

of business activity similar to the effects of many taxes and expenditures included in the operating budget. A better picture of the total effect of Federal finance is, therefore, obtained from the more comprehensive budget. This, of course, implies nothing about the wisdom of balancing the unified budget by running a deficit in the operating budget offset by a surplus in the trust funds.

*Question 2. Reference page 36, last paragraph. Is it not true that, although over the last few years the rate of inflation in major competitor countries has been higher, the rate of inflation in the United States (applied to a higher wage base which has increased at least in an amount to reflect inflation) has diminished our competitive position in world trade?*

Answer. Since 1965, our price level has risen more rapidly than in most industrial countries, and our competitive position has tended to deteriorate. Prior to 1964, our inflation was less rapid than in the industrial countries, and this tended to improve our competitive position.

Our high absolute wage rate does not in itself mean that wage increases will necessarily involve a decline in our competitive position. Even though our wages are higher than in other countries, an equivalent percentage increase in U.S. and foreign wages will not in itself cause a deterioration in the U.S. competitive position, provided that the rate of increase in productivity in the U.S. is as great as the increase abroad. Should the relationship between wage and productivity increases in the U.S. diverge from the relationships in foreign countries, there would be some tendency for price movements to differ among countries, with a consequent change in competitive relationships.

Competitive positions are, of course, affected by costs other than wages, and, at any rate, general price indexes do not give a very precise indication of changes in competitive positions. At this level of generality, however, it is true to say that changes in competitive positions occur, not because of the absolute level of wages as such, but because of changes in relative prices, behind which may be international differences in the percentage rise in wages, or in the percentage improvement in productivity, or both.

*Question 3. Reference page 40, line 14. Would retaliation on our part against the EEC's recent proposal to tax our soybeans be regarded as "prejudicial" to such negotiations so that the Council would oppose such retaliation?*

Answer. Any step which adds to the barriers to international trade, whether in the form of tariffs, quotas, or other nontariff barriers, raises the potential problem of retreat from the policy of trade liberalization which has been pursued by administrations of both political parties in recent decades. The danger exists whether the trade restriction is initiated with the objective of protecting a domestic industry, or whether it constitutes retaliation against objectionable foreign practices.

At the same time, a measured retaliation to foreign actions prejudicial to our exports may persuade foreign countries to modify these actions. Thus retaliation may, under certain circumstances, be instrumental in protecting our access to foreign markets, and contribute to the overall freedom of international trade. However, retaliation should not be undertaken lightly. It is most desirable, by international discussions and negotiations aimed at achieving mutually acceptable solutions, to avoid retaliation.

A number of European agricultural policies, both actual and proposed, involve obstacles to U.S. exports. This is conspicuously true of the proposed soybean tax. We consider it a matter of grave importance that the EEC, in their farm programs, make provision for U.S. agricultural exports.