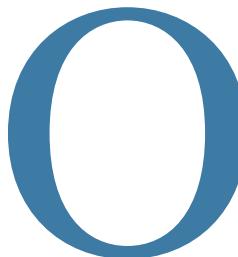


# The Reincarnation of *John Connally*

BY C. FRED BERGSTEN



In August 18, 1971, three days after President Richard Nixon announced the cessation of dollar convertibility into gold for foreign monetary authorities and an across-the-board import surcharge, rocking the world economy and essentially ending the original Bretton Woods system of fixed exchange rates, I and three other economists from outside government—the late

Richard Cooper, Harry Johnson, and Henry Wallich—were invited to the U.S. Treasury Department to meet with Secretary John Connally and his top lieutenants including Under Secretary for Monetary Affairs Paul Volcker. Connally, who was Nixon's chief adviser on these issues and the major proponent of the new U.S. strategy, began the session by indicating “You know what we have done. Please advise us on what we should do next.” It was clear that he did not know what to do next, so we outsiders were immediately extremely worried.

The discussion, led throughout solely by Connally, lasted for six hours. Cooper and I urged the officials to use the new environment to promote lasting reform in the international monetary and trading systems, which needed major improvements. But it became increasingly clear that Connally had no interest in systemic reform. At about 4 p.m., the Secretary indicated that it was time to close and that he wanted to share his own philosophy with us before departing: “The foreigners are out to screw us. It is our job to screw them first. Thank you for your help.”

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I immediately reported this encounter to National Security Adviser Henry Kissinger, whose deputy for foreign economic policy I had been until six months earlier. I warned him that he was dealing with a powerful xenophobe at Treasury, who would severely jeopardize his entire foreign policy. Kissinger was then planning to broker *détente* with the Soviet Union and the historic opening to China. Both of those initiatives required full support from America's traditional allies, who were outraged by the Nixon shocks and refused to even meet with Nixon until the economic crisis was resolved. Kissinger eventually orchestrated that resolution.

The Nixon shocks, and these underlying attitudes in at least some key quarters of his administration, were a watershed in the evolution of U.S. foreign economic policy. They severely disrupted the global financial system and indeed the entire world economy for a couple of years. Both of the key policy steps, though they could arguably be justified in legal terms, violated fundamental norms of the extant international economic order: convertibility between the dollar and gold, which provided the foundation for fixed exchange rates among the major currencies, and the openness of trading markets (especially the U.S. market) to foreign imports.

The Nixon shocks put the world on notice that the United States would defend its own interests even if that meant trampling on the interests of others. They were an eerie precursor of President Donald Trump's "America First" policy and rhetoric almost fifty years later. The immediate and widespread reaction around the world was that the United States had gone rogue and had abdicated its global economic leadership—much as Trump did almost fifty years later. I helped mount the attack on Nixon and

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## "Screw the Foreigners"

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U.S. Treasury Secretary  
John Connally, August 15, 1971.

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Connally, including with immediate Congregational testimony and a lead article in *Foreign Affairs*.

The "Nixon shocks" were clearly undertaken with domestic U.S. politics (especially the upcoming 1972 elections and growing protectionism), as well as international pressures on the dollar, very much in mind. They had little intention of providing positive systemic leadership. Their ultimate results, however, turned out to be highly constructive. Long after Nixon and Connally had lost interest in the issue and handed it off to others, the United States and its allies acquiesced to the pressure from markets to abandon fixed exchange rates altogether and to adopt a wholly new regime of flexible rates. This tectonic shift provided what remains the most fundamental reform of the international monetary system in the postwar period.

The global monetary system, while by no means perfect, has functioned far more successfully ever since. The currency crises among industrialized countries that were so common in the 1960s and early 1970s became a thing of the past (until the Europeans restored fixed exchange rates among themselves by creating the euro and thus fostered currency crises for some individual eurozone countries in the early twenty-first century). The Tokyo Round in the GATT, which originated from the trade component of the August 1971 program, restored the forward momentum of liberalization and significantly extended the disciplines of the global trading system to key non-tariff barriers, incorporating new rules to govern subsidies and government procurement.

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President Trump severely disrupted the world economy in 2017–2020. He applied tariffs of 10–30 percent on more than half a trillion dollars of U.S. imports and threatened to double that coverage. He invoked “national security” to justify trade restrictions against America’s closest allies. He launched trade wars against adversaries and friends alike, and veered sharply toward a new Cold War with China.

Trump left the Trans-Pacific Partnership, one of the largest trade agreements ever negotiated, and forced needless (and largely useless) renegotiations of two others. He jeopardized the future of the World Trade Organization by neutering its Appellate Body, blocking the succession of its leadership and ignoring some of its fundamental rules. He pulled out of the Paris Agreement on climate change and the World Health Organization. He thus struck at the heart of the contemporary global economic order.

Donald Trump was the reincarnation of John Connally, or at least his closest replication in half a century. Connally too was a xenophobe, acting unilaterally and bullying America’s closest allies. He too blamed the foreigners for America’s problems and offered no U.S. contributions to the proposed reforms. He too cared nothing for the extant global economic order. He too quite explicitly pursued “America First” in crude and often embarrassing ways.

Could the contemporary “Trump shocks” nevertheless produce positive results, similar to those that eventually emerged from the “Nixon shocks” of fifty years ago? In particular, can the United States itself get back on track as President Biden is rightly pursuing as preamble to new international initiatives? Can the traditional alliances be restored? Can bilateral confrontation between the United States and China revert to sufficient cooperation to provide the global leadership essential for the functioning of a stable and prosperous international economic order?

Just as Nixon and Connally warned the world that the United States would be conducting a much more aggressive foreign economic policy after 1971, Trump warned

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the world that U.S. policy would be much more aggressive from here. In both cases, both domestic politics (the growing impact of globalization on jobs and incomes) within the United States, and international economics (the recovery of Europe and rise of Japan then, the rise of China now), propelled the changes. To convert the Trump assaults into supporting constructive global economic reforms, the other key countries must heed the warnings and respond accordingly, even as they face the more cooperative and less confrontational variant offered by President Biden and hopefully his successors from both parties, let alone a renewal of Trumpism (with or without Trump himself).

Two sets of steps are needed, just as the Nixon shocks were transformed in positive directions by both monetary and trade reforms. One is for the traditional allies, mainly Europe and Japan but also middle powers such as Canada and Australia, to take a larger share of global economic leadership responsibilities, as they have already been doing, at least temporarily, to fill the Trump vacuum. They need to contribute more real resources to the provision of global public goods, including the common defense. They need to take at least some of the initiatives needed to restore the institutional foundations of the liberal international economic order, including more accurate reflection of global economic power in the governance of the International Monetary Fund and a better dispute settlement mechanism in the WTO.

Most importantly, the allies need to stand firmly with the United States to defend and revitalize the global order in the face of rising China. This includes adapting its rules and norms as may be necessary to accommodate legitimate concerns of the new superpower.

The ability of the United States to restore its essential leadership role will turn importantly on the extent to which others will increasingly share that leadership with it. Their doing

## The Trump Comparison

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so, along with major policy changes by the United States itself, will enable the United States to reinstate a sustainable domestic political foundation for a constructive foreign economic policy. Such increased sharing was in fact required and achieved to a lesser degree with the currency adjustments and trade reforms of the 1970s and 1980s.

The second step, and even more crucial, is the need for China to recognize that some of its trade, investment, and technology policies are unacceptable to most of the world. These policies must be modified to prevent potentially lethal threats to the openness of the global system on which China itself is heavily dependent. Trump's crude use of tariffs got China's attention, but was predictably ineffective in getting it to adopt meaningful policy changes. In pursuing a much more nuanced and skillful approach, the United States is almost certain to continue pressing until the underlying tensions are resolved. This is where the restoration of allied relationships will be crucial: China desperately fears being isolated internationally, and multilateral pressure, deftly applied, will be far more effective than unilateral attacks in eliciting positive responses.

Trump's assaults on the global order, like Nixon's before him, can thus be turned in constructive directions if

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his successors use the leverage and messaging they provide to steer the world more skillfully toward more sensible, and thus more widely shared, objectives. The alternative is to risk continuation, and even further escalation, of Trump's abdication of U.S. global economic leadership and severe erosion in the liberal international order. Down that path lie substantial threats to global economic stability, a new Cold War with China, and further declines in America's global standing. We must hope that history will repeat itself in this highly unusual and counterintuitive manner. ♦