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TO: S/P - Mr. Rostov
FROM: S/P - William J. Jordan
SUBJECT: The Viability of Berlin

Summary and Conclusions

The key to Berlin's future is the confidence of its people in the United States. It must be clear that West Berlin is part of the West and that free access to the city from the West is guaranteed. It must be clear that the full power of the United States stands back of that guarantee. We need not be bellicose or provocative; we must be firm and clear.

If our intentions are unmistakable on this matter, there is little that cannot be done to make West Berlin a thriving and steadily advancing center of industry, commerce and culture. If there are grave doubts about that determination, West Berlin will wither on the vine.

Much is being done now by the Berliners themselves and by the Federal Republic to keep West Berlin alive. Much more is planned. We can help significantly in this effort.

A list of specific recommendations for action is on pp. 9-11 below. The most important of these are:

1. Encourage investment in West Berlin by U.S. companies.
2. Help establish a training center for underdeveloped countries in West Berlin with the emphasis on development of needed technical skills.
3. Assist and encourage development of West Berlin as one of the world's major centers of automation in industry.

These and other recommended programs will have a positive effect on Berlin's economy. Far more important will be their influence on the morale of the Berliners. Here, the dividends promise to be out of all proportion to the relatively small investment involved.

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The Basic Issue.

The key to Berlin's future is the confidence of its people -- in the United States, in the western allies, in the Federal Republic, and in themselves. Of these, by far the most important is the matter of trust in the United States. They look to us as the primary guarantor of their future. There are grave doubts in Berlin about the concern and the fortitude of the British and French. The Berliners are aware, too, that the Federal Republic can do little by itself to protect their interests on the international scene. It boils down, then, to what the United States is prepared to do about Berlin.

It is not just a question of whether the allied garrisons are ready to stand fast and defend their rights. It is a question of our determination to insist on the free flow of persons and material from the West to West Berlin. If we are firm only on the matter of our occupation rights and on the free access of our military personnel, we are likely to reach the point where, as one Berliner said, "four American soldiers will be patrolling the wall and defending the rights of three aged Berlin pensioners."

It must be clear that West Berlin is part of the West and that free access to the city from the West is guaranteed. It must be clear that the full power of the United States stands back of that guarantee. There must be no doubt in the minds of Soviet leaders or of the citizens of Berlin about this matter. We need not be bellicose or provocative; we must be firm and clear.

If our intentions are unmistakable on this matter, there is little that cannot be done to make Berlin, or more accurately West Berlin, a thriving and steadily advancing center of industry, commerce and culture. If there are grave doubts about that determination, then West Berlin will almost certainly wither on the vine. We will find happening again what happened earlier in the East Zone and in East Berlin when people decided that the gate to the West was about to be slammed shut.

If we are not ready to stand up and be counted on this issue, then we might profitably begin to consider the advantages of orderly, planned and voluntary evacuation of the city. We could hardly conceal that this would be a political and psychological defeat of huge proportions. But at least some positive advantages might be derived from the example of perhaps a million and a half or two million people choosing to move rather than be absorbed slowly by the Communist bloc. It might be preferable to the slow bleeding to death of a great city while we, its guarantors, stand by helpless. It is not, I repeat, a desirable course.

If, however, we are prepared to carry out our past pledges and to stand firm, the Berliners will stand at our side. If we begin to move

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forward with confidence, they will move forward with us. So will Germans in the Federal Republic. They are waiting for our leadership and for our decision. If they are confident that their city has a future, Berliners -- with help from us and from the Federal Republic -- will make their city greater than ever.

Berlin Today.

There is a surface calm in West Berlin today. Industry is humming. The shops are well-stocked and busy. New buildings are going up. The streets and sidewalks are crowded. Traffic jams all the main arteries during rush hours. To the casual eye, it is a thriving, busy, prosperous city whose people go about their daily lives in the manner of big city residents anywhere in the West.

But the appearance is deceiving. Beneath the surface of this outer calm and normalcy, there is a deep and disquieting tension among Berliners. The breach of the wall that went up along the Soviet sector border last August hangs on. In one way or another, it intrudes into almost every conversation. It is many things to the Berliners. For seven out of ten, this ragged, badly-built stretch of concrete blocks and bricks and barbed wire is a barrier that separates them from families or loved ones and reduces contact to the wave of a hand or a handkerchief from a distance of several blocks. And even this feeble link is being pinched off by the erection of wooden barriers behind the wall in the East.

For all Berliners, the wall is a constant reminder of their own isolation from the outside world. For many, too, it is a symbol of the indecision of the allied powers. Rightly or wrongly, fairly or not, Berliners ask themselves: "Will the allies move any more decisively the next time the East acts to squeeze us a little more?"

If I were to characterize the mood in West Berlin today in a phrase, it would be "watchful waiting." The Berliners have heard our words and been encouraged by them. But they want now to know what we will do, how we will react to the next "technical difficulty" in access from the West -- a delayed shipment, a demand for passports or visas, the imposition of a customs barrier. At the present stage, each such move -- and our reaction -- will be decisive for thousands of Berliners. If we are weak, they will be weak. If we are not prepared for risks, they will minimize theirs by moving to the West.

Three developments seem the most likely possibilities in the present situation. First, there could be a sudden and dramatic move by the Soviets and/or their East German puppets to seal off West Berlin. Presumably our

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response to such a move would be quick and decisive. Most Berliners and foreign observers are agreed that the reaction of the citizenry would be just as courageous and determined as it was in 1948 under the first blockade. The problem then would not be viability in the broad sense but survival.

The second, and equally unlikely, possibility is that there will be a breakthrough in the diplomatic effort to reach agreement on some form of guaranteed access to Berlin from the West. It is difficult to see any formula emerging for such a guarantee that would not strike a critical blow at the two principal supports of West Berlin's viability -- the U.S. and allied presence and pledges, and the extensive economic subsidies and support of the Federal Republic.

The most likely course would seem to be a continuation of the present situation, possibly exacerbated by the signing of a separate peace treaty by the Warsaw Pact powers with the GDR. Most Berliners expect to be confronted with a prolongation of the current uneasy truce, to be subjected to regular harassment and the now familiar nibbling tactics, periodic reminders served up by Messrs. Khrushchev and Ulbricht of West Berlin's "special," awkward position.

The Communist leaders may be prepared to let the Berlin situation go along on its present course without significant change. They may calculate that we are sufficiently interested in avoiding any new eruptions of tension to desist from positive moves of our own. They may expect, further, that under conditions of vagueness and indecision, West Berlin will slowly stagnate. Nothing would fit in better with this exercise than for us to sit quietly, to do and say nothing about Berlin, and -- as the overworked saying goes -- "not to rock the boat." In doing so, we would, of course, be writing the death warrant for West Berlin in its present form.

I assume that we are not prepared to acquiesce in this kind of "agreement to be silent." I assume that we are deadly serious when we speak of our concern for the freedom and well-being of two and a quarter million West Berliners. If so, there are many things that can be done to assure the viability of West Berlin. The key remains the psychological attitude of the Berliners. If we are prepared for the steps that will make that attitude positive and optimistic, we can then move forward with a program that will not merely keep Berlin alive at its present level but move it forward along lines of new growth and new development.

Before we consider what can and should be done, we should take a quick look at West Berlin's situation today, at what has been done to help it, and at what is now being planned, in Berlin and in the Federal Republic.

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West Berlin's Economy.

If Berlin's morale was lower than I had been led to expect, its inner tensions deeper, I found its economy in considerably better health than the circumstances would have seemed to permit. The gross product for the year was estimated at more than 13 billion marks, ten percent higher than in 1960. Industrial production was still increasing, higher by four percent in October and November than during the same months in 1960. Labor productivity was 7 percent above 1960's level. There were 17,000 unemployed in December but there were 20,000 job vacancies. West Berlin industry received more orders in 1961 than during the previous year. Berlin shares have been doing relatively better on the stock exchange than West German issues.

In short, the economy of the isolated city is faring much better than most observers had expected. This is particularly remarkable when one considers that the wall that went up in August cut off about 63,000 East German workers who had been employed in West Berlin. The loss was in part recovered from the ranks of the unemployed and from West Berliners who formerly worked in East Berlin.

Despite the generally healthy economic picture, there are some disquieting signs. Savings accounts at the end of the year were still below the level of August. The overall level of orders for Berlin industry is good but there has been a decline in the producers goods sector. The level in October, for example, was more than 20 percent below that of October 1960. Construction, especially of private homes and small buildings, has declined. An important factor contributing to the increase in gross product was the sharp increase in West Berlin's transportation system to fill the gap created by the boycott of the East-operated S-Bahn rail line.

Berlin hotel keepers paint a dim picture of their business. Many note a decline of 50 percent or more in the number of guests. In part this decline is attributed to the ending of visits from the East zone, but the number of visitors from West Germany has dropped as well.

To this one must add the most disturbing feature of all -- the slow but steady drain of people from West Berlin. In part, the loss is attributable to Berlin's distorted demographic structure -- twice as many people over 60 years of age as the West German average, and half as many youngsters 15 or under. The excess of deaths over births produces a net loss of 2,000 a month.

In addition, there is a steady flow of people from Berlin to the Federal Republic. The average net loss through migration to the West has been estimated at between 3,000 and 4,000 a month. Many of these are

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elderly persons or pensioners who can live more cheaply in small towns or villages in the West than they can in Berlin. But a significant number are in the middle age brackets and in the middle and higher income groups. The outflow of shipments of household goods appears to have declined recently but the level during the three months after the wall went up was three times as high as it had been during the comparable period in 1960.

In the past, the exigration of Berliners has been more than balanced by the arrival of immigrants from the East. That source of population replenishment now has been effectively cut off. The inflow from the Federal Republic, which is being encouraged by some industries, trade unions and the government, has been averaging between 500 and 1,000 a week in recent months.

Since August, Berlin's newspapers have carried a large number of ads of apartments for rent. Some press accounts of this development have, however, distorted the picture. Many of the apartments thus advertised are too expensive for the average industrial or office worker and thus remain vacant. There is still a significant shortage of housing for middle-income and, particularly, low-income families.

In addition to its serious demographic imbalance, Berlin has a number of other economic disadvantages and weaknesses. Its industrial complex is not too well balanced, with a large portion of the city's income and production dependent on electrical goods, clothing and tobacco products. Many industries have obsolete machinery and plants and a labor force far in excess of their real requirements. Sources of raw materials are distant and the city must import four to five times as much as it exports.

In the face of the built-in difficulties, as well as of the special physical and psychological problems created by the Wall, what is being done to maintain the viability of the Berlin economy?

Direct and indirect aid to Berlin from the Federal Republic has been a decisive factor in keeping the city alive and prosperous. Any study of the types and extent of this aid makes it quite clear why the Soviets have so persistently demanded that Berlin's "special ties" with Bonn be terminated. It would mean a sharp and devastating decline in West Berlin's prosperity.

Federal aid to Berlin takes a variety of forms:

1. Direct budgetary assistance. This amounted to slightly more than 1.1 billion marks in 1961 and about 1.5 billion are provisionally committed for the present year. The budget aid is used for a general subsidy (about 751 million marks last year) and for such things as project loans, sickness insurance and construction projects.

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2. Tax preferences. West Berliners benefit from a 20 percent reduction in their income taxes. Businesses are exempt from the 4 percent turnover tax. Depreciation allowances on investments up to 75 percent over a three-year period represent a major tax saving.

3. ERP loans and credits. 327 million marks were committed during 1960 from revolving counterpart funds. They went into such things as investment loans, order financing, construction and housing for workers and students. More than 330 million marks are budgeted for the current year. In addition, the Federal Property Ministry has announced release of an additional 36 million marks from ERP funds to finance housing for border-crossers and new business buildings.

4. Guarantees for commercial exchanges. The Federal Government guarantees traffic in both directions across the Soviet Zone against confiscation in transit. Guarantees also cover manufacturing and storage risks in Berlin. Road tolls imposed by the Soviet zone on truck traffic are reimbursed by the Government in Bonn.

Construction of the Wall created new problems for Berlin, economic problems as well as psychological. To meet the new situation, the Federal Government adopted special measures. A supplementary grant of 500 million marks was approved in September and is now being spent. It provides: 1) a vacation grant of 100 marks to West Berliners; 2) interest-free loans to newly married couples to be paid back in ten years with a 25 percent write-off for each child; 3) a new housing program; 4) educational and cultural programs including subsidies for movies made in Berlin; 5) travel payments for West Germans moving to Berlin to work.

In addition, the Federal Government has made plans for relief of small businesses particularly hurt by the closing of traffic from East Berlin, for subsidizing air flights by tourists into Berlin, and for other projects.

The Federal Employment Agency has approved credits of 75 million marks from the ERP special fund for rationalization projects in Berlin industries, 60 million marks to finance commercial orders for Berlin, and 115 million to pay travel expenses and separation allowances for young workers who accept jobs in Berlin.

Not all of the measures undertaken to date or planned have proved popular with Berliners and the effectiveness of some moves is questioned. For example, the vacation allowance is known scornfully as "jitters money." The income tax write-off benefits only about one-half the Berlin workers and helps most those with the highest incomes. Most city officials would prefer to use the vacation allowance to pay 5/7ths of the cost of social security payments for Berlin workers -- a move that would mean a five percent increase in their take-home pay.

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Additional Plans.

Economic planning in West Berlin suffered a serious setback with the death in October of Senator Paul Hertz and, shortly thereafter, of his deputy Otto Busack. But a new, intelligent, vigorous and able replacement for the Economics and Credit Senator has been found in Dr. Karl Schiller. Dr. Schiller has launched a careful and systematic study of Berlin's economy and its immediate and long-range needs. He is confident of Berlin's future. He is widely respected in the Federal Republic, by Economics Ministry officials and members of all parties. Though he had not reached any final conclusions when I spoke with him, Dr. Schiller said he thought that rationalization of industry and the promotion of automation held great promise for Berlin's economic future.

City officials in Berlin are eager to promote Berlin as a tourist center and as the site for international conferences, both private and governmental. Mayor Brandt has a commission working on plans for developing Berlin as a major world cultural center.

What Can We Do About Berlin?

I began by noting that the basic problem of Berlin was one of confidence -- the confidence of Berliners and of the Germans in us, and in themselves. But the United States holds the key to this problem. If we make our position clear -- quietly, confidently but unmistakably -- then half the battle will be won. Words can be helpful -- if they are the right words at the right time. But the rest will be in our deeds. We must be prepared to face the probability of new pressures on Berlin and to meet those pressures in such a way as to indicate to the Berliners our clear determination to stand fast and to keep the city alive and prosperous. The way we meet these coming tests -- and they will come -- will determine the future of West Berlin.

We face some hard decisions. I do not underestimate their gravity. But unless these decisions are made, all the most elaborate plans for investment, for conventions, for cultural centers, and the rest will be meaningless.

We need to make up our minds about what we really want in Berlin and to what lengths we are prepared to go to achieve it. We must then make our decision known to the Berliners and to the West Germans. We must make it known, too, to our allies. Once this base has been laid, the possibilities for promoting the economic viability of Berlin are limitless. We can then give West Berlin and its people new confidence, new vigor, new hope.

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A Program of Action

A wide variety of projects and programs have been considered or discussed in connection with Berlin's viability. I consider the following to be the most promising in terms of feasibility and psychological impact:

(Highest priority)

1. U.S. Investment in West Berlin.

Few things would have a more positive effect on the morale of Berliners than the investment, even of token dimensions, by U.S. businesses in Berlin. A case in point is the recent opening of a brokerage office by Merrill, Lynch, Pearce, Fenner and Smith. It is a small office with a small staff but the effect on the Berlin financial community was significant.

General Clay is deeply interested in this effort. He has already written to officials of 21 U.S. companies asking them to consider opening small branches or other facilities in Berlin.

General Clay should continue as the focus of this effort but he needs an assistant working at this end full-time to follow up and expand the effort begun in Berlin. A top-flight individual with good business connections and who also knows the German scene should be appointed to this responsible duty. It would be his task to canvas the business community, generate interest in Berlin, promote investment as being in the national interest as well as economically worthwhile. The effort should have the full backing of the Government and should draw on available facilities in State, Commerce and other departments.

In connection with this program, we might profitably ask our Economic Affairs people to undertake a study of the feasibility of including West Berlin under the MSP investment guarantee.

2. Training Center for Developing Countries.

The purpose of this institution would be to train young men and women from less developed countries in some of the many technical skills needed in their countries - basic engineering, road building, sanitation, power plant maintenance, operating and repairing farm and construction machinery, and the like. It might also serve as a training school for young Germans who may be sent to less developed countries to pass on their skills. It might later prove useful to send a few of our own Peace Corps volunteers to such a center for training.

Basically, this should be a German institution but there should be significant U.S. participation as well as, hopefully, British and French. Instructors from allied countries would be particularly useful in that many

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of the trainees presumably would speak French or English.

The most pressing immediate need is to organize a planning group to study the proposal, determine the scope that would be practicable, survey available facilities and resources, human and economic, determine what would be required in the way of plant, equipment, training staff, housing facilities, and the like and then get some cost estimates. Once this is determined, we and the Germans could explore the possibilities for financing. I suspect that the heaviest burden can and should be placed on the Federal Republic with Berlin and the U.S. making significant contributions, from public or private funds or both.

We should urge the Germans to organize a planning conference as soon as possible. We should encourage a few top-flight Americans with experience in teaching and in the problems of underdeveloped areas -- Max Millikan, if he were available, Litchfield, et al -- to represent us on the group. The committee presumably would include men from German Government departments, from academic life, from vocational training institutes, and from the Tegel Center.

I suggest that General Clay could use someone assigned to his staff to work full time on this project, someone who knows Berlin, has good connections in Bonn and in academic circles, and who could act as a coordinator of the U.S. effort in close cooperation with the Germans.

There has been some discussion of the possibility of locating the planned OECD development center in Berlin. I think this should be kept separate, however, from the proposed Berlin training center. The idea is a good one but I suspect that it will run into some opposition within OECD and, if tied to the above project, would force lengthy and needless delay.

1. An "automation center."

There is a great deal of enthusiasm in Berlin for the possibility of making the city the leader in Germany and probably in Europe for the automation of industry. Senator Schiller is particularly enthusiastic about this. It would seem to meet one of Berlin's basic economic problems--the shrinking labor force--and to take advantage of one of the city's greatest resources, its remarkably advanced electrical and electronic industry.

American specialists could help in many ways. U.S. exhibits at trade fairs like the Berlin Industrial Exhibit could be tailored in part to meet the demand for more information. The possibility of research grants for automation studies should be explored. Our economic people in Bonn and Berlin should be in close consultation with German authorities to discover what can be done and how we could help in this venture.

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(Other programs that can help Berlin)

4. Encourage the use of Berlin as a site for international meetings, conferences, exhibits and conventions. Berlin authorities must take the lead here but we can help with advice and encouragement. A specialist in this field, Robert R. Mullen, plans to go to Berlin soon to discuss with city officials the possibilities of representing Berlin interests in this country with individual companies, trade groups, and the like.

5. Encourage and support a "Buy Berlin" campaign. We could use available resources and groups, such as OKCU, to promote a flow of orders to Berlin from the West. This must be balanced with the flow of German orders, of course, but the psychological effect of making Berlin an international supplier should not be lost. Such a program would also have the effect of making the rest of the world more conscious of Berlin.

6. Study the desirability and possibility of making Berlin the headquarters site for new or existing international organizations.

7. Promote new and more ambitious educational and cultural exchanges with Berlin. The recent agreement between the Juilliard School and the Berlin Academy of Music to exchange three students each this year is a small but encouraging sample of what can be done. Berlin would appreciate a larger exchange of professors of the first rank and our institutions would likewise benefit. We should encourage a program of guest lectureships for some outstanding U.S. scholars like James Conant and others and for leading German thinkers to lecture here.

8. We should encourage fairly regular visits to Berlin by leading Americans -- government officials, businessmen, university presidents, and others.

9. We might survey the housing and other facilities of existing Berlin institutions -- particularly the Free University and the Technical University -- with a view to promoting either government or foundation grants for their expansion.

These are some -- only some -- of the many things that can be done or encouraged to promote the viability of Berlin. Each one will have an effect on the economy of the city. More important than their material effect, however, will be their influence on the morale and attitude of the West Berliners. Here, the dividends promise to be out of all proportion to the relatively small investment involved.

Each one of them will say to the West Berliners:

"We are here -- we are with you -- we plan to stay." And that is what the Berliners want now to hear.

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