

new receipts over the near term. During fiscal year 1968 the German Bundesbank agreed to invest \$500 million in nonmarketable U.S. Treasury securities. This investment counts as a long-term capital inflow, reducing our payments deficit. It does not fully offset our expenditures in Germany.⁷

On the assumption of at least \$800 million of U.S. military expenditures in Germany, the 1967 agreement provides for an offset of only five-eighths of such expenditures at most. Quantitatively, then, this second type of agreement was a retrogression from the first.

Apart from the quantitative difference, however, there are also some qualitative differences that render the second type of agreement preferable to its predecessor, from the German standpoint. In the first place, the termination of a commitment to a particular level of German military procurement in the United States removes the prospect of misallocation of resources that would be involved in purchasing U.S. military items that are either altogether unwanted by the Germans and/or available more cheaply elsewhere. Secondly, the Germans will receive interest income, which was not provided for in the military procurement type of agreement. Thirdly, the Germans, instead of buying outright American merchandise, are merely extending a loan to the U.S. Government, and will accordingly receive repayment of principal. Fourthly, the moderate term to maturity of the loan (4½ years) may be departed from in a German contingency. Fifthly, there is no advance commitment by the Germans to renew the loan when it expires; and if prior to expiration of the loan additional amounts were lent in the next few years, there would presumably be political pressure against an indefinite pileup of such loans in the realization that sooner or later, they must be repaid.

It is of more than passing interest that, before expiration of the third "offset" agreement involving military procurement, internal German political opposition to "offset" agreements was growing in volume and intensity. Indeed, the fall of Chancellor Erhard was partly attributed to German hostility to the "offset" agreements. Correspondingly, the rise of Chancellor Kiesinger is partly associated with his insistence on a different type of "offset" agreement from that involving defense procurement.

The acceptance of the first type of agreement by the Germans in the early sixties is understandable in terms of the buildup of the German Bundeswehr, which had commenced in the late 1950's. As the German defense buildup was beginning to taper off in the middle 1960's, and with the German recession of 1966 evoking calls from German industrialists for more Government orders from domestic industry, the military procurement type of "offset" agreement became increasingly objectionable on both economic and political grounds.

From the standpoint of the United States, the new type of agreement when compared to its predecessor, is a mixed bag. Commendable is the new feature of sparing the Germans the misallocation of resources that would be involved in their purchase of American military equipment that they don't want altogether or that is available more cheaply elsewhere. The United States should take pains to avoid the

⁷ U.S. Treasury Department, *Maintaining the Strength of the United States Dollar in a Strong Free World Economy* (January 1968), p. 81. See also U.S. Department of Commerce *Survey of Current Business*, vol. 47, No. 12 (December 1967), p. 16.