For Release on Delivery
Friday, April 19, 1968
10:00 A.M., C.S.T.
11:00 A.M., E.S.T.

FOREIGN TRAVEL AND THE UNITED STATES BALANCE OF PAYMENTS

A Convocation Address
By

Andrew F. Brimmer
Member
Board of Governors of the
Federal Reserve System

Upon Acceptance of the

Honorary Degree of Doctor of Laws

Awarded by

Nebraska Wesleyan University
Lincoln, Nebraska

April 19, 1968

FOREIGN TRAVEL AND THE UNITED STATES BALANCE OF PAYMENTS

On any agenda of national economic policy issues, the U. S. balance of payments deficit would rank close to the top of the list. In fact, the longevity of the deficit -- and the paucity of results yielded by an array of corrective measures -- may have led a significant number of people to believe that we simply cannot cope with the problem. Moreover, the technical nature of the questions involved may easily convince the typical citizen that the whole arcane business has nothing to do with him. Besides, still others may argue, there are far more pressing (and exciting) national issues confronting us: the war in Vietnam, the decay and disorders in our cities, the quest of equal opportunity and racial equality, crime in the streets -- and a host of other competitors for the nation's attention and resources. I, too, would certainly assign to all of these intractable problems an extremely high priority for national action. But, as a central banker, I am also deeply conscious of the severity of the challenge to our system posed by the large and persistent deficit in our balance of payments. I think we can (because I think we must) get on with the task of reducing this deficit and rebuilding the international position of the dollar.

In these remarks, I do not propose to recount the detailed history of our payments imbalance nor catalogue all of the policies adopted over the years to cope with it. Instead, I wish to focus on one aspect of the problem where the possibility of progress rests directly with each individual citizen: that is the contribution to the deficit made by the rapidly rising expenditures of Americans traveling abroad. This is a major category (merchandise imports is another) in which the adverse impact on the balance of payments has worsened steadily -- despite the vigorous efforts aimed at overall improvement during the last few years. Moreover, it is also an area in which the real objections of public policy are frequently obscured by arguments about the basic right to travel -- or unfortunately -- by still other criticisms which seem to be designed more to safeguard the special position of particular industries or constituencies than to widen public understanding of the sizable contribution made by travel expenditures to our balance of payments deficit.

Let me hasten to add that, having served as a member of the President's Industry-Government Special Task Force on Travel (whose principal assignment was to devise means of promoting increased travel to this country), I am acutely aware of the long-run disadvantages to both Americans and to our foreign visitors of relying primarily on restrictive measures to reduce the travel deficit. On the other hand, I am also convinced that the seriousness of our balance of payments difficulties does necessitate noticaable moderation in the pace of spending abroad by American travelers.

The main points of my comments can be summarized briefly:

- The optimism generated by the President's New Year's Day message on the balance of payments is rapidly

- losing its glow. While the statistical evidence is not yet available, modifications in the original program and Congressional delay in adopting some of the key measures recommended all suggest that we may fall considerably short of the improvement of at least $3 billion targeted for 1968 -- unless we make a much more vigorous effort to press on with the task.

- In particular, there is likely to be a short-fall in the expected improvement of $500 million through the moderation of foreign travel expenditures -- in view of the indifferent Congressional response to the Administration's tax proposals affecting travel outside the Western Hemisphere.

- The promising new programs being developed in the private sector to stimulate the flow of foreign visitors to this country will undoubtedly be helpful. However, this approach alone seems unlikely to yield an increase in foreign receipts large enough to narrow significantly our widening travel deficit.

- Moreover, given the strong cultural, recreational and educational incentives for Americans to travel abroad -- plus their relatively high and steadily rising personal incomes which enable them to satisfy their desires -- the long-run outlook is for much more, not less, foreign travel by U. S. citizens. In fact, our travel expenditures abroad are growing much more rapidly than either our personal income or domestic consumer spending for all services. If foreign travel in 1967 had accounted for the same share of total consumer outlays for services as it did in 1961, our travel deficit last year would have been smaller by some $200 million -- or by roughly 10 per cent.

- Thus, our objective should be to find means to moderate the pace of consumer spending abroad -- and not foreign travel by Americans as such. We should keep in mind a significant fact: As far back as we can go in our balance of payments statistics, we have had a travel deficit. It would be unreasonable to expect it to disappear or change to a surplus at any time in the foreseeable future. On the other hand, it would also be unreasonable to be complacent about the travel deficit becoming larger year-by-year.

Main Trends in the U. S. Balance of Payments

Although the main contours of our balance of payments have been sketched many times before, a brief summary here would serve as a background for the subsequent discussion of our travel deficit. Since late 1957 -- or for more than a decade -- we have run a sizable deficit in our international payments. But 1964 marked a real watershed in our efforts to find a solution to the problem. In that year, the balance of payments deficit (on the liquidity basis) was $2.8 billion. While this was only a modest rise in the total deficit compared with the previous year, there was a conjuncture of several underlying adverse trends which made it necessary to adopt a basically new approach to the deficit in early 1965.

During the years 1960 to 1964, (partly reflecting general price stability at home while prices abroad were rising) there was a substantial expansion in our current account. This resulted in a surplus on goods and services of $8.5 billion in the latter year, while the trade surplus alone amounted to nearly $7 billion. However, the favorable contributions from the balance on goods and services from 1960 to 1964 were erased by a rising trend of capital outflows. While this was dampened somewhat by the Interest Equalization-Tax after mid-1963, we still had a total capital outflow of $6.5 billion in 1964. In that year, net bank lending abroad amounted to $2.5 billion, or more than twice the peak reached in 1960-61. Direct investment outflows (especially to continental Western Europe) rose rapidly and also totaled $2-1/2 billion in 1964.

Against this background, the Administration adopted a number of new measures -- and strengthened existing ones -- to reduce the balance of payments deficit. The principal new action was the launching of two voluntary programs to moderate bank lending abroad and direct foreign investment by industrial corporations.

These programs did enable us to achieve considerable improvement on our overall deficit, which shrank to $1.3 billion and $1.4 billion in 1965 and 1966, respectively. The principal gain centered in the decline of private capital outflow to the neighborhood of $4 billion in those two years. At the same time, however, we were losing ground in another area: Our trade surplus shrank drastically from nearly $7 billion in 1964 to $3.5 billion in 1967. The reason was a much faster rise in imports than in exports, reflecting primarily growing domestic inflationary pressures. For example, between 1964 and 1967, imports rose at an annual rate of 15 per cent while the corresponding rise for exports was less than 7 per cent. In addition, we began to lose ground again on private capital account. By 1967, the total outflow had climbed to nearly $5.5 billion, including $3.0 billion of direct investment, $1.3 billion of foreign securities purchases, and $0.5 billion of net bank lending. Our trade surplus also declined substantially further. The general result was a balance of payments deficit on the liquidity basis of $3.6 billion for the year as a whole. Again, vigorous measures had to be taken, and the outcome was the President's New Year's Day program.

Outlook for the U. S. Balance of Payments

As mentioned above, the President's New Year's Day program visualized an improvement of roughly $3 billion in the balance of payments during 1968. These gains were expected to be achieved in several key areas:

- A saving of $1 billion through direct investment outflow.
- A net inflow of $.5 billion through reduced foreign lending by banks and other financial institutions.
- A gain of $.5 billion on the trade account.
- A reduction of $.5 billion in the travel deficit.
- A saving of $.5 billion in foreign outlays by the Federal Government.

What is the outlook for the achievement of these goals? As of today, the chances are far less promising than they seemed a few months ago.

With respect to direct investment, very little can be said on the basis of quantitative evidence actually in hand. The March decision of the Administration to exempt Canada from the program may well produce a larger direct investment outflow to that country than otherwise would have occurred. Canada received $1,087 million in direct investment from the United States in 1966 and $383 million in 1967. These amounts represented just under one-third of the total outflow of this type of capital in 1966 and one-eighth last year.

The sharp drop in 1967 reflected the completion of very large investments in the automotive industry pursuant to the U. S.-Canadian automotive agreement of 1965. While we have no firm estimate of the outflow in 1968, U. S. subsidiaries in Canada have shown a tendency to increase their plant and equipment expenditures in recent years and may continue to do so. In the past (at least until the advent of the voluntary programs), the growth of such outlays usually had been associated with increased capital outflow from this country.

For other areas it appears that a number of company-by-company rulings have been given under the mandatory regulations of the Commerce Department the result of which is also a net reduction in the amount of savings. Other modifications in the general regulations since the program was announced point in the same direction. Thus, the overall prospect is for a short fall with respect to the projected $1 billion savings in direct investment -- although there is no way to estimate its magnitude.

In contrast, the expected net inflow of $.5 billion through reduced foreign lending by banks and other financial institutions seems fairly assured. As mentioned above, there was a net outflow of $455 million in bank funds last year, following net inflows in 1965 and 1966. Thus, the expected turn-around in lending abroad may amount to nearly $1 billion. During the first two months of this year, there was a net inflow of about $290 million under the bank program administered by the Federal Reserve Board. Further inflows can be counted on because of the lower ceiling on foreign lending, as banks' term loans in Continental Western Europe are repaid, and as they reduce their liquid assets held abroad. The exemption of Canada from the balance of payments program may result in somewhat smaller improvements on the part of nonbank financial institutions, but this adverse impact is not expected to be very large.

Progress in improving the trade account seems to be particularly disappointing. According to the preliminary estimates of the Department of Commerce, our trade surplus in the first quarter of this year amounted to $1.6 billion, and the surplus on goods and services was about $2.6 billion, both at a seasonally adjusted annual rate. The trade surplus rose somewhat from the extremely low annual rate of $1 billion registered in the final quarter of last year, the smallest trade surplus since 1959. For goods and services combined, the surplus shrank further from the annual rate of $3 billion recorded in the previous three months. In the first quarter of 1967, the trade surplus was at an annual rate of $4 billion. Imports of goods in the first three months of this year were at an annual rate of $30.8 billion, or about 7 per per cent above the fourth quarter and 16 per cent higher than in the first quarter of last year. Imports of steel and refined copper (the two commodities principally affected by domestic strikes or strike threats) accounted for a sizable share of the rise in imports. Exports in the first quarter were at an annual rate of $32.4 billion, about 9 per cent larger than in the fourth quarter and 6 per cent above the rate in the corresponding quarter of last year.

Despite the modest recovery of the trade surplus in the early months of this year, it will be a steep up-hill effort to attain the improvement visualized in the President's message. This task will be made even more difficult by the failure (so far) of Congress to enact the President's proposed 10 per cent surtax on corporate and personal incomes. Adoption of the proposal would help appreciably in the dampening of domestic inflationary pressures and hence of the sharp rise in imports. Moreover, Congress has not approved two other recommendations designed to stimulate exports--the creation of a special $.5 billion export financing fund at the Export-Import Bank and the appropriation of $2.5 million for the Commerce Department to help support joint-export associations among U. S. companies. In the light of these adverse developments, the outlook for the trade account seems not to be very bright, even though the export advance is now beginning to be stimulated by a vigorous business expansion in Europe.

So far, little can be said about success of the efforts to reduce foreign spending by Federal Government agencies. A number of steps have been taken by civilian agencies which will yield some savings. Unfortunately, these may be substantially offset by the further deterioration attributable to the military account. In 1967, the net contribution of the Vietnam War to our balance of payments deficit was in the neighborhood of $1.5 billion, having risen from $1 billion in 1966 and about $.8 billion in 1965. While no new estimate is available, it seems virtually certain that the current rate is greater than $1.5 billion--given the further acceleration in military activity in Vietnam through the end of March and the announced rise of $2.5 billion in military spending above the budget estimate for the 1968 fiscal year ending next June 30.

As mentioned above, the outlook for the travel deficit is of particular concern to me, and to it I shall devote the remainder of my remarks.

Foreign Travel and the Balance of Payments Deficit

Travel expenditures by U. S. residents abroad in 1967 are estimated to have increased by $500 million compared to the 1966 increase of $200 million. At the same time foreign visitors in the U. S. spent about $65 million more in 1967 than in 1966. As a result the net U. S. travel deficit in 1967 was about $2.1 billion compared to $1.6 billion in 1966. EXPO '67 adversely affected net U. S. travel by about $400 million as U. S. expenditures in Canada increased, and Canadian expenditures in the U. S. decreased.

Since 1961 U. S. travel expenditures in Europe and the Mediterranean have increased by over 50 per cent; foreign travelers from Europe and the Mediterranean, on the other hand, increased their expenditures in the United States by nearly 140 per cent. The net effect of these expenditures has been a travel deficit for the U. S. with this area of $525 in 1961 which jumped to nearly $650 in 1963, but which increased by only a further $50 million by 1966.

Until 1967, the U. S. travel deficit with Mexico was the next largest, averaging about $150 million each year since 1961. In 1967 the U. S. travel deficit with Canada was about $500; for the previous three years it had averaged $100 million.

With the passing of EXPO, one would normally expect a slackening in the pace of spending in Canada by U. S. residents. However, the location of the Olympic Games in Mexico will undoubtedly result in increased travel by Americans to that country. Yet, the rise in our travel expenditures will probably be substantially less than that recorded in 1967 because of EXPO.

Economics of Foreign Travel

The ratio of U. S. travel expenditures abroad to total domestic consumer expenditures for all services increased from about 1.7 per cent in 1961 to about 1.8 per cent in 1967, exlusive of expenditures attributable to EXPO. At current levels of consumer expenditures on services, this change represents an increase of about $200 million more in outlays abroad than would be true if the 1961 ratio had been maintained.

This tendency for foreign travel expenditures to rise faster than personal income or consumer spending is evident in a number of foreign countries as well as in the United States. The statistics for Americans, showing U. S. foreign travel expenditures as a percentage of disposable personal income, are summarized in Table 1, attached; comparable data for selected foreign countries are shown in Table 2. This last table indicates that in 1965 all foreign countries surveyed (with the exceptions of Japan and Australia) foreign travel accounts for a larger percentage of disposable personal income than in the United States. In most cases, the percentage increased between 1960 and 1965 by more than it did in the United States. While some of the OECD countries still have restrictions on foreign travel, these apparently were not particularly meaningful, at least in 1965, since the percentages in all these countries rose along with the ratios in countries without such restrictions. Since 1965, however, the United Kingdom has imposed new currency restrictions affecting foreign travel which are quite severe.

For our own country, we can get an even better insight into the pattern of demand for foreign travel. This is derived from a review of the comparative percentage rates of growth of passport applications, population and personal income, by geographic areas, during the period 1960 to 1967. (Growth rates are annual average rates of change.)

Area	Passport Applications (1960-67)	Population (1960-67)	Personal Income (1960-66)
U. S.	10.2	1.4	6.5
Northeast	8.5	1.1	7.4
North Central	11.6	0.9	6.3
Nebraska	11.5	0.2	5.8
Pacific	10.3	2.5	7.0
South Atlantic	13.1	1.8	7.7
South Central	12.2	1.4	7.0
Mountain	8.7	1.9	6.1

Using passport applications as a proxy for the demand for foreign travel, it is clear that the growth of such demand has far outstripped both population and personal income in every area of the country. In the North Central region, where both income and population growth lagged that in the nation at large, passport application's climbed more rapidly than in the rest of the country. The situation is particularly striking for the State of Nebraska; it even lagged the North Central region in income and population growth, yet about matched the area in the expansion of passport applications.

On the basis of the above analysis, I am personally convinced that we are likely to be faced with a growing demand for foreign travel -- and a deepening travel deficit -- for quite a few years. For this reason, I am also convinced that we need to exert a particularly vigorous effort to attract more foreign visitors and to moderate expenditures abroad by Americans.

Outlook for the Foreign Travel Program

It is far too early to judge the probably outcome of the efforts to reduce our foreign travel deficit this year. Nevertheless, on the basis of the fragmentary evidence we do have, it seems doubtful that we will achieve the $.5 billion improvement in 1968 visualized in the President's New Year's Day message.

It will be recalled that the travel section of that message called on the President's Travel Task Force to accelerate its recommendations regarding ways of attracting more foreign visitors to this country; it also directed the Secretary of the Treasury to work out with the Congress legislative measures to moderate spending by Americans on travel outside the Western Hemisphere. The President also appealed to U. S. citizens to forego nonessential travel outside the Western Hemisphere for the next two years.

The Travel Task Force submitted its Report in mid-February; this included a number of voluntary actions which (when fully implemented) might yield a balance of payments benefit of more than $100 million per year. With the assistance of private industry and Federal agencies, the Task Force initiated steps which were expected to result in considerable reductions in the cost of travel in the U. S. for foreign visitors. The actions set in motion involved domestic air fares, railroad fares, hotel and motel rates, inter city bus fares, car rental charges, and package tour prices. Reductions in the cost of directional fares to the U. S. were also initiated by international air carriers and steamship lines serving the North Atlantic routes.

The progress to date in carrying out the Travel Task Force's recommendations is noticeable:

- First of all, the President established a Commission on Travel (under the direction of Ambassador Robert McKinney who headed the Task Force) to see that the momentum does not slacken.

- The International Air Transport Association has unanimously approved the recommended family rate for travelers from Europe and the Middle East to the United States. The discount, which ranges from 11 to 38 per cent, is expected to bring some 100,000 new visitors to the United States this year.

- The Civil Aeronautics Board has approved 50 per cent discounts for domestic fares effective April 23. The new fares will provide almost unlimited travel opportunities for foreign visitors within and across the United States at one-half the cost of published regular first-class and coach fares.

  The railroads have filed for a 25 per cent fare reduction for foreign visitors. It will become effective on April 29 if no objections are entered.

  The CAB has approved the U. S. airlines' request for authority to bring 2,000 active travel agents, tour

- operators, and travel editors to the U. S. this year and next for the purpose of familiarization tours.

- Major motion picture studios, under the direction of the Motion Picture Association of America, are producing a series of one-minute television commercials, utilizing the talents of international film stars, to promote more foreign travel to the United States.

- The Advertising Council has agreed to mount a major $5 million domestic campaign geared toward: asking all Americans to invite their friends and relatives from abroad to visit the United States this year and next; and requesting that all Americans be hospitable and courteous to all foreign visitors in the United States.

- A Subcommittee of the House Judiciary Committee is holding hearings on a bill which would grant the Secretary of State and the Attorney General authority to waive visa requirements for business and pleasure visits of up to 90 days.

- Commencing May 5, the new U. S. Government Hospitality Card will be available to foreign visitors. The Card entitles foreign visitors to a broad range of discounts throughout the U. S. A 111-page discount book has also been made available to the travel industry which stipulates what discounts are available and where.

- Work has begun on the creation of a new National Tourist Office which will not only promote abroad to attract more foreign visitors to the United States, but will also organize and coordinate efforts here in the U. S. to host foreign visitors.

The legislative program to moderate spending on foreign travel by Americans has been much less successful. The Secretary of the Treasury, after much discussion with the appropriate Congressional committees, finally presented a set of proposals calling for a foreign travel tax program with the following features: the first $7 of spending per day would be exempt from the tax; between $7 and $15 per day, the rate would be 15 per cent, and above $15 per day the tax rate would be 30 per cent. The tax would apply on trips to Europe, Africa, Asia and the Pacific (except Hawaii and Samoa). The Secretary also proposed that Congress extend to international airline tickets and sea travel the 5 per cent tax which currently applies to domestic airline flights. The tax on sea travel would be temporary. The existing duty-free allowance of $100 for foreign purchases accompanying passengers would be reduced to $10; the present $10 limit on mailed and unsolicited gifts would be set at $1.

Congressional reaction to the entire tax proposal has been particularly cold. To the surprise of no one, the proposal ran into sharp criticism from travel industry representatives, academicians, newspapers and many others who saw in the proposal a threat to the freedom to travel (or to their own business prospects). Reacting to this criticism, the Ways and Means Committee split off the proposed tax on spending and recommended to the full House the main features of the rest of the Secretary's proposal. If finally enacted by the Congress, these minor measures may result in an improvement of about $100 million in the travel account. The much more substantial savings (on the order of $250 million to $300 million) which might have been expected from the tax to moderate spending on foreign trips outside the Western Hemisphere can no longer be anticipated -- unless Congress changes what appears to be a deep-seated conviction against the proposal.

Personally, I wish it would recognize the basic need to moderate the persistently rising trend of spending by Americans traveling abroad. This is the central issue -- and not travel itself.

Concluding Remarks

As I have stressed throughout these remarks, our balance of payments deficit is an extremely serious problem, and it will require a vigorous national effort to correct it. For this reason, all of us -- and especially Congress -- ought to try very hard to get the President's New Year's Day program moving again. At the top of the list should be early passage of the income surtax and reductions in low-priority Federal spending. But, as I also mentioned above, because of the sizable contribution to our overall balance of payments deficit made by foreign travel expenditures, we also need to devise a means to moderate such spending. Some variety of a tax on travel outlays abroad seems the best means of doing this.

TABLE 1

U.S. Foreign Travel Expenditures
as % of Disposable Personal Income
(dollar amounts billions)

Year	(1) Disposable Personal Income	(2) Foreign Travel by U.S. Residents 1/	2 as % of 1
1957	308.5	1.4	0.45
1958	318.2	1.5	0.47
1959	337.3	1.6	0.47
1960	350.0	1.75	0.50
1961	364.4	1.8	0.49
1962	385.3	1.9	0.49
1963	404.6	2.1	0.52
1964	436.6	2.2	0.50
1965	472.2	2.4	0.51
1966	508.8	2.7	0.53

1/ Excludes travel by military personnel and other Government employees stationed abroad and by their dependents and U.S. citizens residing abroad. Excludes international transportation, but includes transportation within the countries visited.

Source: OBE, Department of Commerce

TABLE 2

Foreign Travel Expenditures of Selected Countries as Per Cent of Disposable Personal Income
(dollar amounts in millions)

Country	Disposable Personal Income 1/ 1960	Disposable Personal Income 1/ 1965	Foreign Travel Expenditures 2/ 1960	Foreign Travel Expenditures 2/ 1965	(2) as % of (1) 1960	(2) as % of (1) 1965
Western Europe						
U.K.	50,355	68,054	520	810	1.03	1.19
France	41,540	65,280	265	930	0.64	1.42
Italy	21,386*	35,339*	95	225	0.44	0.64
Germany	49,875	75,175	635	1,370	1.27	1.82
Netherlands	7,856	12,997	125	310	1.59	2.39
Sweden	7,135*	10,748*	85	210	1.19	1.95
Norway	2,653*	3,783*	55	80	2.09	2.11
Greece	2,640	4,494	20	40	0.76	0.89
Western Hemisphere						
Canada	23,465	32,763	645	720	2.75	2.20
Mexico	10,144*	15,568*	288	414	2.84	2.66
Pacific Area						
Japan	29,436	59,481	40	85	0.14	0.14
Australia	21,666	33,090	42	118	0.19	0.36
New Zealand	2,582	3,667	13	40	0.50	1.10

1/ Source: U.N. National Accounts Statistics, 1966. Total personal income minus direct taxes. Amounts marked with asterisk (*) are private consumption expenditures. All amounts converted from local currencies at official exchange rates.

2/ Source: IMF Balance of Payments Yearbook. Includes all payments for goods and services (including internal transportation) provided by foreigners to the reporting country's residents traveling abroad. It covers expenditures on account of tourists, business travelers, students, patients undergoing medical treatment, military personnel on leave, and traveling government officials. Passenger fares and shipboard expenses paid to ships and aircraft on account of international travel are not included.