

problems to weaken the political consensus on which the liberal trading system stands.

The greatest immediate threat to the trading system is the U.S. balance-of-payments problem. Our persistent deficit has not only led to direct controls on capital exports. It has also brought forth proposals for import controls and breathed new life into U.S. protectionism.

But the threats to the liberal trading system are not confined to one country. They are global and many-sided. Agricultural protectionism and the persistence of controls on capital movements by the Common Market countries, for example, thwart the adjustment of our balance of payments. Trade and exchange barriers abroad have added to our deficits and encouraged us to adopt further controls.

The Trade Hearings

The House Ways and Means Committee hearings, which began June 4, will bring all the hardest questions of U.S. trade policy to a head. The first item on the Committee's agenda is the Administration's bill to implement those provisions of the Kennedy Round agreements which require new legislation, including the difficult question of eliminating the American-Selling-Price (ASP) method of tariff valuation, which results in unusually high duties for certain synthetic organic chemicals.

The Committee will also hear testimony on import quota bills, of which the most important are for steel and textiles. A textile quota bill passed the Senate in April as an amendment to the tax bill, but was later eliminated in the conference committee. Nontariff barriers, most importantly European border tax adjustments, are another complex issue likely to be raised.

The atmosphere of the hearings will be colored by the deteriorating U.S. trade balance. The normal, large commercial trade surplus has disappeared. This alarming development is in part the result of special factors—the copper and dock strikes and the anticipated steel strike. But the main cause is the pressure of excess demand in an economy where spending has been growing nearly twice as fast as real output.

The weakened trade balance lends indirect support to protectionist proposals. It also increases the support in the Administration and Congress for a temporary surcharge on imports generally.

The issues before the Committee are affected by a recent proposal put forward by Eric Wyndham White, Director General of the General Agreement on Tariffs and Trade (GATT), on behalf of a group of industrial countries. The proposal is that the Western European nations,

Canada, and Japan accelerate their Kennedy Round tariff cuts by one year, while allowing the United States to delay its own cuts by one year. However, the offer is made on the "hypotheses" that the United States eliminates ASP this year and adopts no new protectionist measures.

Although made in response to a U.S. request for help with its trade balance, this offer is not likely to be very helpful to the Administration. The effect on the U.S. trade balance would be small, while the conditions attached to the offer have irked some members of Congress.

Residual Protectionism

In the United States as in other industrial countries, protectionist sentiment is always present, because there are major industries subject to serious competition from imports. In the United States, these are for the most part older industries, where the U.S. advantage over foreign competitors in labor productivity is not large enough to offset higher labor costs. Textiles, clothing and steel are the most important industries in this category, and they are in the forefront of those now seeking more protection from imports by quotas.

These U.S. industries appear to be at the lower end of the scale of comparative advantage (see accompanying chart) mainly because of higher labor costs. Relative to their foreign competitors, these industries do not benefit to the same extent as other U.S. industries from the large size of the U.S. domestic market. They produce largely staple products, for which domestic demand in many other countries is sufficient to permit operation by local producers on an economical scale. And these industries have not been characterized by the rapid technological advance, based on large-scale research and development, which so largely explains the comparative advantage of the U.S. aircraft, machinery and chemical industries.

The automobile industry also appears to suffer competitive disadvantages. But this may have more to do with foreign nontariff barriers than with cost factors, although the U.S. industry apparently is unable to produce small cars as cheaply as its major foreign competitors. U.S. automobile exports are handicapped by excise and "road" taxes in Europe, Japan and other countries which discriminate against larger cars.

The residual strength of protectionism in the industrial countries is evident in the somewhat selective pattern of postwar trade liberalization. For example, many Japanese manufactured products are still subject to quantitative import restrictions (in Europe) and to "voluntary" restrictions on Japanese exports (to the United States). Japan's lower labor costs constitute a serious