tighten restrictions still further without damage to the balance of payments as well as to the competitive position of American companies abroad. As this program is particularly inimical to the best interests of the United States, we wish to limit the remainder of this submission to an analysis of its effectiveness and discussion of alternative measures to improve the balance of payments.

DIRECT INVESTMENTS AND THE BALANCE OF PAYMENTS

Much misunderstanding has developed in recent years regarding the effect of overseas direct investments on the balance of payments. While analysis of this problem is admittedly complex, a review of the record and the nature of direct investments will, we believe, generally support the conclusion that such investments are beneficial and tend to strengthen our international payments position.

Besides the original capital outflow, the balance-of-payments effects of direct investments involve evaluation of many factors, of which the following are of major importance:

(1) Direct foreign investments tend to develop new markets for U.S. exports of capital equipment. For example, American enterprises overseas have been in the forefront in adopting new methods of production, which have stimulated demand for U.S. exports embodying a high degree of modern technology. Affiliates of American oil companies alone purchased almost $350 million worth of capital goods from U.S. suppliers in 1964, equal to over 46% of the capital for foreign petroleum investment in that year (over-all industry and later data not available). Furthermore, in most cases, there is no alternative but to invest abroad because of foreign tariffs and other quantitative barriers to international trade. Thus, direct investments overseas do not, as often alleged, displace American exports, which would have been lost in any case.

(2) The biggest benefit to the balance of payments comes from the dividends, profits and royalties remitted to the United States from American companies' direct investments overseas. Current remittances, of course, represent the yield from past investments, but, as discussed further below, the period between the capital outflow and the return flow to the United States of sufficient funds to pay back the original investment in balance-of-payments' terms is relatively short.

The return flow to the United States (including fees and royalties) of all direct investments overseas has consistently risen every year except two during the postwar period. In 1966 it totaled about $5.1 billion, over two times the level of ten years earlier, and has remained at this high annual rate during the first nine months of 1967. This increasing contribution to the balance of payments could not have been possible except for the continuing investments made abroad by American companies.

The benefit to the balance of payments of the first factor discussed above is difficult to quantify because of lack of reliable and recent data. But as it is a plus factor, the dividend and royalty return flow for which data are regularly compiled by the Department of Commerce should be considered as the minimum gross benefit of direct investments to the U.S. balance of payments.

As an offset to this gross benefit, account must be taken of the capital transfers from the United States for direct investments overseas. These transfers, however, have risen far less than the increase in the return flow of dividends and royalties to the United States. Over the last ten years, for example, capital outflow increased by approximately 50% to about $3.1 billion in 1966 (excluding $445 million of funds borrowed abroad by American companies). The return flow of dividends and royalties, however, doubled over this period so that the net contribution of foreign direct investments to the balance of payments rose from $450 million in 1956 to about $2 billion in 1966. In the first nine months of 1967, this net benefit had increased to $2.8 billion at an annual rate. The foreign operations of the American oil industry accounted for almost half of the net contribution of overseas direct investments to the balance of payments in 1966, the latest period for which such industry data are available.

The increasing contribution of direct overseas investments to the balance of payments has repeatedly been acknowledged by the Johnson Administration. But in imposing mandatory restrictions, the Government contends that the savings now required in foreign investment outlays are beyond the reach of a voluntary program. Furthermore, it believes that restriction of future investments for a short period will benefit the balance of payments without materially affecting the present increasing return flows of dividends and royalties, which are the result of investments made in the past. The Government, in effect, justifies its case for mandatory restrictions on grounds of short-term expediency.