Trading with the Enemy

Security and Relative Economic Gains

When do security concerns lead states to restrict economic cooperation? Attention to this subject has turned recently from the security effects of resource dependence to those of relative gain. Since wealth is the main source of military capability and other means of influence, cooperation that creates and distributes wealth affects security as well as welfare. Rational states will thus weigh the security implications of cooperation alongside its benefits in making foreign economic policy. The recent debate has been over whether, and under what conditions, states will limit mutually beneficial exchange with rivals who are obtaining disproportionate gains.¹

Understanding the connection between security and economic cooperation is essential for anticipating the future of both. Pessimists on this issue, assuming that states are highly sensitive to unequal gains, predict a spiral of insecurity, sundered trade ties, and possibly war in the post–Cold War era. John Mearsheimer, for example, has argued that as Soviet and U.S. power recedes from Europe, “Western European states will begin viewing each other with greater fear and suspicion. . . . Consequently they will worry about the imbalances in gains as well as the loss of autonomy that results from cooperation. . . .

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Conflict will be more likely. Indeed, some American authors have urged restrictions on trade with Japan to stem disproportionate Japanese gains. Trade conflict bodes ill for peace, since highly interdependent nations might be tempted to regain lost markets and resources by force.

Whether states resist adverse relative gains for security reasons is also important to the theoretical debate between neorealists and neoliberals about the sources of international cooperation. Neoliberal theories have generally assumed that states pursue absolute gains only, and this assumption supports the idea that information-providing and issue-linking institutions significantly heighten international cooperation. Neorealists, on the other hand, contend that sensitivity to relative gains intensifies distributional conflicts and cannot be easily addressed by international institutions. Several relative-gains questions are involved in this debate, including questions of when unequal military gains obstruct cooperation, when economic competitiveness concerns obstruct cooperation, and when power explains the distributional characteristics of agreements. But the question of when states resist relative economic gain to protect their security is also relevant.

Theoretical analyses of relative gains in the literature have argued that relative-gains sensitivity is affected by the political-military relationship between the nations involved, the offense-defense balance, and system structure. They contend that relative-gains sensitivity should be attenuated by a low likelihood of war, by defense dominance, and by multipolarity, and that it should be heightened by the converse of these factors. This is somewhat reassuring, because the post–Cold War era is both multipolar and—because of nuclear deterrence—defense dominant. But while theorizing alone can tell us when states should be more or less sensitive to relative gains, it cannot provide

the empirical referents needed to establish the real-world significance of relative-gains concerns.

There has been some excellent empirical research on relative gains, but much remains to be done. Studies on U.S. economic warfare and embargoes against the Soviet bloc during the Cold War have shown that relative gains can obstruct economic cooperation under bipolarity. In studies of U.S.–European Community (EC) and U.S.-Japan economic relations in the waning years of the Cold War, Joseph Grieco and Michael Mastanduno claim to find instances of relative-gains conflicts that are motivated by security. Since the parties were allies, this would suggest that relative-gains concerns are generally very powerful. But since, as I will argue below, the observed disputes were probably due to welfare concerns, these studies show very little about security-driven economic conflict. Joanne Gowa and Edward Mansfield have shown that allies trade more with each other than do non-allies under bipolarity, but that this relationship virtually disappears under multipolarity. While consistent with the relative-gains hypotheses, this research does not examine relative gains per se, and does not verify that statecraft was responsible (that is, the possibility of war by itself might have made the trading climate less hospitable).

In this article I argue that relative economic gains are unlikely to interfere with cooperation in multipolar international systems. My argument is part theoretical and part empirical. I supplement the arguments advanced in the literature about multipolarity by pointing out that relative economic gains are likely to be fairly even, particularly among the nations most likely to care about them. When gaps in gains are small, relative power shifts slowly, increasing the significance of threat duration and of system structure for relative-gains sensitivity. I also provide two case studies that test the relative-gains hypothesis

in multipolar situations: British trade with Germany prior to the First World War and U.S. trade with Japan in the decade leading up to the Second. British and U.S. officials perceived dramatically increased threats from rivals gaining relatively more. If relative gains matter at all in multipolar systems, they should have mattered here. But neither Britain nor the United States significantly restricted trade until war was virtually upon them. Thus relative-gains theory flunks two fairly easy tests.

This provides grounds for skepticism about the security significance of relative economic gains, and for some optimism about international trade in the multipolar post–Cold War world. If relative-gains concerns have failed to interrupt commerce under multipolarity when the threat of war is great, one would not expect it to block cooperation among much more secure states. And since nuclear deterrence provides a measure of security among the current great powers, security concerns are unlikely to obstruct economic cooperation among them, except perhaps when it comes to the transfer of militarily sensitive technologies or the loss of military-industrial self-sufficiency.

The next section of this article reviews the key conditions affecting states' security concerns about relative gains. The subsequent section explains that relative-gains disputes can be caused by welfare concerns as well as security concerns, and that failing to distinguish the two causes has led to confusion in hypothesis testing. The article then turns to the two case studies, and concludes by analyzing their implications for the relative-gains debate and for the likelihood of economic conflict in the post–Cold War world.

When Do Relative Gains Threaten National Security?

According to realist logic, from which the relative-gains problem is derived, states' sensitivity to adverse relative gains depends on the political-military relationship between the two nations involved, system polarity, and the offense-defense balance. I summarize these factors here, because they have been analyzed only separately in the literature, and because a thorough specification of causes helps in theory testing. In addition, I argue that gaps in gains are likely to be small from trade among those nations most likely to care.

Realism predicts that states gaining less than potential enemies will have a security incentive to re-negotiate terms or to limit their cooperation. Grieco puts this insight into the strongest possible form when he claims that, since states "are fundamentally concerned about their physical survival and their political independence," their "fundamental goal . . . in any relationship is not
to attain the highest possible individual gain or payoff; instead it is to prevent others from achieving advances in their relative capabilities." The result is that each state "will decline to join, will leave, or will sharply limit its commitment to a cooperative arrangement if it believes that gaps in otherwise mutually positive gains favor partners." In this economic analogue of preventive war, states will make sacrifices to stem losses in relative power.

Similar concerns should affect intra- and inter-alliance economic cooperation, even where gains are symmetric. Since all gains, equal or unequal, contribute to military power, states have a security incentive to cooperate with allies rather than with adversaries, even at some economic cost. Gowa has thus argued that the "security externalities" of trade lead states to impose optimum tariffs against adversaries more often than against allies. Although there are some important differences between the security-externalities and relative-gains hypotheses, they spring from a common realist logic, and should be subject to similar qualifying conditions.

The most basic condition affecting a state's sensitivity to relative gains is the degree of military threat posed by its rival/partner. When war is improbable, states worry less about shifts in relative power. The threat posed by a particular nation depends largely on its power, geographic proximity, offensive capabilities, and hostile intentions. In general, states will fear the relative gains of nearby, powerful, offensively armed, and hostile nations more than those of distant, weak, defensively armed, and friendly ones. Threat is also affected by whether the prevailing geography and military technology make military victory easy or difficult, i.e., by the offense-defense balance. Defensive advantage mitigates the security significance of adverse relative gains by increasing the military advantage necessary for a successful attack. For example, to the extent

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10. Thus Grieco argues that sensitivity to gaps in gains—what he calls the coefficient of relative gains sensitivity, "k"—depends on the probability that they will be converted into military threats. Grieco, *Cooperation among Nations*, pp. 45-46.
that having an assured nuclear-destruction capability deters attack by states with superior military-industrial muscle, it also makes relative gains less significant to security.\textsuperscript{13}

The expected duration of a threat also influences sensitivity to the security consequences of relative gains. Duration matters in international politics because short-term threats require immediate action, while remote ones call for preparing for the future. For temporary rivals, the future balance of capabilities is less important than the existing one, in both military and economic competition. Arms racing, for example, is more common among states locked in a protracted antagonism, whether because of geographic proximity or historical grievances, than those with a passing dispute.\textsuperscript{14}

System structure is an important determinant of relative-gains sensitivity because it conditions the direction and variability of threats. These aspects of threat matter because bilateral economic conflict to maintain a state’s position \textit{vis-à-vis} a specific rival would hurt the position of both relative to others who cooperate with each other. This insight is illustrated by Robert Axelrod’s iterated, multi-player Prisoner’s Dilemma tournaments, which Tit-for-Tat won overall despite being incapable of winning any individual match-up.\textsuperscript{15} Snidal’s models of the relative-gains problem similarly show that as the number of players increase from two, relative-gains sensitivity drops sharply.\textsuperscript{16} Axelrod’s and Snidal’s approaches assume, unrealistically, that players cannot be eliminated, that payoffs are symmetric, and that international conflict is undifferentiated (i.e., all international dyads are equally conflict-prone). But these simplifications do not invalidate the basic insight that economic conflict weakens rivals relative to different enemies in the future.

This is significant because rivalries and alliances can change over time, especially under multipolarity.\textsuperscript{17} Superpowers in bipolar systems are locked in rivalry, because they are the only states that can threaten each other. Since the direction of the threat is predictable and enduring, they are extremely sensitive

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\item[16.] Snidal, “Relative Gains”; and Snidal, “International Cooperation.”
\item[17.] Gowa, “Bipolarity, Multipolarity, and Free Trade.”
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to their relative power. Superpowers do not worry that a costly rivalry will weaken them relative to other nations, because the others are so far behind. Unsurprisingly, East-West trade during the Cold War provides a clear demonstration of security-motivated relative-gains policy. Believing that trade would provide greater benefits to the smaller and more backward Soviet economy, U.S. officials halted trade with the Soviet bloc during the 1950s and 1960s, and continued to embargo high-tech exports afterwards.¹⁸

By contrast, as Kenneth Waltz puts it, "in multipolar systems there are too many powers to permit any of them to draw clear and fixed lines between allies and adversaries."¹⁹ Threats can appear from multiple directions, and today's enemy may be tomorrow's ally. The shortened duration of rivalries and alliances makes the great powers in a multipolar system less averse than superpowers under bipolarity to rivals' gains. Even when there is a single, clear enemy, multipolarity reduces relative-gains sensitivity by introducing collective-action problems. Each state tends to shirk the costs of reducing cooperation with a shared adversary for the good of their common security. Great powers in multipolar systems can try to shift security burdens to their allies, while superpowers in a bipolar system (though not their lesser allies) lack this option.

These system-structure hypotheses apply inversely to intra-alliance relations. Under bipolarity, most smaller powers ally with the superpower least dangerous to them, usually the one the furthest away, and security dependence assures their loyalty. Alliance stability increases intra-alliance generosity. Superpowers may even be willing to make large grants, such as the billions of U.S. dollars in Marshall Plan aid to Europe early in the Cold War, to bolster total alliance strength.²⁰ But under multipolarity, alliance fluidity and greater equality of size makes great powers less generous to their allies.

Sensitivity to relative gains is affected, thus, by the specifics of the partners' political-military relationship, the offense-defense balance, and the polarity of the system. But resistance to unequal gain depends on the magnitude of the asymmetry as well as the sensitivity factor. This obvious point must nevertheless be kept in mind, because states will often be able to negotiate equal benefits

¹⁸. Mastanduno, Economic Containment.
or compensatory side-payments. For the relative-gains problem to limit cooperation, therefore, equal bargains or side-agreements must be difficult to negotiate.21

One might expect that negotiating gain-leveling side-payments would be difficult for simple trade, due to the difficulty in estimating the size and distribution of trade gains. Even without side-payments, however, gains from trade are not likely to be very skewed. Trade benefits depend on the supply and demand elasticities in each country for the goods exchanged. These, in turn, depend on the size of a nation’s economy, its level of development, and the composition of its resource endowment. In general, the countries with the greatest to gain from trade are those with the smallest economies relative to prospective trading partners, while gains among equals tend to be fairly balanced.22 But great powers are threatened mainly by each other, not by small nations. As a result, gaps in gains from trade will usually be smallest when they matter most and largest when they matter least.23

Gains can be more skewed, however, for trade in certain goods. While all traded goods contribute to output and economic growth, some contribute more than others. A nation’s economy is particularly dependent on imports of goods for which demand is highly inelastic and domestic production is extremely inefficient, especially those that have multiplier effects on the whole economy. By embargoing such items, a rival nation with a total or near monopoly on production will cause much more damage to the dependent country’s economy than to its own. Conversely, exporting them—at least at prices not reflecting this monopoly power—brings greater relative gain to the importer. Thus nations engaged in economic warfare generally devote extra energy to denving certain “strategic” goods to their foes. For example, since sophisticated technology was an economic bottleneck for the Soviet Union, the Western allies banned high-tech exports to the Soviet bloc longer and more rigorously than other kinds of goods.24

23. This point is alluded to by Grieco, Cooperation among Nations, p. 46; and by Snidal, “Relative Gains Problem,” p. 739.
If the gains are only slightly skewed, relative power will shift gradually. Power shifts will also be gradual because gains from trade work slowly; it takes time for exporters to specialize and achieve economies of scale, for efficiency improvements to be realized, and for income benefits to be translated into military power. Only certain types of economic cooperation, such as the export of militarily sensitive technologies, can quickly alter a military balance. Furthermore, states can compensate for uneven gains in the near term by increasing their military spending rates, unless they are already fully mobilized for war.25 As a result, others’ economic gains pose a security threat not this year or next, but after many years of cooperation. Thus it is future threats that lead states to worry about the security implications of economic cooperation. In contrast, sometimes slight changes in relative military capabilities can harm a state’s security immediately.26 Expected duration of the threat, and hence system structure, are therefore more significant for economic than for military competition.

In sum, a state’s sensitivity to relative gains depends on the degree and duration of the security threat posed by specific economic partners, but this sensitivity is attenuated in multipolar international systems, and when the defense is dominant. Gaps in gains from trade differ significantly from gaps in military gains, moreover, because they accrue more gradually and are proportionate to the power differentials of trading partners. Thus the security implications of relative economic gains should be low in multipolar systems, even among adversaries, and particularly among nuclear-armed states. Under these conditions, policymakers will tend to focus on prosperity or political objectives in formulating trade policy.

Relative Gains, National Prosperity, and Theory-Testing

National security is not the only reason that states might balk at unequal gains. Interest in prosperity alone leads states to forgo absolute but unequal economic gains, when these bring absolute economic losses in the long run. These two sources of relative-gains concerns, the pursuit of security and the pursuit of welfare, need to be distinguished in theorizing and in theory testing. Ambigu-

ity on this point has weakened the conclusions of some theory-testing efforts, and it therefore warrants a brief discussion.

Immediate relative economic gains can result in greater long-run opportunity costs in a variety of ways. An example is agreeing to a division of benefits when holding out would have led to a better bargain.27 Striving for prosperity via economic competitiveness can also lead states to clash over relative gains. Strategic trade theory contends that relative gains in market share confer competitive advantages to certain profitable, high-tech industries. States engaging in strategic trade policy use subsidies or trade barriers to maintain or increase market share, in an effort to maximize national economic growth.28 The transfer of technology or managerial expertise, whether by licensing, co-development, or co-production, can also risk a firm or an industry's competitiveness. States might forbid such transfer, passing up immediate gains that might result in greater long-run losses.29

As Robert Powell has pointed out, security-motivated and prosperity-motivated relative-gains seeking can both be formulated as long-run welfare maximization. The difference is that in the security variant, a nation's long-run welfare can be put at risk from attack or coercion (rather than from underselling) by nations that have gained relatively more in the short run.30 But it is important to keep track of the mechanism by which short-term unequal gains translate into long-term absolute losses. Realist hypotheses apply only when security concerns drive relative-gains worries. System structure, the offense-defense balance, or particular political-military relationships need not systematically affect economic-competitiveness policy. Competitiveness policy and disputes are instead driven by economic variables, specific to certain nations and products, like the capacity to convert temporary market-share advantages or transferred technologies into long-run competitive advantages.

But contributions to the relative-gains debate have sometimes blurred the welfare-security distinction. Studies by Grieco and Mastanduno claimed to demonstrate security-motivated relative-gains conflict, but actually found

30. Powell, "Absolute and Relative Gains."
conflicts over economic competitiveness and prosperity. Grieco shows that during the 1980s, the European Community sabotaged nontariff-barrier agreements with the United States involving government procurement and technical standards, agreements that gave both sides absolute gains but favored the United States. Mastanduno describes U.S. resistance to cooperation with Japan on fighter aircraft co-development, satellite trade, and supercomputer trade, arising from opposition to relative Japanese gains. Both authors, by calling their relative-gains hypotheses "realist," suggest that these conflicts were rooted ultimately in security concerns. Moreover, Grieco claims that his study is a crucial, "least likely" test because "realism is not usually applied to relations among states that are on friendly terms." He concludes that sensitivity to gaps in gains is generally high, because conflict occurred when realist logic predicts that sensitivity should be quite low. Mastanduno does not classify his cases as "least likely," but attributes decreasing U.S. generosity toward Japan to the loosening of their security ties at the end of the Cold War.

But their evidence suggests that welfare concerns were at least as important as security concerns, and perhaps the sole cause of conflict. According to Grieco’s account, "EC efforts regarding technical barriers and government procurement were viewed in Europe as directly affecting the EC’s lagging technological position vis-à-vis the United States and Japan." A very likely explanation is that the EC was willing to forgo short-term gains to foster high-tech industries that would bring prosperity in the long run. Mastanduno admits outright that in U.S. policy towards Japan in the 1980s, "the immediate concern was not military security, but economic well-being." For example, when the United States tried to pry open the Japanese supercomputer market, it did so to advance "the long-term economic interests of the United States, even if it conflicted with the short-term concerns of American firms." Even in

31. The two studies are Grieco, Cooperation among Nations; and Mastanduno, “Do Relative Gains Matter?”
32. Grieco, Cooperation among Nations, p. 14. Since realism has been tested more for political-military rather than economic behavior, Grieco also points out that predictions for the latter also provide a relatively difficult hurdle for the theory.
34. Grieco, Cooperation among Nations, p. 207.
35. Keohane criticizes Grieco, but not Mastanduno, for failing to demonstrate relative-gains motives in empirical research, in “Institutional Theory,” pp. 279–283. My point is a different one: even if both showed relative-gains seeking for competitiveness reasons, that still would not show that security concerns played a role.
U.S.-Japanese fighter collaboration, U.S. officials worried more about the risk to the U.S. commercial aircraft industry than about relative power or autonomy. Indeed the Defense and State Departments—the agencies most likely to worry about U.S. security—favored collaboration, while the Commerce Department and the U.S. Trade Representative were opposed.

While their theorizing stresses concerns for survival and military security, Grieco’s and Mastanduno’s interpretations of their cases stress fears about eroding autonomy. But there are two problems with this tack as a means of maintaining a realist explanation. First, no evidence is provided to show that it was autonomy rather than prosperity that motivated decisionmaking. Second, the causal link between relative economic gains and autonomy is unclear. As Helen Milner has pointed out, following Albert Hirschman’s classic argument, positive relative gains increase rather than decrease dependence on trading partners. It is also unclear how gaps in gains in a particular economic sector—with the possible exception of military industries—would compromise a state’s autonomy overall.

If the conflicts observed by Grieco and Mastanduno were really over long-term prosperity, then they tell us nothing about the effects of security concerns on economic cooperation. The cases are not even “least likely” tests of an economic theory of conflict. For a formulation of the relative-gains problem involving economic competitiveness and prosperity, the status of the test depends on the degree of economic, rather than military, rivalry. Since the EC, Japan, and the United States are each other’s chief potential rivals in aerospace, computing, and other high-technology exports, one would expect to see competitiveness conflicts to erupt among them if anywhere. Lessened U.S. generosity toward the EC and Japan can be explained just as plausibly by growing fears of foreign high-tech competition as by eroding security ties.

*Cases of Antagonism and Trade*

Security-motivated relative-gains seeking may not have been found among Cold War allies, but it has certainly been demonstrated between Cold War adversaries. The U.S.-led embargoes against the Soviet bloc mentioned earlier show that relative-gains concerns sometimes do lead to economic conflict. This

is consistent with the system-structure hypothesis, if not the offense-defense balance hypothesis, and the decline in economic warfare after the 1960s is consistent with the hypothesis that sensitivity depends on the degree of specific threats. But it still remains to be shown whether security concerns lead to relative-gains seeking in multipolar settings.

The two case studies presented in this section indicate that security-motivated relative-gains sensitivity is, in fact, quite low under multipolarity. I examine trade relations between the United States and Britain from 1890 to 1914 and between the United States and Japan from 1930 to 1941. These cases were selected because at least one side in each case perceived both military danger and adverse asymmetric gains. As a result, they should be fairly easy tests for the relative-gains argument, at least for multipolar systems. The case-study method is useful here because perceptions of threat and of relative gain are most accurately measured by qualitative assessments. Tracing officials’ reported motives and calculations also helps to identify alternative explanations, including idiosyncratic ones that might affect generalizability of my findings.

**BRITAIN AND GERMANY, 1890–1914**

For most of the nineteenth century, Britain maintained “splendid isolation” from continental squabbles. The British conception of basic security consisted of a two-power naval standard and the continued political division of the continent. Having a navy as great as the next two combined was needed not only to defend the empire, but also to protect the home islands’ trading lifelines. A balance of power on the continent assured that no European land power could concentrate its forces against Britain. As both of these criteria were easily met, British officials had only to fend off French and Russian encroachments on remote imperial possessions.

But the emergence of a powerful and aggressive Germany at the turn of the century overshadowed these quarrels.\(^{40}\) With new offensive naval forces and

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aggressiveness, and considerable overall power, Germany became a clear threat to Britain after the turn of the century. The offense-defense balance between them was complex. On one hand, the English Channel and North Sea provided a geographical buffer that Germany’s continental neighbors lacked. But if this made invasion difficult, it also made a trade-dependent Britain vulnerable to naval blockade. In addition, the perception of offensive advantages in land warfare forced the British to worry about the prospect of German hegemony over Europe.

The German Navy Laws of 1898 and 1900 launched a massive naval build-up, which in size and warship design was clearly meant to challenge Britain’s naval security and to compel its accommodation to German overseas expansion. The increase in German warship tonnage, from 285,000 in 1900 to 1.3 million by 1914, was not merely a threat to the empire, but to Britain itself. The First Lord of the Royal Navy observed as early as 1902 that “the great new German navy is being carefully built up from the point of view of a war with us.” If the German fleet ever becomes superior to ours,” wrote Foreign Secretary Edward Grey, “the German army can conquer this country.”

British officials also grew increasingly concerned over the German threat to the European balance of power. Germany’s strength had grown relative to France since its decisive victory in the Franco-Prussian War. Russia had been badly bruised by defeat in the 1904–05 Russo-Japanese War, and failed to challenge Austria’s annexation of Bosnia in 1908. This looked especially ominous in light of the German naval build-up. A Germany victorious in Europe could dispense with maintaining land armies on multiple fronts, focus its energies on naval expansion, draw additional resources from vanquished nations, and utilize bases along the English Channel coast. “Invasion would then no longer be a remote danger,” wrote a prominent British politician in 1906, “but a very imminent one.”

43. Quoted in Kennedy, Rise and Fall of British Naval Mastery, p. 215.
45. Viscount Alfred Milner, a prominent Liberal imperialist who had served as governor of the Cape Colony and Transvaal from 1897–1905, quoted in Kennedy, Anglo-German Antagonism, p. 428.
British fears were compounded by evidence of German hostility and aggressiveness. The kaiser’s clamoring for an overseas “place in the sun” was not well-received by the empire with the greatest overseas possessions. Germany began by demanding Moroccan independence from France in 1905 and the outright surrender of the French Congo in 1911. Hardly comforting was the kaiser’s remark to Britain’s naval intelligence chief, during the first Moroccan crisis, that “we know the road to Paris, and we will get there again if needs be. They should remember that no fleet can defend Paris.”46 The militarism fomented in Germany by military and nationalist leagues and by a jingoistic media fueled invasion scares and Germanophobia in Britain, reaching the highest policymaking councils. Even as early as 1903, two years before assuming leadership of the Foreign Office, Grey had concluded that Germany was “our worst enemy and our greatest danger. I do not doubt that there are many Germans well disposed to us, but they are a minority.”47 The permanent under-secretary in the Foreign Office noted in 1906 that it was “generally recognized that Germany is the one disturbing factor owing to her ambitious schemes for a ‘Weltpolitik’ and for naval as well as a military supremacy in Europe”; his successor maintained that “the ultimate aims of Germany surely are, without doubt, to obtain the preponderance on the continent of Europe, and when she is strong enough, [to] enter on a contest with us for maritime supremacy.”48 In an influential 1907 re-evaluation of the Anglo-German relationship, Grey’s senior advisor, Eyre Crowe, argued that German foreign policy was deceitful and hostile to Britain. He concluded that “the vain hopes that in this matter Germany can be ‘conciliated’ and made more friendly must definitely be given up.”49

Conflict with Germany was not considered to be permanent and inevitable. British “interests would not be served by Germany being reduced to the rank of a weak Power,” Crowe argued in his 1907 brief, “as this might easily lead to a Franco-Russian predominance equally, if not more, formidable to the British Empire.”50 Russia’s recovery from its 1905 debacle also provided some

46. Quoted in Kennedy, Anglo-German Antagonism, p. 277.
47. Quoted in Steiner, Britain, p. 40. See also ibid., pp. 57–58, 175–187; and Kennedy, Anglo-German Antagonism, pp. 448, 361–385.
48. Charles Hardinge and Arthur Nicolson, respectively, quoted in Wilson, Policy of the Entente, p. 100.
reassurance about the continental balance of power. In fact, the Anglo-German antagonism seemed to have peaked between 1905 and 1911, and London subsequently cooperated with Berlin on the 1912 Balkan Crisis, the Baghdad Railway, and a possible future division of Portuguese colonies. Nevertheless, Germany’s naval build-up, military superiority over France, and bellicose behavior since the turn of the century had turned it into the greatest danger to Britain since Napoleonic France.

Britain responded to the increased German threat with internal and external balancing. Britain joined in the naval race, increasing naval tonnage from 1 million in 1900 to 2.7 million by 1914. While British military spending did not increase dramatically, much of the far-flung Royal Navy was brought back home. Major redeployments, in 1905–06 and again in 1912, nearly doubled the size of the home-water fleet, leaving Britain’s global imperial interests protected only by new treaties and understandings with other powers. Britain also inched toward a continental commitment. Anglo-French military contingency planning began in 1905, and Grey informed the German and French ambassadors that Britain would not stand aside if Germany attacked France. Planning began in 1906 for the deployment of an expeditionary force to France in the event of German attack, and it was reviewed and extended during the Second Moroccan Crisis in 1911. In 1912 the British promised to protect France’s northern coast in exchange for French protection of British interests in the Mediterranean, and by early 1913 the two navies had begun joint operational planning and had shared signal codes. Britain had also improved ties to Russia in a 1907 accord which not only settled outstanding imperial differences, but also reflected the belief that “an entente between Russia, France and ourselves would be absolutely secure. If it is necessary to check Germany it could then be done.” While still falling short of an explicit alliance, the close military coordination and planning of the Entente in the years leading up to the war indicate that the British believed Germany to be its chief adversary.

52. Kennedy, Rise and Fall of the Great Powers, p. 203; Rise and Fall of British Naval Mastery, p. 229.
53. Kennedy, Rise and Fall of British Naval Mastery, ch. 8.
The British also felt that they were gaining less from Anglo-German trade than were the Germans during this period. The British economy remained larger than Germany’s, fourteen percent larger in 1910, according to one later estimate; this did not include the colonies, which amounted to nearly a quarter of the world’s population and land. British policymakers probably had an exaggerated sense of Britain’s continued economic supremacy, but were quite aware that Germany was gaining quickly. Although German gains had many causes, Anglo-German trade was seen as an important one. Made in Germany, a British best-seller in 1896, contended that “on all hands England’s industrial supremacy is tottering to its fall, and this result is largely German work.” Its author wrote in 1900 that tariffs “would bring Germany to her knees, pleading for our clemency.” A widely-read British journalist argued in 1912 that German “resources will be crippled when Great Britain introduces Protection,” making war against England “impossible.” One history of British views of Anglo-German trade concludes that “there was a wide opinion that the conclusion of a Pan-Britanic customs union would lead rapidly to a decline in German prosperity and the transfer of many German industries to Britain.” Its author, moreover, agrees that “the Germans doubtless would have got the worse” of a tariff war with Britain, “the markets of Britain and her Empire being a great deal more valuable to German business than the German market was to British firms.”

The security implications of German economic gains were not lost on British hawks during the worsening of Anglo-German relations. One prominent observer reported back from a tour through Germany in 1909 that “every one of these new factory chimneys is a gun pointed at England.” But despite heightened security fears and perceptions of adverse relative gains, Anglo-German cooperation in trade persisted. Britain stuck resolutely to its sixty-year old laissez-faire policy, maintaining zero tariffs on industrial imports, even while corresponding German tariffs averaged 13 percent. Private cooperation be-

60. Quoted in Hoffman, Great Britain, p. 293.
Figure 1. British Naval Spending and Anglo-German Trade, 1890–1913 (£ millions).

NOTE: Total trade = imports plus exports, not including British re-exports to Germany.

between British and German firms flourished; over half of the prewar international producer cartels (including one in explosives) were Anglo-German.\(^{64}\) As a result, total trade between the rivals doubled between 1900 and 1914 (see Figure 1). It also increased as a proportion of Britain’s total foreign trade, from an average of about 7 percent prior to 1905 to about 9 percent thereafter.\(^{65}\) Moreover, Britain was importing (and becoming dependent upon) militarily significant German manufactures, including steel bars, wire rods, plates and

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64. Steiner, Britain, p. 63.
sheets, pig iron, khaki dye (for uniforms), optical equipment, high precision tools, and automobiles.66

British trade restrictions were sporadic and minor. Canada extended preferential treatment to U.K. goods in 1897, which terminated the Anglo-German most-favored-nation arrangement of 1865, but this had no effect on British tariffs. The British Patent Law of 1907 obliged holders of patents in Britain to manufacture at least a token amount of their goods within its borders.67 Britain occasionally employed agricultural tariffs for revenue-raising purposes, and raised tariffs on sugar for a time to defend against German and Austrian subsidies.68

The major challenges to free trade in Britain were from Conservative campaigns for fair trade and for imperial preference. Beginning in 1903, Prime Minister Arthur Balfour called for using retaliatory tariffs to knock down foreign trade barriers. Around the same time, his former Colonial Secretary Joseph Chamberlain launched a public campaign for an imperial-preference scheme. But these proposals only led the Conservative Party to a landslide electoral defeat in January 1906 and again in 1910. Public alarm over the invasion of German goods had peaked in 1896, well before the rise of the German military threat.69 Even these campaigns, moreover, were not purely motivated by relative-gains concerns. Balfour’s proposed tariffs aimed at restoring rather than restricting free trade, to maximize British prosperity. Chamberlain was more worried about Britain’s relative decline, because “the greatness of a nation is not to be measured by comparison with its own past, but by its relative position in the councils of the world.”70 But his main interest in imperial preference was to promote imperial integration and thereby keep Britain abreast of the more populous great powers, rather than to reduce unequal trading gains.71

The Liberals elected in 1906 worried least of all about relative gains from trade. The British Foreign Office welcomed German growth right up to the start of the war. As one official put it, “it would have suited us well that Germany should develop peacefully and buy more.”72 Politicians seemed resigned to the

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66. Steiner, Britain, p. 61.
70. Quoted in Friedberg, Weary Titan, p. 72.
71. Friedberg, Weary Titan, pp. 54–77.
72. Robert Vansittart, quoted in Steiner, Britain, p. 65.
loss of British economic supremacy, and to care only about absolute gains. Paul Kennedy has observed that "the protectionists' agitation about the relatively greater expansion of foreign cotton industries meant nothing so long as the British industry was increasing absolutely."73 As one Minister of Parliament admitted resignedly, "we have been doing well and shall continue to do well, but . . . though we are still absolutely going forward we are losing ground and must lose first place."74

In fact, Britain's devotion to free trade in this period was so great that "active commercial diplomacy through tariff negotiation was denied to the Foreign Office."75 By shunning even retaliatory tariffs, British policy may have been inconsistent with maximizing absolute gains, not to mention relative ones. One explanation is that imperial overstretch inclined London towards free trade. Assuring other powers of commercial access to Britain's vast and far-flung empire was thought to mollify their imperial appetites. As Crowe argued, other powers "feel less apprehensive of naval supremacy in the hands of a free trade England than they would in the face of a predominant protectionist Power."76 The role of an influential export and banking sector in domestic politics, or of an enshrined laissez-faire ideology, may also help account for British free-trade policy.77

These factors, along with Britain's off-shore location, limit the generalizability of this case. But the closer proximity of France and Russia to Germany, and their very different domestic politics, did not dampen the growth of trade among these hereditary rivals either. In fact, while Anglo-German trade increased 105 percent over 1900–13, Franco-German trade increased by 137 percent and Russo-German trade increased by 121 percent.78 If the period of rising commerce and arms racing capped by World War I is an obvious counter-example to the theory that economic interdependence deters war, it also provides counter-examples to the theory that political-military rivalries cause economic conflict.

73. Kennedy, Anglo-German Antagonism, p. 302.
74. Quoted in Friedberg, Weary Titan, p. 73.
75. Platt, Finance, Trade, and Politics, p. 147.
THE UNITED STATES AND JAPAN, 1930-41

U.S. trade policy towards Japan in the decade prior to World War II provides another anomaly for relative-gains pessimism. Although Japan was a relatively small power, far removed from American shores, it was capable of regional conquest. Japan’s aggressive challenge to long-standing U.S. interests in the Far East, and to those of Britain, greatly increased the perceived chance of war across the Pacific. Yet, until 1941, the United States did not significantly restrict trade that was benefiting Japan relatively more. Even then, the policy change was neither decisive nor motivated chiefly by relative-gains concerns.

U.S.-Japanese relations had been amicable throughout the 1920s. Japan neither attempted to expand its empire, nor objected to western demands for a commercial “Open Door” in China and the rest of East Asia. The United States, Britain, and Japan negotiated a naval arms accord at the Washington Naval Conference of 1921–22 and renewed it in 1930. These and six other states also signed the Nine-Power Treaty, which called for respecting Chinese independence and territorial integrity as well as equal commercial opportunity.79

But U.S.-Japanese relations progressively soured during the 1930s.80 The first sign of trouble was the Japanese conquest of Manchuria in 1931. The United States protested this violation of the Nine-Power Treaty and refused to recognize the puppet “Manchukuo” regime. In 1935, Japan withdrew from the Washington naval accord and started a massive naval buildup. The Japanese Army invaded North China in July 1937 and proceeded to establish new puppet regimes, seize international settlements, drive out foreign economic interests, and commit atrocities against Chinese civilians. While the American public was most shocked by an unprovoked attack on a U.S. gunboat in December 1937, policymakers worried that the Open Door in China was being slammed shut.

The eruption of war in Europe, and the defeat of France in June 1940, left the British preoccupied, and the French and Dutch literally occupied, by the Nazi onslaught. Japan responded in September by joining the Axis in the

Tripartite Pact and by invading northern French Indochina. Washington saw the latter move not only as an attempt to tighten Japan’s blockade of China, but also as a step towards further southward expansion. This might threaten the Philippines, as well as European possessions that were providing strategic raw materials to Britain. U.S. intelligence discovered that Germany was already pressuring Japan to cut off Britain’s supply lines to the region. By late 1940, Roosevelt believed that “sooner or later [the Japanese] would make a mistake and we would enter the war.”\(^\text{81}\) During 1941, the United States inched towards war with Germany, now Japan’s ally, by conducting aggressive “neutrality patrols” in the Atlantic. Secret talks with Japan in the spring failed to find any common ground, and the German attack on Russia in June appeared to draw Japan closer to the Axis. In mid-July 1941, Roosevelt’s cabinet learned from decoded MAGIC cables that Japan was planning to occupy the rest of Indochina as a jumping-off point for a southern advance.

The United States responded to the increasing Japanese threat with military and diplomatic balancing. Military spending, in reaction to Germany as well as to Japan, jumped from around $700 million in the early 1930s to $6 billion in 1941 (see Figure 2). Roosevelt transferred the bulk of the U.S. fleet from the Atlantic to the Pacific in March 1939, moved it from California to Pearl Harbor in May 1940, and added more ships to Pearl Harbor in October following the Japanese occupation of northern Indochina and the announcement of the Tripartite Pact. Washington also loaned over one hundred million dollars to China from late 1938 to late 1940. Perceptions of Japanese hostility were also evident in the withdrawal of American nationals from China in October 1940, and of American women and children from all of East Asia in February 1941. The “ABCD” entente between the United States, Britain, China, and the Netherlands tightened further with joint military planning in the spring, and in July Roosevelt ordered reinforcement of the Philippines.\(^\text{82}\)

But the deepening conflict had little effect on U.S.-Japanese trade until 1941. In absolute terms, this commerce gradually increased over the course of the 1930s, recovering from the Depression-induced lows of the early 1930s. U.S.-Japanese trade remained a fairly constant proportion of overall U.S. trade: 6 percent in 1930, between 8–9 percent over 1931–37, 7 percent during 1938–39,

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81. Quoted in Utley, Going to War, p. 137.
and back to 6 percent in 1940.\footnote{83} Yet the Roosevelt administration recognized clearly Japan’s dependence on U.S. trade. Because U.S. GNP was about six times that of Japan, U.S.-Japanese trade amounted to less than half of one percent of U.S. GNP, but nearly 7 percent of Japan’s.\footnote{84} In addition, Japan relied heavily on oil, scrap iron, raw cotton, and other hard-to-replace imports from the United States.\footnote{85} As a result, access to U.S. markets and resources was far

more valuable to Japan than access to Japan's was to the United States. Both were profiting from trade, but Japan was gaining relatively more.

Trade continued at such a pace because the United States failed to impose significant embargoes or tariffs on Japan until 1941. The first sign of pressure was a "moral embargo" on aircraft in June 1938, after the Japanese terror bombing of Canton. In July 1939, the Roosevelt administration responded to Japanese infringement on U.S. trade in China by withdrawing from the 1911 commercial treaty with Japan, but did not impose new tariffs. The July 1940 National Defense Act authorized the president to ban exports, except to Britain and the western hemisphere, of strategic commodities whenever shortages loomed. It was designed to facilitate rapid U.S. rearmament and foreign military assistance by controlling the domestic prices of strategic goods. Accordingly, new export restrictions—on the export of high-octane aviation fuel, machine tools, aluminum, and certain ferro-alloys (in July 1940); scrap iron (in September); iron, steel, nickel, copper, and zinc (in December); and oil drums (in February 1941)—were intended to reduce domestic shortages and prices rather than to harm the Japanese economy. American-owned tankers were stripped from the Pacific in early 1941 to replace British merchant shipping losses, aggravating Japan's acute shipping shortage. These restrictions began to bite in the first six months of 1941, cutting aggregate trade levels to 58 percent of 1940 levels.

On July 26, a few days after Japan invaded southern Indochina, the Roosevelt administration finally halted U.S.-Japanese trade. At first, however, the new policy was not fully deliberate, at least on the part of Roosevelt and Secretary of State Cordell Hull. Roosevelt authorized only a qualified freeze of Japanese assets and an embargo of medium-octane fuel. He intended to allow the Japanese to buy low-octane fuel at 1935–36 levels, using assets that the Foreign Funds Control Committee would release upon request on a case-by-case basis.

But hawkish bureaucrats in the Committee obstructed Japanese purchases without Roosevelt's or Hull's knowledge. Thus the severance of trade between July and September, at which point Roosevelt sanctioned the de facto total embargo, was not a clear, deliberate policy.  

Several important officials, however, had been seeking a more aggressive economic policy towards Japan for years. Within the State Department, senior East Asian affairs adviser Stanley Hornbeck had been a vocal proponent of economic sanctions ever since the Japanese seizure of Manchuria. Following the Japanese attack on Nanking in September 1937, Treasury Secretary Henry Morgenthau became the first cabinet official to take this position. Morgenthau and Hornbeck's main rationale was that sanctions would compel Japan to mend its ways, but they also argued that sanctions would undermine the Japanese war economy. While most of their proposals were designed to hamper Japan's military build-up, rather than its overall economic growth, all can be viewed as part of a relative-gains strategy. In mid-1940, Interior Secretary Harold Ickes and two new cabinet appointees, War Secretary Henry Stimson and Navy Secretary Frank Knox, joined Morgenthau's behind-the-scenes campaign for sanctions. By mid-1939, moreover, public opinion was running in favor of a boycott by three to one.  

Until mid-1941, however, Roosevelt refused to take any economic action that appeared to be targeted specifically against Japan, especially a cut-off of oil. Hull firmly opposed sanctions, along with State Department Far Eastern Affairs Chief Maxwell Hamilton, Ambassador to Japan Joseph Grew, and the Navy's top admirals. Three objections to sanctions appear in administrative deliberations between 1937, when they were first seriously considered, and mid-1941: danger of provoking Japan, domestic economic repercussions, and problems of international coordination.

Fear that sanctions would provoke rather than deter Japan was the most important concern. The doves in the Roosevelt administration believed that economic isolation would intensify Japan's quest for autarky, and that political


isolation would strengthen the hand of the militarists in Tokyo.\textsuperscript{91} This risk became particularly grave after Hitler’s victories in Europe made easy prey of European colonies in Southeast Asia. Thus, in October 1940 the President told Hull that “we were not to shut off oil from Japan . . . and thereby force her into a military expedition against the Dutch East Indies.”\textsuperscript{92} Roosevelt and Hull only endorsed sanctions when the Japanese invasion of south Indochina in July 1941 finally convinced them that appeasement was not working. (Ironically, continued trade might have tipped the ongoing debate in Tokyo in favor of an attack on Russia instead of a further southern advance.)\textsuperscript{93}

Another factor militating against sanctions, at least before the danger of Japanese aggression in Southeast Asia heightened in 1940, was an absolute-gains concern for the U.S. economy. American exporters, though concerned about the loss of potential Chinese markets due to Japanese expansion, opposed restrictions on commerce with their Japanese customers. \textit{Business Week} thus asked rhetorically in December 1938, “should diplomats and executives . . . spend all their energies trying to brake the growing power of the new rival in the Orient? Or will they profit more if they work toward a plan, acceptable to them and to Japan, for mutually profitable cooperation?”\textsuperscript{94} In an internal analysis also completed that month, Hamilton and three high-ranking State Department economic advisers listed “widespread domestic economic dislocation” as one of three reasons against sanctions.\textsuperscript{95}

A third objection was the difficulty of coordinating sanctions with other countries. An element of economic and military buck-passing appears in the U.S. reaction to British requests for greater export restrictions in late 1940. State Department officials, according to Jonathan Utley,

were suspicious that Britain intended to lure the United States into a position where it would have to protect British interests in Asia. . . . Moreover . . . what

\textsuperscript{94} Quoted in Wilkins, “Role of U.S. Business,” pp. 349.
\textsuperscript{95} The other authors were the Assistant Secretary of State for Economic and Commercial Policy, the Trade Agreements Division chief, and the Assistant Adviser on International Economic Affairs. U.S. Department of State, \textit{Foreign Relations of the United States, 1938}, Vol. 3 (Washington, D.C.: U.S. GPO, 1954), p. 407; for Hornbeck’s response, see pp. 425–427. Herzberg, however, notes that purely economic concerns took a back seat in congressional debates over sanctions, and that another 1938 study predicted that the impact on the U.S. economy would be minor. “American Economic Policies,” pp. 269, 276–277.
Britain had in ample supply it was not interested in restricting. . . . Hull was not interested in doing Britain’s dirty work and had no intention of imposing economic sanctions against Japan.  

Unless other states fully cooperated, the effect of U.S. sanctions would be blunted to the profit of other nations ready to export to Japan.

**Conclusions**

Thus, in two cases, nations refrained from restricting trade with threatening rivals that appeared to be gaining relatively more. British officials prior to World War I saw Germany as a severe new threat and believed that Germany was gaining more from trade with the British Empire than vice versa. Similarly, U.S. officials in the 1930s recognized that Japan posed new and serious threats to U.S. interests in the Far East, while benefiting disproportionately from mutual trade. However, the British continued to trade freely with Germany until the outbreak of war in 1914, and the United States traded heavily with Japan until mid-1941. Even then, U.S. restrictions were intended as much to coerce Japan as to undermine its economy. Continued cooperation in both cases suggests that sensitivity to relative gains is generally low under multipolarity, at least when compared to other incentives for trade. In addition to an interest in absolute gains, leaders were deterred from economic sanctions by the fear that these would provoke their rival/partner, and thus heighten the risk of expansionism and war.

These may not be the easiest multipolar tests of relative-gains theory. Because of geography, the Anglo-German and U.S.-Japanese antagonisms were not the most dangerous or protracted that can be found in multipolar systems. But the perceived degree of threat increased significantly over time, to the point where war was thought likely. Gains from trade were also not particularly skewed in the Anglo-German case. The greater asymmetry in gain in the second case, due to the relative size of the U.S. economy and to reduced trading options in Europe, may explain why the United States gave more serious consideration of economic sanctions, and finally cut off trade in mid-1941. But if relative gains block cooperation among states only at the brink of war, relative-gains sensitivity must be generally quite low.

Decisionmakers were influenced by other factors as well. In addition to interest in absolute gains, leaders were deterred from economic sanctions by the fear that they would provoke aggression. This may be a general incentive against using economic sanctions as a means of maintaining relative position, but idiosyncrasies of the two cases selected made it unusually important. The vulnerability of Britain’s vast and exposed empire provided added reason to maintain free trade. Analogously, the vulnerability of the oil-rich Dutch East Indies gave the United States an incentive to keep providing Japan with American oil. Free trade ideologies may also have curtailed U.S. and British interest in using trade as a weapon.

These factors limit the generalizability of the two cases, making them “very likely” rather than “most likely” tests of the relative-gains hypothesis under multipolarity. Further research is needed to establish the conditions under which great powers limit trade or other types of economic cooperation to prevent shifts in relative power. However, the fact that Franco-German and Russo-German trade increased even faster than Anglo-German trade prior to World War I, despite mounting tension and disputes, suggests that the British case may have been quite typical, and that these conditions are likely to be quite rare.

This would be consistent with the hypothesis that multipolarity reduces the security ramifications of relative gains. I found little evidence that leaders were consciously impressed by the effects of system structure. But since the international system had been multipolar for centuries prior to the Cold War, one would not necessarily expect to find explicit references to it in policy deliberations. Even if officials were oblivious to multipolarity itself, one can see its effect in officials’ awareness of the limited durability of specific conflicts and alliances.

This finding provides a basis for optimism about the future. The post–Cold War world is not only multipolar, but also well-armed with nuclear weapons. Prior to the nuclear era, economic size correlated strongly with the ability of a country to defend and deter. But insofar as survivable, second-strike nuclear forces deter aggression by wealthier powers, they reduce the military significance of relative economic size. Military, diplomatic, and economic competition between the United States and Soviet Union during the Cold War suggest some limits to the impact of the nuclear revolution. Leaders may conclude that mutual fears of nuclear escalation make conventional war or coercion feasible, or at least fear that their counterparts think this. The possibility that military science might eventually produce strategic defenses or disarming offensive
capabilities also leads states to care about relative economic size. Still, when compared to the situation prevailing prior to 1945, nuclear deterrence has dampened the military significance of economic advantage and mitigated the security component of the relative-gains problem.97

If security concerns failed to obstruct economic cooperation among non-nuclear enemies on the brink of war, they are very unlikely to interfere among nuclear-armed nations, certainly those with lesser political-military rivalries. Thus even if multipolarity, as pessimists argue, increases the likelihood of war, this insecurity will not generate the kind of economic envy that pessimists predict will hinder economic cooperation.

This does not mean, however, that states will cooperate readily when differential short-term gains threaten long-run economic competitiveness and growth. Conflict of this type may even increase slightly as the Cold War’s end eliminates the positive security benefits of trade among bipolar allies. But if the United States is going to bargain more toughly with Europe and Japan, it will do so out of concern for its own economic prosperity rather than for its relative military power. Research on when economic competitiveness concerns limit cooperation will be helpful in predicting strategic trade conflict.98 But it would be misleading to call the resulting hypotheses “neorealist,” even if they contradict neoliberal institutionalism, because neorealist theory is about relative power and the pursuit of security, not relative economic competitiveness and the pursuit of profit.