a similar turn as the preceding US-German ones. The German side promised to step up arms purchases in the UK (to about DM280m a year), to assume more foreign aid, to prematurely repay their remaining postwar debt, and to leave a £25m sum, which was the remainder of German prepayments on arms orders, in the Bank of England.<sup>44</sup> Satisfaction with this unbinding promise did not last very

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<sup>40</sup> *'...if we let the Americans get away with a deal in which our more real and pressing needs are overlooked, it will be a fatal blow'*, Macmillan to Treasury, 14 November 1960, PRO, PREM 3773.

<sup>41</sup> *ibid.*, Report by Treasury Officials on Mutual Defence Costs, 5 December 1960. Kennedy informed Macmillan immediately of the new US emphasis on conventional troops which he expected the UK to follow. See: NSA, The Berlin Crisis, Doc.2024, Macmillan-Kennedy Meeting, 5 April 1961.

<sup>42</sup> FRUS 1961-63, XIII, Kennedy to Macmillan, 16 February 1962, p.1059-61; PRO, PREM 11/4217, Home to Macmillan, 14 February 1962; *ibid.*, Meeting at Admiralty House, 12 March 1962.

<sup>43</sup> PRO, CAB 129/105, Anglo-German talks, 23 March 1961.

<sup>44</sup> KCA 1961, 18002A.

long. In July 1961, Britain invoked the NATO resolution of 1957 which requested NATO to investigate and propose solutions for countries in payments difficulties due to troop stationing abroad.<sup>45</sup> The NATO experts supported the British case and the Germans agreed to open formal negotiations. These were clearly prejudiced by the parallel German-American talks which were in their final phase. The Strauß-Gilpatric agreement in October 1961 put the British and the French in an even more disadvantageous situation on the German arms market than before. Soon it became clear that the Germans would not formalize the promises given to Lloyd in March. They also refused to offset the whole British troop cost, contrary to the agreement with the Americans.<sup>46</sup>

In the end, the British accepted less than full offset - a result which owed much to the political considerations outlined above.<sup>47</sup> They also agreed, first, to count 'civilian purchases' as offset and, second, to consider the assumption of British foreign aid obligations by the German government as offset measure.<sup>48</sup> Both provisions caused endless quarrels between officials from the Federal Ministry of Finance and the British Treasury on the kinds of projects to be credited against the German obligation.

The agreement was signed in March 1962.<sup>49</sup> It covered April 1962 through March 1964. The sum of DM1200m (\$300m) was split up in military purchases(DM920m), civilian purchases(DM180m), and DM100m for foreign aid projects. Difficulties in reaching these targets soon arose. The Germans viewed British goods as uncompetitive.<sup>50</sup> British weapons were considered as second rate quality, not fit for the kind of military operations German

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<sup>45</sup> NA, RG 84, Bonn Embassy 1959-61, Box 16, Airgram A-11: UK Statement at NATO Council Meeting, 27 July 1961; KCA 1961, 18443.

<sup>46</sup> This put the Americans in an uneasy position which should last for many years. On the one side, they wanted the British to keep their troops in full strength and the pound strong, and supported the British offset efforts, on the other side, they were not ready to share part of the German weapons market.

<sup>47</sup> A folder with extensive documentation on the negotiations is in: BBA, A270/13168; an account by British officials is PRO, FO 371/172175, Stationing Costs of British Forces in Germany: Report by Officials, autumn 1963.

<sup>48</sup> 'Civilian purchases' meant orders of civilian equipment above normal levels by official German agencies; purchases of goods for the foreign aid projects Germany financed were to be placed in England.

<sup>49</sup> HMSO, Cmnd.1766 (1962).

<sup>50</sup> BA, B136/3133, memorandum for cabinet meeting, 29 September 1961.

planners foresaw, and generally disadvantaged because of the British reluctance to agree to common research projects.<sup>51</sup> In April 1963, German orders had reached a level of only about DM400m. Further prospects were bleak, and the British government officially stated its disbelief in the German capability to see through their promise.<sup>52</sup> The overall political situation in which the agreement operated had also changed for worse. The EEC application had been checked by the General, and the Americans seemed to have second thoughts on the wisdom of a further conventional build-up. The British Defence White Paper of 1962 clearly demonstrated the doubts of the Conservative government about its European commitment.<sup>53</sup> Although the British Cabinet Defence Committee once more decided to avoid troop reductions in Germany, it was obvious that the firmness of this resolve hinged on the status of sterling.<sup>54</sup>

The lingering hostility towards Germany in financial matters remained strong, as a handwritten note of Macmillan on a memorandum regarding a Schröder-Lord Home discussion illustrates: *'It is a very depressing story. The Germans have no sense of guilt and shame...there is nothing about the financial agreement, on which they are in default. What about the huge commitment to buy American? Every time they mention Eastern Germany, we ought to remind them of the intolerable financial situation.'*<sup>55</sup> This comment on the troop cost problem, shortly before Macmillan left office, struck once more the emotional tone which had pervaded so much of the conflict in the preceding years. The trace of hostile remarks left by the Prime Minister in connection with this problem shows some characteristics of his policy towards Germany: a sense of frustration at the inexorable falling behind of Britain's economy; an unwillingness to cooperate with the former enemy which had so rapidly been

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<sup>51</sup> Interview of the author with Minister von Hassel, 17 August 1994. BA, B136/6894, BMV to Erhard: Technological cooperation with Britain in the Military Field, 18 May 1966. British sales consisted as during the 1950s mostly of minor items, like tank guns and spare parts; see: NA, RG59, SF 1963, FN15WGER, Box 3455, Bonn A-2535: UK-RG Offset Agreements, 5 June 1963. Not only regarding quality but also in the professional manner of selling the British had nothing to equal the Americans.

<sup>52</sup> BA, B136/3133, AA to Chancellor's Office: Cabinet Memorandum, 25 May 1963.

<sup>53</sup> Darby, *British Defence Policy East of Suez, 1947-68*, 1973, p.223-27.

<sup>54</sup> PRO, PREM 11/4726, Thorneycroft to Macmillan, 24 April 1963.

<sup>55</sup> PRO, PREM 11/4259, Macmillan to Lord Home, 21 August 1963.

rehabilitated; a strong insistence on the symbols of British power, nuclear weapons and the reserve role of sterling; the annoyance about being stuck in Europe with troops whose military importance seemed doubtful, of whom Germany benefitted economically, and whose political importance Macmillan saw mainly in relations to the US, but not to the Federal Republic. Thus, support costs and offset acquired a disproportionate place in determining the state of Anglo-German relations. Macmillan's position on the support cost question lacked flexibility which was characteristic of the whole British approach to Germany during those years. This approach reflected the state of the debate in the British press and parliament.<sup>56</sup> Few steps were taken by the Macmillan government to get out of this cul-de-sac in mutual relations. After all, Britain did not have much to offer as compensation if it was not ready to support the rigid German position in the East-West conflict.

The 1962-64 agreement was fulfilled by the Germans despite British apprehensions. This was probably due to a change to leaders who were more cooperative than the Macmillan-Adenauer duo. Erhard and Alec Douglas-Home both assumed office in October 1963. The snag of the offset success was that it had only been possible by large prepayments on prospective military and civilian orders (the civilian part of the agreement had turned out an almost complete flop). The next agreement was heavily mortgaged.

Negotiations commenced in late 1963.<sup>57</sup> The German government wanted to abolish the foreign aid and the 'civilian' component which had drawn increasing criticism from the German industry. Furthermore, it wanted to reduce the military order targets.<sup>58</sup> The negotiations were concluded in a quite cooperative mood in April 1964, due to the relative calm in monetary markets and the absence of troop reduction threats. The Germans, originally proposing a two-year level of DM500m(\$125m) for military orders, agreed in the end that they would try to offset the whole estimated £84m(\$235m) foreign exchange cost 'as far as

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<sup>56</sup> Watt, *Britain looks to Germany*, London 1965, p.130-45.

<sup>57</sup> The Federal Ministry of Finance had waged and lost a fight in the cabinet to get rid of its responsibility for the talks. PRO, FO 371/172174, Roberts to Reilly, 10 September 1963; Melville to Reilly, 20 September 1963; Bonn embassy to FO, 8 October 1963; PA-AA, Ref IIIA5, 384, Dahlgrün to Westrick, 24 January 1964.

<sup>58</sup> AAPD 1964, Erhard/Douglas-Home talks, 15 January 1964, p.62-63; Memorandum Lahr (State Secretary, AA), 3 January 1964, p.8-9.



possible', counting also civilian purchases.<sup>59</sup> The British accepted that no fixed target should be set; a crucial difference to the American-German agreement of May 1964. They had early on resigned themselves to getting less than the US. An unspecified commitment was thought to be more acceptable to the public than a specified level far short of the actual cost.<sup>60</sup> A mutual working group was established which was to meet regularly to identify projects and review the progress made.

Shortly after the agreement was signed, general elections were held in Britain resulting in a Labour-victory. The new government under Harold Wilson had hardly settled down when a new violent currency crisis rocked the boat. The election campaign had been accompanied by speculation caused by the political uncertainty and rumours of a prospective £800m payments deficit in 1964. During November, an unprecedented run on British reserves ensued. Within two days, the new government had made its mind up and decided firmly against devaluation.<sup>61</sup>

The reasons were mainly political: apprehensions that Labour, after it had devalued the pound in 1949, would retain the stigma of a devaluation party, the moral commitment to the Commonwealth and other dollar holders, and the belief that it were structural weaknesses in the British economy which caused the pressure on the pound and which could be corrected by measures to improve the competitiveness of British goods. Diagnosis and reactions were strikingly similar to Kennedy's response to the US payments deficit some years earlier. Like the Democratic president, the Labour Prime Minister was elected on a very small margin and shied away from showing supposed 'weakness' in monetary policy, laying the emphasis of his action on strengthening the domestic economy. Devaluation acquired a status of 'the unmentionable'. An effective ban against even discussing the issue stifled the debate within

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<sup>59</sup> For the agreement: HMSO, Cmnd.2434 (1964). For the negotiations: BA, B136/3133, Memorandum for Cabinet Meeting, 9 March 1964; Dahlgrün to Erhard, 23 March 1964; Dahlgrün to Erhard, 15 May 1964; AAPD 1964, Memorandum Carstens, 29 April 1964, p.495-96; Carstens to Dahlgrün, 6 July 1964, p.796-97; Memorandum Lahr (AA), 24 July 1964, p.877-78.

<sup>60</sup> PRO, CAB 128/38, CM 64(39), concl., 17 July 1964; CM 64(41), 23 July 1964; CAB 129/118, CP(64)155, Memo by Chief Secretary to Treasury, Boyd-Carpenter, 22 July 1964.

<sup>61</sup> Wilson, *The Labour Government 1964-1970*, 1971, p.5-7. Browning, *The Treasury & Economic Policy 1964-85*, 1986, p.5; Woodward, *Labour's Economic Performance*, in: Coopey/Fielding/Tiratsoo(eds), *The Wilson Governments, 1964-70*, 1993, p.82-3.

the government, and even the British press, then more patriotic than nowadays, shied back from speculation.<sup>62</sup>

On 16 November, Wilson declared emphatically: *'If anyone, at home or abroad, doubts the firmness of the government's resolve and acts upon these doubts let them be prepared to pay the price.'*<sup>63</sup> No speculator felt deterred, and the government was forced to various restrictive measures, such as a 15% surcharge on imports, which ignited both EEC and EFTA countries and violated GATT rules. A belated rise in the interest rate did not help either and only annoyed the US, which had had solemn promises to the contrary.<sup>64</sup> The sterling crisis of November 1964 was overcome only by a hastily organized international credit of \$3bn, later supplemented by a \$1bn drawing from the IMF.<sup>65</sup> It showed the British dilemma clearly: either they had to take measures which irritated their major allies or they had to accept their 'help' or 'recommendations', and take vigorous actions in the domestic economy which often were among the conditions for help.

The Federal Republic played a central role in the international rescue effort of December 1964. In this context, the Germans were urged by some Americans, like Ball and Acheson, to use their monetary leverage to get the British to full-heartedly support the MLF.<sup>66</sup> I have found no direct proof that the Germans followed this advice. The Americans felt fewer inhibitions. For them, either devaluation or a large reduction in Britain's overseas defence expenditure was unacceptable as it was thought to have unforeseeable repercussions on the dollar position or on the Western and Pacific security structure. They, therefore, felt a strong temptation to use their good services in preserving the sterling value in order to get British assurances on these points.

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<sup>62</sup> G.Brown, *In My Way*, 1971, p.114; Cairncross/Eichengreen, *Sterling in Decline*, 1983, p.166-67; Browning (1986), p.5.

<sup>63</sup> Quoted from Cairncross/Eichengreen (1983), p.169.

<sup>64</sup> The step forced the US to do likewise, and LBJ did not hide his irritation on the occasion of Wilson's first visit; FRUS 1964-68, XIII, McG.Bundy Memo on LBJ-Wilson conversation, 7 December 1964, p.137-39.

<sup>65</sup> A vivid description of the international rescue action by one of the participants is provided by Coombs, *The Arena of International Finance*, 1976, p.110-23.

<sup>66</sup> AAPD 1964, Schröder to Erhard, 26 November 1964, p.1404-05.

Taking stock after the storm on the markets had passed, the Labour government, like its predecessors, took British overseas expenditure under closer scrutiny. Probably even less than Macmillan, Wilson had a clear idea as to what purpose the Rhine Army should still serve. The offset agreement he had inherited he considered insufficient. Already the first meeting of the mixed working group for the implementation of the offset agreement, in December 1964, had shown the new government's discontent with the achievement of their predecessors. The British noted the absence of any significant German requests for British civilian or military goods, and did not hide their disappointment.<sup>67</sup>

One specific project acquired particular importance in this context. London pressed for a positive decision of the German *Lufthansa* to purchase the BAC 1-11 aircraft for its fleet, an order of probably over \$50m. The UK representatives put on the record that a *'rejection would be regarded as an indication that the offset agreement meant little to the German side.'*<sup>68</sup> The *Lufthansa* order was deemed essential for the success of the aircraft on the European market where not a single order had been accrued until then.<sup>69</sup> During his first meeting with Erhard, Wilson strongly pressed the case citing the disappointing German performance under the offset agreement.<sup>70</sup> Once more, the British had to compete against an American producer, Boeing. The US ambassador in Bonn intervened on the highest political levels to support the American aircraft - a further instance for the contradictory nature of US policy towards British financial problems.<sup>71</sup> In the end, it was the alleged technical superiority of the US aircraft which was decisive for the *Lufthansa* managers, despite an intervention of Erhard on behalf of the British firm.<sup>72</sup> Her Majesty's government was not amused.

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<sup>67</sup> BA, B126/34106, Record of Meeting of Joint Committee in London, 8 December 1964; B136/3133, German embassy London to AA, 8 December 1964.

<sup>68</sup> *ibid.*

<sup>69</sup> PRO, FO371/183099, FO Brief for Bonn talks 1/1965: Offset Agreement.

<sup>70</sup> PRO, FO 371/183042, Record of PM-Erhard discussion, 30 January 1965; also in: AAPD 1965, p.224.

<sup>71</sup> Osterheld (1992), p.125-26; BA, B136/3133, Federal Ministry of Transport to AA, 14 December 1964.

<sup>72</sup> BA, B136/3133, Dahlgrün to Chancellor's office, 25 February 1965; Erhard to Abs, 4 March 1965.

When Wilson visited Bonn in March 1965, he told Erhard that he was '*profoundly disappointed, surprised and shocked*' by the Lufthansa decision and that he regarded the whole offset agreement as 'dirty work' which had to be renegotiated.<sup>73</sup> In a letter soon afterwards the Prime Minister warned the German government of any '*misunderstanding between us on the importance of this question for the future development of good Anglo-German relations*'. He added that the British had taken the firm decision that while '*naturally they wish to play their full part in the common defence of the West, they can no longer accept the very large share which they have to bear of the foreign exchange burden of maintaining British forces in Germany at its present level of £90 million a year.*'<sup>74</sup>

With this letter the acrimony which had marked British-German offset dealings in the Macmillan era had returned. The troop cost issue proved to be no less disruptive for Anglo-German relations than under the Conservative government. This is also reflected in Wilson's letter to the American President, in which he reviewed the proceedings of his meeting with Erhard. The Prime Minister displayed no intention to make any constructive move towards ameliorating and intensifying British relations with West Germany, despite the opportunity the anglophile Erhard government represented. He assumed that the Federal Republic would continue its support for the pound in the international markets and that it would also offset the foreign exchange cost of British troops: '*We had some very tough sessions on the offset agreement but since you have yourselves virtually equipped the German armed forces there does not seem much for us in that line...We left the Germans in no doubt that if we did not get satisfaction on this part, we should be forced to agonizing re-appraisals*'.<sup>75</sup>

The frustration resulting from the feeling of growing financial dependency on an ally (particularly obvious during the late-1964 attack on Sterling) which, on the other hand, was protected by a British security commitment reached new peaks. The Chief Secretary of Treasury, Diamond, mentioned this frankly during the offset re-negotiations in Bonn: '*In order that Britain should never again need to seek emergency assistance from its Allies, the*

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<sup>73</sup> PRO, FO 371/183046, Record of Wilson-Erhard discussion, 8 March 1965, 8am.

<sup>74</sup> BA, B136/3133, Wilson to Erhard, 31 May 1965; Federal Ministry of Finance: Cabinet Paper, 11 June 1965.

<sup>75</sup> FRUS 1964-68, XIII, 11 March 1965, p.190-91.

*British government needed to reorganise its affairs, and, in particular, its expenditure across the exchanges. In many respects British policies were directed and redirected by the balance of payments problem; it lay behind every Cabinet decision concerning economic affairs and defence, and the Government would never feel free to carry out its policies....until it had solved its foreign exchange difficulties.*<sup>76</sup> British FO officials became increasingly preoccupied with the emotional state of government thinking on Germany. Citing a top-level discussion in Chequers, Undersecretary of State Gore-Booth, wrote to his Minister, Michael Stewart: *'One may have what emotions and sentiments one likes about Germans - fair enough. But we cannot conduct...foreign policy like this.'*<sup>77</sup> The Foreign Office tried in the successive months to exert a calming influence on the PM and the Chancellor of Exchequer without much success.

The German government could hardly refuse to re-open the negotiations, due to its failure to come anywhere near its promises to Douglas-Home. At a time when French-German relations were at a low ebb, an open row with Britain would have been doubly inconvenient. The talks started immediately after Wilson's visit to Bonn. In June, Diamond, and the German Finance Minister, Dahlgrün, agreed to extend the existing agreement by one year and to set fixed targets for all three years now covered.<sup>78</sup> A German advance payment of DM464m, additional to the DM336m worth of orders placed until then, brought the level for the first two years up to DM800m. For the third year, the Germans undertook to offset DM 600m(\$150m). With this agreement the German government took up two heavy commitments: first, to equal the advance payment, borrowed from the Bundesbank, by orders until March 1966 or otherwise to repay it out of the Federal budget; second, to identify orders of DM600m in 1966/67.

At the end of 1965, when budgetary problems became apparent, the situation became critical. German officials were desperately seeking suitable projects to fulfil the promised amounts. A Bundesbank memorandum on one of the meetings of the British-German commission

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<sup>76</sup> PRO, FO 371/183101, Record of Dahlgrün-Diamond Meeting, 28 June 1965.

<sup>77</sup> PRO, FO 371/183044, Gore-Booth to Stewart, 15 June 1965.

<sup>78</sup> HMSO, Cmnd 2731 (1965); BPI 112/900, 1 July 1965.

recommended that, before they were forced to pay á fonds perdu, the German ministries should equip their car park with Rolls Royce limousines.<sup>79</sup> The German Finance Minister urged his colleague from Defence to step up military orders; otherwise the government would have to repay the advanced funds from the Federal budget which was already stretched to its limits.<sup>80</sup>

The British meanwhile had other problems. The German prepayment had almost immediately been spent during the next currency crisis in Summer 1965.<sup>81</sup> Again, the British turned to the US for multilateral help, only to hear that strings were attached to such help. McGeorge Bundy wrote to the President in July 1965 that the *'British are constantly trying to make narrow bargains on money while they cut back their wider political and military responsibilities. We want to make it very sure that the British get it into their heads that it makes no sense for us to rescue the pound in a situation in which there is no British flag in Vietnam, and a threatened British thin-out in both East of Suez and in Germany'*.<sup>82</sup> This shows the scope of the intense discussion regarding the nature of those strings which was going on in Washington. Treasury demanded a guarantee against devaluation of Sterling, McNamara urged for an increased British commitment in South East Asia, and the State Department wanted a forthcoming policy towards Germany, including a stable BAOR level.<sup>83</sup> I have no record of the decisive bilateral discussions, but the rescue operation took place successfully, and presumably the Americans put it to the British on all those points,

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<sup>79</sup> BBA, A270/13168, memorandum department A21, 25 October 1965.

<sup>80</sup> BA, B136/3134, Dahlgrün to von Hassel, 20 October 1965.

<sup>81</sup> Crossman, *Crossman Diaries*, vol.1, 1975, p.290.

<sup>82</sup> LBJL, NSF, Memos to the President: McG.Bundy, Box 4, 28 July 1965.

<sup>83</sup> Numerous documents in the LBJ Library relate to this discussion, for ex., Ball Papers, Box 1, telcon Bator-Ball, 27 July 1965; telcon Bundy-Ball, 29 July 1965; NSF, Memos to the President: Bundy, Box 4, McG.Bundy to President: Sterling Devaluation, 28 July 1965; NSF, Country File: UK, Box 215, Ball on Pound Crisis, 6 August 1965; Fowler Papers, Box 4, Ackley to President, 9 August 1965. DDRS 1978/211A, Bator to Bundy: The UK Problem or 'Thinking about the Unthinkable', 29 July 1965. The British were deeply irritated by these requests. To quote from a letter of Wilson to Stewart, 23 March 1965: *'Should the President try to link this question [Vietnam; HZ] with support for the pound I would regard this as most unfortunate...If the financial weakness...is to be used as a means of forcing us to accept unpalatable policies or developments regardless of our thoughts this will raise very wide questions indeed about Anglo-American relationships;* quoted from: Ziegler P., *Wilson. The Authorised Life*, London 1993, p.222-23. For a first assessment of British-American financial diplomacy in this period, see: Kunz, in: Kunz(ed), *The Diplomacy of the Crucial Decade*, 1994, p.80-114.

refraining only from asking for direct military support in Vietnam. In any case, the Labour government was surprisingly cautious regarding the European commitment. The US position was certainly one reason for the absence of serious reductions in overseas defence expenditures in Wilson's austerity program of August 1965.<sup>84</sup> One further reason might have been that just before the 1965 Sterling crisis broke loose, the Wilson government managed to renegotiate the previous offset agreement, and it would have been difficult to justify reductions at this stage.

The restraint lasted until the beginning of 1966. In February, London published a White Paper which mentioned the possibility of troop cuts because the foreign exchange cost of the BAOR was only insufficiently covered by the offset agreement.<sup>85</sup> Negotiations in early 1966 on the implementation of the agreement had become increasingly rough, with the British uttering dark threats and the Germans manoeuvring round the issue.<sup>86</sup> With a vigorous effort, including subsidies to German firms to induce them to place orders in Britain, the Germans reached the 1964/66 target.<sup>87</sup> Sighs of relief were premature. During Erhard's last state visit in London, Wilson and his Chancellor of Exchequer, Jim Callaghan, demanded full offset for 1966/67 instead of 80% as agreed in 1965. This meant transferring an additional DM 500m(\$125m) to the British Treasury. Erhard, deeply in budgetary trouble, refused.<sup>88</sup> Subsequent talks between Callaghan and Dahlgrün brought no results.<sup>89</sup>

The sterling crisis which erupted in mid-1966 added urgency to the British case. Speculation reached new record levels. Including the losses in these months, total British foreign exchange losses in the currency battle had reached a shattering \$4bn of owned and borrowed reserves

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<sup>84</sup> Cairncross/Eichengreen (1983), p.178.

<sup>85</sup> HMSO, Cmnd.2901 (1966).

<sup>86</sup> BA, B136/3134, memorandum on BMF-Treasury Talks, 7 February 1966; attachment to BMF Cabinet Memo, 25 February 1966; B126/34106, BMF memorandum: Offset UK, 29 March 1966.

<sup>87</sup> BA, B136/3134, Memorandum on British Offset, 11 May 1966; PA-AA, IIA7, 835, AA note: Meeting of the Mixed Anglo-German Commission on Offset, 6 April 1966. The German industry protested against such methods; BA, B136/3134, Berg (President of BDI) to Erhard, 17 May 1966.

<sup>88</sup> BA, B136/3134, de la Croix to Dahlgrün, 7 June 1966; Osterheld (1992), p.318-19.

<sup>89</sup> BA, B136/3134, Dahlgrün-Callaghan talks, 30 June 1966.

since the 1964 elections.<sup>90</sup> Though even ministers now recommended devaluation, Wilson decided to hold the line once more.<sup>91</sup> A huge program of deflationary measures (the so-called July program) was hastily pulled together, including a £100m cut in overseas expenditure, a freeze in wages and prices and deflation of domestic demand by various measures designed to check consumption.<sup>92</sup> In his statement in the Commons on 20 July, Wilson announced that expenditure on the BAOR *'would be cut so that total foreign exchange costs were at a level covered by offset and other payments.'*<sup>93</sup> Callaghan was asked to go immediately to Bonn to ask the German government to bring up payments up to the full level of the British foreign exchange cost -to no avail. The Germans told the British flatly that no budgetary funds were available to fulfil their requests.<sup>94</sup> Departing, the Chancellor of the Exchequer made public that London would now start with preparations to reduce its troops. The British government invoked the NATO and WEU procedures for a revision of its NATO commitment.<sup>95</sup> This move, which together with de Gaulle's actions and the German-American problems seemed to forebode the end of the traditional structure of NATO, finally pushed the US government to take the initiative in trying to disentangle the mess.

#### d) Domestic Constraints in Washington and Bonn

Whereas in Britain the troop cost issue always had led to acid comments in parliament and press concerning German stinginess, it had only rarely been a matter of public debate in the German-American context. The far-reaching consequences of the offset agreements were hardly discussed. These 'fortunate' circumstances changed during 1966. The Johnson administration saw itself confronted with a serious motion by Congress members to reduce the American commitment in Europe. One main argument in this debate was insufficient burden-sharing by the Europeans. In the background hovered the nascent struggle between Congress and the Executive in the shadow of the Vietnam quagmire, in which critics of

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<sup>90</sup> Yeager (1976), p.458.

<sup>91</sup> George Brown, (1971), p.114-115.

<sup>92</sup> Wilson (1971), p.258-59.

<sup>93</sup> *ibid.*, p.259.

<sup>94</sup> BBA, A270/13168, Interdepartmental Meeting, 27 June 1966.

<sup>95</sup> Haftendorn (1994), p.232-33.



Johnson's policy emphasized the over-commitment of the United States not only in Asia, but also in Europe.<sup>96</sup>

Ever since the Great Debate in 1951 over the decision to send ground troops on a large scale to the European Cold War theatre, there had been voices in Congress criticising the lasting commitment of the United States in Europe. However, only in 1966 this sentiment took an organized form. What made it doubly inconvenient for the administration was that the initiative originated from the party of the President. In July, the Democratic Majority Policy Committee had expressed its concern about the 'excessive and unchanging' deployment of troops in Europe.<sup>97</sup> Shortly afterwards, a group of eminent Senators introduced a Sense of Senate resolution which, after its main sponsor, the Democratic Majority leader Mike Mansfield, came to be called the Mansfield resolution.<sup>98</sup> Mansfield did not force his resolution to a vote, but the government had received a warning of what was to come.

Already in early 1967 the resolution was re-introduced and the issue of troops in Europe became a major subject of debate between the administration and Congress until the mid-1970s. The Mansfield resolution was not only 'scare tactics'<sup>99</sup> to get the Germans to be forthcoming for offset. Certainly it was of help in this sense and McNamara might have even welcomed it because it gave him further arguments. The White House, however, perceived the move, quite correctly, as an attempt by Senate to regain lost influence in foreign policy formulation. As a result of the Vietnam escalation, Congress had become increasingly restive about its limited influence on foreign policy formulation. The balance of payments, the pressure of military expenditure, prospects of détente, and the prosperity of Europe made the US troops there an obvious target, as long as the majority dared not to challenge Johnson's Vietnam policy directly. The administration tried to keep the situation under control and to preserve its freedom on such a vital foreign policy question. Offset became a weapon in this

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<sup>96</sup> The most comprehensive treatment of this debate is Williams (1985). See also: Thiel (1978), p.157-171.

<sup>97</sup> LBJL, NSF, NSC Histories: Trilaterals, Box 51, Trilaterals Background Paper (DoS/EUR): Mansfield Resolution, 17 November 1966.

<sup>98</sup> Congressional Records, Senate, 31 August 1966, p.20554.

<sup>99</sup> As Nelson (1987), p.82, suggests. Williams (1985) shows the much broader background, p.145.

controversy. In order to defeat the Mansfield initiative the government needed a presentable offset agreement.

The conflict in Germany aimed not only at the Chancellor's authority regarding the formulation of German foreign policy, it also became directly linked with Erhard's political future. Offset was only a side issue in the mid-1960s' acrimonious political controversies in the Federal Republic. In the end, however, it became an important element in Erhard's fall from power.

It had been predictable from the start that Erhard would not have an easy life as Chancellor. Main rivals, like ex-chancellor Adenauer, who was still leader of the Christian Democrats (CDU), the main party forming the government, and Strauß, the chef of the Bavarian counterpart of the CDU, the CSU, remained aloof from the government and kept enough power to exert a strong influence. This was particularly dangerous for Erhard, as a deep rift on foreign policy issues went right through the governing parties ever since the last years of Adenauer's chancellorship. This rift separated the so-called 'Gaullists' from 'Atlanticists'. The former were pleading for a policy of closer alignment to France, more European independence from the US, and resistance against American inclinations to pursue a cautious detente policy.<sup>100</sup> Strauß, for example, strongly emphasized in a letter to Erhard the supposed unreliability of US policy, the consequent danger of being dependent on the American nuclear guarantee, and the necessity to create an independent European deterrent.<sup>101</sup>

The Gaullists stepped up their pressure on Erhard when German-French relations deteriorated and Erhard's government stumbled over numerous other issues. The 'Atlanticists' - Erhard, Foreign Minister Schröder, and von Hassel led this group - emphasized the paramount importance of US-German relations.<sup>102</sup> The debate was intensified, and partly created by

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<sup>100</sup> The most important protagonists of this 'group' (characterized more by their common opposition to Erhard than by the similarity of their political concepts) were former Chancellor Adenauer, former Defense Minister Strauß, the CSU representative Freiherr zu Guttenberg, and the President of the Federal Parliament, Gerstenmaier. For a detailed portrayal of these men and their ideas, see: Grabbe (1983), p.469-489; Laitenberger, *Ludwig Erhard. Der Nationalökonom als Politiker*, 1986, p.168-181.

<sup>101</sup> BA, NL 397, von Guttenberg, 187/1, Strauß to Erhard, 10 November 1965.

<sup>102</sup> The Socialdemocrats also were mostly 'Atlanticist'. See: Grabbe (1983), p.540-88.

domestic rivalries. It can only be understood in this context. Most leading politicians saw Erhard as a Chancellor in transition, and regarded his Foreign Minister Schröder as a main rival in the struggle for succession. Foreign policy became a main battlefield. During 1966, Erhard was increasingly challenged by his opponents. Adenauer continued to publicly criticise Erhard's and Schröder's policy towards de Gaulle.<sup>103</sup> Strauß questioned one of the paradigms of German foreign policy, the insistence on a stable level of allied troops on German soil. In an interview with 'US News & World Report', he argued for a stronger European component in Western defence which then would allow the withdrawal of one or two US divisions.<sup>104</sup> These remarks were promptly cited by McNamara during Congressional hearings as evidence for the European capacity to do more for defence, and for the willingness to accept limited US troop reductions.<sup>105</sup>

As a consequence of the ceaseless pressure, Erhard felt compelled to emphasize the importance of German-American relations in a much stricter way than he would have probably done in the absence of this domestic opposition. A more independent course towards the US would have confirmed his opponents. Unfortunately for Erhard, American policy did not provide much support. He had to take several snubs, all resulting from the questioning of traditional policies towards Europe which was going on in Washington. The arguably most severe blow was the quiet but inexorable dismissal of the MLF by the Johnson administration. Erhard and Schröder had placed their credits on the scheme which should secure the Germans some kind of *Mitspracherecht* (right to say) in the nuclear affairs of the Alliance. Critics like Strauß and, looming in the background, de Gaulle saw it as just another device by the Americans to perpetuate their nuclear hegemony.<sup>106</sup> In 1965/66, the project disappeared

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<sup>103</sup> Göllner, *Politisch-historische Beiträge zu Ludwig Erhard's Kanzlerschaft und Sturz*, phil Diss., 1986, p.120-25.

<sup>104</sup> Time to Start US Pull-back in Europe: Interview with F.J.Strauß, in: US News & World Report, 18 April 1966. See also: Strauß, *Entwurf für Europa*, Stuttgart 1966, p.19 (According to Strauß it wasn't necessary for the Germans, 'to go hysterical every time an American battalion is withdrawn from Europe').

<sup>105</sup> To McNamara, the interview demonstrated that the Europeans were capable of increasing their defence outlays and that the US 'must assume the responsibility for persuading them to do so'; PSSD, XIV, 2207, Hearing before Senate Committee on Appropriations: Foreign Assistance, 89th cong., 2nd sess., 30 April 1966.

<sup>106</sup> On the MLF see: Hoppe, *Zwischen Teilhabe und Mitsprache. Die Nuklearfrage in der Allianzpolitik Deutschlands 1959-1966*, 1993; Kelleher, *Germany and the Politics of Nuclear Weapons*, 1975; Mahnke, *Nukleare Mitwirkung: Die Bundesrepublik Deutschland in der atlantischen Allianz, 1954-1970*, 1972; Steinbruner, *The*

more and more from the agenda, and the only government to still try to keep it alive was Bonn. Erhard also felt undercut because the Americans pursued their cautious *détente* policy without consulting the German government.<sup>107</sup> Conflicts on troop levels and offset came on top of this.

What made the offset issue, in particular, so dangerous for Erhard was that it was connected with the problems his adversaries cited over and over again: the eroding credibility of American policy towards Europe, Erhard's weak leadership qualities, and, finally, the quarrel about the 1966 and 1967 Federal budgets.

Erhard silenced his critics temporarily by an impressive victory in the 1965 federal elections. However, in order to placate and co-opt as many interest groups as possible, the government had greatly expanded public expenditure prior to the elections. About DM 6bn were spent in this effort.<sup>108</sup> The electoral pledges threatened to unsettle the 1966 budget. Some of them had to be revoked almost immediately after the elections. Despite the cuts, government expenditures were running too high and a supplementary budget became necessary to honour the government's offset commitment. The presentation of this appropriation (to the tune of one billion DM) to parliament was, however, delayed until it was too late.<sup>109</sup> A parallel problem was that a balanced budget for 1967 seemed only possible in case of the increased tax revenues or new tough spending cuts which were politically very difficult to sell. At that time, a balanced budget was seen as a central task of the government in public opinion;<sup>110</sup> the Federal Republic had never practised deficit spending. To the contrary, it rather accumulated surpluses, like the *Juliusturm*.

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*Cybernetic Theory of Decision*, 1974.

<sup>107</sup> Hanrieder (1989), p.170-94.

<sup>108</sup> Hildebrand, *Von Erhard zur Grossen Koalition 1963-68*, 1984, p.135; Morsey, *Die Bundesrepublik Deutschland*, 1987, p.86-91; Roepert, *Die D-Mark*, 1979, p.145-47.

<sup>109</sup> In June, von Hassel urged his colleague from Finance, Dahlgrün, to bring the supplementary budget finally on the way; otherwise, the offset agreement was unrealizable. Dahlgrün responded that because of the critical situation of the 1967 budget a supplement for 1966 had to await the passing of the former. In the end, both budgets were approved only after Erhard's fall. See: BA, B136/3231, von Hassel to Dahlgrün, 20 June 1966; Dahlgrün to von Hassel, 22 June 1966.

<sup>110</sup> Fels, *1966/67: Anatomie einer Rezession*, 1988, p.10.

The expansion of government expenditures in 1964/65 fueled a rapidly expanding economy. Prices began to rise perceptibly, endangering the main postulate of German economic policy, the stability of the currency. Consequently, the Bundesbank put on the brakes and pursued an increasingly restrictive credit policy, successful in so far as it decisively slowed down economic activity.<sup>111</sup> Problems such as low investment rates and a contraction of demand came together to produce *angst* of a major recession in the offing. Though modest in its economic effects, the recession had a strong impact on public perception as it was the first economic slow-down since the early 1950s.<sup>112</sup>

An early effect of the slowdown (which was actually to take hold from mid-1966 on) was that the tax revenues the government counted upon were much lower than hoped for. Erhard was forced into a difficult dilemma. All during 1966 the government struggled to fight the recession while at the same time trying to reduce government expenditure. Erhard's authority seriously waned in his own domain, economic policy, and all he could still draw on was his role during the 'Wirtschaftswunder'. During the election campaign for the Land Nordrhein-Westfalen, widely seen as a test for Erhard's government, the Chancellor lost his temper and attacked a crowd of protesting steel- and mine workers: *'And before I go I'd like to tell you louts that you would have perished in your nappies without me and my policy.'*<sup>113</sup> The election result on 10 July 1966 was a resounding victory for the Social Democrats. This blow made Erhard's domestic position almost untenable. His fate became dependent on a solution of the budgetary crisis and, as mentioned above, on a more convincing foreign policy. On both issues, offset had a strong impact.

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<sup>111</sup> From January 1965 to May 1966, the Bank raised the discount rate from 3% to 5%. It repeatedly took the unusual step of criticising the government publicly for its anti-cyclical spending policy. See the speeches by Bundesbank President Blessing 'Central Bank Policy Today', 8 December 1964, and in Mainz, 24 February 1966; in: Blessing, *Im Kampf um Gutes Geld*, 1966, p.185-203, 275-287. See also: Schlesinger/Böckelmann, in: Holbik (ed), *Monetary Policy in Twelve Industrial Countries*, 1973, p.191-195; Röper (1979), p.149-153.

<sup>112</sup> It is probably more correct to speak of a slow-down of growth than of a recession. The figures are not very impressive. The GDP sank by 0.1%, unemployment rose to 2.1% in 1967, and investment stagnated. Nevertheless, the political effect was powerful. First, because certain branches (like mining and steel producing) were strongly affected, and second because of a shaky political climate which tended to produce a flood of alarmed statements, leading to a feeling of crisis which was intensified by the government's inability to get a grip on its budget problems; see: Giersch/Paque/Schmieding, *The Fading Miracle*, 1992, p.142-45; Kießmann, *Zwei Staaten, eine Nation. Deutsche Geschichte 1955-70*, 1988, p.193-199; Fels (1988).

<sup>113</sup> SPIEGEL, 43/1966, p.50.

### e) US Decision-Making prior to Erhard's Visit

With the German government slowly sinking into the budget imbroglio, American apprehensions about the continuation of offset grew rapidly. However, they did not take alarming hints from Bonn regarding the current agreement too seriously. Every agreement had seen a critical phase, yet, in the end, funds had arrived (though the last agreement, as we have seen, was only fulfilled by huge prepayments on future orders). On 5 July, Erhard wrote a letter to Johnson in which he urged for different means of offset *'than the purchase of weapons and military equipment alone. In my view, which I hope, is shared by you, this set of problems should, however, not be linked with the question of the future presence of U.S. troops in Germany. This would be all too easily give rise to an approach that would not do justice to the friendship between our two countries...'*<sup>114</sup> The letter sparked a vivid debate in the US government about the future of offset and, increasingly, also about the future of the commitment in Europe. The front-lines were the same as they had been during the troop reduction debate in 1962/63. For a strict weapons military offset approach and, in case of non-compliance by the FRG, a corresponding reduction of US troops were McNamara's Pentagon, the Treasury Department under Henry Fowler, and, in the background, parts of Congress. A shrinking but still influential group in the State Department, the White House, and the ambassador in Bonn, McGhee, defended the traditional orientation of American policy towards Europe and did not want to see it endangered by a rigid offset policy. President Johnson and Rusk navigated somewhere in the middle until they were forced to take positions.<sup>115</sup>

The loudest voice in this debate, and the one held to be the most decisive by all the literature on the Erhard visit, was certainly the one of Robert Strange McNamara<sup>116</sup> who, due to his

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<sup>114</sup> DDRS 1994/181, Erhard to Johnson, 5 July 1966.

<sup>115</sup> An unsurpassed account of American decision-making prior to the Erhard-visit is Treverton's analysis (1978), p.100-24. The very descriptive account by Schertz, *Die Deutschlandpolitik Kennedy's and Johnson's*, 1992, confines itself to translating almost literally the major documents from the LBJ Library. The following paragraphs try to expand Treverton's analysis by taking a closer look at the structural political and monetary problems involved.

<sup>116</sup> See for example his remarks on offset during a press conference on 6 June 1966: *'This agreement was renewed under the instructions of President Johnson, confirmed by Chancellor Erhard, signed by Minister von Hassel. We fully expect it to be met.'* (PSSD, pt.3, reel XIV, p.12), and, just prior to Erhard's visit, on 15 September: *'Question: Do you want to renew the offset agreement? McN.: Oh, of course, we do! Q.: For military equipment?'*

rigid insistence on a continuation of offset by military purchases, subsequently earned himself the title of a *'tireless arms merchant with shockingly high-pressure sales techniques'*.<sup>117</sup> McNamara's position on offset is usually characterized by such titles and he is portrayed as the main culprit in the deterioration of US-German relations; the roots and motives behind his policy are rarely adequately analysed.

In the following paragraphs I will try to present a more elaborate picture than the usual slogans suggest although the documentary record is still incomplete. It has been suggested that McNamara's stance was only a tactical position, pursued to preserve the American bargaining leverage before the inevitable re-negotiation and diversification of offset would commence.<sup>118</sup> It is true that McNamara showed strong doubts as to the possibility of continuing offset by weapon purchases, at the latest in early 1966.<sup>119</sup> However, he had a real and deep interest in prolonging the military offset scheme as long as possible.

It has been noted before that soon after the first offset agreement had been signed a powerful coalition which benefitted from the agreement had formed in the US government. This coalition included State Department members searching for arguments to preserve an undiminished US presence in Europe, monetary authorities which needed offset to keep the payments deficits under control, and, finally and most insistent, a kind of military-industrial complex which developed out of the enormous sales activities of the Pentagon during the 1960s with West Germany as the main market(see ch.IX). This military sales effort had become the major source of income for the Pentagon. Government-mediated sales were counted on the income side of the Pentagon balances though the benefits went mostly to the about twenty major weapon exporting enterprises. The sales were credited as positive item in the traditionally negative military payments balance which was the target of particularly

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*McN.: Yes,...there is no question that they have a requirement for more military equipment.* (PSSD, pt.3, reel XVIII, p.819-39).

<sup>117</sup> The phrase, repeated in most accounts of the events, had been coined originally by Theo Sommer in his article 'Bonn Changes Course', in FOREIGN AFFAIRS, April 1967, p.477-491.

<sup>118</sup> Raj (1983), p.222-23.

<sup>119</sup> *'Realistically the FRG cannot continue indefinitely to provide a full offset'*, McNamara during a discussion with the UK Foreign and Defence Ministers, 27 January 1966, in: FRUS 1964-68, XIII, p.304.

energetic efforts by McNamara. At times of growing congressional unease regarding the huge defence budget, swollen with Vietnam related expenditures, it became increasingly important to have a guaranteed income and a counterweight to the growth of military expenditure entering the balance of payments. The higher production numbers associated with a successful selling of material abroad also made the Pentagon's own orders cheaper due to the lower cost of producing a bigger output. A sudden reduction of foreign military sales would have unsettled all the savings which had been achieved by McNamara's vigorous managerial programs since the first days of the Kennedy-administration.

McNamara's main concern in the mid-1960s was the conduct of the Vietnam War and the justification of this war at home. This conflicted with the allocation of resources for the European theatre. Offset was vital to balance these contradicting objectives, particularly regarding the payments component of expenditures in Europe. Diversifying offset to other means, such as German investment in Treasury bonds as Erhard had suggested, did not make much difference from an overall balance of payments perspective; it would, however, make a huge difference for McNamara who with one stroke would loose about \$700m a year, if not in budgetary, than at least in foreign exchange terms.

Those were the reasons why McNamara publicly was so outspoken in his insistence on a continuing need for weapon purchases for the German forces. He left no doubt on this matter during Congressional Hearings, when pressed by Senators who demanded a reduction in US forces in Europe<sup>120</sup>, and during his conversations with German representatives. Within the government he fought until the very last for a continuation of the old offset approach. In a straightforward memorandum to the President, prepared for the Erhard visit, he repeated his conviction that the Federal Republic's military posture was deficient, that it still had huge requirements for military hardware, and that German statements to the contrary were 'clearly untrue.'<sup>121</sup> He emphasized that the US could not accept any different method for offset, and that it could not accept the balance-of-payments drain if the Germans stopped their orders. He recommended for this case a troop reduction of about 50.000 men, and the dual-basing

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<sup>120</sup> The Atlantic Alliance: Hearings before the Subcommittee on National Security, Committee on Government Operations, 89th Congress, 2nd sess., 21 June 1966, in: PSSD, pt.3, reel XV, p.215.

<sup>121</sup> LBJL, NSF, NSC Histories: Trilaterals, Box 50, 19 September 1966.



(alternately in the US and in Europe) of about half the US Air Force in Germany.<sup>122</sup> Underlying his memorandum was the speculation that if he kept the pressure on the Germans high enough they might in the end agree to American troop reductions (and Strauß remarks had given him some encouragement).<sup>123</sup> This was the only scenario which would make him renege on a full offset.

The considerable risks of such a policy of brinkmanship did not go unnoticed: a prolonged deterioration of German-American relations, a further blow to the already shaky NATO cohesion, an almost certain loss of US prestige in Europe, and a weakening of the military posture in Europe. Those were the main arguments used by a group of advisers in the US administration who became increasingly preoccupied with the state of European-American relations in the shadow of the Vietnam War. Among them were, for example, W.Rostow (Johnson's security adviser), F.Bator, (the Deputy Assistant of National Security Affairs in the White House, very close to the President, and, because he organised all meetings and screened and commented all memos before the President, a central figure in offset deliberations), and a State Department group, led by George Ball. A deepening conflict had emerged between a more European minded traditional group, which had dominated US foreign policy after the War, and others who saw America's future for the good and bad in the Pacific.<sup>124</sup> The 'Europeanists' argued for the over-riding priority of keeping the traditional structure of the Alliance intact despite such pressures as the balance of payments, Vietnam, East-West detente, and domestic criticism. The decisive voice in determining the American position towards Erhard, however, turned out to be neither McNamara nor the State Department, but the Treasury (see para.g).

The first move in the hot phase of the quarrel on offset within the Johnson-administration was

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<sup>122</sup> *ibid.* In his conversation with the British McNamara saw the solution in '*first, a modification of our force structure, and second, a substantial increase in the FRG financial and force contribution*', 27 January 1966, in: FRUS 1964-68, XIII, p.304.

<sup>123</sup> FRUS 1964-69, XIII, Briefing Memo Bator to LBJ, 23 August 1966, p.454-455.

<sup>124</sup> See for example the heated dispute between McCloy, who accused the Johnson administration of having no European policy at all, and Harriman, who argued that no movements in Europe were possible without getting the Germans 'in a stew' and located the future in China, not in Europe (Library of Congress, Manuscript Collection, Harriman Papers, Box 486, note on a conversation with McCloy, 22 January 1966).

the plan of a multilateral payments union, destined to avoid the bilateralism of the US-German offset relationship and proposed once more by Rostow.<sup>125</sup> However, McNamara and Fowler put up strong resistance against this idea and warned of the very protracted bargaining which would be necessary, particularly at a time when NATO was already in disarray.<sup>126</sup> This killed the project quickly.

The main conflict emerged on the issue of how to respond to Erhard's 5 July letter which had asked for a diversification of the offset approach. The situation was complicated by the simultaneous public declaration of the British government that it intended to reduce its troops on the European continent. The hard-liners in the American government wanted to send an immediate response to Erhard demanding full military offset for the period after June 1967 (tacitly hoping that this would make significant troop reductions possible either by a German refusal to continue offset or by forcing them to give up their insistence on an undiminished American presence).<sup>127</sup> Ball, Bator, Rostow, McGhee, and others, however, were determined to 'not let Bob wreck this thing' with unforeseeable consequences for the US position in Europe.<sup>128</sup> They therefore tried to delay the answer to Erhard.<sup>129</sup>

When in early August, however, the US embassy in Bonn reported that the German cabinet was about to finalize its budget for 1967 with heavy cuts into defence in the air, McNamara urged for an immediate and tough response. Once more, his opponents argued against the dangers of this approach which in all likelihood would not force Erhard to revise his spending program: *'It would be a very poor trade for us to take serious risks with the stability of German and alliance politics, and hence with our security position in Europe, in order to make marginal gains on our balance of payments.'*<sup>130</sup> They recommended that the President

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<sup>125</sup> DDRS 1994/63, Bator to LBJ, 9 June 1966; Rostow, *The Diffusion of Power*, 1972, p.395-96; Treverton (1978), p.114-118.

<sup>126</sup> LBJL, Ball Papers, Box 4, telcon Bator-Ball, 17 June 1966; telcon Bator-Ball, 20 June 1966.

<sup>127</sup> FRUS 1964-68, XIII, Bator to LBJ, 23 August 1966, p.453-55.

<sup>128</sup> LBJL, Ball Papers, Box 4, telcon Ball-McGhee, 23 July 1966.

<sup>129</sup> Treverton (1978), p.118.

<sup>130</sup> FRUS 1964-68, XIII, Bator to LBJ, 11 August 1966, p.446.

postpone the reply to Erhard once more and bring together all principals before a firm position was to be decided.

Johnson agreed.<sup>131</sup> That gave the proponents of a compromise line two more weeks to elaborate a proposal which would deal with both the German and the British problem, and at the same time would not put further strain on European-American relations. The result was a plan to get all three concerned nations together and try to trilaterally work out a mutually acceptable financial offset framework.<sup>132</sup> During such discussions it would also be possible to talk comprehensively about the actual threat in Europe, about the necessary force-levels, and probably also about the troublesome nuclear problem. An immediate British cut which would encourage the Mansfield-group in Congress could be postponed. If no solution was found, troop cuts could be legitimately founded on the insolubility of the problem. During the decisive meeting on 24 August the President endorsed the 'Trilaterals' proposal.<sup>133</sup>

The idea had been floated by the State Department at least since mid-1965, originally as a response to expected actions by de Gaulle;<sup>134</sup> however, only in the emergency situation of autumn 1966 Alliance problems became so intricate that the necessary political impetus was created to get the US government moving towards a major diplomatic exercise. In order to start immediately, the United States planned to join the Anglo-German commission which at that moment dealt with the British offset issue and to try to explore alternatives to military offset.<sup>135</sup>

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<sup>131</sup> LBJL, Ball Papers, Box 4, telcon Bator-Ball, 13 August 1966.

<sup>132</sup> LBJL, NSF, NSC Histories: Trilaterals, Box 50, Leddy to Secretary Rusk: UK Financial Problem with BAOR, 23 August 1966.

<sup>133</sup> LBJL, NSF, NSC Histories: Trilaterals, Box 50, Bator Notes on 23 August Meeting.

<sup>134</sup> FRUS, 1964-68 XIII, Leddy to Ball, 23 September 1965, p.244-47. The British had been already approached with the idea; see: PRO, FO 371/183103, FO Brief for Stewart visit to Washington, 29 September 1965; Excerpt Stewart letter to Lord Hood, 20 September 1965; For the discussion within the US-administration: FRUS XIII, 1964-68, Memcon Bundy, McNamara, Ball, JCS, et.al., 8 October 1965, p.253-57.

<sup>135</sup> FRUS 1964-68, XIII, Bator to LBJ, 23 August 1966, p.454.

Letters were sent to Erhard and Wilson inviting them to participate in trilateral talks<sup>136</sup>. The letter to Erhard proposed immediate trilateral discussions on the future offset modus and related themes; there was no give in regarding the current offset. *'I know that you and I are agreed that the current offset agreement will be fully met and provided for in your new budget and legislative program.'*<sup>137</sup> Erhard, in his reply, suggested only the delaying of the Trilaterals until after his visit in September.<sup>138</sup> Due to the complicated preparations for such a large undertaking, this delay occurred anyway. Still, the Americans displayed considerable activity, trying to prevent the participating governments from moves which would prejudice the exercise. LBJ wrote twice to Wilson so that the British Prime Minister would not commit himself irreversibly to reductions in the BAOR.<sup>139</sup> At the same time, the government tried to hold the line in the domestic scene where the Mansfield resolution was introduced on 31 August. However, a further blow was to disturb the smooth proceeding of the plan: the realization that the current agreement was not going to be fulfilled. This proved to be the most serious factor in the mass of problems accumulated prior to Erhard's visit.

#### f) German Troubles

The Germans for some time had pondered as to how to put the cards on the table. The question involved not only changing the rules of future offset<sup>140</sup>, but also whether there was any money at all available for offset and -in particular- whether the current agreement could be fulfilled. After the government had realized already in March that offset targets could be reached only with a supplementary budget for 1966, it had put off this idea because of internal divisions on the 1967 budget, particularly between the Christian Democrats and the

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<sup>136</sup> FRUS 1964-68, XIII, LBJ to Wilson, 26 August 1966, p.457. Wilson, in his not yet declassified response, apparently requested preceding bilateral talks with the US. This was denied by the US government. See: *ibid.*, Johnson to Wilson, 1 September 1966, p.460-61.

<sup>137</sup> LBJL, NSF, NSC Histories: Trilaterals, Box 50, LBJ to Erhard, 25.8.1966.

<sup>138</sup> FRUS 1964-68, XIII, Erhard to Johnson, 7 September 1966, p.464-65.

<sup>139</sup> FRUS 1964-68, XIII, LBJ to Wilson, 26 August 1966; 31 August 1966; DDRS 1985/1008, Rusk to Ball in London, 7 September 1966.

<sup>140</sup> In July, the US offset negotiating team, headed by Kuss, was told in Bonn that 'superior levels' had given order not to proceed with the negotiations on the old terms; McGhee Papers, 1988add., Box 2, 23 July 1966.

Free Democrats. The former pleaded for tax increases whereas the Liberals insisted upon cuts in government spending.<sup>141</sup> From mid-66 on the government struggled to present a more or less balanced budget for 1967. All proposals submitted by the ministries were vigorously cut. This affected, in particular, the Defence Ministry. It had planned for a budget of DM19.8bn and ended up with DM18.5bn.<sup>142</sup> In a Cabinet Meeting, von Hassel stated that *'with such a budgetary situation the offset agreement could be neither fulfilled with orders nor -even approximately- with payments.'*<sup>143</sup> In a letter to Erhard on 12 September, he specified that payments would probably only reach \$267m at the end of 1966 (target March 1967: \$1392m). Orders made up to this date would heavily mortgage future budgets, so that future offset agreements were to stay within a limit of \$350m military and civilian orders, including a complete moratorium on orders in 1967.<sup>144</sup> Von Hassel also added that the interests of German defence industries could no longer be neglected.

This reflected mounting criticism in the public regarding the agreements. After the von Hassel visit to Washington in May, the Bundestag had for the first time taken up offset. Von Hassel had to deny the allegation that unnecessary material had been purchased. Helmut Schmidt from the Social Democrats criticised the political and economic consequences of the agreements. *'For reasons of security and alliance policy we can't permit ourselves to purchase all the heavy material we import from abroad exclusively from the United States. It just won't do. I would like that we buy and commonly develop parts of this equipment in France, whenever this is possible, so that relations to France in this area would not suffer from the gigantic volume of payments we owe to America.'*<sup>145</sup>

A further factor in increasing criticism in the military offset deals was that the quality of the US material came to be increasingly questioned due to a series of crashes by the Luftwaffe's

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<sup>141</sup> SPIEGEL 45/1966, p.31.

<sup>142</sup> Military Diary von Hassel, 26 August 1966.

<sup>143</sup> *ibid.*, Entry 4 August 1966 on Cabinet Meeting the day before.

<sup>144</sup> *ibid.*, von Hassel to Erhard, 12 September 1966.

<sup>145</sup> Verhandlungen des deutschen Bundestags, 5.Periode, 44.Sitzung, 26 May 1966, p.2142. Schmidt's critical remarks were shared even by members of the governing parties, *ibid.*, p.2144-45.

principal aircraft, the Starfighter. Von Hassel had to face embarrassing questions in the Bundestag as to the wisdom of buying American.<sup>146</sup> To obtain further authority for funds to fulfill the offset agreement was impossible under these circumstances.

Various ideas were floated as to how avoid a breach of the agreement and an open row with the Americans. Negotiations were, independently of offset, already under way on a premature repayment of the last tranche (\$214m) of German postwar debts to the United States. The Federal Ministry of Finance wanted such a procedure to be counted as offset. However, the US Treasury refused.<sup>147</sup> Another idea, pushed by Erhard, was the possibility of increased cooperation in space technology which might make some investment in US technology possible. However, the expected sums were much too low to have great significance, and the Americans also raised doubts as to the 'additionality' of this investment because in their opinion it would have been made anyway.<sup>148</sup> With the same argument they refused to consider 'civil' purchases, like aircraft for the *Lufthansa*. The only escape route seemed offset by financial measures, like German investment in mid- or long-term US treasury securities, thus transferring the accumulated dollars back. In pursuing this alternative the Erhard government was confronted with two formidable obstacles: the first was that it was unclear whether the Americans would agree, and the second was the *Bundesbank* which would have to advance the money because of the sad state of the government's budget. However, by law the *Bundesbank* was prohibited to extend credit in order to finance government programs; and the Central Bank Council considered the government's request to be such a case. Only major concessions by the Americans would save Erhard from the budgetary trouble which threatened to bring down his government.

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<sup>146</sup> VdB, 5th period, 33d sess., 24 March 1966, p.1510-17.

<sup>147</sup> LBJL, Fowler Papers, Box 51-52, memo: Present Status of German Debt Prepayment Question, 19 July 1966.

<sup>148</sup> McGhee Papers, 1988 add., Box 2, Blaser to McGhee, 16 July 1966.

## g) The Erhard-Visit

On 9 September, the US ambassador was informed that the German government felt unable to fulfill its current offset obligations.<sup>149</sup> This was a very bad surprise. The money had been already earmarked for various purposes, particularly in the Defense and Treasury Departments. *'The importance...of the past FRG offset receipts is indicated by the fact that the offset receipts of about \$700 million in FY 1965 were equal to about one-half of the total Defense Department global military receipts....The U.S. balance of payments deficit for CY 1965 was \$1.3 billion on the over-all balance, liquidity basis. We rely heavily on those receipts in our total balance of payments program, and our CY 1966 and 1967 estimates are based on FRG honouring its commitments.'*<sup>150</sup> These considerations were decisive for the US response to Erhard, despite continued warnings by the adherents of a softer line against an uncompromising US stance.<sup>151</sup> Fowler and McNamara, both saw their policies in serious danger and urged the President to get Erhard to fulfil the present agreement. McNamara requested authority to commence with troop cuts, if the Germans would not stand up to their promises.<sup>152</sup>

On the order commitment and on future offset, various compromises were considered. However, on the essential point, the US administration decided to remain hard: the payments had to come across the exchanges as planned. The agreed paper for the President recommended a tough line regarding the fulfilment of the offset obligation by any means, even if it included investments in Treasury Papers; this clearly reflected the concerns of the

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<sup>149</sup> Treverton (1978), p.120.

<sup>150</sup> LBJL, Papers of H.Fowler, Box 69, Treasury Background Paper: Trilateral talks (U.S./German Military Offset Relationship), 24 October 1966.

<sup>151</sup> The arguments were summed up by the American Ambassador in Bonn, G.McGhee. He sent a long cable to Washington on the possible consequences of a hard American response, the points of which he later repeated in a memorandum for the President. He listed up the danger that Erhard fell with the U.S. appearing as culprit; a decisive weakening of NATO; the end of Flexible Response; a decisive military weakening of US forces in Europe; a political victory for the Soviet Bloc; a blow to US-European relations and a corresponding loss in the American ability to influence events there; a possible reorientation of German security policy. See: LBJL, NSF, Country File: Germany, Box 193, Bonn 3361: The Offset and American Troop Levels in Germany, 20 September 1966; McGhee Papers, 1988 add., Box 2, Memo for the President: Your Meeting with Chancellor Erhard, 22 September 1966.

<sup>152</sup> LBJL, NSC Histories: Trilaterals, Box 50, McNamara to President, 19 September 1966.

Treasury department. The order period was to be stretched out, with Fowler and McNamara insisting on eventual military orders and the Bator/Ball group pledging for substitution by other means<sup>153</sup>. The essential consideration was the balance of payments. Fowler stated categorically that he *'can't take a nickel's loss in the balance of payments this year.'*<sup>154</sup> The last instruction, the President received prior to the meeting reflected this: the President was advised to insist upon full payments and on an immediate start of the Trilaterals.<sup>155</sup>

These instructions showed clearly how much the US government now relied on a continuation of offset payments despite an awareness of its character as a temporary expedient. Even if we take into account that the US government suspected that Erhard was bound to fall in any case, the decision to bluntly refuse his request was a risky one which might have poisoned mutual relations for some time to come - as subsequent events demonstrated. The contradicting aims of an expansive Cold War policy, including Vietnam, the continuation of the dollar-gold standard, and the refusal to take drastic action in the domestic economy were to an important degree hold together by the creation of offset. The US government found itself trapped. In one way or the other, it would have to compromise its policy, either by reducing its Cold War commitments, by diluting the monetary system, or by restrictive measures in the domestic economy. For the moment, however, there was still hope that Erhard would come up in some miraculous way with additional funds.

Just prior to his departure for Washington, Erhard's domestic problems took a dramatic turn for the worse. The coalition government agonized over the budget imbroglio. Statements that the Chancellor should offer his resignation multiplied. The attacks were not only pointed against the Chancellor, but also against his advisers. Foreign Minister Schröder and Finance Minister Dahngrün had since long been harshly criticized for their policies. Two of von Hassel's chiefs of staff left office in protest on the issue of union representation in the armed forces. Both vehemently criticized the Minister.<sup>156</sup> On 21 September 1966 von Hassel

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<sup>153</sup> LBJL, NSF, NSC Histories: Trilaterals, Box 50, Bator to President: Erhard-Visit, 25 September 1966.

<sup>154</sup> LBJL, Ball Papers, Box 1, telcon Rostow-Ball, 26 September 1966.

<sup>155</sup> LBJL, NSF, Country File: Germany, Box 193, Rostow to President, 11am, 26 September 1966.

<sup>156</sup> Hildebrand (1984), p.211-215.



survived by a small margin a vote of non-confidence in the Bundestag. The disorganized working of the government also made the Head of the Chancellor's Office, Erhard's closest collaborator Westrick, a target of incessant attacks. In early September he resigned. It turned out to be extremely difficult to find a successor. Nobody wanted to enter the sinking ship.

Erhard had been advised prior to the visit that it was better not to go into such an uncertain mission under those disadvantageous circumstances, but he had brushed this advice away. He had also refused American attempts through lower official channels to discuss the problems beforehand.<sup>157</sup> On the main issue, the Germans had received no positive signs. On 23 September, during a NATO meeting, von Hassel had briefly spoken to McNamara. The Secretary of Defence told him that the US government would probably be flexible regarding future offset, however, there would be no give in regarding the current offset.<sup>158</sup>

When the state visit drew nearer, Erhard saw no alternative left but to ask his friend, the President, to extend the current offset, to change the rules for further agreements, to avoid immediate US troop cuts, and to reaffirm the American support for the MLF.<sup>159</sup> Out of fear of being presented with an united US-UK front on the issue, Erhard also wanted to achieve a postponement of the trilateral exercise until after his US visit.<sup>160</sup> A diplomatic success on these issues together with an impressive reaffirmation of German-American friendship might have given him some breathing space on the domestic scene. However, on the main problem, the offset agreement, no conclusive alternative plans existed. Efforts to convince the Bundesbank to advance a short-term credit continued until the very last minute - and failed.<sup>161</sup>

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<sup>157</sup> Treverton (1978), p.144; Osterheld (1992), p.350; McGhee Papers, 1988 add., Box 2, General Klein on Erhard's present mood, 13 September 1966.

<sup>158</sup> Military Diary von Hassel, entry of 23 September 1966.

<sup>159</sup> Much has been made out of Erhard's alleged naivety and a quote of him 'I love Mr. Johnson, and Mr. Johnson loves me' appears in almost all accounts of the events. If all the sources cited for this quote are correct, Erhard must have made this comment on quite a number of occasions.

<sup>160</sup> LES, Talking Points for Washington, 26/27 September 1966; NHP, Ref.IIA7 Chancellor's Visit in Washington: Problems of European Defence, 17 September 1966.

<sup>161</sup> SZ, 29 September 1966; SPIEGEL, 3 October 1966.

The reception in Washington was not very auspicious. Only Ball, who had left the government service already, welcomed the German delegation in which, strangely enough, the Finance Minister was not present; probably a reflection of the state of the coalition, as Dahlgrün was an FDP member. The first rounds of talks took place in the State Department. Erhard pledged for prior bilateral consultations concerning the proposed trilateral exercise. Regarding offset he explained that the Federal Republic would not be able to fulfil the current agreement, and needed a stretch-out of the target as well as a diversification and decrease in future offset payments.<sup>162</sup> His interlocutors responded that this problem would have to be dealt with in the face to face talk with the President the following day.

During this famous meeting, Erhard repeated his points citing the cooperative attitude of his government in the whole field of bilateral issues.<sup>163</sup> He also hinted that in case his government fell, the succeeding one might be less cooperative. Johnson did not take up any of Erhard's proposals. He expressed deep disappointment at the fact that his German friends had broken their word and had put him in an extremely difficult position. He suggested that experts on both sides should start to work on the problem. There was no indication of any give-in on Erhard's basic pledge, a payments stretch out in the current agreement. It was obvious that the Chancellor's hopes had failed. When both joined their waiting delegations, Erhard, according to McGhee, looked 'utterly dejected.'<sup>164</sup> The German delegation which had not formulated a consistent position for the emergency that Erhard's pledge might fail worked feverishly to present an acceptable alternative. The only solution to fill the enormous order and payments gap<sup>165</sup> was US acceptance of large-scale German investment in Treasury papers and of premature repayment of the remaining German postwar debts (\$214m) as offset.

The Bundesbank acquired a central role in the deliberations. Bundesbank President Blessing

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<sup>162</sup> *ibid.*, 26 September 1966; Osterheld (1992), p.350-53.

<sup>163</sup> The complete text has been published recently in the FRUS, 1964-68, XIII, p.471-77.

<sup>164</sup> McGhee (1989), p.193; Osterheld (1992), p.354; LBJL, NSF, NSC Histories: Trilaterals, Box 50, memcon President/advisers - Chancellor/advisers, 12:30, 26 September 1966.

<sup>165</sup> Estimated Orders shortfall on 31 December 1966: \$567m; payments shortfall on 30 June 1967: \$892m. Both of these figures were only reached by counting some questionable items. See: LBJL, NSF, NSC Histories: Trilaterals, Box 51, Minute of US-FRG discussion, 27 September 1966.

was in Washington for the Annual IMF Meeting; however, in consultations with the German delegation, he put hard conditions on any help which would come close to Bundesbank lending to the Federal Government. In case the Bundesbank should agree to convert its short-term reserves to mid-term US treasuries, thus depriving itself of flexibility in a potentially unstable monetary environment, he demanded a supplementary budget for 1966 of DM 1 billion and an augmentation of the 1967 Defence budget by another billion.<sup>166</sup> Those funds would allow the Federal government to gradually acquire the bonds from the Central Bank, and to repay the funds for the debt prepayment mentioned above. The snag was that this offer was contingent upon approval by the Bundesbank board, and budget augmentations had to be approved by parliament. The German delegation informed the Americans that they would not be able to present more than suggestions for filling the \$892m payments gap.<sup>167</sup> These went as follows: \$428m transfer of short-term Bundesbank funds to Treasury bonds which would count as positive items in the US Balance of payments; \$214m prepayment of postwar debts; \$250m funds coming from an augmented defence budget.<sup>168</sup> Regarding future agreements the Germans proposed a level of \$350m/year on a five year base.

McNamara and Fowler rejected this last point out of hand as a question which had to be dealt with at the Trilaterals. Regarding the proposed purchase of Treasury bonds, Fowler demanded that those were non-negotiable, non-convertible, with a term of 6-8 years and later on to be settled by arms purchases.<sup>169</sup> This would make them a kind of pre-payment on future military orders, preserving the military offset scheme. The Americans compromised on counting the debt prepayment and on a stretch out of the order period. The main consideration for them was getting the payments across exchanges one way or the other. On this base, both delegations tried to formulate a face-saving communique. The result was the longest of all postwar German-American communiqués.<sup>170</sup> It stated that the Federal Republic would 'do

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<sup>166</sup> Military Diary von Hassel, 25 September 1966.

<sup>167</sup> LBJL, Ball Papers, Box 4, telcon Carstens-Ball, 26 September 1966.

<sup>168</sup> Military Diary von Hassel, entry of 27 September; LBJL, NSF, NSC Histories: Trilaterals, Box 51, Minute of US-FRG discussion, 27 September 1966.

<sup>169</sup> *ibid.*

<sup>170</sup> EA 21(1966), p.D522-25.

its best' to meet the current agreement, but would not be able to continue offset at the same level. The Federal Republic also agreed to an immediate start of the trilateral exercise. The MLF was not mentioned anymore.<sup>171</sup>

The long-winded communique could hardly veil the fact that the German delegation had not reached its objectives of getting relief from its offset obligation. Soon, harsh criticism centred on various aspects of the trip. Not only the press<sup>172</sup>, but also parliament<sup>173</sup> and voices from Erhard's own party joined ranks.<sup>174</sup> During Erhard's absence several conspiratorial meetings had taken place, but Erhard's rivals could not agree on a successor. Meanwhile, the budgetary chaos took on ever more disastrous forms. Shortly after Erhard returned, new estimates put tax revenues even lower than already expected. The budget which was finally prepared was ruled out by the Bundesrat (Council of the Länder) as unconstitutional because important obligations like offset were not even mentioned, let alone covered by funds. The alternatives now were either cuts in government programs (which the CDU/CSU resisted) or tax rises (which the FDP abhorred). In October, the Free Democrats left the government when the cabinet decided for tax rises. Erhard tried to cling to his chair with a minority government. On 8 November a majority in the parliament asked him to pose the Vertrauensfrage (vote of confidence).<sup>175</sup> The CDU had to act. One day later, the party elected the Minister President of the Land Baden-Württemberg, Kiesinger, as Erhard's successor. Kiesinger immediately got together with the Social Democrats to form a Grand Coalition. On 1 December, the Kiesinger government was elected by the Bundestag with Brandt as Foreign Minister, Strauss as Finance Minister, and Schröder pushed to the Defence

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<sup>171</sup> Hoppe (1994), p.357-58.

<sup>172</sup> For example: SPIEGEL, 41/1966, p.26-28; The Frankfurter Rundschau of 29 September 1966 spoke of a thinly veiled fiasco on all counts.

<sup>173</sup> For the debate see: VdB, 5th period, 60th session, 5 October 1966, p.2939-2970. Speakers of the opposition (H.Schmidt; H.Weher) mentioned the absence of the Finance Minister, the secretiveness surrounding the commitments, and the committing of enormous funds on the base of insufficient budgets. FDP speakers joined this chorus, stating that present budgetary estimates were void in view of the offset commitment. Universally the absence of a clause of best efforts was strongly criticized.

<sup>174</sup> Strauß found fault with the absence of a clause of best efforts and the naive one-sided reliance on US policy; SPIEGEL 42/1966, p.31.

<sup>175</sup> For the agony of the Erhard government, see: Göllner (1986), p.140-49; Laitenberger (1986), p.211-217; Mintzel, *Geschichte der CSU*, 1977, p.380-91; Hildebrand (1984), p.217-231.

Ministry.

The question as to how much the fatal visit to Washington contributed to Erhard's fall and whether the US government deliberately took this possibility into account is open to speculation. It is true that the US were fully aware of Erhard's problems and probably saw him as a lame duck anyway. Any concessions would have been tactically unwise as Erhard's future was so uncertain. The problem was the danger that the Americans appeared the culprits which would have damaged German-American relations considerably. However, as we have seen, the US government also felt under very strong pressure not to compromise. The US didn't escape all the blame<sup>176</sup>, but the prevailing opinion was that Erhard's fate was sealed anyway and that the visit was just the last straw.

The indirect impact of the offset problem was decisive for Erhard's fall. The exact role of offset commitments in the budget problem is, due to the scarcity of available sources, not answerable; it seems, however, that it was the biggest problem.<sup>177</sup>

These questions, however, are only of secondary importance to the main argument. The central purpose of this chapter has been to show the multi-faceted nature of domestic and international, economic and political, structural and temporary factors which shaped events and decisions on a complicated issue like offset. In the instance of the Erhard visit a melange of longterm factors (balance of payments problems, British economic crisis, de Gaulle's challenge, détente, crisis of German foreign policy, Vietnam) was exacerbated by the impact of short-term developments like the Sterling crisis in July 1966, German budgetary problems, the sudden motion in the US congress, and the dim prospects for the 1966 US balance of payments. Offset had been a kind of glue keeping together all those disparate elements. It had become institutionalised in a rather rigid form, particularly in Washington. When its further implementation became impossible, an immobilized German government was not able to change the modus and escape from the commitment.

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<sup>176</sup> Sommer, in his influential *Foreign Affairs* article, April 1967, wrote that 'it was American insensitivity which brought Erhard down', p.483. In the same vein: Morgan, *The US and West Germany 1945-73*, 1974, p.146-48.

<sup>177</sup> SZ, 27 October 1966; 29 October 1966.

The most important function of offset became temporarily unfeasible: to provide a protective shield for the currencies under pressure, pound and dollar, and to guarantee the continuity of military protection by the Alliance, symbolized by the troop commitments. The issue in the Trilateral negotiations was whether another form of 'glue' could be found or whether either Anglo-American monetary policies or German security policies had to be revised profoundly. These revisions would have signified the abandonment of longstanding fundamentals of either foreign policy. It is no surprise that the negotiations turned out to be everything but smooth.

CHAPTER XI  
THE TRILATERAL NEGOTIATIONS 1966/67

a) Fulfilling the McNamara-Von Hassel Agreement

On 11 October 1966, President Johnson announced that the governments of the Federal Republic, the United Kingdom, and the United States were about to '*undertake a searching reappraisal of the threat to security and -taking into account changes in military technology and mobility- of the forces required to maintain adequate deterrence and defense in Central Europe. The reappraisal will also deal with: equitable sharing of defense and other comparable burdens, the impact of troop-deployments and force levels on the balance of payments of the US and the UK, the effect on the German economic and budgetary situation of measures designed to ameliorate balance of payments problems*'.<sup>1</sup> I will deal with the first part of this program, the reappraisal of NATO strategy, and with the diplomatic process of the ensuing negotiations in the Alliance only parenthetically. Previous research has emphasized the importance of the Trilaterals as a first step towards the restructuring and reconsolidating of NATO in the late 1960's, paving the way for the Harmel Report at the end of 1967.<sup>2</sup>

However, the most significant aspect of the trilateral negotiations were the financial ones and their consequences. The public German statement not to convert its accumulated dollars to gold has been termed '*the most important postwar step in insulating the United States from external pressure on its reserves*'.<sup>3</sup> The questions as to how this different kind of offset came into being and which factors led up to it have been barely analyzed. I will look at the genesis, consequences, and actual significance of the unprecedented commitment by the German

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<sup>1</sup> Statement by President Johnson on the forthcoming talks between Washington, London, and Bonn, in: PP Johnson (1966), II, p.1139.

<sup>2</sup> The best analysis of the Trilaterals is in Haftendorf, *Kernwaffen und die Glaubwürdigkeit der Allianz: Die NATO-Krise von 1966/67*, 1994. Furthermore: Whightman, in: *Rivista di Storia Economica* 5/1988, p.26-75; Duckwitz, *Truppenstationierung und Devisenausgleich*, in: *Aussenpolitik* 8/1967, p.471-75; Treverton, *The Dollar-Drain and American Forces in Germany*, 1978. Schertz, *Die Deutschlandpolitik Kennedy's und Johnson's*, 1992, devotes a lengthy chapter to the Trilaterals (p.379-405) which is nothing but a chronologically arranged transcription of some documents in the LBJL.

<sup>3</sup> Bergsten, *The Dilemmas of the Dollar*, 1973, p.31.

government not to convert dollars to gold. The impact of the Trilaterals on the continuity of Anglo-American troop levels in Germany will be assessed. Once more, the way the monetary problems of the Western World intersected with the management of mutual security will receive particular attention. Much more material needs to be declassified before a comprehensive analysis can be given. This thesis will make a start though some documents consulted cannot be referred to as they still fall under the thirty years rule.

Before any serious negotiations about the future of Atlantic burden-sharing and force structures could start, the three participating governments had to solve several immediate problems. The most pressing of these was a legacy of the unfortunate Erhard-visit, namely the problem of the 1965/67 agreement. The issue of how this agreement was to be honoured was -by German-American agreement- to be treated separately from the trilateral exercise. Upon his return, Erhard faced the enormous challenge of obtaining the necessary funds for fulfilling the German offset obligation on which Johnson had insisted so strongly. This obligation was the biggest element in the budgetary gap which would cause the break-up of the CDU/CSU/FDP coalition and seal the end of Erhard's chancellorship. Erhard complained bitterly to McCloy, the US Chief Negotiator at the Trilaterals, about Johnson's refusal to grant him an extension of the commitment. He accused his Defence Minister of carelessness when concluding the May 1964 agreement with McNamara.<sup>4</sup> However, it had been the Chancellor's own imprudence which had prevented the exemption clause of the agreement from becoming effective. At the point in his personal meetings with Johnson and McNamara when he should have insisted strongly on a mutual revision of the agreement's provision he had been vacillating and irresolute.

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<sup>4</sup> LBJL, NSF, NSC Histories: Trilaterals, Box 50, Bonn 4833, 21 October 1966. Prior to the Erhard visit, the Germans and the Americans had disagreements on the interpretation of the McNamara-Von Hassel protocol. The Germans thought that the safeguard-clause, on which Strauß had insisted as part of the 1962 agreement, was still valid. The Americans denied that such a condition existed. The German version of the protocol is ambiguous. The Strauss safeguard clause made the offset commitment 'subject to the availability of funds', whereas the 1964 agreement coupled it to a German need for new weapons and to the economic competitiveness of the US 'goods'. (See: McGhee Papers, 1988 add., Box 2; AAPD, 1964, p.526, fn.2). This is why McNamara in his public statements emphasized the insufficient equipment of the Bundeswehr as well as the competitiveness of US weaponry. Erhard had committed himself several times to fully executing the agreement without reservations, most conspicuously in the communique of the December 1965 meeting with Johnson. Probably for this reason, the Germans did not attempt to argue about the safeguard clause during the talks in September 1966. A stronger German government could well have insisted upon another interpretation.



Now in a hopeless political situation, the Chancellor was unable to offer more than vague suggestions. The only chance seemed to be help from the *Bundesbank* with which, according to Erhard, his government had 'a lively debate' going on.<sup>5</sup> However, the Bank remained adamant in its refusal to help Erhard. The Bank's Council (ZBR) informed the government that confidence in the German currency would be impaired if the *Bundesbank* was dragged into closing budgetary gaps. The *Bundesbank* was unwilling to tie up a huge amount of liquid funds in longterm Treasury bonds of a foreign country and such lose a good deal of flexibility in its monetary policy. The bankers argued furthermore that such an investment would be tantamount to the extension of a credit to the Federal Government which was illegal according to *Bundesbank* law.<sup>6</sup>

The Bank was ready to offer substantial help only if two conditions were fulfilled: first, the parliamentary approval of the supplementary Federal budget for 1966 the Bank had demanded since months and, second, increased defence appropriations for 1967 so that the Central Bank could be reimbursed if it gave the requested emergency help. The *Bundesbank* President, Blessing, confirmed this later to the US ambassador, McGhee: '*Blessing had no desire to move to help Erhard until he took the necessary steps to help himself by an increase in the budget...Blessing would not advance funds until he was assured of later repayments through the military budget*'.<sup>7</sup> Erhard's government, however, could not force the *Bundesbank* to moderate its conditions, nor could it push an augmented budget with corresponding tax increases through a hostile parliament. The politically explosive idea to invest some of the reserves of German social security funds in US Treasury bonds had to be abandoned as soon as the first rumours became public.<sup>8</sup> The impression that German pensioners paid for the government's offset obligation would have been difficult to avoid. The only concession Erhard achieved was that the *Bundesbank* advanced funds for the prepayment of postwar

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<sup>5</sup> *ibid.*

<sup>6</sup> BA, B136/3327, Records of 224. and 225. ZBR Meeting, 6./20. October 1966; BBA, B330/10245, Tüngeler (*Bundesbank*) to Carstens, 28 October 1966.

<sup>7</sup> LBJL, NSF, NSC Histories: Trilaterals, Box 51, Bonn 6967: Meeting with *Bundesbank* President Blessing, 9 December 1966.

<sup>8</sup> McGhee Papers, 1988 add., Box 2, Memo: Basic Considerations in a Solution of the Current and Future German Offset Problems, 15 October 1966; SZ, 19.10./2.11.1966.

debts, as it had done previously in 1961.<sup>9</sup>

The whole episode is the culmination of an increasingly assertive *Bundesbank* policy towards Erhard's government in 1965/66. The Bank had stated repeatedly its disapproval of the government's anti-cyclical spending policy (see ch.X, fn.110). Confronted with a weak Chancellor, it was able to withstand pressure by the government to relax its restrictive monetary policy. In the final phase of Erhard's chancellorship, the Bank was not ready to extend significant concessions. First, because its conditions were not fulfilled, and second, because it expected, like almost all observers, soon a new government. As we shall see later, the *Bundesbank* became and remained an important player in a question which previously had been the exclusive domain of the government: the financial management of the Western Alliance. Until then, the *Bundesbank's* policies regarding the defence of the dollar had been - on the surface- separated from the government's efforts to neutralize the US troop cost. The events of 1966/67 made the continuation of this rather artificial separation impossible. The crisis of the monetary system and of the security system were not separable any more - not even on the surface.

Kiesinger's 'Grand Coalition', in power from 1 December 1966 on, decided to honour Erhard's financial pledges. Its huge majority in parliament enabled it to prepare a supplementary budget for 1966 and effect spending cuts for 1967 without the furious opposition Erhard had encountered.<sup>10</sup> Combatting the recession was the first priority for the new government, represented in this field by the colourful couple of Economics Minister Schiller and Finance Minister Strauß. Schiller and Strauß took official recourse to Keynesian policy and deficit spending for the first time in the Federal Republic's existence.<sup>11</sup> This made the honouring of the von Hassel-McNamara agreement possible. Government bonds were placed on the market by the *Bundesbank* which yielded enough income to pay \$250m to the

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<sup>9</sup> BA, B 136/3135, Memorandum for Chancellor: ZBR Meeting, 6 October 1966; Blessing to Westrick, 10 October 1966.

<sup>10</sup> Hildebrand (1983), p.283-301.

<sup>11</sup> Giersch/Paqué/Schmieding, *The Fading Miracle*, 1992, p.146-48; Abelshauser, *Wirtschaftsgeschichte der BRD, 1945-80*, 1983, p.106-116.

to the US at the end of the year and another \$125m in 1967.<sup>12</sup> These funds were placed at the disposal of the government and were to be repaid out of later defence budgets. The settlement of postwar debts, which as a gesture of goodwill by the US had not to be matched by military orders later on, covered another \$192m. That left \$325m of the gap as established during the Erhard visit (\$892m). By mortgaging future defence budgets with further advance payments on prospective military purchases, the Federal Republic was able to transfer this sum in the first half of 1967.<sup>13</sup> With its budgetary policy the new government had fulfilled the *Bundesbank's* requests; however, that was to turn soon into a Pyrrhic victory for the bankers.

In June 1967, the level of German advance funds on future military orders from the US had risen to almost \$1 billion. The German government announced that it would not be able to place any new orders in 1967 which, of course, greatly reduced the options for any new agreements.<sup>14</sup> The advance payments, however, were of great value for the American monetary position. In 1966, the liquidity deficit would have amounted to about \$2.6bn instead of the official \$2.15bn (which was only a slight deterioration compared to 1965). The payments also were the major element in the 'special transactions' which kept the deficit in the first half of 1967 to \$1 billion rather than to \$2.7bn in the absence of these transactions.<sup>15</sup>

#### b) The British Problem Again

Parallel to these efforts, work on a new offset mechanism continued. The actual trilateral negotiations got off to a very slow start. The prime reason was the German government crisis which precluded firm decisions until January. The British, who had joined the exercise very unenthusiastically, posed another substantial difficulty. They had continued to pursue their bilateral offset talks with the Erhard-government even after they had already agreed to the

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<sup>12</sup> Bundeshaushaltsplan 1967 and Nachtragshaushalt 1966; SZ, 28 December 1966.

<sup>13</sup> DDRS 1992/3537, Background Paper for Brandt Visit: Current US/FRG Offset, 6 February 1967; McGhee Papers, 1988 add., Box 1, Bonn 15302, Kiesinger Visit: Military Offset, 27 June 1967.

<sup>14</sup> BPI 21, 28 February 1967, Probleme der Devisenhilfe für die USA und Großbritannien, p.171.

<sup>15</sup> The figure also includes the \$500m purchase of US Treasury bonds by the Bundesbank which was a result of the Trilaterals; LBJL, Fowler Papers, Box 49-50, Meeting in the President's Office, 10 August 1967.

Trilaterals. A gap of DM 500m had remained between the German offer and the British request of DM 850m when, in the end of October 1966, the talks were suspended.<sup>16</sup> This was the moment the British government had waited for to start finally with troop reductions. Time was pressing, because the measures should take effect before the new budget in April 1967 was put together. A comprehensive review of strategic and military questions was considered a 'luxury' in this respect, and UK representatives told the Americans openly that they were only interested in the financial aspect of the Trilaterals.<sup>17</sup> There was to be no illusion that for the British the commitment to Sterling and to budgetary exigencies had absolute priority over any NATO strategic doctrines or cordial relations with Germany. The situation on the currency markets was so tight that the government saw no margin left for compromising on the troop cost problem.

On the other side, London still seemed to be unprepared for the practical and political problems a large withdrawal would cause. First, there was the old problem of where to house the returning troops.<sup>18</sup> Furthermore, the 'special relationship' once more demanded restraint. After the Erhard visit, Johnson had urged London in strong terms to refrain from actions which would undoubtedly prejudice the Trilateral exercise.<sup>19</sup> Reductions in Europe, therefore, required careful advance preparation with the Americans to limit the effect of possible adverse reactions in Washington. A third obstacle in the way of reductions was the new bid for EEC membership the British government planned at the end of 1966, placing the UK again in the dilemmas of the late 1950s-early 1960s(see ch.IV). These reasons appeared to have convinced Wilson that if he went ahead with reductions straight away he would find himself between all stools. The snag of a delay, however, was that the Labour government had publicly already committed itself to a rigorous position which would have made a renunciation of cuts look like backing down because of pressure from abroad.

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<sup>16</sup> SZ, 18.10; 20.10.1966.

<sup>17</sup> DDRS 1993/323, Memorandum of Brown-Rusk Conversation, 14 October 1966; LBJL, NSF, NSC Histories: Trilaterals, Box 51, Leddy to Rusk, 8 November 1966; Box 50: Memorandum of Healey-McNamara Conversation, 14 December 1966.

<sup>18</sup> Crossman, *Diaries of a Cabinet Minister*, Vol.II, 1976, p.145. Disbanding them would have meant a risky quarrel with the Americans and with Britain's NATO partners. It would also have made the balance of payments argument seem to be just a pretext for saving budget money.

<sup>19</sup> FRUS 1964-68, XIII, LBJ to Wilson, 6 October 1966, p.477-78.

Therefore, Wilson needed some compensation to solve the dilemma. The Americans came to the same conclusion. They made an offer which Johnson outlined as follows: 'Would it help if I placed in the United Kingdom in the near future \$35 million in orders beyond those already agreed to? I think I could do so on assurance from you that you will stay with us and the Germans in completing this fundamental review....., making no change in your troop and supply dispositions there until after the completion of the review...This procurement would supplement the accruals of dollars to you associated with the recent shift of our forces and installations to Britain from the Continent'.<sup>20</sup> The background of this offer was the American fear that if the British started to reduce, they would set in motion a wave which might well have led to irresistible pressure in the US to follow suit. This would have rendered the Trilaterals absurd before they even started. Accepting the offer, the British announced a delay in any final decision for 6 months, at the end of which they would call on NATO and WEU to set the reduction process in motion.<sup>21</sup> This delay also had the great advantage of giving the German and the US governments valuable time to consider thoroughly the issues which emerged during the negotiations already under way.

The representatives chosen by the governments for the talks were John J. McCloy on the American side, Carstens from the AA on the German side (after the government change replaced by Duckwitz), and G. Thomson from the Foreign Office for the British. The choices signalled important institutional changes. McCloy, former High Commissioner in Germany, was a strong supporter of 'Atlanticist' policy in the US government. In his person, the State Department acquired an important ally in the struggle against the seemingly inevitable reduction of the US commitment in Europe.<sup>22</sup> In Germany, the appointment of Carstens signalled that the AA had now taken on the principal responsibility for offset, and that it was removed from the Finance and Defence ministry track. This assured that the broader objectives of German foreign policy would carry more weight than they had in the offset

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<sup>20</sup> FRUS 1964-68, XIII, Johnson to Wilson, 15 November 1966, p.492; on the genesis of the American offer: Treverton (1978), p.123-24.

<sup>21</sup> FRUS 1964-68, XIII, London 4234: E. Rostow talks in London, 22 November 1966, p.499; LBJL, NSF, NSC Histories: Trilaterals, Box 50, memcon Healey-McNamara, 14 December 1966.

<sup>22</sup> Treverton (1978), p.124.

negotiations of the 1960s.<sup>23</sup>

The first meetings of the negotiators were devoted to setting an agenda for the talks. The rest of the remaining 14 NATO countries -after the French walk-out- had to be convinced that they were not going to be faced by *fait accomplis* and that they would be fully consulted by the three big members.<sup>24</sup> For this reason the General Secretary of NATO, Brosio, participated in the talks. Three working groups were formed which were to look at the interrelated issues of Warsaw Pact military capabilities, NATO capabilities, and the balance of payments effects of troop stationing. This last group had the task to establish the real net foreign exchange drains and gains resulting from the troops presence in Germany.<sup>25</sup> In the first two groups, tentative agreement was soon achieved leading to a series of further talks on NATO strategy which lay beyond the scope of this research.<sup>26</sup>

#### c) The American Debate on the Trilaterals

More crucial than the deliberations of these working groups were the debates in the participating governments themselves. Unfortunately, a sufficient archival base is only available for the American government as yet. I will have to concentrate therefore mainly on American decision making.

The US government was divided on an old question which for the first time was strongly influenced by public disputes: the troop reduction debate, or in other words whether to continue its traditional European policy or to give priority to the pressing political and financial exigencies of the moment. The Mansfield-resolution and the end of the previous offset mechanism introduced important new elements into the debate. After the disaster of Erhard's visit, McNamara felt that he now, finally, would be able to effect a large reduction of US forces in Europe. As we have seen, this was motivated not only by Vietnam, as most

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<sup>23</sup> On British decision-making during the Trilaterals there is only the scarcest evidence derived from some memoirs until the PRO opens the pertinent files under the 30-years rule.

<sup>24</sup> LBJL, NSF, NSC Histories: Trilaterals, Box 51, Paris 6006: McCloy Briefing for NATO representatives, 22 October 1966.

<sup>25</sup> *ibid.*, Terms of Reference for Working Group on Balance of Payments, 19 November 1966.

<sup>26</sup> On this subject, see the literature cited in fn.2.

contemporary observers suspected, but even more by McNamara's now six year old effort to achieve a modern and economically rational posture for US forces abroad.<sup>27</sup> Immediately after the Erhard visit he circulated a memorandum on 'NATO strategy, Force Levels and Balance of Payments' in which he argued for a reduction of US forces in Europe by 50,000 men and the dual-basing of almost all the US airforce deployed in Europe.<sup>28</sup> Clearly, the US government would not be able to participate meaningfully in the Trilaterals if it had not taken a basic decision on the fundamental issues posed by the McNamara memorandum. This time, the adherents of a stable troop level were to have a much more difficult stance because of the multiple pressures and the powerful military, economic, and now even electoral arguments for reductions in Europe. The discussion was to drag on for months.

The first voice against McNamara's proposals was raised by the Joint Chiefs of Staff which asserted that there was no military rationale justifying them.<sup>29</sup> McCloy also voiced his strong disapproval of McNamara's plans. In a lengthy report for the President on the basic issues of the Trilaterals he emphasized above all the 'historical' argument of the US forces as pacifiers of Europe which had prevented the outbreak of another war in Europe. He diagnosed NATO as being on the brink of falling apart. This development would be decisively accelerated by American and British troop withdrawals.<sup>30</sup> However, both the JCS and McCloy realized that the circumstances made some reductions almost unavoidable and included in their memoranda recommendations on the least damaging ways of effecting them. Their interventions had the effect of delaying the immediate decision McNamara sought. Another basic intention behind McCloy's arguments, namely to sever the link between troop levels and money by forcing first a purely political and military decision on troop levels,

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<sup>27</sup> A summary of DOD measures to reduce foreign exchange losses during McNamara's tenure is in: LBJL, H.Fowler Papers, Box 1, Statement Summarizing Actions by the DOD....FY 1961-67. Attempts to convince US personnel abroad of the gravity of the balance of payments problem took sometimes quite unconventional forms. In 1966, for example, the GI's were subjected to a film, titled 'Gold and You', which described actions every army member could take to help alleviate the dollar drain.

<sup>28</sup> The memorandum, dated 4 October, is not yet open to research. Its contents can be deduced from the JCS response to it: LBJL, NSF, NSC Histories: Trilaterals, Box 51, JCS to McNamara, 27 October 1966.

<sup>29</sup> Cf. the memorandum mentioned in the previous footnote.

<sup>30</sup> LBJL, NSF, NSC Histories: Trilaterals, Box 50, McCloy report: Political Effects of NATO Troop Reductions; Military Effects of US Force Changes in Europe, 21 November 1966.

failed.<sup>31</sup> The credo of the majority in the US government remained as it had been for years: *'the final decision on US forces will inevitably depend in part on how much money McCloy can get out of the Germans'*.<sup>32</sup>

Time was pressing. The British government became increasingly restive about the delay and news from Germany bode ill. In the beginning of February, it became public that the Federal Republic intended to put a virtual stop on offset for both the US and the UK for some time to come.<sup>33</sup> The British government immediately reacted with renewed preparations for withdrawals. If the Americans wanted to avoid the undoing of their initiative, and the risk of severe damage to both the security and the monetary system, they had to present a position which made the basic intentions of the US clear. Would they try to preserve the traditional structure of the Alliance or would they rather take the lead in initiating far-reaching changes? McCloy pressed for a position which assured the allies that the United States saw the preservation of the Alliance as its overriding goal. This implied a positive statement on the future presence of American military forces in Europe. A presidential decision was required.

The opposing sides in the US government summed up their arguments in a series of memoranda. Invoking balance-of-payments savings and the eroded military rationale of the troops, the civilian leadership of the Pentagon recommended the withdrawal of two out of five divisions and of the major part of the American tactical airforce, that is six out of nine air wings in Europe. They were to remain allocated to the European theatre and periodically be brought there for training purposes by way of a rotational scheme. The State Department, the JCS and McCloy brought up a familiar range of counter-arguments: -the relocations would save only relatively small amounts of foreign exchange; -they would undercut the Flexible Response strategy; -they would lead to corresponding European reductions; -they would encourage Soviet pressure on Europe; -they would result in declining American influence over Europe; -they would destabilize Western Europe and NATO; -they would increase the danger

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<sup>31</sup> Treverton (1978), p.143.

<sup>32</sup> LBJL, NSF, Memos to the President: W. Rostow, Box 11, Rostow to President, 23 November 1966.

<sup>33</sup> BPI 20, 24 February 1967, Strauß speech at DIHT, 15 February, p.64.



of German nationalism; -they would impair gravely American combat effectiveness in Europe.<sup>34</sup> The State Department therefore advocated a reduction/rotation of only one division and three air wings; McCloy was against any reduction.

Several meetings were held with the President on the troop level question, in which Johnson made his opposition, in principle, to cuts clear. He pointed, however, to the insufficient defence efforts of the UK and the Federal Republic, and, in particular, to domestic pressures. In mid-January, Mansfield had re-introduced his Sense of Senate resolution calling for large-scale reductions as a reaction to the slow progress of the talks in NATO.<sup>35</sup> The President met with the Congressional leadership to sound out the strength of the Mansfield group.<sup>36</sup> Faced with the arguments of the Senators, Johnson was reluctant to take a definite position in the decisive meeting, although he indicated again that he preferred to remove as few men as possible. When, during the meeting prior to his departure to Europe, McCloy complained about the vague guidelines, LBJ explained his position in a monologue coloured by graphic hill county metaphors.<sup>37</sup> What emerged, apart from the President's asides about 'stinginess' as part of the German national character, about ways to deal with the 'babies' on the Hill, and about his indignation at being lectured in public by allies<sup>38</sup>, was not very much to McCloy's satisfaction: he should go to Europe and find out what the Europeans were ready to do. Only then would the President take a decision on the troop-level issue.

McCloy was provided with three basic principles for conducting the negotiations: '*Force levels should be determined through agreement among the Allies on the basis of only security*

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<sup>34</sup> LBJL, NSF, NSC Histories: Trilaterals, Box 50, McCloy to E.Rostow, 9 February 1967; McCloy to President: Force Levels in Europe, 23 February 1967; Ibid., Box 51, JCS to Secretary of Defense: Military Redeployments from Europe, 2 February 1967; Rostow, Bowie, Leddy, Kitchen to Rusk: OSD Proposals for Reducing US Forces in Europe, 30 January 1967.

<sup>35</sup> Williams, *The Senate and US Troops in Europe*, 1985, p.148-53.

<sup>36</sup> LBJL, NSF, NSC Histories: Trilaterals, Box 50, Record of President's Meeting with the Congressional Leadership, 27 February 1967.

<sup>37</sup> *ibid.*, Box 50, Memo of President's Conversations with McCloy, 1 March 1967.

<sup>38</sup> In February 1967, Kiesinger had given a speech, in which he had used the phrase 'atomic complicity' describing US-Russian negotiations on a Non-Proliferation Treaty. This had infuriated Johnson and poisoned the relations between the two men for a long time. See: Hildebrand (1983), p.310.

*considerations, broadly construed; -- Germany should decide what levels of procurement in the U.S. and Britain it wishes to undertake in order to bring its military forces up to the appropriate strength levels; -- Simultaneously, the Allies should deal with the remaining balance of payments consequences of allied troops stationed in Germany by cooperation in its management of monetary reserves.*<sup>39</sup>

These guidelines were probably not as precise as McCloy had wished; they embodied, however, important preliminary positions on several issues. The first principle indicated that the allies would have a voice in the decision about troop levels. Therefore, it would be politically very difficult to reduce by as much as McNamara envisaged. That only 'security considerations' were to decide future force levels was, however, -even 'broadly construed'- wishful thinking. The second principle put an end to 100% military offset. The new German government had clearly stated its opposition to any new fixed commitments of this kind. Public criticism had been so outspoken in Germany that a continuation of the US sales operations on the previous scale was ruled out. Even in the United States, apprehensions emerged. McNamara had to defend the operations of his sales division against mounting criticism in Congress.<sup>40</sup>

The third principle pointed to the direction into which the solution of future offset agreements would move: towards the field of monetary cooperation between the United States and the Federal Republic. In a cover memo to the President for one of the meetings on the troop level question, Bator had outlined two further issues which Johnson should keep in mind before making a decision: *'how the troop decision will affect German cooperation on money; and, most crucially, your judgment about the feedback on politics at home'*.<sup>41</sup> On the latter issue the President was particularly sensitive and needed no reminder, faced as he was by an increasingly rebellious Congress and elections drawing nearer. Bator predicted that if NATO would go down this would give the Republicans and Johnson's Democratic rivals (among

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<sup>39</sup> FRUS 1964-68, XIII, President to McCloy, 1 March 1967, p.536-37.

<sup>40</sup> See for example the remarks by Congressman Ellender and Senator Fulbright accusing McNamara of arming the whole world indiscriminately; PSSD, reel XV, House Committee on Armed Services, January 1967, p.32; US 90th cong., Senate Committee on Foreign Relations, 2 March 1967, p.137-140.

<sup>41</sup> LBJL, Bator Papers, Box 4, Memo for the President: US Position in Trilateral Negotiations, 23 February 1967.

them Robert Kennedy) a valuable issue.<sup>42</sup>

These apprehensions were probably foremost in the President's mind when he hesitated to accede to McNamara's proposals. The problem was how to sell this restraint to Congress. To escape the dilemma between the danger of becoming the President who had greatly weakened NATO and the prospect of an uproar over no cuts at all, Bator recommended a monetary deal with the Germans which could shield the President from domestic criticism, if he decided to keep the reductions to a minimum. *'There is no hope for any sort of new 100% military offset deal with the Germans. However, we may be able to get them to agree to financial steps which would be far more valuable. Specifically: --that they will not use their dollars, old or new, to buy gold, --that they will join us in pushing the other Europeans, ex-France, to agree to the same sort of rules; --to support us against France in negotiations on longer-range monetary reform; --to neutralize the military imbalance by buying and holding securities which would count against our balance of payments deficit. If we can also get the Italians, Dutch and the Belgians, as well as the U.K., Canada, Japan, to play by such rules, we will have negotiated the world onto a dollar standard. It will mean recognition of the fact that, for the time being, the U.S. must necessarily play banker of the world and that the continuing threat to convert to gold is simply unacceptable.'*<sup>43</sup>

This was a sweeping proposal, combining openly the large security and money issues which had previously formed the background of the offset story. If implemented, it would be unavoidable that the final decision regarding troop levels in Europe, with all its implications for Alliance policy and the European security structure, would depend on a basic agreement between the Federal Republic and the United States regarding the continuation of the dollar-gold system. The previously informal agreement between the Americans and the Germans regarding the structure of the Alliance and international monetary relations would be placed on a new level, a clear quid-pro-quo which would allow both sides to pursue -with the clear-

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<sup>42</sup> *ibid.*

<sup>43</sup> *ibid.* In a conversation with the President one week later, W.Rostow drew the same connection between monetary concessions by Germany and congressional acceptance of a continued stable troop level in Europe: *'If we get a good money bargain with the Germans, which will really help stabilize the monetary situation and provide protection for the dollar, then perhaps we can turn the situation around in Congress'* (LBJL, NSF, NSC Histories: Trilaterals, Box 50, Memorandum for the Record, 2 March 1967).

cut support of the other- essential foreign policies which were crucial for the shape of international politics during the 1960s. The US would support a security structure in Europe the rationality of which it had serious doubts. The Federal Republic would help stabilize an international monetary structure which it thought to be increasingly irrational. How had this far-reaching idea germinated?

#### d) The Blessing-Letter and its Implications

Towards the end of 1966, it appeared that the offset talks in the framework of the Trilaterals would lead nowhere. The trilateral studies on war capability and strategy which had been concluded relatively fast played an increasingly secondary role compared to the pressing financial questions. One of the ambiguous goals of the Trilaterals had been to establish new ways for dealing with the troop's foreign exchange cost. The first necessary step seemed to consist in establishing a commonly accepted measure for net drains and gains.

The Federal Republic hitherto had accepted the figures supplied by the United States and Great Britain. It claimed, however, that its true gains were considerably less because of the numerous side-effects of troop expenditures. The Working Group on balance of payments in the framework of the Trilateral negotiations was to review comprehensively this question.<sup>44</sup> The result of the exercise made it clear that to arrive at precise figures was impossible as long as there was no agreement on economic methods and on the extent of the side-effects of military spending. How the German reserve position would have looked without foreign troops on its soil was ultimately incalculable. The Americans, for example, arrived at a considerably higher figure for German net balance of payment gains than the Germans: \$630m as opposed to \$350m.<sup>45</sup> Even on the easier question of actual foreign exchange conversions a considerable gap remained. For 1966, the English and the Americans estimated

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<sup>44</sup> LBJL, NSF, NSC Histories: Trilaterals, Box 51, Treasury Paper: Net Balance of Payments Costs in the Military Accounts, 28 October 1966; Terms of Reference for the Working Group on Military Balance of Payments, 19 November 1966.

<sup>45</sup> *ibid.*, Box 50, Attachment to McCloy report: Balance of Payments Issues, 21 November 1966; Duckwitz, in: *Aussenpolitik* 8/1967, p.473.

their conversions at \$950m, the Germans arrived at a figure of \$825m.<sup>46</sup> The differences were irreconcilable. At the end of December, on German initiative, the task of reaching a common position was declared insoluble. The old practice of the stationing countries providing estimates was re-established and the negotiations turned to the old problem of finding a compromise despite those differences and uncertainties.

The United States estimate for troop costs in 1967-1969 was \$850-900m a year.<sup>47</sup> The relatively simple objective was to have this sum covered by offset to the maximum possible extent. First priority still was accorded to military sales; however, hardly more than the \$350m promised by Erhard were expected, and the large prepayments made to fulfil the 1965/67 offset left no space for new orders in 1967/68. A second possibility was civilian purchases, like space equipment, foreign aid projects, etc; the Germans because of their bad experience with the British and recalling the strong protests of the German industry were very reluctant in this field. More promising was the third option: German investment in US bond issues. Negotiations on such transactions were pursued between the *Bundesbank* and the US Treasury.<sup>48</sup> This would have been an extension of the various German investments in US issues to support the American balance of payments. A final idea emerged slowly and it was to prove decisive for US/German offset in 1967/68: the idea of a formal no-gold-conversion pledge by Germany, putting an end to speculations that the Federal Republic might follow the example of General de Gaulle. Such a pledge would 'crown' German monetary cooperation with the US on the whole range of issues posed by monetary problems of the 1960s. This was the core of the proposal Bator had outlined to the President.

The idea suggested itself to US planners since Kennedy's times. A standstill-agreement on gold-conversion between Europe and the United States had been debated in 1962. Dillon and Roosa, however, thought that this would be an unnecessarily alarming signal and that the

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<sup>46</sup> Osterheld (1992), p.375.

<sup>47</sup> DDRS 1994/3538, WH Background Paper for Brandt visit, 6 February 1967.

<sup>48</sup> The US government wanted Kiesinger to put pressure on 'the Bundesbank to play the kind of flexible game that is required for offsets in terms of long-term bonds'; LBJL, NSF, Memos to the President:W.Rostow, Box 11, Rostow to President, 23 November 1966.

dollar problem could be brought under control by less drastic measures.<sup>49</sup> During deliberations in the State Department on how to continue offset after the Erhard visit the proposal had been considered anew.<sup>50</sup> The Germans were immediately informed that such a pledge would be of great help to the United States and probably useful with regard to offset. These first tentative approaches remained vague because the *Bundesbank* refused to consider a commitment with such potentially enormous consequences. In late 1966, there was still hope for different solutions to the offset muddle. However, it became soon clear that a hardware solution was out of the question and that other measures were inadequate to bridge the conflicting positions.

The major problem was that Germany had no acceptable suggestions to offer. One of the common points of the coalition partners in the German government had been to avoid Erhard's mistake of getting locked into an agreement which would become a constraint and liability in both foreign and domestic policy.<sup>51</sup> Finance Minister Strauß, in particular, was against any material concessions to the US and the UK. First, the mortgaging of future budgets caused by the previous agreement curtailed funds for any purchases. Second, he and many others thought that military orders should be diverted towards the German industry and towards France.<sup>52</sup> This would have been a step towards escaping the embrace of the US government in military matters. After the Erhard visit, resentment about assertive American policies had not been limited to the Gaullists any more. The simple question was whether the American security guarantee was still worth sacrifices. The discussion on future offset in the Kiesinger Government became inevitably embedded in a larger conflict about the future course of German foreign policy.

It had been one of the central objectives of the Kiesinger government to reach a new

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<sup>49</sup> FRUS 1961-63, IX, Heller to Kennedy, 9 August 1962; Kennedy to Dillon and Ball, 24 August 1962, p.138-141; Wightman (1988), p.54-55.

<sup>50</sup> LBJL, NSF, NSC Histories: Trilaterals, Box 51, Knowlton to McCloy: Treasury Paper on Future German Offset Agreements, 8 November 1966.

<sup>51</sup> Haftendorn (1994), p.263.

<sup>52</sup> BA, B 136/3135, Memoranda for the Chancellor, 13/28 December 1966; Memo for Cabinet Meeting, 28 December 1966.

understanding with France after the nose-dive relations had taken during Erhard's tenure. The new government rapidly achieved an agreement with France on a question which had poisoned relations during the last months of Erhard's chancellorship: the status of French troops in Europe.<sup>53</sup> Technological cooperation was intensified. The Federal Republic made an effort to achieve a common EEC position for the ongoing negotiations on the creation of new reserve assets for the monetary system. This effort was closely linked to the European pressure for a reform of voting procedures in the IMF, which had until then given only the US a veto capacity whereas the Six even united had not enough votes to veto measures.<sup>54</sup> This attempt at Franco-German rapprochement coincided with a phase of unprecedented mistrust in German-American relations during the 1960s, sparked off by the rude treatment Erhard had received in Washington, by US overtures to the East, and, above all, by the proposed Non-Proliferation Treaty which to many Germans seemed like a device to discriminate against Germany indefinitely.<sup>55</sup>

It soon became obvious, however, that France and Germany, too, still had deep divergences, whether it was on European policy, on French policy towards the East, or on security policy. De Gaulle had not much to offer Bonn and much of his policy remained gestures leading nowhere.<sup>56</sup> There was no way around the Americans, at least as long as the reunification goal remained the center piece of German foreign policy and pitted Germany in hostile opposition to the Warsaw Pact. Every opening of German policy would ultimately depend on American backing. The first tentatives of 'Ostpolitik' by Brandt needed a credible 'Westpolitik'. These constraints underlined the necessity to put a stop to the rapid decline of NATO which would be certainly speeded up by large-scale reductions of US troops. The alliance with the United States remained vital for the Federal Republic and the US troop presence as a major symbol of this alliance, too. The Kiesinger government, like its

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<sup>53</sup> For the text of the agreement: BPI 161/1966, p.1304. For details on the negotiations: Willis, *France, Germany, and the New Europe, 1945-67*, 1968, p.353-6; Osterheld (1992), p.309-26; Haftendorn (1994), p.222-27.

<sup>54</sup> KCA 1967, p.22691.

<sup>55</sup> For a typical reaction to the NPT by German Conservatives, see: Grewe, *Rückblenden 1976-51, 1979*, p.689-702. For an assessment of the German response: Haftendorn (1994), p.160-66; Häckel, *Die Bundesrepublik und der Atomwaffensperrvertrag*, Bonn 1989; Kuentzel, *Bonn und die Bombe*, 1993.

<sup>56</sup> Hanrieder, *Germany, America, Europe*, 1988, p.267-68; Willis (1968), p.359-65.

predecessors, could not escape the necessity to address seriously the troop cost problem on which the US government placed such an importance.

The government itself, however, under the restraint of a very tight budgetary situation, had only very few resources for a solution at its disposal. The defence budget, the source of previous offset payments, underwent deep cuts. The further amassing of public debts to serve US offset demands was, after Erhard's experience, politically unfeasible. The only practical way out seemed to lay in the American proposals - which, however, signified to shovel the burden on the *Bundesbank's* shoulders. Thus, in a temporary alliance with the Americans, the government asked the *Bundesbank* to be more forthcoming in its talks with US officials, both on the issue of investment in US Treasury bonds and on general monetary cooperation.<sup>57</sup> The 'Grand Coalition' had already reasserted its leadership in macroeconomic policies. In December 1966, it had put publicly pressure on the *Bundesbank* to lower its interest rates. This actually happened in January 1967. Now, the government requested the *Bundesbank* to compromise its monetary principles in order to provide support for basic security policy objectives the government judged more fundamental. Though hardly any archival evidence is available it is very likely that the government and the *Bundesbank* had a hard argument over this question in which the government finally prevailed.

In both the German and the US government, the non-conversion pledge had transformed from a technical proposal to the major hope for solving the offset impasse. As in the German case, US policy in this respect can only be understood in the context of the general monetary and political circumstances in early 1967. The formation of the Kiesinger government had been accompanied by much speculation in the US about the course of future German foreign policy, -a similar situation to the one after the signing of the Franco-German treaty in 1963. Prominent politicians who were seen as exponents of a 'Gaullist' line, such as Strauß and von Guttenberg had assumed high posts. Doubts about German policy also extended to monetary policy. As already mentioned, 1967 was the decisive year for the American effort to create a new form of liquidity, Special Drawing Rights, which should relieve the pressure on the

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<sup>57</sup> Haftendorn (1994), p.266; Donfried (1991), p.128-29; Trevorton (1978), p.91.



dollar. French and American conceptions were diametrically opposed.<sup>58</sup> In early 1967, leading American commercial banks voiced open doubts about the future of the dollar-gold exchange guarantee. A lively public debate followed, reenforced by hints of Fowler that the US might take drastic steps if foreign Central Banks would not behave cooperatively.<sup>59</sup> The pressure put on the American balance of payments by the Vietnam War and the government's expansive domestic spending programs have already been mentioned in ch.X. As deficits were getting out of control, hidden only by dubious statistical tricks, and as Washington embarked on a major initiative in monetary diplomacy, formal support of the new German government for US monetary policy would be doubly important. A parallel consideration was the Kennedy-round of trade talks which approached its final phase and of which the Americans expected a positive impact on their external balance.<sup>60</sup> The US needed German support on this issue, too. These were essential interests and a confrontational German policy would have posed a very serious challenge to these policies.

As we have seen, these considerations were clearly spelled out during the US debate on the troop-level question. The argument of the necessity of German cooperation was to prove decisive. The military and political arguments of McNamara in favour of troop reductions had to stand back. If the troops could serve once more in the interest of important economic objectives, in particular to shore up the monetary system, the Treasury department would become an incidental ally of the State Department on the issue of troop levels in Europe. Thus, the non-conversion pledge became a way out of the difficult dilemma which the end of the previous offset mechanism had created.

The talks between the Bundesbank and the US Treasury had, after the slow start, accelerated in early February. The German government kept itself out of the actual negotiations to disperse the impression of government infringement on the Bundesbank's authority over monetary policy. Agreement was found quite rapidly on the question of German investment

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<sup>58</sup> Cohen S., *International Monetary Reform, 1964-69*, 1970.

<sup>59</sup> Cohen (1970), p.123; Strange, *International Monetary Relations*, 1976, p.245.

<sup>60</sup> On the Kennedy Round: Shonfield(ed), *International Economic Relations of the Western World, vol.I: Politics of Trade*, 1976; Zeiler, *American Trade & Power in the 1960s*, 1992.

in US Treasury bonds. The Bundesbank representatives declared themselves ready to acquire \$400-500m of mid-term bonds during US FY 1968. In fact, this was an extension of the book-keeping investments in Treasury Papers which had served in the years before to limit the extent of American deficits. The difference was the longer term of four years. The Bundesbank declared it 'extremely important, because of the Bundesbank law, that the transaction be cast in such form so as to not to appear that the Bank was directly or indirectly financing the government...'<sup>61</sup>. Another condition of the Germans was that the Bundesbank would be allowed to redeem the bonds prematurely if German reserves fell below a critical level.<sup>62</sup> An implicit problem was that this 'loan' supposed an amelioration of US deficits at the time the bonds were due.

The transaction was explicitly connected to the trilateral exercise. The Germans demanded that the bond purchases were counted as covering the troop cost not offset by military orders. The US Treasury accepted this conditions. Anyhow, its interest concentrated on a further request: a hardening of the German non-conversion policy in such a way that it could be used in public discussion, either by a letter or by a public declaration of the *Bundesbank* and German government.<sup>63</sup> I have found only very scarce documentation on the further course of the negotiations between the Treasury and the Bank, as well as between the German government and the Bank, and within the Bank itself. Such material certainly would be a first level source for clarifying the Bundesbank's international monetary policy, its relations to the government, and the important events in international monetary policy during the late 1960s. A detailed account of the negotiations is therefore impossible as yet and I will limit myself to results and consequences.

On 30 March, Blessing sent the famous letter. It started with the somewhat euphemistic statement that the US 'occasionally' had expressed concern over the impact of its troop dollar losses on its balance of payments. Blessing then stated his view that these costs were only

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<sup>61</sup> LBJL, Fowler Papers, Box 39, Draft Letter Deming (Undersecretary of Treasury) to Tüngeler (Bundesbank director), 18 February 1967.

<sup>62</sup> This actually happened after the DM revaluation of 1969 when Germany lost a large volume of its reserves.

<sup>63</sup> 'A large part of our difficulties relate to the public understanding as to the Bundesbank's policies, and we would like --in fact, we need-- public recognition of this policy; cf. fn.58.

one aspect in a much more complicated picture and pointed out that German reserves had not risen significantly over the past several years. However, he continued, the Bundesbank had for years refrained from conversions of dollars into gold and -the decisive phrase in the letter- the United States '*... may be assured that also in the future the Bundesbank intends to continue this policy and to play its full part in contributing to international monetary cooperation*'.<sup>64</sup>

Interestingly, Blessing later regretted the letter. In a 1971 interview he remarked that he should have been '*more rigorous towards the US. We simply should have converted the dollars we accumulated rigorously to gold until they were driven to despair*'.<sup>65</sup> That statement certainly has to be put in the context of the tumultuous events on monetary markets from 1968 on. It indicates, however, that serious misgivings existed in responsible German circles before signing the letter. It is true that the letter only confirmed a policy which had been followed for years. Such a policy was, however, open to reversal at any time. There are strong indications that the German government discussed the option of joining de Gaulle in asking the US for a raise in the price of gold.<sup>66</sup>

The disadvantages of signing a pledge of non-conversion were obvious from the German point of view. It would foster an increasing link of the DM with the Dollar because of a progressive accumulation of dollar reserves. In 1966, the share of dollars in German reserves had increased greatly (see Appendix I, table 1). These reserves would be slashed in the event of a dollar-devaluation. Germany, therefore, would have a strong incentive to support every action which helped avoid this. With the Blessing-letter, the Bundesbank deprived itself of an important part of its monetary autonomy. A foreign country acquired an increasing influence over the value of Germany's reserves. Some years later, when the Nixon administration adopted its policy of 'benign neglect' towards payments deficits and flooded the market with dollars, the Federal Republic as a main recipient was still bound by the

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<sup>64</sup> LBJL, NSF, NSC Histories: Trilaterals, Box 50, Blessing to Martin (President of the Federal Reserve), 30 March 1967.

<sup>65</sup> Brawand, *Wohin steuert die deutsche Wirtschaft?*, 1971, p.61.

<sup>66</sup> In early 1965, for example, the former Bundesbank President Vocke suggested this to Erhard; see: BA, B 136/3322, Blessing to Erhard, 25 February 1965.

pledge.<sup>67</sup>

Probably even more important than these economic aspects were the political arguments against the letter. First, Germany would lose the possibility to exert, like France, pressure on the United States via monetary policy; second, with the pledge Bonn hampered the chance to pursue a common and independent European monetary policy.<sup>68</sup> It is not without irony that at the same time when the German government was looking for a *rapprochement* with France, it effectively lined up with Washington in the vital field of monetary policy. This recalls the Strauß-Gilpatric-agreement which had condemned the military sections of the later Franco-German treaty to ineffectiveness.

These counter-arguments did not carry enough weight. The political objectives -outlined above-proved decisive once more : the deal assured the continuation of a large American troop presence, symbolizing the American adherence to the basic principles of German foreign policy. In this interest the Bundesbank had to forfeit part of its autonomy, pressed by a strong German government and the dominant monetary power, the United States.

Why did the Bundesbank concede to the pressure? Unfortunately, a definite answer will have to await the opening of the pertinent files in the *Bundesbankarchiv*. However, as this question goes right to the center of the argument in this thesis, some tentative arguments might be advanced. Research has been divided on the issue. Treverton and Donfried<sup>69</sup> assert that the Bundesbank would have continued its policy of non-conversion anyway and that the move was made to accumulate goodwill for the future. Contrary to these arguments, Volger<sup>70</sup> argues that in the absence of the pledge the Bundesbank would probably have followed de Gaulle's policy. Wightman makes a valid point when he says that the Blessing letter was signed because the Bundesbank would not want to see the dollar gold system go down on its account (although his assertion that it was signed independently from the Trilaterals is

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<sup>67</sup> Hoffmeyer (1993), p.89.

<sup>68</sup> BA, B136/3135, Memorandum for Chancellor: Trilateral Talks in Bonn, 28 November 1966.

<sup>69</sup> Treverton (1978), p.86; Donfried (1991), p.129.

<sup>70</sup> Volger, *Zahlungsbilanzausgleich...*, in: *Konjunkturpolitik* 20/1974, p.359.

astonishing).<sup>71</sup> However, whether this interest was strong enough to make acceptable such a serious limitation on the Bank's autonomy during a highly volatile international situation is very doubtful to me. Without political pressure from both the German and the American governments it is doubtful that the Bank would have agreed to a written statement. The Blessing letter was a case of the government asserting its primacy over the formation of German monetary policy in the interest of furthering essential foreign policy goals. The monetary leverage the strong DM provided was used to pursue political objectives.

The Blessing letter was the codification of the major factor behind all the offset agreements and monetary measures taken by German financial authorities to bolster the dollar: the effort to neutralise the huge amount of freely navigating dollars which threatened the American gold stock. Thus, an interpretation of the Blessing-letter cannot be limited to the letter itself and to its connection to the Trilaterals: it has to be embedded in the whole story recounted in the previous chapters. A central thesis has been that the monetary support of Germany for the US rested to a good part upon the former's dependence in security matters. Certainly, German cooperation depended not solely on the German interest to keep a guaranteed US troop presence.<sup>72</sup>

First, the international monetary system had served the Federal Republic well during most of its existence, inflationary pressure was low at almost all times during the 1950s and 1960s. Even if we allow for the special measures with which the Federal Republic had to neutralize the accumulating dollars, the Bundesbank and the Federal Government would rather incur the disadvantages of some of these measures than assume responsibility for the breakdown of the system.<sup>73</sup> The consequences of such a breakdown were unforeseeable. Maybe it might have resulted in better protection against imported inflation, but a likely result might also have been the revaluation of the DM forced by speculative pressure. The dollar gold standard had given governments and Central Banks for a long time unprecedented control over currency

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<sup>71</sup> Wightman (1988), p.555.

<sup>72</sup> As, for example, Susan Strange (1976), p.270-75, maintains.

<sup>73</sup> For German monetary policy and German measures to support the dollar gold system, see: Thiel (1978), p.137-50, especially the table on p.147.

markets, but the rising uncontrolled money flows in the 1960s, particularly the Eurodollar market seemed to erode this control. It was natural that governments and Central Banks would collaborate to avoid losing increasingly control over the use of monetary instruments.

The price, however, German monetary authorities had to pay for the continuation of the system grew continuously during the 1960s. In the earlier years, the government bore a huge part of the burden by committing itself to offset agreements with all the intended and unintended consequences pointed out in the previous chapters. Parallel to this, the Central Bank took a constructive part in the various monetary reform proposals advanced during the 1960s, partly in collaboration with the government, partly independent from it. Various other steps belong to this list. The 1961 revaluation was an important move to stabilize the situation after the gold crisis, although it probably owed more to the inherent undervaluation of the DM after the parities realignment of 1949 than to the flaws of the dollar gold system. Another case in question is German support for the Pound. This certainly constituted a big inconvenience for Germany as it had grave doubts about the wisdom of British monetary policy and must have felt like throwing money in a bottomless hole. Nonetheless, the Federal Republic was always in the forefront of the rescue actions and this has its roots in its common interest with the US to stabilize the system. This interest also has a strong connection with the stabilization of Germany's security relationships.

In the mid-1960s, the German government's part in preserving the dollar-gold system - military offset- became an increasing burden on its policies (and budget) until it was no more possible to continue with it. As the US showed no intention of abandoning the system the burden of dealing with the imbalance would fall not only on the budget of the government but also on German monetary policy. Investment in US Treasury bonds and the Blessing letter were the expressions of this fact. That the Federal Republic despite the increasing risks of supporting the dollar gold system pursued this policy, even when it infringed on its monetary autonomy, cannot be explained by economic reasons alone. From the evidence discussed over the previous pages, the conclusion is inescapable that the security relationship with the US was a - and probably the - major factor in this German support for American monetary policy.

It is difficult to assess the consequences of the Blessing letter without a detailed analysis of the developments in the monetary system after it had been signed. The US government had hoped that the pledge by the Federal Republic to refrain from conversions of dollars into gold would go far freeing the US finally from the balance of payments constraints which had bothered Eisenhower, Kennedy, and Johnson so much since 1958. *'If we succeed ... we will no longer need to worry about reasonable balance of payments deficits ... This arrangement ... will permit us to live with moderate deficits indefinitely.'*<sup>74</sup> These far-fetched hopes foundered on the impossibility of 'moderate' deficits in the next years. Already one year later, the US had to suspend the dollar-gold convertibility for the private market. Regarding the official market, however, the Blessing letter was the first step away from the dollar-gold standard. It is doubtful whether the letter prolonged the dollar-gold standard significantly.<sup>75</sup> However, this was not foreseeable in 1967, and the US would have hardly accepted it as an offset measure if it had considered the step insignificant.

#### e) Results of the Trilateral Talks

With the conclusion of the talks between the US Treasury and the Bundesbank it seemed as if the biggest obstacle to success in the Trilaterals was surmounted. However, further problems awaited resolution, in particular the British offset. At the end of January 1967, the State Secretary of the AA, Schütz, informed the British during a visit in London of the German cabinet's thinking that no offset money would be available for the British in 1967/68. This seemed a retreat from the German position in the bilateral negotiations of 1966 when the Germans had offered \$87.5m (DM 350m). The British reaction was immediate: such a position would inevitably lead to a withdrawal of large parts of the BAOR.<sup>76</sup> When the Germans retreated and tabled the October proposal anew, the British still thought the offer absolutely insufficient. The trilateral negotiations arrived at their lowest point.

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<sup>74</sup> LBJL, NSF, NSC Histories: Trilaterals, Box 50, Bator to President: Your Meeting with McCloy, 8 March 1967.

<sup>75</sup> It might have even had the paradoxical effect of impairing confidence in the dollar, as Hoffmeyer suspects: *'That the United States felt it necessary to put so much political pressure on Germany in order to protect the gold reserves was taken as a sign of weakness'*; Hoffmeyer, *The International Monetary System*, 1992, p.63.

<sup>76</sup> LBJL, Bator Papers, Box 4, London to Dept.of State on Schütz-Brown talks, 25 January 1967.

The Americans immediately communicated their disapproval in case the German cabinet made its final decision before consulting its allies.<sup>77</sup> The Germans reassured them that they would continue to participate in the talks; however, they saw themselves faced with a very serious financial situation.<sup>78</sup> A controversial debate had been going on in the Grand Coalition practically since its start about how to tackle the British offset problem with regard to the budgetary bottlenecks and the mortgaging of future defence budgets by the 1965/67 agreement. The main resistance to new obligations came from Finance Minister Strauß.<sup>79</sup> He thought that the British would reduce their troops anyway and that it was senseless to take on new commitments.

McCloy, returning in March to Europe after his consultations with the President, tried to get the adversaries to compromise. At the first meeting of the negotiators he expressed the grave concerns of the US government about the unproductive attitude taken by the other participants which explained to the poor results obtained until then.<sup>80</sup> Soon afterwards, McCloy saw Wilson and Kiesinger to impress upon them the seriousness of the situation. The long conversation with the Chancellor was a tour-de-force on the critical aspects of mutual relations.

Much of the conversation was taken up by McCloy informing the Chancellor of Johnson's annoyance about the recent public denunciation of the American non-proliferation policy by Kiesinger. The Chancellor tried to explain his government's problems with the envisaged treaty.<sup>81</sup> Switching to the Trilaterals, McCloy stated that British and American troop levels were strongly linked and that the US was likely to follow suit in case of deep cuts in British forces. Kiesinger retorted that British statements suggested that they would reduce regardless of any German offer and that the British government did not have a record of showing much

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<sup>77</sup> McGhee Papers, 1988 add., Box 1, Bonn 8678, 26 January 1967.

<sup>78</sup> *ibid.*, Bonn 8683: Cabinet Decision on Offset, 26 January 1967; Bonn 8747: McGhee Meeting with Brandt, 27 January 1967.

<sup>79</sup> FAZ, 4 February 1967.

<sup>80</sup> LBJL, NSF, NSC Histories: Trilaterals, Box 50, London 7112/7113: Trilateral talks, 3 March 1967.

<sup>81</sup> FRUS 1964-68, XIII, Rostow to President: Kiesinger-McCloy Meeting, 6 March 1967.



concern for German foreign policy interests. The budgetary situation was critical and the UK had hardly enough useful military or civilian goods on offer to achieve sufficient offset value.<sup>82</sup> However, Kiesinger promised an attempt to raise the German offer. Towards the end of the discussion, McCloy asked how Germany would react to the reduction of one US division. Kiesinger merely replied that it was an 'interesting suggestion'.

This was the first time a German Chancellor had abandoned the dogma of a stable US troop level which had been upheld since the Radford-episode. Already in 1966, troop reductions had been regarded as unavoidable by the German government. However, only Kiesinger felt that the international and domestic situation permit him to accede to the American request, and only if the redeployment was of a limited nature. Finally, McCloy warned the Chancellor of the unfortunate impression which would be created in the US if the Federal Republic, as had been reported, were to switch its military procurement towards France. Kiesinger replied -not entirely correctly - that this was not seriously contemplated.<sup>83</sup>

In a discussion the following day with Foreign Minister Brandt, McCloy went over much the same ground. He was, however, clearly told that there were few chances to get more for the UK than the amounts suggested in October 1966.<sup>84</sup> Back in Washington, McCloy informed the President that the major remaining problem for a successful conclusion of the trilateral negotiations was the gap between the German offer and British expectations. The US government considered whether it would be feasible to pick up part of the bill. Both McNamara and Fowler were against picking up any of the gap; the latter was still embittered that his push for a decisive reduction had failed once more.<sup>85</sup> However, after some hectic work on possible alternatives, Johnson told McCloy that he '*would not see NATO go down over \$40m*', (which was the size of the gap). He instructed McCloy to conclude the talk on

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<sup>82</sup> *ibid.*, p.541.

<sup>83</sup> *ibid.*, p.547.

<sup>84</sup> LBJL, NSF, NSC Histories: Trilaterals, Box 50, Bonn 10267, 5 March 1967.

<sup>85</sup> LBJL, NSF, NSC Histories: Trilaterals, Box 50, Bator Memo for President: Your 12:45 meeting with McCloy, 8 March 1967; Record of the President's March 8 meeting with Rusk, McNamara, et. al.

the basis of limited reductions<sup>86</sup>, and to try to get as much out of the Germans before the US would put in its own money.<sup>87</sup> In the meantime, the British had indicated that they would possibly settle for less than 100% offset, that is £60m (\$168m), and would limit their withdrawals to one brigade in this case.<sup>88</sup> All depended now on the German willingness to raise their offer. LBJ wrote a letter to Kiesinger urging upon him once more the importance of keeping the British forces on the continent.<sup>89</sup>

The German decision was made during a very heated cabinet meeting on 15 March. Against Strauss' bitter resistance, Kiesinger forced through an increase of the German offer to DM400-450m (\$100-112m), split equally between military and civilian material.<sup>90</sup> The British, under pressure from Washington, decided to count the US help from December and the gains from the relocation of US forces from France to Britain as part of the offset, and thus reduced the gap to about \$20m. This was a sum the US felt able to pay as a price for the rapid conclusion of the talks: it promised to procure a corresponding amount of military material in the UK.<sup>91</sup>

After this breakthrough, the only problem remaining was whether the Germans would formally accept the American plan to redeploy 35000 men from the 7th army and over 50% of its tactical aircraft. Having evaluated the US proposals, the Germans expressed strong concern with the huge cut in air forces. They thought it a heavy impairment of NATO strike capacity and the start of a denuclearization of Europe.<sup>92</sup> Shortly after Johnson's meeting with

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<sup>86</sup> For the US: reduction/rotation of one division and three air wings; for the UK: one brigade.

<sup>87</sup> LBJL, NSF, NSC Histories: Trilaterals, Box 50, Record of President's Meeting with McCloy, 9 March 1967.

<sup>88</sup> *ibid.*, Brown to Rusk, 9 March 1967.

<sup>89</sup> In this letter, he also requested German cooperation in reserve creation for the monetary system. FRUS 1964-68, XIII, 11 March 1967, p.546-49.

<sup>90</sup> LBJL, NSF, NSC Histories: Trilaterals, Box 50, Bonn 10754, 15 March 1967.

<sup>91</sup> FRUS 1964-68, XIII, Memcon McCloy-Rostow, 15 March 1967, p.549-50; LBJL, NSF, NSC Histories: Trilaterals, Box 50, Bator to President: Trilaterals Status Report, 17 March 1967; Aide-Memoire US Government to HMG, 21 March 1967.

<sup>92</sup> *ibid.*, Memorandum received from German embassy, 21 April 1967; US Government memo to German embassy, 22 April 1967; McGhee Papers, 1988 add., Box 1, McGhee to LBJ: Suggested Talking Points with Kiesinger, 25 April 1967; Box 2, Bonn 12415, Discussion with Carstens, 18 April 1967; DDRS 1985/1021, Bonn

Kiesinger on the occasion of Adenauer's funeral, the McCloy-State Department faction won another victory over McNamara: LBJ decided to cut only 96 aircraft instead of the 144 planned. Again the argument, that this would make the Germans more forthcoming on international money and the Kennedy round, carried the day.<sup>93</sup> This settled the last open issue and at the end of April a series of Agreed Minutes was signed recording the results of the Trilaterals.<sup>94</sup> Regarding troop levels this meant reductions of 5000 men and 2 squadrons of aircraft in the case of the British, and 35.000 men and 96 of 216 aircraft in the case of the US. One third of the US forces to be redeployed would always remain in Germany on a rotational base. This costly rotation system was soon abandoned. What counted, in the end, was that the continuity of the large-scale presence of American and British soldiers in the Federal Republic was for the moment secured.

Once more, in a series of closely fought compromises, all sides were able to save their basic positions. The British government had assured that their troop commitment in Europe would place no strains on the embattled position of their currency. They had achieved a small reduction to silence their critics at home. The Americans had been able to present a satisfactory solution to Congress, they had managed to avert the danger of a break-down of NATO, and had set the Alliance on the way towards a new strategic assessment. Most importantly, however, they had with one single big stroke achieved unparalleled cooperation by the strongest monetary surplus country, the Federal Republic. The latter had safeguarded the traditional security structure and the allies' adherence to forward defence. They had assured the security guarantee of their powerful military allies symbolized by their troop maintenance. The Atlantic Alliance, the essential framework for German foreign policy, had been preserved.

In hindsight, one is struck by a certain irony inherent in this hard fought result. Most of the basic positions which it was to shore up would be swept anyway by inexorable developments.

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12730: McCloy to Rusk, 24 April 1967.

<sup>93</sup> LBJL, NSF, NSC Histories: Trilaterals, Box 50, Bator to President, 27 April 1967; Rusk to McCloy, 27 April 1967.

<sup>94</sup> FRUS 1964-68, XIII, p.562-69.

Sterling would go down in the whirlpool of a new monetary crisis towards the end of the year. In November 1967, it was devalued by 14%.<sup>95</sup> Pressure on the American currency augmented despite German support. The devaluation of Sterling had directed the attention of the markets to the other reserve currency. In early 1968 a new record run on American gold reserves started.<sup>96</sup> At the end, the American government was forced to abandon the dollar gold convertibility for the free market. In a way, this was the end of the dollar gold system because most Central Banks had already been negotiated on a dollar standard.

The Federal Republic undertook a major revision of its policy towards the East which became known as Ostpolitik. As a result, the strict dogma against allied troop reductions in Germany was dissolved and Bonn achieved new flexibility in its foreign policy.

#### f) Outlook

These events did not mean the end of offset. Already at the end of 1967, negotiations for new agreements commenced.<sup>97</sup> These agreements, continuing until the mid-1970s, were still heavily contested.<sup>98</sup> However, a decisive change in their character took place, at least in the American-German context. The Mansfield Resolution in August 1966 was the first shot in a prolonged, intensive debate in the United States about the necessity and purpose of its troops in Europe, and, in the end, about the US engagement in Europe in general.<sup>99</sup> Offset had an important place in this debate. The Nixon and Ford administrations were forced, like LBJ, to demonstrate to Congress that the American troop engagement was, at least regarding the

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<sup>95</sup> Odell (1982), p.173-8.

<sup>96</sup> LBJL, NSF, NSC Histories: The Gold Crisis, Box 53, narrative.

<sup>97</sup> DDRS 95/2139, Read memorandum for Rostow: US-FRG Military Cost Neutralization Talks, 7 May 1968.

<sup>98</sup> On those agreements see: Baumann, 'Devisenausgleich und Sicherheit', in: WEHRKUNDE, Vol.17/1968, p.245-251; Boeck/Krägenau, 'Devisenausgleich und Burden-Sharing', in: WIRTSCHAFTSDIENST, 51/1971, p.91-94; Medick, 'Burden-Sharing als deutsch-amerikanisches Problem', in: Knapp(ed), *Die Deutsch-Amerikanischen Beziehungen nach 1945*, 1975, p.188-228; Thiel, *Dollar-Dominanz, Lastenteilung und Amerikanische Truppenpräsenz in Europa*, 1979; Thiel, 'Dollarkrise und Bündnispolitik', in: EUROPA-ARCHIV 28/1973, p.373-381.

<sup>99</sup> For this important debate in the US, see: Newhouse J.(ed), *US Troops in Europe. Issues, Costs, and Choices*, 1971; Williams (1985); Yochelson, 'The American Military Presence in Germany. Current Debate in the US', in: ORBIS 15(1971), p.784-807.

monetary problem, no burden on the US. The Offset agreements of 1967 and 1968, consisting mainly in purchases of Treasury bonds by the Bundesbank<sup>100</sup>, were not at all helpful in calming the heated debate and Mansfield styled them *'the phoniest deal I have ever seen ... not sharing cost but making a profitable investment.'*<sup>101</sup> The Nixon/Kissinger administration, however, accorded to the Atlantic Alliance a much more important place than Johnson. They were determined to resist the calls for troop reductions and succeeded in the end despite some extremely close votes in Congress. Paradoxically, it was Leonid Brezhnev who provided the most valuable help in this effort by agreeing to open negotiations on Mutual Balanced Force Reductions (MBFR). This would have made unilateral reductions by the US a gift to the Soviets and Congress was hesitant to go this far. Within the logic of 'double containment', Brezhnev's intervention made even some sense.

The traditional offset approach was finally made completely obsolete by the breakdown of the dollar gold system in 1971-73 and the US policy of 'benign neglect' towards the accumulating dollar reserves in Europe.<sup>102</sup> The monetary movements during the turmoil in the markets were so large that offset measures were not sufficient to stem the tide. The unilateral actions by the US government during the currency crises convinced the Europeans of the necessity of an independent policy and they undertook an abortive effort to create a European Monetary System; their possibilities remained, however, limited.

The Federal government was increasingly unwilling to accede to pressures from the US for burden sharing and take on unnecessary burdens only to avoid troop reductions. Helmut Schmidt, then Defence Minister, declared in 1970 in the United States: *'I do not belong to the people who start to wince if only the Pentagon redeploys a kitchen brigade from the officers' mess in Heidelberg. And I am the first to admit that essential changes in the international situation may justify a revision of the numbers of troops needed in Europe. There is no dogma that the US troops have to remain once and for ever in the present*

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<sup>100</sup> See Appendix II.

<sup>101</sup> NYT, 19 August 1968, p.9.

<sup>102</sup> Cohen B., 'A Bargain Comes Unstuck. The Revolution in Atlantic Economic Relations', in: Hanrieder(ed), *The United States and Western Europe*, 1974, p.406-37.

*strength in Europe.*<sup>103</sup> Later, Schmidt termed offset '*a camouflage for occupation costs, which was certainly long outdated*'.<sup>104</sup> He used the first opportunity to bury the old offset scheme formally. In the summer of 1976 the US government declared itself ready to take such a step. It published a common declaration with the Federal Government: '*Given the recently introduced changes in the international monetary area, specifically flexible exchange rates, as well as the notably improved strength of the dollar and a more acceptable United States balance-of-payments position, the President and the Chancellor consider that the traditional offset arrangements approach has lost its relevance*'.<sup>105</sup>

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<sup>103</sup> Speech to the Council of Foreign Relations, New York, 8 April 1970, in: BPI 49/11 April 1970, p.466.

<sup>104</sup> Schmidt H., *Menschen und Mächte*, 1987, p.176.

<sup>105</sup> Keesing AdG 1976, 20373F.

## CONCLUSIONS

Allied troop maintenance in Germany gave rise to a series of problems which underlined the interrelation of security and monetary issues in British-German and American-German relations. NATO had given security questions a strongly interdependent character. This was paralleled by increasing interdependence in the international monetary policies of roughly the same countries. Not only the direct evidence of the support cost and offset negotiations but also related factors like, for example, the positive influence of foreign troop stationing on the German balance of payments (ch.I), the financial consequences of German rearmament (ch.II), the allied use of these troops to relieve their payment's balance from serious pressure, or the use of the arms trade to balance payments disequilibria, have been cited in this thesis.

The Atlantic security system and international monetary system were two sides of the same coin. Changes in one sphere invariably influenced the other. Expansive American security policies after the war, whether those were troop commitments abroad, foreign aid, or political pressure in the interest of shaping the Alliance, played an essential part in putting the dollar-gold system into existence. These policies were only possible in a system which protected the US economy from the disruptive effects of its balance of payments deficits. The European side of the bargain was military protection and an international environment conducive to economic reconstruction and growth. Countries like the Federal Republic, which saw the provision of security by the US as essential, would adapt to the monetary system and actively support it. Britain, being less dependent was pursuing a more independent policy, though at a high cost.

The most fundamental underlying structural change analysed in this thesis has been the slowly widening incompatibility of the Atlantic security structure and the international monetary system. This became increasingly evident during the 1960s whereas in the 1950s these two spheres complemented each other by and large and formed the foundation for transatlantic economic and political relations. The monetary system was no more able to cope with burdens imposed by expensive American policies abroad, many of which, like troop stationing in Germany, had been answers to specific political problems in the 1950s. The tensions deriving

from fundamental economic changes and, later on, from changes in the Cold War environment manifested themselves in the crises of the monetary system. The straw that broke the camel's back was probably the burden imposed by the Vietnam War. These changes were reflected in the financial problems connected with British and American troop deployments in Germany which form the empirical base of the thesis.

The first part of the study concentrated on the British-German conflict, placing it in a variety of contexts. The support cost question has only a limited importance if it is seen apart from these contexts. The problem of the foreign exchange cost of British troops in Germany has to be set in particular in relation to British sterling policy. This policy, emphasizing the role of Sterling as the second reserve currency, was placed under heavy strain by fundamental British political choices, most notably the maintenance of the remains of Britain's imperial past and the attempt to hold on to an independent military posture. In order to fit into the Atlantic system as it evolved during the early 1950s, the British would have had to abandon the reserve currency role of Sterling, accept a European role, and bring its defence policies into line with those of the rest of NATO. Those were the more or less secret hopes of American policy-makers. However, the UK was not willing for such a sweeping transformation of its traditional policies. It tried to allievate the pressures on its policies by reforming features of the Atlantic security system, particularly those related to the defence of Europe.

This collided with German interests. The Federal Republic saw in the specific security structure which emerged in 1955, that is conventional forward defence under the protection of the American nuclear umbrella, the best guarantee of its survival as long as it was not able to defend itself autonomously. British policies to reform the structure thus invariably met German resistance.

The conflict about troop costs shows this clearly. It derived not primarily from a financial problem but from the fundamental ambiguity in British policy about the rationales of its security commitment in Europe. British governments never developed a consistent policy towards their troop commitment and the perceived imperatives of the Sterling policy provided a lasting incentive to withdraw from the commitment, as evidenced in the debate on the



British White Paper 1957 (ch.III) or, later, during the Trilateral Negotiations of 1966/67. The British monetary argument was strongly interrelated with an emphasis on a cheaper nuclear deterrence, a general belief in the economic counter-productivity of high military expenditure, and perceptions of declining East-West tensions.

However, the British efforts to retreat from the WEU commitment failed. Somewhat paradoxically, they failed largely because of the political importance the troops had acquired despite the British dislike of the commitment. The BAOR had become an essential element of the Atlantic security structure. Whether it was pressure from the partner in the 'special relationship', problems of accomodating to European integration (ch.IV), political advantages regarding monetary cooperation or problems like the armaments trade (ch.V), on all those issues the credibility of the British troop commitment had a strong bearing. Those political rationales in favour of a continuation of the troop commitment proved to be extremely persistent. In 1967, Sterling was devalued while British troops remained in Germany in roughly the same strength until the 1990s. British politicians and the British public in general portrayed their troop commitment continuously as a burden and nuisance. This deprived the UK of any chance to make a positive use of the troop commitment to reap political or substantial economic benefits (ch.IV). The support costs, in any case, had not at all the intended effect of stabilizing the British currency.

Troop costs remained an issue in Anglo-German relations until the mid-1970s. The decisive part of the German government perceived British policy after 1955 as a continuing series of challenges to some of its basic foreign policy principles. The troop reductions debate and the British disarmament proposals were interpreted in this way. This was also true for the creation of EFTA. More economic cooperation without a corresponding political commitment was of little value for the Federal Republic which was painfully aware of the contrast between economic power and limited political influence. This awareness was sharpened by support cost conflicts. The major potential leverage of Britain -collaboration in security matters and East-West policy- withered away during these conflicts and other instances in which the British displayed their unwillingness to cooperate with the Federal Republic politically, economically, and militarily.

Consequently, the Germans were very reluctant to meet the British on European policy or on financial matters (ch.IV). They could have done so easily and the increasing strength of the German currency provided the Federal Republic with an important lever. Unfortunately, a political history of German monetary policy in the late 1950s and the 1960s, which scrutinizes the importance of this instrument more comprehensively, is still lacking and my analysis can cover only a few aspects. German monetary power worked often by default rather than through a direct use of the financial instrument. Bonn (and Frankfurt) collaborated with their allies to a higher or lower degree, in a way closely related to political objectives. Collaboration with the US thus remained very strong throughout the period under research, whereas collaboration with the UK was pursued reluctantly, with many qualifications, and often more related to German-American relations than to any objectives in the British-German context.

Germany's confrontational policy towards Britain over the support cost issue was made possible because the US commitment seemed more or less guaranteed after the Radford plan was blocked (and because France provided an alternative to Britain on the regional level). However, the relative certainty regarding the American commitment was to wane rapidly in the following years, when the US balance of payments plunged into deficit and forced the Americans to take a close look at the cost of their security commitments (ch.VII). The American response to this predicament, however, was neither a radical reform of their monetary policy nor a reappraisal of their security policy. Expedients were sought which would offer relatively painless possibilities of perpetuating both the security and the monetary systems.

An important part of the solution were the offset agreements. The first offset agreement was not - as most of the literature suggests in an ex post facto rationalization - the simple result of an assertive American use of its security leverage. The agreement was an elaborate compromise combining vital interests of both sides and the Federal Republic obtained important concessions (ch.VIII). Only when offset became an institutionalized factor, did tensions grow over the years and an increasing gap emerged between American and German objectives.

Offset was an important palliative in place of radical reforms either in the international monetary system or in American economic and security policies. It was necessary because a decisive breakthrough of the American government in its battle against the balance of payments deficit was a long time in coming and because the surplus countries got increasingly restive about the dollar glut (particularly France which directly challenged the US).

The receipts from military sales in the framework of the agreements became a vital factor for the military payments balance (ch.IX). Together with the Dillon/Roosa policy of 'peripheral' defences for the dollar, offset allowed the US to carry on their expansive domestic and military policies and to preserve at the same time the dollar-gold system. Furthermore, the offset system served to justify the continuation of an essentially unchanged American security commitment in Europe, first against critics within the administration and, after 1966, increasingly against Congressional initiatives.

At this point, the interests of the Germans and parts of the American government converged. Essential security concerns and important domestic political objectives made a stable troop level a central interest of the Adenauer and Erhard governments. With offset payments, that is in effect by using German monetary power, they succeeded in perpetuating this status despite the powerful counter-current emanating from new strategic ideas, financial constraints, Vietnam, détente, etc. In the first years, the offset agreements also provided the Federal Republic with important military benefits such as access to advanced military equipment and crucial logistic support for the *Bundeswehr* (ch.VIII).

The benefits of the offset agreements, however, were increasingly overshadowed by serious political and financial disadvantages. Offset became a straightjacket for German foreign policy in so far as it impeded military and political cooperation with other countries, particularly France, and fostered increasing dependence on the US. The financial burden connected with offset limited funds for other government programs, contributing thus to a serious budgetary crisis in 1965-67 (ch.X). Constraints also became increasingly visible in the conduct of German monetary policy.

However, after the disastrous Erhard visit in September 1966, the Federal Republic saw itself

confronted once more with the choice of allowing the erosion of the traditional security structure in which its foreign policy was embedded or to bind itself even more strongly to an international monetary regime it considered increasingly irrational. Once more, security considerations and alliance policy proved overriding concerns. The Blessing letter, even if it signified no great change of monetary policy (it robbed the FRG, however, of the option to initiate such a change) and even if it was insufficient to preserve the dollar-gold system, symbolised the bargain once more: monetary support for security in the framework of the Atlantic Alliance (ch.XI). However, the turmoil in the monetary markets of the late 1960s soon swept these desperate stopgaps away.

The results of the thesis also have shown clearly that German foreign policy in the postwar period cannot be understood if solely seen with the approach of traditional diplomatic history separating economic and security (or alliance) policies. A perspective linking those two spheres has to be included in accounts of Bonn's external policy much more systematically than hitherto. *Offset* provides only one aspect, though an unusually illuminating one.

At the end, one feels strongly that much more needs to be done to place the results of this research in a comprehensive framework. Many questions remained unanswered or open to revision. An archive-based political history of international monetary relations in the 1960s, and of respective policies by essential countries, is the first big gap that comes to my mind. The economics of defence and security policy have not received enough consideration and are essential for understanding many security issues of the 1950s and 1960s on which innumerable pages have already been written. Only then can the question of the intricate relationship between the economy of the Western World and Cold War security policy during the first three postwar decades be adequately answered.

**APPENDIX I:**

Table 1: Basic Figures on German Reserve Position and Federal Budget (Defence), 1950-1969

Table 2: Selected American and British Balance of Payments Figures, 1954-68

Table 3: Allied Troop Levels in Germany, 1954-68

Table 4: Estimated Foreign Exchange Cost of Allied Troops in Germany as Stated by the Sending Countries, 1955-69

Table 5: Military Transactions in the German Balance of Payments, 1952-1964

Table 6: Bundeswehr expenditure for Material, Maintenance, R&D, 1956-67

Table 7: Pre-Payment of German Postwar Debts

**APPENDIX II:**

Support Cost and Offset Agreements between Germany and the Sending Countries USA, United Kingdom, France, Belgium, Netherlands, Denmark, Canada, 1955-1969

note: Figures in the Appendices are cited in the currency in which they appear in the source text, if not otherwise indicated. Exchange rates of dollars, pounds, and marks in the 1950s and 1960s were as follows:

Dollar - DM:           September 1949 - March 1961: 1\$ = DM 4.20;  
March 1961 - October 1969: 1\$ = DM 4.00;  
from October 1969: 1\$ = DM 3.66

Sterling - Dollar:     September 1949: 1£ = \$2.80;  
from November 1967: 1£ = \$2.40.

Sterling - DM:         September 1949 - March 1961: 1£ = DM 11.76;  
March 1961 - November 1967: 1£ = DM 11.20;  
November 1967 - October 1969: 1£ = DM 9.60

## APPENDIX I:

Table 1:

**Basic Figures on German Reserve Position and Federal Budget,  
1950-1968 (in billion DM)**

	German Currency Reserves	Gold Reserves	Dollar- Reserves	Federal Budget - Expenditure	German Defence Expenditure
1950	0.80	—	0.63	14.7	4.6
1951	1.91	0.12	1.42	20.9	7.9
1952	3.11	0.59	2.08	23.1	7.9
1953	5.67	1.37	3.54	27.9	7.4
1954	8.77	2.63	5.44	28.2	8.0
1955	10.48	3.86	5.76	29.7	6.1
1956	14.76	6.27	7.30	33.3	7.3
1957	17.58	10.67	6.12	36.3	7.5
1958	20.09	11.09	7.41	40.4	8.8
1959	20.17	11.08	7.26	42.7	9.4
1960	29.59	12.48	14.98	33.1	8.2
1961	28.72	14.65	10.89	52.3	12.9
1962	27.86	14.71	10.79	57.9	17.2
1963	29.52	15.37	11.67	58.8	19.5
1964	28.83	16.99	7.71	65.5	18.8
1965	27.32	17.64	5.17	69.1	19.3
1966	30.72	17.17	8.31	72.5	19.7
1967	30.21	16.91	8.51	80.6	21.6
1968	34.89	18.16	8.56	80.7	18.7

**Sources:**

col.1-3: (year end figures): Deutsche Bundesbank (ed), *40 Jahre Deutsche Mark. Monetäre Statistiken 1948-87*, 1988, p.346.

col 4-5: (until 1959: years from 1 April - 30 March; 1960: 1 April - 31 December; 1961-68: calendar years) Bundesministerium der Finanzen, *Finanzbericht 1969*, p.446-449.

Table 2:  
Selected American and British Balance of Payments Figures, 1954-68

This table is to give some illustration of one of the major developments influencing the events described in the thesis: the strain on the American and British monetary position. It can not substitute a commented, comprehensive picture of the US and UK balance of payments.

	-----UNITED STATES (\$ million)-----				-----BRITAIN-----		
	Liquidity Balance	Net Military Expenditure	Total Reserves Assets	Gold Reserves	Current Balance (£ m)	Balance for Official Financing (£ m)	UK Official Reserves (\$ m)
1954	-1541	-2460	22978	21793	+117	+126	2762
1955	-1242	-2701	22797	21753	-155	-229	2120
1956	-0923	-2788	23666	22058	+208	-159	2133
1957	+0621	-2841	24832	22857	+233	+13	2273
1958	-3348	-3135	22540	20582	+360	+290	3069
1959	-3648	-2805	21504	19507	+172	+18	2736
1960	-3677	-2753	19359	17804	-228	+325	3231
1961	-2252	-2596	18753	16947	+47	-339	3318
1962	-2854	-2448	17220	16057	+155	+192	2806
1963	-2713	-2304	16843	15596	+125	-58	2658
1964	-2696	-2133	16672	15471	-362	-695	2315
1965	-2478	-2122	15450	13806	-43	-353	3004
1966	-2151	-2935	14882	13235	+113	-547	3100
1967	-4683	-3228	14830	12065	-289	-671	2694
1968	-1611	-3143	15710	10892	-273	-1410	2421

Sources:

- US Figures: column 1: 1954-59: Gross Liquidity Balance; 1960-68: Net Liquidity Balance; source: Survey of Current Business 10/1972, 6/1975, p.26-27.  
column 2: Direct Expenditures minus Military Sales; Economic Report of the President 1975, p.350  
column 3/4: Economic Report of the President 1975, p.356.
- UK Figures: note: British balance of payments accounts have undergone substantial revisions since the time they were published first. Contemporary figures cited in the text therefore do not coincide with the figures in this table which are useful to indicate general longterm trends.  
column 5: The Current Balance combines the visible and invisible trade balance.  
column 6: Total sum (current balance + capital transfers + net investment and other capital transactions + balancing item) that has to be met by (or contributes to) official financing.  
1967/68 figures include special losses due to the devaluation in 1967. High minuses indicate years with strong pressure on Sterling.  
column 7: gold + foreign exchange  
source: CSO, Economic Trends. Annual Supplement, 1981, p.124, 144.

TABLE 3

## Allied Troop Levels in Germany 1954-68 (in Thousands)

Year	United States	Great Britain (BAOR + RAF)
1954	251.5	82.0 (+ 26)
1955	247.6	80.0 (+ 26)
1956	250.3	80.0 (+ 25)
1957	235.2	77.0 (+ 25)
1958	227.8	63.5 (+15.5)
1959	229.7	56.0 (+15.5)
1960	226.5	56.0 (+ 15.5)
1961	232.9	51.0 (+ 8.7)
1962	277.6 <sup>1</sup>	51.0 (+ 8.7)
1963	251.6	51.0 (+ 8.7)
1964	263.0	51.3 (+ 8.7)
1965	262.3	51.0 (+ 8.7)
1966	236.7	53.3 (+ 8.5)
1967	215.0	52.0 (+ 8.5)
1968	210.0	52.0 (+ 8.5)

Sources: US 1954-63: NSA, *The Berlin Crisis*, Doc.1924: USAREUR Report: *The Replacement and Augmentation Systems in Europe (1945-63)*, March 1964, after 63: Nelson, *A History of US military forces in West Germany*, 1987, p.81. Mahncke, *Amerikaner in Deutschland*, 1992, p.138-39.

UK: 1954-63: own compilation on the base of source material in the PRO; 1963-68: KCA, various years.

<sup>1</sup> DDRS 1993/754, Presidents Talking Points for Erhard Visit, 26.12.63 state following figures: 1961 pre-Berlin crises 242.000; post-Berlin crises 273000; Dec 1963: 242000



**TABLE 4:**  
**Local Foreign Exchange Cost of American and British Troops in Germany**

note: Estimating the local DM cost of Allied troops in Germany was a very complicated task, and figures differ considerably from source to source, particularly in the British case. The table gives the figures brought forward publicly by the stationing countries. These often do not coincide with figures cited in archival sources. Prior to 1955 the local DM costs were almost entirely covered by German payments. UK figures below are net figures, excluding German payments after 1955. From the US figures, 1955-57, German payments are deducted.

	UK forces (£ million)	US forces (\$ million)
1955	69	291
1956	64	345
1957	63	479
1958	57	660
1959	51	664
1960	59	649
1961	60	636
1962	68	749
1963	73	691
1964	84	694
1965	84	714
1966	82	770
1967	90	837
1968	94	877

**Sources:**

- UK:** 1955-56: PRO, CAB 134/1209, Treasury Note on Organisational and Administrative Economics, 5 June 1956  
 1957-63: PRO, FO 371/172175, Stationing Costs of British Forces in Germany: Report by Officials, autumn 1963.  
 1964-68: Keesings Contemporary Archives, various years  
 1959-68: Freedman, 'Britains Contribution to NATO', in: IA 54, 1978
- US:** 1955-59: Mendershausen, *Troop Stationing in Germany. Value and Cost*, 1968, p.63.  
 1960-68: Survey of Current Business, December 1969, p.44.

TABLE 5:

**Military Transactions in the German Balance of Payments, 1952-64**  
(million DM)

	-----Receipts-----			-----Expenses-----		
	total receipts	thereof: receipts from foreign military agencies	thereof: receipts from US agencies	thereof: Arms Exports	Prepayments on Military Orders	Arms Imports
1952	814	814	800	-	-	-
1953	1110	1110	1077	-	-	-
1954	999	999	956	-	-	-
1955	1192	1192	1112	-	-	-
1956	1673	1673	1516	-	236	4
1957	2519	2519	2130	-	1741	346
1958	3598	3598	2843	-	-285	1650
1959	3956	3956	2981	-	1429	1330
1960	4100	4100	3064	-	1109	1497
1961	3824	3824	2708	-	211	1584
1962	4300	4300	3119	-	248	2508
1963	4955	4289	2960	655	-273	4398
1964	4715	4220	2857	439	832	2895

Source: Bundesbank-Archiv B 330/10245, Vermerk: Militrische Transaktionen mit dem Ausland, 25.8.65

note: Receipts do not show the actual amount of foreign exchange needed by the stationing countries in given years. They represent conversions by the stationing countries at German banks. Occupation costs and support costs, that is marks used directly by the troops, lowered the total amount of conversions, contrary to offset payments. In the years after 1955, the stationing countries used turn-over occupation funds, which had not been used during the occupation period.

TABLE 6:

**Foreign and Domestic Bundeswehr Expenditures for Materiel, Maintenance, and R&D, 1956-67 (\$ million)**

Year	Domestic	US	UK	France	Italy	Others	Total
1956	339	126	—	13	—	18	496
1957	265	301	26	22	6	95	714
1958	530	276	9	32	2	18	867
1959	427	390	28	77	28	91	1042
1960	504	147	17	74	18	173	933
1961	865	226	18	60	38	112	1320
1962	1250	367	50	82	40	177	1966
1963	1278	568	95	134	35	219	2328
1964	1198	530	19	172	51	167	2137
1965	1097	430	23	130	22	120	1823
1966	1162	156	39	106	22	66	1551
1967	1476	222	37	123	13	82	1953

Source: Mendershausen, *Troop Stationing in Germany: Value and Cost*, 1968, p.132.

note: Once more, the most plausible figures had to be chosen among several widely diverging sources. The figures of Mendershausen correspond best to the dispersed data in archival documents.

TABLE 7

**Prepayment of German Postwar Debts**

The London Debt Agreement, February 1953, had settled the amount West Germany had to repay of prewar debts and reimbursable postwar aid. Due to the positive development of its external account and in connection with payments offsetting the foreign exchange cost of allied troops in Germany, Germany managed to repay these debts earlier than scheduled.

	USA(\$m)		UK (in £m)	France(\$m)
	Postwar Aid	STEG-Agreement		
original debt	1000	200.4	150	11.84
payments on schedule until 1961	62.63	183.9	60	4.736
prepayments 1959	150	-	22.5	1.776
status March 1961	787.37	16.5	67.5	5.328
prepayment March/April 1961	587	-	67.5	5.328
payments on schedule	-	5.9	-	-
Status end 1962	200.37	10.6		
December 1966	-	-	-	-

Source: Bundesbankarchiv, B330/10245, Note on German Postwar Debts, 15 January 1963.

## APPENDIX II

## Support Cost and Offset Agreements between Germany and the Stationing Countries, 1955-1970

before 1955: occupation costs	April 1952 - April 1955 DM 600m/month
1955-56	<p>NATO Finance Convention, Art.IV, amended by Schedule III to the Protocol on the Termination of the Occupation Regime in the FRG, 23.10.1954</p> <p>Term: 5.5.1955 - 4.5.1956</p> <p>Content: Prolungation of German occupation costs: \$762m (DM 3200m) a year</p> <p>British share: \$140m US share: \$350m</p> <p>Sources: FRUS 1952-54, V/2, p.1342-43; HMSO, cmd.9304(54).</p>

Support Cost Agreement  1956-1957	<p><b>BRITAIN:</b></p> <p>29.6.1956</p> <p>Term: 5.5.1956-31.3.57</p> <p>Content: DM 400m support costs; declaration of intention by the German government to buy British weapons in Britain up to \$524m/year</p> <p>Reference: HMSO, Cmd 9802(1956)</p>	<p><b>UNITED STATES:</b></p> <p>7.6.1956</p> <p>Term: 5.6.56-5.5.57</p> <p>Provisions: DM 650m support costs</p> <p>Reference: KCA 1956, p.15288</p>	<p><b>OTHERS:</b></p> <p>29.6.1956: France (DM278m)</p> <p>6.7.1956: Denmark (DM2.275m)</p> <p>10.7.1956 Netherlands(DM0.773m)</p> <p>20.7.1956 Belgium(DM118m) Canada (DM6.585m)</p> <p>Reference: KCA 1956, p.15288</p>
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Support Cost Negotiations 1957-1958	<b>BRITAIN</b>	<b>UNITED STATES</b>	<b>OTHERS</b>
	7.6.1957 term: 1.4.1957-31.3.58 content: - support costs: DM 588m - deposit of £75m by the BdL at the Bank of England to be used for settlement of outstanding German postwar debt - enlargement of the German account for arms purchases at the BoE to £30m - intention of Fed.govt. to buy a "considerable" amount of weapons in the UK  Reference: HMSO, Cmnd 256 (57) BGBL, 1959,II, p.414-17.	7.6.1957 term: 6.5.57-5.5.58 Content: DM 325m support costs  further: US reserves itself the right to request a supplementary contribution during 1957  Reference: BGBL II, 1959, p.410-411	7.6.1957 Support Costs to France: DM 225m Belgium: DM 59m Denmark: DM 1.2m NL: DM 0.4m  Reference: BGBL II, 17, 1959, p.419-431.

Support Cost Negotiations 1957-1958	<b>BRITAIN</b>	<b>UNITED STATES</b>	<b>OTHERS</b>
	3.10.1958 Term: 1.4.1958-31.3.1961 Content: - UK declaration to keep 55.000 men in Germany during 1958 and 45.000 until 1961 - support costs: DM 141.2m/year in 1958-1960 - interest free deposit of £50m by German government at the Bank of England to be used for payments of arms orders in Britain - advance repayment of postwar debts (1962-64 instalments): £22.5m  Reference: BGBL, 1959, II, 545-548; HMSO, Cmnd.588(1958)	24.3.1959 Term: unspecified Content: prepayment of postwar debts: \$150m  Reference: (not identified in published form) BA, B 136/3132, Kabinettsvorlage AA, 10 March 1959.	FRANCE 17.9.1959 Term: unspecified Content: prepayment of postwar debt (1962-64 instalments): \$1.776  Reference: see US

Offset Agreements during the 1960s

United States	Britain
<p>24.10.1961 term: 1.7.1961-30.6.1963 content: military purchases (\$ 1425m; DM 5700m) reference: AAPD 1963, p.864, fn.37</p>	<p>6.6.1962 term: 1.4.1962-31.3.1964 content: Germany makes purchases (mainly arms) to the tune of £54m (DM600m) in the UK Reference: HMSO, Cmnd.1766 (1962); Bundesanzeiger, 8.6.1962</p>
<p>14.9.1962 term: 1.7.1963-30.6.1965 content: military purchases (\$1400m; DM5600m) reference: not published; McGhee papers, 1988add, Box 2</p>	<p>27.7.1964 term: 1.4.1964-31.3.1966 content: undertaking by German government to offset British costs 'as fully as possible' Reference: BPI, 28.7.1964; HMSO, Cmnd 2434 (1964)</p>
<p>11.5.1964 term: 1.7.1965-30.6.1967 content: military purchases (\$1.35bn); advance payments on military procurement (DM 3.14bn); reference: AAPD 1964, p.526,fn.2</p>	<p>20.7.1965 term: 1.4.1965-31.3.1967 content: renegotiation of previous agreement; - immediate non-returnable payment of £42m on contracts already placed or foreseen - financing of additional British exports: £45m - offset for the year 66/67 (£54m) reference: BPI 125/1965, p.1009; HMSO, Cmnd.2731 (1965)</p>
<p>28.4.1967 term: 1.7.1967-30.6.1968 content: Germany buys mid-term US treasury bonds (DM2bn); formal statement by Bundesbank to refrain from exchanging dollars to gold reference: DOS Bulletin, 22.5.1967; BPI, 47/6.5.1967.</p>	<p>5.5.1967 term: 1.4.1967-30.3.1968 content: German purchases of £18m(DM200m) of military equipment and £22.5m(DM250m) of civilian equipment; £9m (DM100m) made by private German firms reference: HMSO, Cmnd.3293 (1967)</p>
<p>10.6.1968 term: 1.7.1968 - 30.6.1969 content: Offset \$785m (\$100m military equipment; \$500m Bundesbank investment in mid-term Treasury bonds; Lufthansa buys Boeing aircraft for \$60m) reference: BPI 74, 15.6.1968, p.627; DOS Bulletin, 7/1968, p.14</p>	<p>28.3.1968 term: 1.4.1968-31.3.1969 content: offset of £54m(DM510m) (£22m defence purchases; £21m civilian purchases by public authorities; £10.5m civil private purchases) - Bundesbank invests about £21m(DM200m) in British medium term government bonds reference: KCA 1968, 22618;</p>
<p>9.7.1969 term: 1.7.1969-30.6.1971 content: military procurement (DM 3.2bn) renunciation of interest rewards (DM 130m); civilian purchases (DM 500m) long-term financial transactions (DM 2.25bn) thereof: 10-year loan by Federal Government of DM1bn; Germany buys claims of the EXIM bank and from the Marshall-Plan (DM 475m); debt pre-payment (DM 175m); direct investment of the FRG in the US (DM 600m) reference: BPI 92, 11.7.1969, p.792; DOS Bulletin, 4.8.1969, p.92.</p>	<p>22.7.1969 term:1.4.1969-31.3.1971 offset: £106m (£47m defence purchases; £36m civilian purchases; £33m government promoted private civil purchases, loan to UK government of DM500m (£52m) at 3.5% interest, repayable after 10 years reference: KCA 1969, p.23753-4.</p>





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## ACKNOWLEDGEMENTS

Writing this thesis has been for most of the time an enjoyable experience. The EUI and my friends here deserve most of the credit for this.

The EUI and the German Historical Institute in Washington provided me with funds to carry out the extensive research which went into this thesis. The staff of these institutions and of the various archives I visited deserve special mentioning. Its impossible to name them all.

Prof. Griffiths always supported me and never allowed me to loose the goal of a completed thesis out of sight, not even in the Bar Fiasco.

My thanks go to Prof.Krieger who permitted me to use the NHP sources at his Lehrstuhl and -most importantly- gently pushed me towards the subject of this thesis quite some years ago. Prof.Milward and Prof.Abelshauser also read and commented parts of the thesis, the latter allowing me to present some results at his research colloquium in Bielefeld (as did Prof.Krieger in Marburg). Special thanks go to Prof.Trachtenberg, Philidalphia, for his very helpful comments on my work.

Sir Frank Roberts and Bundestagspräsident a.D. von Hassel (whom I thank also for permitting me to use his military diary written during his tenure as Defence Minister) granted me interviews.

Many other people had the 'great pleasure' of reading drafts of my work: Monika Dickhaus, Francis Gavin, Claire Hancock, Christine Knudsen, Rory O'Connell, Lorenza Sebesta, Carlo Spagnolo. Thanks to all of them and to those I forgot.

Florence

October 1996











