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INTERNATIONAL ECONOMIC COMPARISONS

Economic prospects remain moderately favorable in the industrial world. The constraining influences of rising U.S. interest rates, structural shifts in the Japanese and West German economies, and large international imbalances all corroborate the new outlook for a slowing expansion of world output and trade. At the same time, business indicators, which have accurately foretold postwar recessions, have not signaled that the 54-month world economic revival is even close to an end. Growth in the combined economies of the industrial countries is expected to be 2.4 percent in 1987, compared with 3.0 percent in 1986.

Analysts caution against overestimating the strength of the U.S. economy on the basis of the sharp, 4.3-percent annual rate of upturn in the Nation's real GNP during the first quarter of 1987. Much of the growth came from the accumulation of business inventories and even more spending by heavily indebted consumers. Many private economists now believe that the U.S. economy will expand 1.0 to 2.0 percent during the second quarter of 1987 and that expansion for the full year will approximate the 2.5-percent pace of the previous 2 years. Contradictory clues about the likely evolution of domestic consumption and investment explain the current extreme caution of forecasters. Higher interest rates are expected to weaken both investment and consumption, but actual and projected rises in corporate earnings should strengthen investment, and recent gains in employment should boost consumption. Also, there is no clear indication of how much impetus rising exports will give to U.S. economic growth in 1987.

Trade

The deficit in U.S. merchandise trade declined from $15.1 billion (c.i.f. imports) in February to $13.7 billion in March 1987. This $1.4 billion improvement was the net result of a $2.4 billion increase in exports and a $1.0 billion increase in imports. The March deficit was roughly the same as the average monthly deficit for January–February 1987. U.S. exports of manufactured goods increased by $1.8 billion from February to March, and imports of manufactures by $0.9 billion. After worsening from January to February, the monthly U.S. deficit in trade with Japan showed improvement, declining from $5.1 billion in February to $4.9 billion in March. But the monthly deficit in trade with West Germany climbed back to its November 1986 level of $1.6 billion in March, up from $1.1 billion in February. The U.S. trade deficit in constant (1982) dollars declined from $147.8 billion during 1986 to an annualized value of $134.2 billion during the first quarter of 1987.

With exports of $243.3 billion, West Germany became the world's largest exporting nation in 1986. U.S. exports were valued at $217.3 billion in 1986, and Japanese exports amounted to $210.7 billion. It must be noted, however, that the depreciation of the dollar distorted international trade statistics for 1986. (For more on the subject, see article under International Trade Developments.)

On the basis of the latest annual data available for international comparisons (1982–1984), 73 percent of the value of Japan's imports consists of food, crude materials, and mineral fuels (SITC sections 0, 2, and 3). The corresponding number for West Germany is 39 percent; and for the United States, 32 percent. Exports of machinery and transportation equipment (SITC section 7) account for 58 percent of Japan's exports, 46 percent of West Germany's, and 41 percent of the value of U.S. exports. In explaining the spectacular increases in Japan's trade surpluses during the 1980's, analysts point to declines in the prices of its major imports and the Japanese population's high propensity to save. The high Japanese saving rate appears likely to persist for some time into the future, which means continuing trade surpluses for the country. Trade policies of other countries would reduce these surpluses only if they caused a recession in Japan, thereby reducing saving, or if they encouraged Japan to follow policies that spurred domestic investment or government spending to soak up the excess saving.

Industrial Production

Led by cutbacks in motor-vehicle output, U.S. industrial production declined by 0.6 percent in April. Further declines in U.S. and global car demand are expected to reduce the worldwide sale of automobiles from 33.2 million units in 1986 to 32.3 million units in 1987. According to Data Resources Inc., the Japanese will assault the U.S. car market through more direct investment this year. Japanese cars produced in this country are not subject to the 2.3 million-unit U.S. import quota established for fiscal year 1988.

The annual rates of industrial growth in the major industrialized countries, calculated by comparing the latest available monthly output with the output in the corresponding month of the previous year, were as follows: Canada, 0.3 percent; France, -2.0 percent; Italy, 2.0 percent; Japan, 0.2 percent; the United Kingdom, 2.6 percent; the United States, 1.8 percent; and West Germany, 0.3 percent.

Investment

The willingness of Japanese financial investors to purchase U.S. stocks and bonds has a significant influence on U.S. interest rates and, consequently, on domestic real investment. Some analysts worry that the price of coaxing Japanese capital into financing the U.S. budget deficit and private capital projects will substantially increase. This could raise the costs of borrowing in this country. Fears were triggered earlier this month when Japanese investors showed little interest in purchasing U.S. T-bonds despite the very large 5.5-percent spread between yields in long-term U.S. and Japanese bonds. Financial analysts cited Japanese concerns over an extended trade conflict with the United States and a further fall in the international value of the dollar. According to the prevalent view, however, bilateral efforts to defuse tensions over trade and the yen-dollar rate and the sheer size of Japan's current investment in this country will prevent any major Japanese flight from the U.S. capital market. One often-quoted factor that supports this point of view is the accelerated rate of Japanese investment in U.S. property. The Japanese are believed to have invested $5.0 billion in U.S. real estate during the first 5 months of this year. Their 1986 U.S. real estate investments were an estimated $3.5 billion to $5.0 billion.

Employment

The rate of unemployment in the United States (on a total labor-force basis, including military personnel) declined from 6.5 percent in March to 6.2 percent in April.

The national statistical offices of other countries reported the following unemployment rates: the March rate was 9.6 percent in Canada, 11.1 percent in France, 14.7 percent in Italy, 11.0 percent in the United Kingdom, and 8.9 percent in West Germany. The February rate was 2.9 percent in Japan. (For foreign unemployment rates adjusted to U.S. statistical concepts, see the tables at the back of this issue.)

U.S. unemployment decreased from 7.5 percent in 1981 to 6.9 percent in 1986, despite increasing trade deficits. In contrast, unemployment increased in the European Community and Japan, although both showed significant trade surpluses over the period. Unemployment in the EC increased from 8.0 percent in 1981 to 11.0 percent in 1986; and in Japan, from 2.0 percent to 3.0 percent. This is the highest annual Japanese jobless rate since 1953. Most of the new jobs created in the United States were in the service sector. About 1 million U.S. manufacturing jobs were lost over the period.

Prices

The U.S. Consumer Price Index rose at a seasonally unadjusted 0.4-percent rate in March, identical to the February increase. The seasonally adjusted annual rate of inflation was 5.1 percent in March and 6.2 percent during January–March 1987. April's 0.7-percent jump in the Producer Price Index and rising interest rates reawakened inflationary worries. However, based on the performance of acknowledged inflation indicators such as labor contracts and industrial input prices, economists do not expect the annual rate of inflation to exceed 4.0 percent in 1987.

The price level in West Germany declined by 0.2 percent from March 1986 to March 1987; and that of Japan, by 1.0 percent from February 1986 to February 1987. In a similar comparison of monthly price indexes over the 1-year period ending in March 1987, the rate of inflation was 4.0 percent in Canada, 4.2 percent in Italy, 4.0 percent in the United Kingdom, and 3.6 percent in the United States. The monthly price index over the 1-year period ending in February 1987 was 3.4 percent in France.

Forecasts

U.S. debts

The Administration's latest estimate for the 1987 U.S. merchandise trade deficit is $155 billion. This would be $15 billion, or roughly 9 percent, less than the $170 billion record deficit registered in 1986, but still more than the $149 billion deficit in 1985. The Office of Management and Budget projects a decline in the Federal budget deficit from $221 billion in fiscal 1986 to $173 billion in fiscal 1987. The Congressional Budget Office's estimate for the 1987 fiscal deficit is $176 billion. Since the trade and fiscal deficits are strongly linked, several private analysts find these forecasts inconsistent. For example, The Conference Board estimates a decline of only 9 to 10 percent in the Federal deficit in fiscal 1987, to roughly $200 billion.

The Brookings Institution predicts that the U.S. external debt (the sum of current account deficits) will reach $700 billion by 1990. The payment of interest on this debt will require about 1 percent of the Nation's GNP, and debt payments will lower U.S. living standards by reducing the population's disposable income.

World trade

The volume of world merchandise trade will grow by only 2.5 percent in 1987, compared with 3.5-percent growth in both 1985 and 1986, according to the General Agreement on Tariffs and Trade (GATT). The GATT bases its forecast on the trade-slowing effects of structural changes in the Japanese and some West European economies, an increase in inflation in other industrial countries (including the United States), and the prolonged debt crisis and trade frictions. ■

INTERNATIONAL TRADE DEVELOPMENTS

Telecommunications Services: One More Trans-Pacific Trade Dispute

The United States and Great Britain have joined forces to oppose recent Japanese proposals that would limit foreign participation in that country's market for international telecommunications services. The current dispute dates back to the liberalization of Japan's telecommunications market on April 1, 1985. At that time, the Government of Japan agreed to allow foreign firms to compete with Kokusai Denshin Denwa (KDD), Japan's monopoly in international telecommunications services.

Citing a lack of frequencies and limited demand for services, Japan's Ministry of Posts and Telecommunications (MPT) announced that only one consortium would be awarded a license. However, two consortia, International Digital Communications Planning Corp. (IDC) and International Telecom Japan (ITJ) were formed and began bidding for the right to compete against KDD. IDC is composed of 30 Japanese firms (led by C. Itoh & Co.), two U.S. companies (Toyota Motor Corp. and Pacific Telesis), and a British firm (Cable and Wireless Ltd.). This group intends to provide services by constructing a trans-Pacific fiber optic cable. The second all-Japanese consortium, ITJ, is led by Japanese trading houses that include Mitsubishi Corp., Mitsui Co., Sumitomo, and Matsushita Electric Industrial Co. ITJ has proposed to offer services by leasing cables from KDD.

In March 1986, MPT employed the Federation of Economic Organizations as a mediator and began urging the two consortia to merge. However, the U.S. and British firms resisted. The merger proposal would have reduced foreign ownership in the consortium to 3 percent per company and Japanese participation to 5 percent per company. The United States and Great Britain immediately charged that the proposal would violate a 1985 agreement and a subsequent Japanese deregulation law, which permits equity participation by foreign companies in telecommunications ventures of up to 33 percent.

There were strong reactions to the merger proposal on both sides of the Atlantic. In Washington, Secretary of Commerce Malcolm Baldrige wrote a letter of protest to Japan's Minister of Posts and Telecommunications on March 13, 1987, and United States Trade Representative Clayton Yeutter fired off a letter to the Japanese Ambassador in Washington. The Senate jumped into the fray by passing S. Res. 164 on March 19, calling for the President to "immediately take appropriate actions to communicate with the Government of Japan" to ensure that Japan's commitments under the market-oriented, sector-selective (MOSS) talks are fulfilled. On March 25, 10 other companies, including General Electric, Ford Motor, and Citibank requested participation in any telecommunications venture authorized to compete with KDD. ITJ supported the inclusion of these new applicants in a merger, but opposed participation by Cable and Wireless Ltd. and other foreign firms capable of providing direct telecommunications services.

Both President Reagan and Prime Minister Margaret Thatcher wrote letters to Prime Minister Nakasone reportedly protesting the merger proposal and urging him to uphold his promise to liberalize Japan's telecommunications market by allowing increased participation of U.S. and British firms. The Japanese then offered a compromise plan under which six Japanese firms, Cable and Wireless Ltd., and Pacific Telesis would be offered equal equity participation in a new consortium. Although the new plan would increase foreign participation in the project to 33 percent, Cable and Wireless would still hold less than the 20-percent-equity share it originally demanded. Currently, merger negotiations have reached a stalemate and it appears that each of the original consortia will apply for a license unless the Japanese firms accept Cable and Wireless' proposal to build a new cable. To complicate matters, AT&T, British Telecom, and 27 other companies have entered into a joint venture with KDD to lay a new trans-Pacific fiber optic cable. KDD claims that an additional cable is necessary because of high traffic volume.

In a related development, on February 26, 1987, Senator John Danforth introduced S. 596, a bill that would require the United States Trade Representative to identify countries that deny U.S. firms reciprocal access to their telecommunications services and equipment markets. Upon completion of the investigation, the President would be required to enter into negotiations with those countries identified and obtain agreements giving U.S. firms competitive opportunities in foreign markets equal to those available to foreign firms in the United States. The President must take retaliatory action if he is unable to reach agreement with any of the designated countries within 18 months. If the United States Trade Representative determines that a country has denied benefits to the United States under any trade agreement, he is authorized to take whatever actions "are necessary to (1) fully offset such acts, policies and practices, and (2) to restore the balance of concessions between the United States and such foreign country." The Senate Finance Committee approved Senator Danforth's proposal as an amendment to the Senate omnibus trade bill (S. 490) on May 7, 1987. ▪

South Korea's New Trade Measures

On April 17, South Korea announced plans to freeze its growing trade surplus with the United States at current levels by discouraging exports to the United States and encouraging its exporters to seek markets elsewhere. The United States absorbed about 40 percent of Korea's exports last year and realized a bilateral deficit of $7 billion, up from $4.5 billion in 1985. Unchecked, the U.S. deficit with Korea could reach $10 billion this year.

Korea's announcement is reportedly an attempt to ease the type of trade frictions that led the United States to impose sanctions on Japan. (It was made on the same day that President Reagan announced retaliatory tariffs on Japanese electronics.) Although specific details of the program have not been released, Korea's proposed package of economic measures is said to also contain incentives to encourage imports.

The package reportedly calls for encouraging imports through increased investment in plants and equipment by South Korean companies and expanded public works spending. The proposals also call for a reduction in the number of products currently on the import-restricted list and for a substantial relaxation of foreign-exchange regulations. To help Korean companies buy more imports, particularly from the United States, the Government will earmark $3 billion in foreign exchange from its current account surplus for special loans. Conversely, Korea hopes to slow export growth by reducing officially supported export financing. Details of all the proposals will be announced soon.

Secretary Baldrige, who visited Korea for trade talks just after the program was announced, said the new package of measures is an important step in U.S.-Korean trade relations, although he added that "the success will lie in the implementation." Secretary Baldrige's visit ended with a number of agreements, including Korean concessions to end import restrictions on semiconductor chips and to lift some barriers to car imports. Korea also agreed to lift local content requirements in certain industries to help U.S. machinery imports. No progress was reported in opening Korea's market to agricultural imports or foreign advertising companies. For its part, the United States pledged not to restrict imports of Korean cars, semiconductors, and machine tools as long as they do not violate existing trade laws. ▪

Taiwan's Bid to Lower U.S. Pressure on Trade

The rapid growth of the U.S. trade deficit with Taiwan—$14 billion in 1986, up from $10 billion in 1985—has seriously strained bilateral trade relations and made Taiwan a prime target of trade legislation moving through Congress. Amid mounting concern in Taiwan about U.S. protectionist leanings, the latest round of talks between the United States and Taiwan ended on April 16 with Taiwan agreeing to significant tariff cuts. Tariffs have long been a source of bilateral conflict, with the United States arguing that Taiwan's high rates effectively exclude many U.S. products.

Taiwan agreed to cut its tariffs of 50 percent or higher on 62 agricultural and industrial products that U.S. negotiators said offer considerable export potential for U.S. farmers and manufacturers. Items receiving the duty reductions include wood and paper products, industrial adhesives, certain household goods, turkey meat, raisins, walnuts, chocolate confectionary, soybeans, sunflower seeds, and sausages. Only four agricultural products, including beef and potatoes, will not receive tariff cuts for fear of damaging domestic farm interests. In addition, on May 1, Taiwan lifted the import ban on fresh peaches, thereby eliminating the island's last nontariff barrier on fresh fruit imports.

In addition to tariff cuts on the 62 items of particular interest to the United States, Taiwan also announced cuts ranging from 20 to 50 percent on 800 other products, including textile products, footwear, umbrellas, and certain luxury items.

Finance Ministry officials say that a further round of cuts on these items will be made final in about 3 months. ■

China's Mounting Foreign Debt

China's outstanding foreign debt is estimated to have nearly tripled between 1983 and 1986—an unprecedented development for a country that until recently had minimal external borrowings. Moreover, International Monetary Fund (IMF) officials are reported to have warned China that its debt structure is irrational (the proportion of short-term obligations is too large) and that its debt management is not well coordinated. In February, Chinese leaders initially responded to the situation by announcing that foreign-exchange expenditures and foreign borrowing will be strictly monitored to ensure that only those projects deemed necessary by the central authorities receive funding. Since then, a freeze was reportedly imposed on imports by State enterprises, but the policy was not extended to imports for projects operated by provincial governments or their affiliates. Nevertheless, this action indicates a further overall tightening of centralized control over China's foreign-exchange expenditures.

Estimates of China's foreign debt vary considerably among various analysts and international organizations. According to unpublished IMF estimates made available through diplomatic sources, China's outstanding debts grew from $9.61 billion in 1983 to $19.88 billion at yearend 1985. An estimate independently made by the World Bank puts the figure for yearend 1985 at $20.6 billion, but both organizations have calculated that China's short-term debt amounted to $9 billion, or nearly one-half the total, at that time. Western bankers and diplomats have estimated that China's borrowing last year increased its gross external debt to within the range of $25 billion to $27 billion by yearend 1986. Wharton Econometric Forecasting Associates has calculated an even higher figure of $28.1 billion.

Most analysts agree, however, that the size of China's foreign debt is not a cause for alarm, given the size of the Chinese economy and the country's potential foreign-exchange-earning capacity. The most serious problem, reportedly voiced by IMF officials, is that China has assumed too many short-term obligations. Reacting to a sharp decline in its foreign-exchange reserves during the final months of 1984 and the first half of 1985, China is believed to have borrowed heavily in the interbank market during the remainder of that year, in an effort to cover its current merchandise-trade deficits that then were averaging more than $1 billion monthly. This practice apparently was continued in 1986, although on a scale much lower than that in 1985. Nonetheless, Wharton estimates that China's short-term debt still amounted to $7.5 billion at yearend 1986.

The abrupt increase in China's external debt was a direct result of the urban industrial reforms that were officially instituted on a comprehensive basis in October 1984. Under this reform program, China's leaders extended more decision-making authority in foreign trade to provincial and city governments and began to decentralize the operation of business enterprises, allowing them to retain for their own use part of the foreign exchange they generated. This resulted in an unprecedented surge in China's imports of durable consumer goods, which were bought mainly from Japan, and in a sharp rise in its imports of industrial machinery and equipment, owing partly to an excessive duplication of purchases. After 3 successive years of large favorable balances, China's merchandise-trade surplus narrowed from $2.0 billion (exports and imports f.o.b.) at the end of 1983 to only $14.0 million at yearend 1984. The problem was compounded by a slowdown in export growth during 1985, when China registered a merchandise-trade deficit of $12.1 billion, according to its customs statistics. This was followed by a $8.7 billion deficit in 1986. China paid for the imbalance in its trade account by drawing down its holdings of foreign-exchange reserves—from an estimated high of $16.7 billion in September 1984 to $10.5 billion at yearend 1986—and by sharply increasing its external borrowing.

How long China's central authorities will maintain tight control over foreign-exchange expenditures will depend on a number of factors. The reduction in last year's deficit was largely the result of higher export revenues that China may not be able to sustain. It is still heavily dependent for export earnings on apparel and other textile products—items that may be subject to more intense protectionism—and on oil and oil products. On the other hand, China will probably find it difficult to restrain import demand, given its requirements for industrialization. Since mid-1985, however, China's depleted foreign-exchange holdings have been sufficient to cover only about one quarter's imports, and official Chinese policy is to not let reserves fall below the level of 3 months of imports. Government leaders are therefore likely to maintain a tight rein on import spending in an effort to limit foreign borrowing until they succeed in rebuilding a debt structure based on more medium- and long-term loans. ■

OECD Ministers Tackle Trade Issues

On May 12 and 13, representatives from the 24-member Organization for Economic Cooperation and Development (OECD) met in Paris for their annual ministerial conference. Highlights of the conference were a commitment made by the ministers to advance reform of agricultural trade and a pledge by West Germany to expand its domestic economy.

On the subject of agricultural trade, the final communique issued by the ministers urged member countries to develop a more rational approach in their domestic agricultural policies. They pledged "a progressive and concerted reduction of agricultural supports" across all commodities and countries. Despite the political difficulty of the task, the ministers declared that the swelling farm production supports, which artificially boost prices and lead to immense agricultural surpluses, must be supplanted by a new system. Specifically, the communique stated that price guarantees or other production support measures should be replaced by direct farm income support. The United States greeted the consensus on agriculture as a significant step forward, one giving political impetus to the Uruguay Round of GATT negotiations currently underway.

The question of how to reform world agricultural trade has been a part of ongoing OECD work for several years. Singling out distortions in agricultural trade as the issue that requires the most immediate attention, an economic report presented by the OECD Secretariat at the ministerial meeting cited the necessity of reversing the erosion of the international trading system as the top priority of member governments. Agricultural support programs, the report noted, are an economic cost and breed tension among trading partners that potentially threatens the open-trading system as a whole. The report stated that there is no economic justification for protecting agricultural trade from market forces. It noted that if social grounds for farm support policies exist, such assistance should be separated from production incentives.

A method developed by the OECD in its recent work on agricultural support programs measures the relative levels of subsidies among member countries. The system uses so-called producer and consumer subsidy equivalents to determine the share of subsidies in the value of each country's agricultural output. For 1985, the OECD determined that 70 percent of the value of output of major agricultural products in Japan represented the subsidy element. The comparable figure for the United States was 20 percent, and for the European Community (EC), 40 percent.

The OECD, which released its report on the subsidy equivalents during the ministerial meeting, found that, during 1979–81, about 30 percent of the sales value of the 11 commodities studied consisted of the subsidy element. The OECD also found that the bulk of the subsidies in member countries are accounted for by Japan, the United States, and the EC. Dairy products and rice top the list of individual commodities subsidized in OECD countries, according to the report, with the subsidy element making up over 60 percent of their sales value. Wool and soybeans, at about 10 percent each, had the lowest subsidy element in the sales values of the commodities studied.

The OECD research concluded that world markets are unable to further absorb the surplus production brought on by the high subsidy levels, which, it pointed out, sharpen trade tensions, increase commodity price fluctuations, hamper economic growth, precipitate retaliatory trade measures, hinder growth in the developing countries, and do not effectively support farm incomes. The OECD concluded that such circumstances, if allowed to continue, could cause "dire consequences." It also warned that "the economic, social, and political consequences of all this could cause the system to collapse and bring in a cycle of gluts and shortages that could not fail to damage the world economy."

In another development at the conference, West Germany made a commitment to expand its economy in June if domestic economic growth falls below a 2-percent annual rate. The United States has long been urging West Germany and Japan to take action to stimulate domestic demand, thereby relying less on export-led growth and helping to cut the U.S. trade deficit. The German commitment was part of an agreement in which Japan repeated its pledge to stimulate its domestic economy and the United States pledged to reduce its budget deficit. ■

Changing Patterns of World Trade in 1986—What Do They Really Show?

There were some historic changes in world trade patterns in 1986 according to preliminary data recently released by the International Monetary Fund (IMF), the General Agreement on Tariffs and Trade (GATT), and the European Community (EC):

- The United States lost its preeminent position as the world's leading exporter, dropping to second place after the Federal Republic of Germany (West Germany).

- The world's leading trading countries reached record trade imbalances: the United States had a record trade deficit, and West Germany and Japan had record trade surpluses.
- The EC registered its first trade surplus ever.
- Manufactured goods replaced primary commodities as the leading source of export revenues for developing countries.

It is important to interpret these statements with the utmost care because the data were reported in dollar terms, and world trade patterns were strongly affected in 1986 by the rapid increase in the dollar price of German and Japanese goods, the continued sharp decline of petroleum prices, and the weakening of non-oil primary commodity prices.

The replacement of the United States by West Germany as the world's leading exporter reflects, to a large extent, the appreciation of the Deutsche Mark vis-a-vis the U.S. dollar. According to IMF data, the dollar value of West German exports increased by 32.3 percent in 1986. Yet when measured in the EC accounting unit (ECU), Germany's exports declined by 10 percent. However, the volume of West Germany's exports remained almost unchanged, declining by only 0.9 percent.

Similarly, Japan's export performance, expressed in dollars, represents mainly the effect of the yen's appreciation. Although Japan's exports increased by 19.0 percent in value in 1986, they decreased by 1.3 percent in volume. U.S. exports hardly changed in 1986, edging up by 2.0 percent in value and by 1.0 percent in volume. This means that the changes in the ranking of these three major exporting countries largely reflect the effects of the year's sharp currency shifts.

Exchange rate changes in 1986 also lowered import prices for both West Germany and Japan in 1986 (measured in their own currencies). By the same token, currency realignments made imports more costly for the United States. Primarily because of changes in terms of trade rather than volume shifts, the U.S. trade deficit and the trade surpluses of Japan and West Germany all set new records.

Measured in ECU's, there was a 17-percent reduction in the EC's imports. This reflected a 23-percent import price reduction and a 7-percent increase in the volume of imports. The large price reduction was largely a reflection of plummeting petroleum prices and the weakening prices of many other primary commodities that were tied to the dollar. Thus, a favorable shift in its terms of trade was primarily responsible for the EC's first trade surplus ever.

Larger 1986 foreign-exchange earnings from manufactures than from primary products could be hailed as the long-awaited result of the developing countries' efforts to diversify and industrialize. Indeed, during 1986, the volume of manufactured exports by developing countries grew at a faster rate than the manufactured exports of advanced industrial countries, which turned in their poorest performance in decades. Yet, the story has another side: the terms of trade shifted sharply during the year in favor of manufactured exports and to the detriment of mineral exports, particularly fuels. This development was anything but favorable for developing countries, some of which suffered from the steep fall of oil prices, and most of which were affected by the decline of other primary commodity prices.

The slide in oil and other commodity prices caused the developing countries' share in overall world exports to decline and, by the same token, raised the share of the advanced industrial countries. Paradoxically, the decline in developing countries' earnings from primary-product exports in 1986 was a major reason manufactured goods were their leading source of export revenues for the first time. ■

Differing U.S. and Canadian Trade Statistics Lead to a Bilateral Resolution

During the years 1984–86, the bilateral merchandise-trade balance between Canada and the United States was US$21.8 billion, US$23.9 billion, and US$25.2 billion, respectively, all in Canada's favor. However, Canadian trade statistics differ from the U.S. figures. Statistics Canada reported that Canada's trade surplus with the United States declined significantly in 1986. This reflects an ongoing discrepancy between U.S. and Canadian measures of bilateral trade flows.

The United States reported that merchandise trade with Canada was off by 2.4 percent in 1986. According to U.S. statistics, the drop in U.S. exports to Canada was 4.5 percent, and U.S. imports from Canada fell by 1.1 percent. Overall trade, the sum of exports and imports, was measured at just over US$111 billion. With the drop in U.S. exports to Canada being four times greater than the decrease in imports, the bilateral trade deficit increased by 5.5 percent from 1985 to 1986.

However, the figures cited have not yet been reconciled with Canada's 1986 trade statistics.

In 1985, the U.S. Department of Commerce preliminary data measured the U.S. merchandise-trade deficit with Canada at US$24 billion. Statistics Canada, on the other hand, measured the the U.S. bilateral deficit at close to US$14 billion. The two countries agreed on a reconciled figure of nearly US$16 billion. The 1986 measures, in U.S. dollars, are $25 billion (U.S. statistics) and $11 billion (Canadian statistics). The discrepancy is serious enough to produce a significant difference in trade results for 1986: U.S. data show exports to Canada declining compared with their value in 1985, but Canadian data indicate a 4.4-percent increase in imports from the United States from 1985 to 1986.

Discrepancies in trade data are a source of ongoing concern between Canada and the United States. One of the main reasons for Canadian concern is that legislation has been introduced in the Congress (and passed by the House) that would require certain corrective actions on the part of countries with whom the United States has a trade deficit. Understandably, an accurate measurement of bilateral trade flows must precede any determination of a trade balance statistic.

The U.S.-Canadian discrepancy problem results from the inaccuracy of U.S. (and, to a lesser extent, Canadian) export statistics and stems mainly from the easing of trucking regulations and the subsequent increase in cross-border trade shipped overland. A number of companies fail to file export documents with U.S. Customs before their goods leave the United States to enter Canada. This has resulted in an underreporting of U.S. exports, and the size of the U.S. bilateral trade deficit is therefore overstated.

Since import statistics are a more detailed and a more accurate measure of trade, their use alone would result in more reliable trade data. For this reason, both countries have agreed to use one another's import statistics as a basis for trade balance calculations by 1990. Between now and 1990, the reconciliation process will take place quarterly rather than once a year. An announcement of the reconciliation results for calendar year 1986 is expected in June. ▪

European Community Publishes List of U.S. Trade Barriers

In early April, the European Community (EC) issued a report listing U.S trade practices that pose obstacles to EC exports. Thirty-three barriers were identified, ranging from tariffs to government procurement policies. In presenting the updated version of a December 1985 report, the EC emphasized that the purpose of the list is to "make clear that trade practices which impede exports are not a unique problem only faced by U.S. exporters. Europeans face similar problems in the United States."

The 26-page document is presented in a format similar to that of the *Report on Foreign Trade Barriers* issued in November 1986 by the United States Trade Representative. Over 30 examples of trade barriers are described, followed by an estimate of the potential amount of EC trade affected by each practice and a description of the actions taken or intended to be taken by the EC. The list is not meant to be inclusive; barriers to trade in services (e.g., cargo preferences) and unjustified or discriminatory phytosanitary measures (sanitation regulations for plants and animals) are excluded. Also, some of the measures cited are not necessarily inconsistent with U.S. international obligations.

The EC is the United States' largest trading partner, accounting for over one-fifth of total U.S. trade in 1986. Last year, the value of two-way trade reached $125.7 billion. Because of the importance of the United States and the EC in the world trading system, Willy De Clercq, EC Commissioner for External Relations, commented in reference to the report that "both parties [therefore] have a joint interest and responsibility for monitoring and furthering the world's free trade system. [The EC is] ready to work with the United States in eliminating trade barriers either through bilateral discussions or within the Uruguay Round of trade negotiations."

The EC has already brought some of its complaints against U.S. practices before the GATT under its dispute settlement provisions. For example, GATT dispute settlement panels have been instituted to determine whether or not new customs user fees and taxes on chemical derivatives and petroleum products imposed by the United States last year conform with GATT rules. The U.S. customs user fee, introduced on December 1, 1986, requires that a tax of 0.22 percent ad valorem be applied to imports to cover the cost of processing the merchandise through U.S. Customs. On the basis of its 1985 exports to the United States, the EC estimates the processing fee will cost the EC about $175.5 million in 1987. The EC also alleges that the U.S. Superfund, established to finance the clean-up of toxic waste sites, discriminates against imported products. According to EC officials, the Superfund taxes imported petroleum and chemicals at a higher rate than similar domestic products, which could cost the EC an estimated $39.8 million annually.

The EC intends to discuss other trade barriers at the Uruguay Round of trade negotiations. Such issues include tariffs, the Export Enhancement Program that subsidizes U.S. agricultural exports, and import quotas on a variety of agricultural goods, including dairy products, sugar, peanuts, and cotton. With regard to this last restriction, the EC alleges that U.S. import quotas on certain farm products, established under section 22 of the Agricultural Adjustment Act of 1933, are unjustified. Although these section 22 quotas are covered by a GATT waiver, the EC points out that the waiver was granted over 30 years ago.

Certain major provisions of U.S. trade legislation are also the subject of EC concern. Among the provisions cited are section 337 of the Trade Act of 1930, which covers intellectual property rights; U.S. legislation and practice on countervailing and antidumping duties; and section 301 of the Trade Act of 1974, which grants the United States unilateral authority to redress unfair trade practices. Other U.S. trade restrictions identified in the report include standards, testing, labeling, and certification rules; public procurement policies; export subsidies; export controls and restrictions on technology transfer; tax policies; customs practices such as rules of origin; and the U.S.-Japanese semiconductor agreement. ■

STATISTICAL TABLES

Industrial production

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

Country	1984	1985	1986	1985 IV	1986 I	II	III	IV	1986 Nov.	Dec.	1987 Jan.	Feb.	Mar.	Apr.
United States	11.2	2.0	1.0	1.9	1.2	-2.1	1.9	3.3	6.9	6.2	-1.9	5.8	-2.4	-4.9
Canada	8.8	4.3	–	6.1	-.9	–	–	–	–	–	–	–		
Japan	11.1	4.6	-0.3	-2.9	.7	.9	-2.1	-2.4	-21.0	-19.0	-5.7	4.0		
West Germany	3.3	3.9	2.2	.8	-.1	10.2	-4.5	-.1	9.6	–	-30.2	–		
United Kingdom	1.3	4.7	1.8	.7	2.7	0.6	5.6	.5	2.2	-7.4	3.3	21.3		
France	1.7	.8	.7	.0	-5.8	6.2	5.4	-5.1	9.2	-23.3	-21.3	43.1		
Italy	3.3	1.2	2.7	-1.8	13.5	6.0	-12.8	7.3	-1.2	-20.5	25.7	-5.8		

Source: *Economic and Energy Indicators*, U.S. Central Intelligence Agency, May 8, 1987.

Consumer prices

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

Country	1984	1985	1986	1986 I	II	III	IV	1987 I	1986 Oct.	Nov.	Dec.	1987 Jan.	Feb.	Mar.
United States	4.3	3.6	1.9	1.4	-1.7	2.6	2.8	6.6	1.8	3.3	2.4	8.3	5.2	6.2
Canada	4.3	4.0	4.2	4.7	3.0	4.7	4.9	3.5	6.3	5.0	3.7	2.0	3.1	5.6
Japan	2.3	2.0	.6	.4	.9	-2.0	-.1	.1	1.2	-5.8	-2.4	-4.7	0	4.9
West Germany	2.4	2.2	-.2	-1.0	-1.0	-.5	-1.5	1.0	-4.9	-1.4	1.4	1.6	.9	.6
United Kingdom	5.0	6.1	3.4	4.0	.7	2.4	6.5	3.9	3.0	11.4	8.9	6.7	3.4	1.6
France	7.7	5.8	2.5	1.0	1.7	2.6	3.2	4.5	2.0	3.0	5.2	9.8	3.0	.6
Italy	10.6	8.6	6.1	5.9	5.0	5.0	3.2	4.0	1.9	3.4	4.3	5.0	2.2	4.7

Source: *Economic and Energy Indicators*, U.S. Central Intelligence Agency, May 8, 1987.

Unemployment rates

(Percentage; seasonally adjusted; rate of foreign countries adjusted to be roughly comparable with U.S. rate)

Country	1984	1985	1986	1986 I	II	III	IV	1987 I	1986 Nov.	Dec.	1987 Jan.	Feb.	Mar.	Apr.
United States	7.5	7.2	7.0	7.1	7.1	6.9	6.9	6.7	6.9	6.7	6.7	6.7	6.6	6.3
Canada	11.3	10.5	9.6	9.7	9.6	9.7	9.4	9.6	9.4	9.4	9.7	9.6	9.6	
Japan	2.8	2.6	2.8	2.7	2.8	2.9	2.9	–	2.8	3.0	3.0	2.9	–	
West Germany	7.8	7.9	7.6	7.8	7.7	7.5	7.4	7.4	7.3	7.3	7.4	7.4	7.6	
United Kingdom	11.7	11.3	11.5	11.5	11.7	11.6	11.3	11.1	11.3	11.2	11.2	11.1	11.0	
France	9.9	10.4	10.7	10.4	10.6	10.8	10.8	11.2	10.6	10.7	11.1	11.2	11.3	
Italy	5.9	6.0	6.2	6.1	6.1	6.0	6.6	–	–	–	–	–	–	

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, May 1987.

Trade balances

(Billions of U.S. dollars, f.o.b. basis)

Country	1984	1985	1986	1985 IV	1986 I	1986 II	1986 III	1986 IV	1986 Oct.	1986 Nov.	1986 Dec.	1987 Jan.	1987 Feb.	1987 Mar.
United States[1]	-107.6	-133.5	-153.4	-147.2	-154.4	-139.6	-155.6	-166.8	-130.8	-206.4	-150.0	-108.0	-171.6	-145.2
Canada	16.0	12.8	7.3	11.6	6.8	7.6	6.4	8.0	7.2		8.4	6.0	10.8	
Japan	43.9	55.8	92.5	67.6	71.6	89.6	104.8	104.0	98.4	115.2	104.4	116.4	115.2	
West Germany	18.8	25.4	52.6	29.6	41.2	51.6	60.4	57.2	46.8	57.6	64.8	57.6	74.4	
United Kingdom	-5.7	-2.6	-12.1	-1.2	-8.4	-9.6	-17.2	-14.8	-14.4	-18.0	-13.2	-9.6	-3.6	
France	-2.8	-2.6	-.1	-1.6	.4	-4.4	0	1.6	.0	-1.2	7.2	-4.8	-1.2	
Italy	-11.0	-12.1	-2.1	-14.4	-10.8	.0	1.6	-.8	-6.0	2.4	3.6	-3.6	-9.6	

[1] Exports, f.a.s. value, unadjusted; imports, customs value, unadjusted.

Note.—Beginning with January 1986, the U.S. Department of Commerce stopped reporting export and import data on a seasonally adjusted basis. U.S. data for prior periods have been changed accordingly. This does not affect the comparability of U.S. and foreign trade balances on an annual basis.

Source: *Economic and Energy Indicators*, U.S. Central Intelligence Agency, May 8, 1987.

U.S. trade balance, by major commodity categories and by selected countries

(Billions of U.S. dollars, customs value basis for imports)

Item	1984	1985	1986	1986 I	1986 II	1986 III	1986 IV	1987 I	1986 Oct.	1986 Nov.	1986 Dec.	1987 Jan.	1987 Feb.	1987 Mar.
Commodity categories:														
Agriculture	18.4	9.6	4.5	1.7	.0	.5	2.3	1.4	.8	.6	.9	.6	.4	.4
Petroleum and selected products, unadj	-52.5	-45.9	-31.8	-10.6	-7.2	-7.2	-6.8	-7.6	-2.2	-2.5	-2.1	-2.1	-2.8	-2.7
Manufactured goods	-78.9	-102.0	-134.3	-31.1	-32.4	-36.1	-34.7	-32.7	-10.2	-15.6	-8.9	-10.3	-11.7	-10.7
Selected countries:														
Western Europe	-14.1	-23.3	-28.2	-6.6	-8.0	-7.3	-6.3	-5.2	-1.0	-3.4	-1.9	-1.5	-1.6	-2.1
Canada	-20.1	-21.7	-23.0	-5.9	-5.8	-5.9	-5.4	-4.9	-1.5	-2.8	-1.1	-1.6	-1.9	-1.4
Japan	-33.8	-46.5	-55.3	-14.3	-12.5	-13.5	-15.0	-13.6	-4.7	-6.4	-3.6	-4.1	-4.8	-4.7
OPEC, unadj	-12.3	-10.2	-8.9	-3.5	-1.5	-2.1	-1.8	-2.4	-.6	-.7	-.5	-.6	-1.1	-.7
Unit value (per barrel) of U.S. imports of petroleum and selected products, unadj	$28.11	$26.59	$15.02	$22.70	$13.40	$11.41	$12.60	$15.55	$12.28	$12.57	$12.94	$14.36	$16.07	$16.23

Note.—Beginning with January 1986, the U.S. Department of Commerce stopped reporting export and import data on a seasonally adjusted basis. U.S. data for prior periods have been changed accordingly. This does not affect the comparability of U.S. and foreign trade balances on an annual basis.

Source: *Summary of U.S. Export and Import Merchandise Trade*, U.S. Department of Commerce, March 1987.

Money-market interest rates (90-day certificate of deposit)

(Percentage, annual rates)

Country	1984	1985	1986	1986 I	II	III	IV	1987 I	1986 Nov.	Dec.	1987 Jan.	Feb.	Mar.	Apr.
United States	10.7	8.3	6.5	7.6	6.5	6.0	5.8	6.1	5.7	6.0	5.9	6.1	6.2	6.5
Canada	11.3	9.7	8.6	11.1	8.9	6.1	8.3	7.4	8.4	8.1	7.6	7.5	7.1	
Japan	6.7	6.5	4.9	6.0	4.7	4.7	4.4	4.1	4.4	4.3	4.2	4.0	4.0	
West Germany	6.0	5.5	4.6	4.5	4.6	4.5	4.7	3.9	4.7	4.8	3.9	3.9	3.9	
United Kingdom	9.9	12.1	10.8	11.9	10.1	9.9	11.3	10.5	11.4	11.4	11.1	10.2	10.1	
France	11.7	10.0	7.7	8.7	7.4	7.2	7.6	8.2	7.5	7.9	8.5	8.3	7.9	
Italy	15.9	15.0	12.8	15.5	12.9	11.4	11.2	10.9	11.1	11.6	11.4	11.1	10.1	

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; percentage change from previous period)

Item	1984	1985	1986	1986 I	II	III	IV	1987 I	1986 Nov.	Dec.	1987 Jan.	Feb.	Mar.	Apr.
Unadjusted:														
Index number	122.4	127.1	106.0	117.8	106.7	102.8	102.7	97.1	103.5	102.5	98.5	96.9	96.0	89.9
Percentage change	7.2	3.8	-16.6	.4	-9.4	-3.7	-.1	-5.5	1.4	-1.0	-3.9	-1.6	-0.9	-6.4
Adjusted:														
Index number	119.6	122.5	101.6	106.3	99.1	96.9	98.3	93.4	99.1	98.0	94.5	93.3	92.5	93.9
Percentage change	6.1	2.4	-17.1	-5.1	-6.8	-2.2	1.4	-5.0	1.4	-1.0	-3.7	-1.3	-1.0	1.5

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 United States 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 Co. of New York.

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