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International Economic Indicators

U.S. real GNP in the second quarter grew at an energetic 3.1-percent pace compared with the first quarter's anemic 0.3-percent. The official U.S. forecast of 3.9 percent growth in 1985 will have to be revised downward, however, since growth at that rate would require over 6.0 percent annual growth in the second half of 1985. Although this rate would not be unparalleled during the current U.S. recovery, most analysts find such a surge in U.S. economic expansion highly unlikely in the coming months.

The slower than expected economic growth for 1985 means that the Federal budget deficit could be greater than the $213 billion previously forecast for the current fiscal year, since deficit forecasts are based on growth forecasts. Pressure exerted on the United States by the partner countries to cut this deficit has increased. Both the International Monetary Fund (IMF) and the Organization for Economic Cooperation and Development (OECD) have expressed concern over the financial imbalance in the United States. In a recent report, the OECD warned that without a reduction in the U.S. deficit, foreign holders may start to question U.S. economic stability. A loss in investor confidence could play havoc on international financial markets and lead to higher U.S. interest rates with negative effects on U.S. and global recovery. After reaching an historical high against major currencies in February 1985, the dollar dropped to its lowest point this year in July. The period of the superdollar may be over. Analysts differ widely in assessing how a weaker dollar will effect U.S. and Western economic recovery.

Industrial production

U.S. industrial production declined 0.1 percent in May, following a 0.2-percent drop in April and a 3.0-percent gain in March. The annual rates of industrial growth in the key developed countries, calculated by dividing the latest available monthly output by the output in the corresponding month of the previous year, were as follows: the United States, 1.5 percent; Canada, 4.0 percent; France, 1.6 percent; Italy, 4.6 percent; Japan, 6.8 percent; the United Kingdom, 5.0 percent; and West Germany, 3.0 percent.

Japan's industrial output (as measured by the country's mining-manufacturing index) dropped 0.7 percent in the first quarter of 1985. This was the first quarterly decline in 9 quarters. A decline in exports over the period is partially blamed for this drop.

Employment

The rate of unemployment in the United States (on a total labor force basis including military personnel) remained 7.2 percent in June, the same as during the previous 4 months. Unemployment rates in May as reported by national statistical offices were as follows: Canada, 10.5 percent; France, 9.9 percent; Italy, 12.9 percent; Japan, 2.5 percent; the United Kingdom, 13.1 percent; and West Germany, 9.4 percent. (For foreign unemployment rates adjusted to U.S. statistical concepts, see tables at the back of this issue.)

External balances

The monthly deficit in U.S. merchandise trade widened from $11.9 billion in April to $12.7 billion in May. This was the second largest monthly deficit on record, exceeded only by the $13.8-billion deficit registered in July 1984.

The U.S. current account deficit amounted to $30 billion during the first quarter of 1985. At this rate, the United States could incur a $120-billion deficit on its current account in 1985. The deficit amounted to $101 billion in 1984. The net U.S. international investment position (U.S. investment abroad minus foreign investment in the United States) was $104 billion at the end of 1983, $28.2 billion at the end of 1984, and close to zero at the end of the first quarter of 1985. This means that the United States may now be a net debtor country.

The aggregate trade deficit of the industrialized countries increased to $29.4 billion in January-March 1985, from $27.3 billion in the same period of 1984 and from $11.3 billion in October-December 1984, according to the IMF. This increase is largely explained by improvements in the trade balances of the developing countries of Asia, Europe and the Western Hemisphere.

Prices

The U.S. consumer price index rose only 0.2 percent in May, the smallest increase since January. In June 1985, the annualized rate of consumer price inflation was 8.7 percent in Italy and 2.3 percent in West Germany. The May rate was 3.9 percent in Canada, 6.5 percent in France, 1.6 percent in Japan, and 7.0 percent in the United Kingdom.

Consumer prices in industrial countries rose at an average annual rate of 4.3 percent during the first quarter of 1985. This was the fourth consecutive quarterly decline in the rate of increase.

Forecasts

Forecasts of overall economic performance of leading industrial countries are generally favorable. The economists of the Basel-based Swiss Bank Corporation consider medium-term growth prospects of the Western economies so good that economic history, they claim, might characterize the current decade as the "Golden Eighties." But the majority of analysts are less sanguine and believe that, at best, economic growth in the major industrial nations will show a moderate improvement from the current modest rate in the years ahead. According to the latest forecast of the European Commission, the Community's combined Gross Domestic Product will grow 2.3 percent in both 1985 and 1986 compared with 2.1 percent in 1984. Unemployment in the European Community is expected to rise from 10.4 percent in 1984 to 11.2 percent in 1985, before declining slightly to 11.1 percent in 1986.

There is serious disparity among forecasts of U.S. economic performance. Some analysts foresee a recession, while others expect a return to 1984's star performance.

Official statements by multilateral financial organizations (World Bank, the IMF, and the Bank for International Settlements) suggest that the international debt problem may have passed its critical stage. In a recent study, for example, the World Bank says that developing debtor nations could re-establish credit worthiness and resume steady economic expansion in the next 5 years. Bank analysts cite a reduction in industrial country "protectionism" as one of the conditions for this.

The consensus among trade analysts is that the meeting of the General Agreement on Tariffs and Trade (GATT) council, scheduled to take place in Geneva on July 22, will endorse the start of preparatory talks for a new round of negotiations to liberalize trade. If these preparatory talks are authorized, an announcement on the start of substantive negotiations is expected in early 1986.

International Trade Developments

Group of Ten endorses floating exchange rates: Opponents emphasize need for greater stability

Finance ministers and central bank governors representing the Group of Ten (Belgium, Britain, Canada, France, Italy, Japan, the Netherlands, Sweden, West Germany, and the United States joined by Switzerland) met on June 21 in Tokyo to consider the results of a 2-year study on refirming the international monetary system. The Group-of-Ten study, touched off by the 1983 Williamsburg Economic Summit, examined suggestions to improve international economic cooperation and promote greater exchange rate stability.

The Group of Ten acknowledged that exchange rate fluctuations under the current system of "managed floating" have been considerable, yet it opposed a return to the system of fixed parities in effect during the 1950's and 1960's. With this decision, the Group rejected a French proposal to create target zones, a mechanism designed to foster stability in exchange rates by permitting currency values to fluctuate only within certain ranges. A system of target zones currently operates among the members of the European Monetary System. Members are expected to intervene in exchange markets when the value of their currency strays outside its upper or lower limit.

The French proposal, supported strongly by many developing nations and tacitly by some European countries, coupled with the Group's concern over undesirably large swings in exchange rates, has fostered discussion on the potential benefits and costs of achieving increased stability in exchange rates. Proponents of a more stable system argue that exchange rates pegged into target zones would enhance the predictability of export revenues. This, in turn, would encourage the expansion of most national economies and of international trade. Developing nations, particularly those depending on export revenues from only a few commodities, would benefit most from exchange rate stability. Currently, erratic fluctuations in the export earnings of these countries often impede their ability to import from the industrialized West, thereby disrupting their plans for economic development. Many developing nations may thus find it advantageous to peg the value of their currencies within certain ranges, even if they must then draw upon their available monetary reserves to support the pegged rates. Like bilateral clearing arrangements--giving rise to barter and countertrade--and industrial targeting, the demand for stable exchange rates reflects the developing nations' search for more predictable export earnings.

Those who advocate target zones state that major industrialized nations might also benefit from their introduction, since a steady expansion of developing economies would stimulate economic activities in their own. Further, they argue that the successful operation of the system would lead to an increased coordination of economic policies among the industrialized countries, spurring further growth of the international division of labor.

Despite the positive aspects of target zones, the analysis of the Group of Ten countries demonstrated that such a system has its own costs and that the current one has significant benefits. According to this view--one which also receives solid support in the international community--the current regime is more helpful in improving national economic structures than the fixed rate system. This is so because the allocation of resources is demonstrably more efficient under a system of floating rates. At present, the reshaping of national economic structures is vitally important to the process of eliminating world debts that reflect the structural imbalances of many national economies. Moreover, this system diverts a smaller amount of capital from productive to speculative uses since speculation under this system entails larger risks. A system of fixed or quasi-fixed rates, supporters of the current system argue, would require much management and frequent adjustments to currency valuations. Fixed or pegged exchange rates are also said to reduce the effectiveness of a country's monetary policies. In addition, supporters of the current system claim that, by imposing coordinated monetary and fiscal policies on governments, the maintenance of a fixed exchange rate system in the long run would reduce the domestic economic autonomy of nations. The Group of Ten countries expressed the desire, however, to narrow fluctuations in exchange rates and achieve greater stability in world markets while retaining the current system.

The debate between the supporters and opponents of the system of floating exchange rates is far from over. The French have announced their intention to reintroduce the target zone concept at the October meeting of the 148-member International Monetary Fund in Seoul, Korea. In addition, the developing countries will present their own proposal for reforming the international monetary system at that meeting. This proposal will likely contain suggestions for pegging exchange rates.

Truce is called in citrus-pasta "war"

The United States and the European Community recently called a truce in their citrus-pasta trade dispute, while negotiators try to reach a compromise. Both sides have agreed to a 4-month moratorium on the retaliatory actions. The Reagan administration has temporarily suspended the tariff increases announced last month on pasta imports from the EC. Similarly, the EC has agreed to delay counterretaliatory measures on its imports of lemons and walnuts from the United States.

A tentative compromise has been reached with respect to the pasta issue in which the EC made an offer to cut in half the internal subsidies paid to pasta exporters. The 4-month moratorium will be used to try to settle the dispute over EC citrus preferences that originally sparked the U.S. retaliation against pasta. If the two countries have not arrived at a satisfactory solution on citrus by October 31, the United States plans to go ahead with the tariff hikes on pasta.

Frustrated by European refusal to settle the score on citrus preferences (see IER, May 1985), the United States last month announced plans to retaliate. In a memorandum to Office of the United States Trade Representative (USTR) on June 20, President Reagan characterized the EC tariff preferences on lemons and oranges from the Mediterranean countries as "unreasonable and discriminatory." The President ordered withdrawal of "equivalent concessions" with respect to imports from the EC in the form of duty hikes ranging from 25 to 40 percent on EC pasta imports. Upon hearing of the impending retaliation, the EC warned the United States that any unilateral move would invite counter-retaliation against U.S. exports of lemons (raising the tariff to 20 percent from the current 8 percent) and walnuts (to 30 percent from the present 8 percent).

The citrus issue dates back to November 1976, when the Florida Citrus Commission first filed a section 301 petition with the USTR. In its petition, the citrus association alleged that EC preferences on imports of orange and grapefruit juices and fresh citrus fruits, granted to the Mediterranean countries, adversely affected U.S. citrus producers. After the 1979 Tokyo Round, in which a duty reduction was obtained only on fresh grapefruit, consultations were resumed with the EC on the other citrus products concerned. In 1982 the United States formally complained to the GATT about the EC duty preferences, and in 1983 a GATT dispute settlement panel was set up. In December 1984 the panel completed its findings.

Although the GATT panel declined to rule that the EC preferences violated GATT rules, it did conclude that the United States had been adversely affected and that it should be compensated. The panel suggested that the EC lessen the adverse effects on the United States by reducing the MFN tariff rates on lemons and either reducing or extending the period of application of MFN rates on oranges. The panel noted that, under the system, U.S. exporters pay full import duties while, for example, Morocco pays only 20 percent of the full duty; Israel, 40 percent; and Spain, 60 percent. According to the panel, only 6 percent of these fruits imported by the EC comes from the United States while 80 percent comes from Mediterranean countries.

Refuting the panel findings, the EC cautioned that the decision opens a Pandora's box of new problems. The EC feared that the panel findings set a dangerous precedent for the future of all trading arrangements the EC has signed, especially under the Lomé convention. The preferential agreements, it argued, were concluded for essentially political reasons and were consistent with GATT provisions governing free trade areas (article XXIV). The EC also described the preferences as part of a policy of development aid to countries of the Mediterranean region. The EC has expressed disappointment with U.S. handling of the case, pointing to its acquiescence to similar U.S. arrangements--such as the Caribbean Basin Initiative and the U.S.-Israel Free Trade Agreement--without requesting compensation.

Although GATT mechanisms do provide for retaliation under certain circumstances, the United States was forced to act outside GATT auspices because the panel report was never formally adopted by the GATT Contracting Parties. The EC exercised its ability to block the consensus necessary for the report's adoption. If the report had been adopted, the United States could have requested approval of the Contracting Parties for some form of compensation or retaliation.

The United States was hard pressed to find supporters for adoption of the panel report. Individual EC member states would not break ranks, arguing that the issue was one solely within the purview of the EC Commission and not up to the panel to decide. Other countries, particularly developing countries, feared repercussions in their own trade negotiations with the EC and, at best, agreed to remain silent in GATT council meetings considering the report. Hong Kong, Chile, and Brazil did speak in favor of adopting the report at the May Council meeting. Brazil proposed that the EC Mediterranean preferences be extended to all developing countries through the EC's GSP program.

Some of the types of products the United States initially considered as retaliation prospects included canned ham (Denmark), canned tomatoes and pasta (Italy), cut flowers and bulbs (Holland), fruit juice and rye bread (Germany), and mineral waters (France and Belgium). However, by retaliating on pasta, another product subject to controversy, the United States has addressed the problem of unresolved disputes with the EC over other agricultural products. In a separate case brought by the United States before a GATT subsidies code panel, EC subsidies on pasta had been found in violation of the code but the United States had also been unable to obtain concrete results in this case.

New Canadian investment agency to stress the positive

Legislation creating a new foreign investment agency in Canada became effective on June 30. The Investment Canada Act establishes a new agency, Investment Canada, to replace the Foreign Investment Review Agency (FIRA).

The legislation was introduced into Parliament in December 1984 (IER, January 1985) and received final passage in late June. The requirements for review of potential foreign investments have been changed: New foreign investments in Canada are exempt from all Government review, and takeovers of existing Canadian companies are subject to review only when such acquisitions involve assets of Can$5 million or more. The legislation is expected to result in faster, simpler decisionmaking, with the total number of investments subject to review being reduced by 90 percent.

FIRA, the old review agency, had come into being in the early 1970's at a time of heightened Canadian nationalism and increased sensitivity to the significant investment presence of U.S. capital in Canada. U.S. protests of certain FIRA policies culminated in a GATT case in 1982. The panel established to settle the bilateral dispute found that certain aspects of the Canadian investment review process were not in conformity with the General Agreement and recommended that changes in the review process be made. Following that finding, the rate of approvals for new investment from both Western Europe and the United States increased. Nevertheless, the process by which FIRA reviewed foreign investments into Canada came to be viewed as burdensome and even to constitute an unreasonable impediment to foreign direct investment.

In announcing passage of the Act, Industry Minister Sinclair Stevens remarked that it will bring about a new era for investment in Canada: "It will stimulate investment, technological developments, and the creation of jobs for Canadians." The new act provides the Government the means to ensure that important investments by non-Canadians will be of benefit to Canada. Special consideration for foreign investment in cultural industries (e.g., film production and book and newspaper publishing) is contained in the legislation. These are the only specific sectors in which investments will receive special attention and review beyond that set out in the general threshold criteria.

The current willingness on the part of Canada to explore the possibility of closer economic and trading ties with the United States is closely related to the new emphasis on promoting Canada as a safe and profitable place to invest. Tomorrow's trade is seen as dependent on today's investment flows. Canada's heavy dependence on its trading sector is now working to bolster its economic performance by changing old perceptions. The presupposition of the Investment Canada Act is that any new foreign investment is viewed as favorable--a source of the new capital, technology, and jobs Canada needs to attain its economic potential.

The United States and the European Community finally work out compromise on further access of EC steel pipe to the U.S. market

Steel trade has once again been the subject of intense and drawn-out negotiations between the United States and the European Community (EC) about EC access to the U.S. steel market. The recent flurry of negotiations that began earlier this year ended on June 7, 1985, after the two sides--led by U.S. Commerce Secretary Baldrige and EC External Relations Commissioner de Clerq--reached a package agreement permitting the EC to ship 100,000 tons of steel pipe to the United States in addition to the import quota already in effect. The additional shipments will now enable the EC to supply steel pipe for construction of the All-American Pipeline that will stretch from Texas to California.

In return, the EC committed itself to renegotiate the terms of the 1982 U.S.-EC Arrangement Concerning Trade in Certain Steel Products (the Arrangement), which expires at the end of this year. The 1982 Arrangement places limits on U.S. imports of EC carbon steel products. The EC also agreed to the U.S. request to negotiate extension of the Arrangement to steel products not currently subject to consultations, including tin-free steel, black plate, and alloy wire rods. Negotiations on renewal and extension of the 1982 Arrangement were expected to be completed by mid-July.

The EC will now be able to exceed the 1985 quota agreed upon in January 1985--an agreement that limits EC exports to 7.6 percent of the U.S. steel pipe and tube market for calendar years 1985 and 1986 except when these products are in short domestic supply. The U.S. concession allows the EC to operate under the January agreement's "short supply" clause. The use of this clause had been in dispute since the January agreement was reached because U.S.steel producers claimed they could supply enough steel for the construction of the All-American pipeline without the increase in European shipments. The European steel producers claimed that U.S. steel does not meet sufficient quality standards for use in the pipeline and that domestic demand outstripped supply.

Although U.S. imports of steel pipes and tubes from the EC were not ammong the steel products included in the 1982 Arrangement, the two sides exchanged letters of understanding as part of the Arrangement holding the EC to 5.9 percent of the U.S. market for pipes and tubes. According to the understanding, consultations were to be held should EC shipments exceed this level. The U.S. position was that the exchange of letters was a formal agreement holding the EC to a fixed percentage of the U.S. market. The EC position was that the exchange of letters was an informal agreement that only committed the EC to confer with the United States.

U.S.-EC negotiations in late 1984 failed to limit the surge in U.S. imports of EC steel pipes and tubes which had reached a level of almost 14 percent of apparent U.S. consumption--far exceeding the 5.9 percent level that was agreed upon in the 1982 exchange of letters. When negotiations to set limits for EC shares of the U.S. market broke down last winter, the United States embargoed all imports of EC steel pipes and tubes from November 29 through December 31, 1984. The embargo was lifted after the two sides negotiated the January agreement.

Mexico relaxes import controls

There are indications that Mexico is departing from its long-standing policy of strict protectionism. On June 5, 1985, the Mexican Government announced a program granting exporters easier access to imported materials, machinery, and parts. This program is intended primarily to facilitate Mexico's nonoil exports--an objective the de la Madrid administration is actively promoting. The new measures are expected to make Mexican producers, who have traditionally concentrated on the home market, more interested in exporting.

Officials also hope that, by being forced to face the competition of imported inputs, Mexican suppliers of materials, machinery, and parts will attain greater efficiency of production. In addition, officials consider the program instituted in June, like other import-liberalizing measures imposed earlier this year, helpful in tempering inflation. Inflation has been the least manageable economic problem thus far faced by the de la Madrid administration, whose stated objective is to reduce the average annual rate of inflation to 40 percent in 1985 from 59 percent in 1984.

The new regulations authorize exporters to use up to 30 percent of their export earnings to purchase foreign producers' goods without having to apply for import permits. Bank certificates called "DIMEX" (the Spanish acronym for Certificate of Right to Import for Export) will be used for such imports in lieu of the earlier permits. These certificates will also give eligible imports duty-free status since users will receive refunds of the duties they pay.

Exporters are allowed to freely allocate the authorized amount between purchases of foreign machinery, equipment, or materials as needed, provided the chosen items are not excluded from the program. The current list of exclusions contains items that are classified as "non-productive" or that compete directly with those Mexican products that continue to enjoy strong protection, such as petrochemicals and pharmaceuticals.

Concerned about their diminished home market protection, Mexican industry groups hotly opposed several proposals leading to the new regulations. Although unable to stop the DIMEX program, its opponents nonetheless managed to expand the list of excluded items and were successful in lowering to 30 percent the share of export revenues that is allowable for DIMEX. The original proposal was 40 percent.

Mexico instituted other measures earlier this year in an effort to liberalize imports and stimulate exports. The most notable action was taken in March, when the Government eliminated the import licensing requirements for 519 items covering a broad range of products, including steam turbines, agricultural machinery, dairy products, and dairy cows. This move was also justified on grounds that the competitiveness and export orientation of domestic industries must be raised. Then, as in June, the Government argued that phasing out excessive protection will be helpful in keeping inflation under control. Mexican officials had been quoted as saying that the domestic industry needed "a deliberate shock treatment."

U.S. exporters, by far the largest source of supplies (especially of machinery and transportation items) for Mexican production, stand to benefit from this apparent shift in Mexico's import policy. By the same token, U.S. products will face more competition from Mexico to the extent the new policy truly promotes its exports.

Singapore is using its ASEAN muscle to fight New Zealand's decision to revise its GSP program

New Zealand has instituted major reforms in its trade regime in an attempt to dismantle its import protection policies and restructure its domestic industry. In addition to ending import licensing and lowering tariffs, the reforms will significantly alter New Zealand's GSP program, resulting in lost GSP privileges for over a dozen countries, including those of two ASEAN members, Sinapore and Brunei. Under the reform, countries with a per capita GNP exceeding 70 percent of that of New Zealand's will no longer be considered less developed nor eligible for GSP.

Singapore is more concerned about losing its less developed status than with the relatively small amount of trade that will be affected. In the last fiscal year, Singapore's merchandise exports to New Zealand amounted to about $103 million, of which roughly 75 percent was petroleum products not included in the GSP scheme. Beginning July 1, Singapore will lose tariff exemptions on about $5 million worth of exports to New Zealand. Yet despite the small fraction of its trade involved, Singapore views New Zealand's action as an alarming precedent that may be adopted by its other major trading partners, such as the United States, the European Community, and Australia. New Zealand's position has been that these countries are no longer significantly worse off than New Zealand and the loss of developing country trade privileges is the result of their economic successes.

Other countries are currently considering revisions to their GSP programs. Since the U.S. program was recently revised, however, Singapore will likely remain eligible for these benefits until 1990. The United States has established $8,500 per capita GNP as the trigger point for country graduation from its GSP program. Singapore is not likely to reach that threshold until at least 1988.

After several bilateral ministerial meetings, Singapore has been unsuccessful in getting New Zealand to alter its plans. Thus, as chairman of ASEAN's Committee on Tourism and Trade (COTT), Singapore has enlisted the help of this group of six nations to fight New Zealand's reforms. A memorandum from COTT to the New Zealand Government criticizes New Zealand for excluding entire countries from its GSP scheme instead of using a product-by-product graduation plan. COTT is also asking New Zealand to postpone implementation of the new GSP scheme until further negotiations. New Zealand insists that the gains that will accrue to Singapore as a result of easier access to New Zealand's market far outweigh the lost GSP benefits.

Congress revises export administration law

Concluding two and one-half years of often acrimonious debate and numerous meetings between House and Senate conferees, Congress approved the Conference Report on the Export Administration Amendments Act of 1985 (S. 883) on June 27. The new legislation amends and extends the Export Administration Act of 1979 through September 30, 1989. Major areas of controversy included the President's authority to impose foreign policy controls and the division of responsibility for licensing and enforcement.

Many members of Congress were concerned that the use of foreign policy controls jeopardized the U.S. reputation as a reliable supplier. But many were also concerned with preserving the President's options to respond to international crises without resorting to force. The bill passed by the Senate in 1984 would have effectively prohibited retroactive foreign policy controls under the EAA, while upholding the President's authority to impose export controls during an international emergency under the International Emergency Economic Powers Act (IEEPA). The bills passed by the House in 1984 and 1985 also included a contract sanctity clause, but they authorized the President to impose retroactive foreign policy controls in response to certain circumstances--acts of aggression or international terrorism, gross violations of internationally accepted human rights, or nuclear weapons tests. The conferees agreed on a contract sanctity clause prohibiting retroactive controls except when a "breach of the peace" poses a "serious and direct threat" to the U.S. strategic interest and the control would be "instrumental in remedying the situation posing the direct threat." In addition, the new legislation requires the President to make a detailed certification to Congress when imposing new controls and expands the list of factors he must consider. The conferees stressed that the new language required "a clear and direct relationship between the proposed control that requires the breaking of a contract and the remedying of the event posing the direct threat. . . ." In their view, the new provision "significantly narrows, but does not entirely eliminate," the President's authority to impose retroactive controls. The conferees' statement did not, however, define "breach of the peace," an issue that arose during Congress' effort to pass export administration legislation last year.

A proposed amendment to section 10(g) of the 1979 act clarifying the role of the Department of Defense (DOD) in the licensing of exports to non-Communist countries contributed to the collapse of the 1984 Conference. At that time the conferees were unable to reach a compromise between the Senate bill, which explicitly authorized DOD to review applications to export goods and technologies to non-Communist countries when there was a clear risk of diversion to "controlled" (i.e. Communist) countries, and the House bill, which retained the original language of section 10(g). Senator Garn (R-UT), the amendment's author, and others argued that section 10(g) authorized DOD to review any license application, but that Commerce interpreted it as limiting DOD review to applications for exports to Communist countries. In the view of the amendment's supporters, DOD's role in licensing had to be expanded to counterbalance what they viewed as an inherent contradiction in Commerce's dual roles of promoting and controlling exports. Many members, particularly in the House, believed that section 10(g) did not authorize DOD review of licenses to countries other than controlled countries and opposed the amendment on the grounds that DOD would not be any better at licensing decisions and that expanded DOD participation could lead to delays in license processing.

Between the first and second conferences the President signed a National Security Council memorandum authorizing DOD to review applications to export selected goods and technologies to as many as 15 non-Communist nations (IER, May 1985). Following the President's action, Senator Garn and other supporters of the amendment to section 10(g) announced that the amendment was no longer necessary. This paved the way for a compromise in the 1985 Conference, in which the controversial amendment was omitted. The Conference Report and floor statements by supporters and opponents of expanded DOD review suggest that the issue is likely to be revived in the future.

The conferees resolved the issue of the division of responsibility for enforcement between Commerce and Customs by giving Commerce responsibility for enforcement in the United States and Customs responsibility for enforcement overseas. However, Commerce was authorized to conduct certain enforcement activities overseas--pre-licensing investigations, post-shipment verification, and antiboycott investigations--and Customs was given the major responsibility for enforcement activities at ports of entry and exit in the United States. Both agencies were also given new powers to enforce the act.

A number of other significant provisions were added in the new legislation. It authorizes controls on imports into the United States by violators of U.S. national security export controls and, under certain circumstances, of COCOM controls; provides authority for controls on transfers of goods and technologies to embassies of controlled countries; and makes possession of goods and technologies with intent to violate the act and conspiracy to violate the act punishable offenses. The new legislation also decontrols low-level technology exports to COCOM countries; provides for expedited licensing of exports of higher-level technology to these destinations; shortens deadlines for license processing by one-third; and authorizes Comprehensive Operations Licenses (COL's) for multiple shipments between U.S. firms and their overseas subsidiaries in free-world countries. In addition, it concludes a number of provisions relating to foreign availability.

Developing countries agree in principle to a new round of trade talks

The major obstacle to beginning a new round of multilateral trade negotiations was recently removed when the developing countries agreed in principle to launch a new round. Two meetings held in June were the source of this forward movement. At the June 6 Council session of the General Agreement on Tariffs and Trade (GATT), the developing countries agreed to launch a new round of trade talks provided certain conditions are met. A few days later, a "breakthrough on procedural issues" occurred at an informal meeting of trade ministers in Stockholm.

GATT Council meeting.--On June 6, 23 developing nations, led by India and Brazil, presented a "negotiating paper" to the GATT Council in Geneva. The paper lists the conditions that must be met before the developing countries will agree to begin a new round of trade talks. Although officials from the United States and the European Community oppose several of the demands set forth in the paper, they consider the paper a significant step forward as it represents the first move to spell out the developing countries' position on the prospective new round.

Ambassador Shrirang Shukla of India said the paper is not a list of final demands; rather, it is negotiable. It "sets out our basic position . . . and is new in that it specifies the subjects we want included in the new round." Most of the original demands of the developing countries remain intact. They would like to see the talks cover all tariff and nontariff barriers to trade in agriculture, raw materials, and manufactured and semi-processed goods, but they continue to rule out discussion of trade in items of particular interest to the United States, such as services, high technology, and counterfeit goods. Also, prior to the start of a new round, the developing nations call for individual "standstill and rollback measures"; i.e., the developed countries must make a commitment not to introduce any new restrictive measures inconsistent with GATT and to roll back "measures inconsistent with the General Agreement either by elimination forthwith or, at least, through a phase-out . . . ." At the same time, GATT members must recognize the need to establish special rules for the developing countries. Other demands of the developing nations set forth in the paper include:

--return textile negotiations to GATT after the Multifiber Arrangement expires in July 1986;

--establish a timetable to liberalize trade in tropical products;

--restrain "use of export subsidies which compete with the exports of developing countries to third country markets";

--restrain "recourse to countervailing and antidumping procedures against imports from developing countries" and limit initiation of new procedures;

--conclude a better agreement on safeguards;

--strengthen dispute settlement and enforcement mechanisms; and

--conduct a "parallel process to review and reform the international financial and monetary system in appropriate form to be agreed upon by all interested parties and review in depth in GATT all the effects of exchange-rate fluctuations on international trade."

The United States had hoped that a senior-level meeting designed to begin preparations for the new trade round could be held in July. Instead, this preparatory meeting was delayed indefinitely when the GATT Council directed the Secretariat to discuss the next steps in the new round process and to report back to the next Council session in mid-July.

<u>Trade ministers' meeting in Stockholm</u>.--Further progress towards a new round occurred at an informal meeting of senior trade representatives from 21 industrialized and developing countries on June 8-9. Willy de Clercq, External Relations Commissioner of the European Community, called the outcome of the Stockholm meeting a "breakthrough on procedural issues." Participants agreed to submit position papers, including a list of preferred topics for negotiation, to the next GATT Council meeting in mid-July. The Council is then expected to fix a date for the preparatory meeting of senior government officials in September. This move followed an unexpected statement by a Brazilian official, supported by other developing countries, that nonbinding discussions on liberalizing trade in goods should begin in September.

Despite the developing countries' consent to discuss an agenda, important differences remain between the participating ministers. The developing world continued to resist covering services in the new negotiations, although a compromise was struck when they agreed to hold parallel talks on services outside GATT. India reiterated demands for improved access to western markets prior to the start of a new round, and asked that previous GATT "standstill and rollback" commitments, particularly on textiles and agriculture, be honored. The chairman of the meeting, Sweden's Trade Minister Mats Hellstroem, noted that participants supported the French proposal to conduct parallel negotiations on the reform of the international monetary system, but said that they had agreed that "monetary problems should not be conditioned to GATT negotiations on trade." Although the developing countries' consent to begin nonbinding preparatory talks before the end of September is a positive step, building a consensus for negotiations will be a long, hard process.

The Stockholm meeting was the third in a series of meetings among industrialized and developing countries designed to discuss issues related to GATT on an informal basis. Previous meetings were held in Washington, D.C. and Rio de Janeiro. The Stockholm meeting was attended by representatives from Argentina, Australia, Brazil, Canada, the European Community, Finland, France, GATT, India, Italy, Japan, Mexico, New Zealand, Norway, the Philippines, South Korea, Sweden, Switzerland, United Kingdom, United States, West Germany, Uruguay, and Yugoslavia.

Industrial production
(Percentage change from previous period, seasonally adjusted at annual rate)

Country	1982	1983	1984	1984 I	1984 II	1984 III	1984 IV	1985 I	1984 Dec.	1985 Jan.	1985 Feb.	1985 Mar.	1985 Apr.	1985 May
United States	-8.1	6.4	10.7	11.4	8.6	6.4	-2.3	2.0	0	2.2	2.2	3.7	-2.9	-1.4
Canada	-10.0	5.7	8.7	2.4	3.3	13.1	0.7	1.1	6.0	-8.7	-4.9	-7.3	10.5	
Japan	0.4	3.5	11.1	13.5	11.6	6.1	11.6	-2.6	-7.7	3.0	-1.0	-15.7	39.0	25.1
West Germany	-3.2	0.3	3.1	2.5	-10.9	16.5	5.5	-5.6	-13.5	-1.2	-1.2	10.2		
United Kingdom	2.0	3.9	1.0	-2.4	-7.9	0.4	3.4	7.8	8.5	5.9	4.7	29.9	7.0	
France	-1.5	1.1	2.6	7.4	-4.0	9.5	-9.5	-3.0	-24.1	-24.6	74.8	19.8	-23.8	
Italy	-3.1	-3.2	3.1	4.5	2.1	7.7	-6.9	7.4	6.5	-37.9	174.3	3.7	-42.6	

Source: Economic and Energy Indicators, U.S. Central Intelligence Agency, July 5, 1985.

Consumer prices
(Percentage change from previous period, seasonally adjusted at annual rate)

Country	1982	1983	1984	1984 I	1984 II	1984 III	1984 IV	1985 I	1984 Dec.	1985 Jan.	1985 Feb.	1985 Mar.	1985 Apr.	1985 May
United States	6.2	3.2	4.3	5.0	3.7	3.7	3.5	3.3	2.3	2.3	4.2	5.8	4.6	2.7
Canada	10.8	5.8	4.3	5.7	2.7	3.3	3.3	5.5	6.4	6.0	5.2	2.0	6.4	2.0
Japan	2.6	1.8	2.3	3.6	1.0	1.3	3.3	2.3	6.7	4.9	-4.3	-0.3	2.2	-4.9
West Germany	5.3	3.6	2.4	2.8	2.0	0.6	2.8	3.8	1.3	4.3	5.2	5.6	2.2	1.9
United Kingdom	8.6	4.6	5.0	4.4	3.0	5.5	6.0	7.0	2.6	7.4	9.9	2.7	12.4	6.3
France	12.0	9.5	7.7	7.3	6.2	7.3	6.5	5.7	5.7	5.3	5.9	6.6	5.7	7.1
Italy	16.4	14.9	10.6	11.1	10.4	8.0	6.0	10.2	13.2	10.0	10.6	1.1	11.9	9.3

Source: Economic and Energy Indicators, U.S. Central Intelligence Agency, July 5, 1985.

Unemployment rates
(Percent; seasonally adjusted; rates of foreign countries adjusted to be roughly comparable to U.S. rate)

Country	1982	1983	1984	1984 I	1984 II	1984 III	1984 IV	1985 I	1985 Jan.	1985 Feb.	1985 Mar.	1985 Apr.	1985 May	1985 June
United States	9.7	9.6	7.5	7.9	7.5	7.4	7.2	7.3	7.4	7.3	7.3	7.3	7.3	7.3
Canada	11.0	11.9	11.3	11.4	11.4	11.2	11.1	11.1	11.2	11.0	11.2	10.9	10.5	
Japan	2.4	2.7	2.8	2.8	2.7	2.8	2.7	2.6	2.5	2.6	2.6			
West Germany	5.9	7.3	7.4	7.2	7.4	7.5	7.3	7.9	7.4	8.0	8.0	8.0	8.1	
United Kingdom	12.2	13.1	13.4	13.2	13.3	13.6	13.5	13.2	13.6	13.2	13.2	13.4	13.3	
France	8.7	8.8	10.0	9.5	10.0	10.2	10.3	10.5	10.5	10.6	10.5	10.5	10.5	
Italy	4.8	5.3	5.6	5.5	5.6	5.5	5.6							

Note.--Italian unemployment surveys are conducted only once a quarter, in the first month of the quarter.

Source: Statistics provided by Bureau of Labor Statistics, U.S. Department of Labor, July 1985.

Trade balances
(Billions of U.S. dollars, f.o.b. basis, seasonally adjusted at annual rate)

Country	1982	1983	1984	1984 I	1984 II	1984 III	1984 IV	1985 I	1984 Dec.	1985 Jan.	1985 Feb.	1985 Mar.	1985 Apr.	1985 May
United States 1/	-31.6	-57.5	-107.9	-104.8	-104.8	-124.4	-96.4	-114.8	-82.8	-106.8	-121.2	-116.4	-126.0	-135.6
Canada	14.4	14.4	16.1	14.4	16.4	16.4	17.6	16.0	13.2	12.0	15.6	19.2	19.2	
Japan	18.6	31.5	44.1	40.0	40.0	40.0	53.6	45.6	52.8	55.2	42.0	38.4	46.8	
West Germany	21.1	16.6	18.8	18.8	12.8	20.0	23.6	17.6	20.4	16.8	19.2	16.8	26.4	
United Kingdom	4.1	-1.8	-5.7	-0.4	-6.8	-8.4	-6.4	-6.0	-2.4	-1.2	-3.6	-13.2	-3.6	
France	-14.0	-5.9	-2.8	-6.0	-4.8	1.6	-1.6	-4.4	-1.2	-4.8	-7.2	-1.2	-4.8	-0.4
Italy	-12.8	-7.9	-10.7	-9.6	-12.8	-6.4	-14.8	-15.2		-14.4	14.4	15.6	-19.2	

1/ Exports, f.a.s. value; imports, customs value.

Source: Economic and Energy Indicators, U.S. Central Intelligence Agency, July 5, 1985.

U.S. trade balance, by major commodity categories and by selected countries
(Billions of U.S. dollars, customs value basis for imports, seasonally adjusted unless otherwise indicated)

Item	1982	1983	1984	1984 I	1984 II	1984 III	1984 IV	1985 I	1984 Dec.	1985 Jan.	1985 Feb.	1985 Mar.	1985 Apr.	1985 May
Commodity categories:														
Agriculture	21.6	20.0	18.4	5.2	4.4	4.0	4.6	3.3	1.8	1.4	1.2	.7	1.1	.5
Petroleum and selected products, unadj	-54.6	-49.1	-52.5	-13.1	-13.4	-13.2	-12.8	-9.5	-3.7	-3.7	-3.2	-2.6	-4.2	-4.1
Manufactured goods	-4.9	-31.3	-78.9	-19.0	-18.1	-25.1	-17.5	-23.2	-5.4	-6.6	-8.4	-8.2	-7.7	-8.0
Selected countries:														
Western Europe	7.6	1.2	-14.1	-3.6	-2.9	-4.5	-2.6	-4.5	-.7	-1.6	-1.6	-1.3	-1.3	-2.4
Canada	-12.6	-12.1	-20.1	-4.3	-5.1	-5.3	-5.7	-4.9	-2.1	-1.1	-1.8	-2.0	-2.0	-1.6
Japan	-17.0	-19.6	-33.8	-7.0	-7.8	-11.0	-7.9	-10.2	-2.5	-3.4	-3.9	-2.9	-3.7	-3.9
OPEC, unadj	-8.3	-8.2	-12.3	-2.6	-3.7	-3.7	-2.5	-1.3	-.6	-.6	-.5	-.2	-.8	-1.1
Unit Value (per barrel) of U.S. imports of petroleum and selected products, unadj	$31.48	$28.60	$28.11	$28.31	$28.45	$27.98	$27.69	$26.96	$27.49	$27.19	$26.98	$26.71	$26.91	$27.34

Source: Summary of U.S. Export and Import Merchandise Trade, U.S. Dept. of Commerce, May 1985.

Money-market interest rates
(Percent, annual rate)

Country	1982	1983	1984	1984 II	1984 III	1984 IV	1985 I	1985 II	1985 Jan.	1985 Feb.	1985 Mar.	1985 Apr.	1985 May	1985 June
United States	12.4	9.1	10.4	10.9	11.5	9.4	8.6	7.9	8.1	8.7	9.0	8.5	7.9	7.4
Canada	14.4	9.5	11.3	11.4	12.5	11.2	10.6	9.9	9.7	10.6	11.4	10.2	9.8	9.6
Japan	6.8	6.8	6.3	6.3	6.3	6.3	6.3	6.3	6.3	6.3	6.3	6.3	6.3	6.3
West Germany	8.8	5.7	6.0	6.0	6.0	5.9	6.1	5.8	5.8	6.1	6.4	6.0	5.8	5.7
United Kingdom	12.2	10.1	9.9	9.2	11.1	10.1	12.9	12.6	11.6	13.7	13.5	12.7	12.6	12.4
France	14.6	12.4	11.7	12.3	11.4	10.7	10.6	10.5	10.4	10.6	10.7	10.5	10.2	10.8
Italy	20.0	18.0	17.1	17.0	16.8	17.0	15.8	15.0	15.8	15.8	15.8	15.2	14.9	15.0

Note.--The figure for a quarter is the average rate for the last week of the quarter.

Source: Statistics provided by Federal Reserve Board.

Effective exchange rates of the U.S. dollar, unadjusted and adjusted for inflation differential
(Index numbers, 1980-82 average=100; and percentage change from previous period)

Item	1982	1983	1984	1984 II	1984 III	1984 IV	1985 I	1985 II	1985 Jan.	1985 Feb.	1985 Mar.	1985 Apr.	1985 May	1985 June
Unadjusted:														
Index number	109.8	114.2	122.3	118.8	125.1	128.2	135.1	131.3	132.0	136.4	136.8	131.7	131.9	130.4
Percentage change	10.4	4.0	2.5	1.4	5.3	2.5	5.4	-2.8	2.0	3.3	0.3	-3.7	0.2	-1.1
Adjusted:														
Index number	109.8	112.4	118.3	114.9	120.8	123.0	128.8	124.3	126.2	130.0	130.2	124.8	124.6	123.5
Percentage change	9.0	2.4	1.9	0.5	5.1	1.8	4.7	-3.5	1.9	3.0	-0.5	-4.1	-0.2	-0.9

Note.--The foreign-currency value of the U.S. dollar is a trade-weighted average in terms of the currencies of 15 other major nations. The inflation-adjusted measure shows the change in the dollar's value after adjusting for the inflation rates in the U.S. and in these other nations; thus a decline in this measure suggests an increase in U.S. price competitiveness.

Source: World Financial Markets, Morgan Guaranty Trust Company of New York.

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