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IMPORT CONTROLS AND DOMESTIC INFLATION

A Paper by

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By

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The new drive for protection, epitomized in the proposals to impose quotas on imports of shoes and textiles, could have serious adverse effects on U. S. consumers, on workers generally, and on the economy as a whole. At the same time, the imposition of import quotas on shoes and textiles would do little to solve the basic problems plaguing those two industries. This is the lesson we should have learned from the experience of the petroleum and sugar industries which are already protected by quotas.

This latest campaign to erect barriers against imports has sparked a new round of arguments about the merits of free trade vs. protectionism, and a phalanx of industry and labor organizations has been arrayed on the side of protection. Opposition to the proposals has also been vigorous, most of it coming from importers,

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This paper is based on work which I initiated last spring. Several members of the Board's staff have participated at various stages of the analysis. Mr. Daniel Roxon and Mrs. Betty L. Barker did most of the statistical and trade analysis on which the paper rests. Mr. Bernard Norwood and Mrs. Helen B. Junz, respectively, provided valuable counsel with respect to U. S. trade policy and the use of imports by foreign governments to strengthen general stabilization policies. Mr. Samuel Pizer helped to coordinate work on the project.

academic economists, and communications media. Spokesmen for the Federal Government have been heard on both sides of the issue -- and with varying degrees of support for quotas on particular commodities.

However, one crucial voice -- that of the American consumer -- has been scarcely heard. Few questions have been raised about the costs to consumers of import quotas on shoes and textiles. Yet, it is the American consumer who ultimately would bear the burden of such restrictions: his range of choice would be limited, his costs of clothing would rise appreciably, and further pressure would be exerted on the general level of consumer prices. Moreover, among consumers, the burden would fall most heavily on those low income groups that can least afford to bear it.

These are among the main conclusions emerging from an assessment of the probably effects of import quotas on shoes and textiles which I have had underway -- from time to time -- since last spring. Essentially, the assessment is based on an analysis of domestic consumption and foreign trade patterns during the 1960's and a projection of demand and supply conditions to 1975. The main provisions of the proposed trade legislation (H.R. 18970) serve as the framework for the inquiry. The assumptions (and limitations) of the analysis are spelled out below, but the most important results can be summarized briefly at this point:

- If quotas on footwear stipulated in the proposed bill were adopted, the extra cost to consumers would be in the neighborhood of $1.9 billion in 1975, compared with the level of expenditures that might be expected in the absence of quotas.

- In the case of textiles (where apparel would be the main item affected), the extra cost to consumers might be about $1.8 billion in 1975.

- In the absence of quotas on footwear and apparel, domestic prices of these commodities would probably decline by an amount large enough to result in a modest decrease in the general level of consumer prices. However, with quotas imposed, the total consumer price index in 1975 (using a base of 1969=100) would be almost 1 percentage point higher -- and the index excluding foods and services would be about 1-1/2 percentage points higher -- than might be expected in the absence of quotas.

These estimates are obviously tentative and should be interpreted with considerable caution. Nevertheless, they do suggest the general direction and rough magnitude of the additional burdens consumers would have to sustain if the legislation is adopted and if quotas on imports of shoes and textiles were imposed as specified. Moreover, these costs would probably be close to the minimum, since quotas on other types of consumer goods might soon follow.

The evidence on which these estimates are based is presented below. First, however, it might be helpful to summarize those provisions of the proposed legislation that are most relevant to the first part of the present discussion. Other provisions are referred to at later points in this paper.

Legislative Proposals to Impose Import Quotas

Under H.R. 18970, proposed as amendments to existing tariff and trade laws of the United States,[1/] the President's authority to enter into trade agreements with foreign countries would be extended until July 1, 1973. This authority was granted originally under the Trade Expansion Act of 1962; but with the expiration of this Act three years ago, the President has not had such authority.

The President would be able to reduce the rates of duty to which the U. S. was committed on July 1, 1967[2/] by not more than 20 per cent or 2 percentage points, whichever is lower. Such tariff reductions must take place in at least two stages with one year intervening between each reduction. The intention of this provision is apparently to give the President authority to compensate our trading partners for actions the U. S. may take to restrict imports under the proposed legislation.

1/ The bill was drafted and adopted by the House Ways and Means Committee in mid-August, and it cleared the House Rules Committee in early September. The full House of Representatives is expected to vote on the measure soon after the end of the election recess in mid-November. The Senate Finance Committee has adopted a bill similar to that approved by the two House Committees. The Senate as a whole is also expected to vote on the matter before the end of the year.

2/ In effect, this means the rates of duty which will exist when the final stage of the Kennedy Round tariff reductions takes place on January 1, 1972.

The bill strengthens the President's powers to retaliate against foreign countries which "unreasonably" or "unjustifiably" restrict U. S. exports. Under the bill, the President would be able to impose tariff duties or other import restrictions on the products of a foreign country which is discriminating against U. S. products -- whether agricultural or non-agricultural -- whereas previously he could do so only in the case of agricultural products.3/ In addition, subsidies provided by a foreign country on its exports to foreign markets which unfairly affect U. S. exports to those same markets are specifically listed as "unjustifiable" discriminatory acts and as such would be grounds for U. S. retaliation.

The bill outlaws the use of tariff duties to limit imports for national security reasons; only quantitative controls can be used. This provision would prevent the President from abolishing the oil import quotas and imposing tariffs instead.

Quotas would be imposed on textiles and footwear, by country and by category. In 1971, imports of each category of textile and footwear articles in each country would be limited to the average annual quantity of such articles imported from that country during the years 1967, 1968, and 1969. Beginning in 1972, the quantities permitted by this base level formula may be increased by not more than 5 per cent of the amount authorized in the preceding year. Cotton textiles already covered by quotas under the Long-Term Cotton Textile Arrangement will be exempt from the proposed quotas.

3/ As before, the President can also prevent a foreign country who unreasonably or unjustifiably restricts U. S. exports from receiving the benefits of U. S. trade agreement concessions.

Also, specific textile or footwear articles may be exempted if they cause no market disruption, if it is in the national interest to do so, if total supply from domestic and foreign sources is inadequate, or if voluntary quotas with exporting countries are negotiated. The import quotas on textiles and footwear may be extended by the President but for no more than 5 years at a time. If they are not extended, the quotas will expire on July 1, 1976.

Quotas vs. Structural Problems in the Textile Industry

As I stressed above, the imposition of import quotas will do little to correct the basic problems with which textile producers are confronted. The textile industry is undergoing a major structural adjustment of which the rise in imports in recent years is only one symptom -- despite the attempts to associate all the difficulties of the industry with imports. In fact, curtailing imports will only delay and distort the adjustment process which is necessary for the viability of the industry in the long run.

The adjustment problems faced by an individual textile firm are determined partly by the extent to which it concentrates on a particular sector of the industry. The scope of the textile industry can be defined in at least two ways. In terms of materials, textiles include all products of cotton, man-made fibers, wool, and silk -- and combinations and mixtures of these and other fibers and substances. In terms of stage of processing, textiles encompass

fiber (but not the raw material in its natural state), fabrics and apparel. Fabrics may be finished materials (capable of being made into final products) or "gray goods" (requiring further processing before final use). The proposed quotas would have their heaviest impact on imports of man-made materials and manufactures -- especially on apparel and fabrics.

The rise in market penetration of imported textiles reflects in part the slowness with which a traditionally small unit industry adapts to new technology. Even in industries where the average unit of production is large, the adaptation to technological change may be slow. This is illustrated dramatically by the time it took the steel industry to convert its facilities to the new oxygen process -- partly under the spur of competition from rising imports. The lag is even more pronounced for a small unit industry such as textiles. However, that the process is underway is demonstrated by the continuing trend toward concentration in the industry and by the rate of profitability of the larger corporations.

Between 1958 and 1967, the number of firms manufacturing textiles declined sharply. For example, during this period, the number of companies producing woven cotton fabrics declined by 30 per cent; the number making synthetic fabrics dropped by 17 per cent, and the number producing items of apparel such as men's suits and shirts and women's suits and underwear decreased between 20 per cent and 35 per cent. The result was that by 1967 the 50 largest companies accounted for about two-thirds of the industry's output.

Yet, as suggested by statistics relating to the 500 largest industrial corporations in the United States, even the largest firms in the textile industry -- on the average -- appear to be smaller than their counterparts in other industries.*

	1961	1969
Assets Per Employee		
All corporations	$16,264	$21,545
Textile manufacturers	11,035	14,609
Apparel manufacturers	7,982	10,204
Sales Per Employee		
All corporations	$20,506	$27,986
Textile manufacturers	14,572	20,195
Apparel manufacturers	12,234	15,799

In general, the largest textile firms appear to be about two-thirds to three-quarters as large as the top industrial firms in the economy as a whole. The typical large apparel manufacturers appear to be roughly one-half to three-fifths the size of their counterparts in other industrial sectors. Moreover, while the gap in terms of sales per employee was closed somewhat for apparel firms during the 1960's, the overall lag for both textile and apparel firms remains large.

In terms of profitability, the largest firms in the textile industry have continued to improve their position, compared with their counterparts in other manufacturing industries. Again, this

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* Source: Fortune magazine, as reported in U. S. Bureau of the Census, Statistical Abstract, 1963 and 1970.

conclusion is supported by statistical information relating to the 500 largest industrial corporations:*

	1961	1969
Sales per dollar of invested capital		
All corporations	$1.92	$2.41
Textile manufacturers	1.93	2.66
Apparel manufacturers	2.44	3.30
Return on invested capital (per cent)		
All corporations	8.3	11.3
Textile manufacturers	6.1	7.9
Apparel manufacturers	8.8	11.9

Sales by textile firms per dollar of invested capital were roughly the same as those for all large corporations in 1961, and they were moderately higher in 1969. For apparel firms, reflecting the relatively smaller investment required to enter the field, sales per dollar of investment were one-quarter to one-third higher in both years. Partly for the same reason, net profits of apparel firms as a percentage of invested capital were slightly higher in both years than for large manufacturers generally -- and considerably higher than for firms producing textiles, for whom the rate of return was more than one-quarter below that for all large industrial corporations.

For textile and apparel manufacturers, data on net profits after taxes as a percentage of sales give an even clearer picture of the divergent trends among large and small firms within these industries:

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*Source: Same as that shown on p. 8.

	1961		1969	
	All Corps.	Largest Firms	All Corps.	Largest Firms
All manufacturing	4.30	4.20	4.79	4.60
Textile manufacturing	2.09	3.00	2.85	3.20
Apparel manufacturing	1.27	3.00	2.31	3.60

For all textile and apparel manufacturers in 1961, net profits in relation to sales were about one-half to seven-tenths below the rate for all industrial firms combined. But for the largest firms in both segments of the industry, the short-fall was only 30 per cent. During the 1960's, the rate of return on sales for all textile and apparel firms rose much faster between 1961 and 1969 than for manufacturing as a whole. For the largest textile and apparel producers, the rate of advance was less than that for all firms in these sectors -- partly reflecting the fact that only the most successful smaller units remained active over the decade. Nevertheless, the largest textile and apparel producers in 1969 were still substantially more profitable per dollar of sales than was the average firm in the industry.

The general conclusion to be reached from an analysis of the above information seems clear: the textile industry in the United States is in the process of consolidating into larger, more profitable units. The largest firms in the industry (and the number of such firms remains large enough to assure vigorous competition) have been maintaining their profitability compared with manufacturing as a whole. Given the economies of scale afforded by a rapidly changing technology, they should achieve further improvement.

Competition from imports is only an added feature -- not the major cause -- of the problems currently facing the weaker units in the industry. Protection from imports will not preserve the smaller firms facing competition from the larger, more adaptable and efficient domestic enterprises. Instead, the burden of quotas designed to provide such protection will be borne primarily by the American consumer. Let me make it perfectly clear -- as I will explain later -- I would like to see the businesses and workers who suffer in this rapid technological shift helped by the Federal Government to make an adjustment -- we cannot be indifferent to their problems.

Import Quotas vs. Structural Problems in the Shoe Industry

The shoe industry is also suffering from serious structural problems, and the imposition of import quotas would contribute little toward their solution. As is generally known, the shoe industry is a labor-intensive industry, with low wages, low productivity, a relatively low rate of investment, and with a large portion of its output concentrated in small plants.

For example, in 1967, there were about 1090 establishments in the United States producing leather footwear. Employment per establishment averaged about 200 workers. With so many producers, no single firm -- or small group of firms -- controlled a large enough share of the market to serve as a focal point for the industry. It is estimated that, in 1967, the largest producer accounted for about 6-1/2 per cent of domestic output; the four largest accounted for 25 per cent, and the top eight accounted for 34 per cent.

Within the industry -- even among the larger firms -- factories are usually highly specialized. Not only is production capacity likely to be geared to a particular segment of the market -- such as women's vs. men's shoes -- but it may be even further subdivided within these categories. This lack of diversification means that individual firms are highly exposed to short-run shifts in demand for products which are themselves subject to sharp changes in fashion. The smaller firms in particular have great difficulty in coping with such changes in styles. Moreover, the purely seasonal variation in output is also considerable.

The production process in the shoe industry necessitates great reliance on labor. In fact, a substantial number of processes in shoe manufacturing are essentially handicraft operations. The reasons for this center mainly in the unevenness of the materials employed (e.g., no two pieces of leather are identical) and the considerable variety of widths and lengths required for each shoe model. Thus, because of these constraints, technological advances have been slow, and automation has made little progress in the shoe industry.

The entry of new firms into the shoe industry is fairly easy. The amount of capital investment required is fairly modest. By long-standing trade practices, a considerable part of the machinery needed for shoe manufacturing is leased -- rather than purchased -- from equipment producers. The lease arrangement

also normally provides for the payment of a fixed monthly rent and a payment based on the rate of production. The result is that a new firm avoids both a large initial capital investment and the high fixed overhead cost of idle equipment during periods of low seasonal activity. Consequently, while failures are frequent, new entry is also frequent, and the industry remains populated by a large number of small, high-cost firms.

Partly reflecting these characteristics, the profitability of the shoe industry historically has been low. This remains true today, but the industry did improve its relative position during the 1960's. This improving trend is evident in the following figures:+

Year	Net Profits After Taxes				
	As Per Cent of Sales			As Per Cent of Net Worth	
	Mfg. Total	Nondurable Goods	Leather & Leather Products*	Nondurable Goods	Leather & Leather Products*
1961	4.3	4.7	1.1	9.6	4.4
1962	4.6	4.7	1.7	9.9	6.9
1963	4.7	4.9	1.8	10.4	6.9
1964	5.2	5.3	2.6	11.5	10.5
1965	5.6	5.5	3.8	12.2	11.6
1966	5.6	5.6	3.0	12.7	12.9
1967	5.0	5.3	2.9	11.8	11.3
1968	5.1	5.3	3.3	11.9	13.0
1969	4.8	5.0	2.6	11.5	9.3

* Nonrubber footwear accounts for approximately two-thirds of the value of output in the industry.

+ Source: Securities Exchange Commission -- Federal Trade Commission and the Federal Reserve Board.

In the early 1960's, net profits after taxes as a percentage of sales in the shoe industry averaged about one-third of the profit rate in nondurable goods industries and in manufacturing generally. But since the mid-1960's, the relative rate for the industry has been one-half or higher. When net profits after taxes are compared with net worth, the profitability of the shoe industry is shown to have improved even more markedly. While the rate of return on this basis in the shoe industry was about two-thirds that for all nondurable goods producers in the early 1960's, it was roughly on par with the rate for the group as a whole through 1968. Last year, the ratio declined to about four-fifths, but this was well above the proportion recorded in the early years of the last decade.

From this brief survey of the shoe industry, I conclude that -- rather than adopting import quotas -- efforts should be made to cope with some of the basic structural problems facing the industry. I will return to this point in a later section of this paper.

Demand for and Supply of Textiles and Footwear

To estimate the costs of the proposed quotas to the American consumer, it is necessary to make a judgment about the conditions that may govern the future demand for and supply of the commodities that would be subject to the restrictions. This is an extremely difficult task, and only the roughest kind of quantitative

estimate can be made. And even to do this requires one to make several highly simplified assumptions about consumer behavior and other factors that will influence the market. But even though the estimates derived below are highly tentative and show only the direction and rough magnitude of the cost to consumers of imposing import quotas on textiles and shoes, I believe it is important at least to attempt to quantify what this issue means to consumers.

The statistical information used in the analysis and the method of deriving the estimates are shown in Table 1, attached.

The analysis turns on a set of simplified assumptions about the pattern of imports and consumption of textiles and footwear in 1975. In carrying out the analysis, an examination was made of data on consumption, imports, the relationship of imports to consumption, prices of the domestically produced commodity, and prices of the corresponding import. The behavior of these variables during the decade of the 1960's was studied. But trends in the period 1965-69 were used as benchmarks for the projection of the demand for and supply of nonrubber footwear and apparel (the most important consumer goods component of the textile category) to 1975.

The tasks to be performed were (1) to estimate the domestic demand for each type of commodity in 1975, (2) to estimate the division of the supply of each type of commodity between domestic production and imports, and (3) to estimate the difference (in dollars) of meeting a larger share of demand from domestic suppliers rather than from importers.

In estimating consumption in 1975, it was assumed that per capita consumption will continue to increase between 1969 and 1975 at

the same rate recorded between 1965 and 1969. As shown in Table 1, for apparel, the average annual rate of growth in the 1965-69 period was 3.2 per cent, and for footwear it was 1.0 per cent. Extending these rates of change in per capita consumption to 1975, and given the Census Bureau's projection of U. S. population in 1975, total volume of consumption of apparel and footwear in 1975 was derived. This volume was then converted to dollar terms.

It was further assumed that -- in the absence of the quota -- the ratio of imports to consumption in 1969-75 would maintain the same annual average rate of increase that occurred in the 1965-69 period. For apparel, the rate of increase in that ratio was 10.5 per cent, and for footwear it was 18.0 per cent. By extending the rates of change in the import/consumption ratio to 1975 and applying the resulting ratio for 1975 to total estimated consumption in that year, the volume of imports, without quota, was obtained. In converting consumption and imports from volume to value terms, it was assumed that prices of both domestically produced and imported goods would remain the same in 1975 as they were in 1969. Such prices in themselves are only very rough estimates. (In other words, expenditures were expressed in 1969 prices.) It was also assumed that there were no supply constraints, either foreign or domestic.

It was assumed that -- if quotas were imposed -- the amount of imports authorized would be that stipulated under H.R. 18970: in 1971, imports would be held to the 1967-69 average; then, beginning in 1972, the amount authorized would be increased by 5 per cent of the amount authorized in the immediately preceding year.

Given the 1975 consumption level, it remained to determine what the dollar cost to the consumer would be if he had to shift his purchases from the cheaper foreign to the more expensive domestic product as a result of the imposition of a quota.

Cost of Quotas to Consumers

The above assumptions and calculations provided very rough estimates of the dollar cost to consumers of imposing quotas on apparel and footwear. For apparel, the extra cost might be in the neighborhood of $1.8 billion in 1975. In the case of footwear, it might approximate $1.9 billion. As stressed several times, these are only tentative estimates, and they should be interpreted with considerable caution. However, even if they were cut in half, they suggest that the adverse impact on consumers of putting quotas on these commodities would be considerable.

A brief discussion of recent trends in demand and supply in the two industries might help place the estimates in perspective.

The Case of Apparel:[4/] In 1969, consumer expenditures on apparel amounted to about $42.3 billion, an increase of 39 per cent -- or an annual average rate of about 8-1/2 per cent -- since 1965. Measured in physical volume,* the annual average rate of

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4/ This part of the discussion was restricted to apparel -- and fabrics were excluded -- for several reasons. In the case of cotton and man-made materials (particularly finished goods), import prices exceed domestic prices, so a small net saving might result if a quota were adopted. In the case of wool, no cost would be incurred because the quota would not be restrictive. In each of these cases, the estimates were calculated but not included because of lack of space.

* Measured in pounds, raw fiber equivalent.

increase was about 4 per cent. In 1969, imports represented 7.8 per cent of total consumption (by volume), compared with 5.2 per cent in 1965. In the 1965-69 period, imports rose at an annual average rate of 15 per cent -- far outstripping the 4 per cent rate of expansion of domestic production. As indicated above, the ratio of imports to total consumption rose at an annual average rate of 10.5 per cent between 1965 and 1969.

This sharp swing to imports was due to several factors, but the differential in prices between the imported and domestically produced items undoubtedly played a major role. For example, in 1969, the unit value of apparel of all kinds consumed (which can be interpreted as an average price) was $10 compared with just over $6 for the unit value of imports, adjusted to a retail basis.

Given this evidence of a strong demand for imported apparel, it seems reasonable to assume that consumers would continue to turn in the direction of foreign suppliers. If the projected rise in per capita consumption in 1975 were to be achieved -- despite the imposition of a quota -- the greater demand would have to be satisfied by domestic producers.

This could only be done at higher prices than would be the case if imports are not subject to a quota. As

indicated in Table 1, the unit value of apparel consumption in 1975 was estimated at $9.74 without a quota and at $10.08 with a quota. In other words, prices probably would decline slightly without a quota, but the imposition of restrictions would prevent this and perhaps cause a small rise in the average price. Since it was assumed that the physical volume of consumption would remain unchanged -- with or without a quota -- the higher unit value resulting from a quota is translated into a higher level of consumer expenditures.

Without a quota, consumer outlays for apparel in 1975 were estimated at $52.7 billion; with a quota, outlays were estimated at $54.5 billion. This difference of $1.8 billion is the cost of the quota to consumers. This is an extra cost of about 3-1/2 per cent.

The Case of Footwear: Imports of nonrubber footwear have grown much more rapidly than domestic output in recent years. However, the growth has been concentrated in certain types.

In 1965, domestic purchases of nonrubber footwear totaled 720,000 pairs; by 1969, the total had risen to 781,000 pairs. This was an increase of 8-1/2 per cent, or an annual average rate of 2.1 per cent. Imports rose at an annual average rate of 20 per cent in these years and accounted for 26 per cent of total consumption (by volume) in 1969 compared with 13 per cent in 1965.

Whether consumers would have increased their purchases to this extent if less expensive imported shoes were not available is very doubtful. The recently released report of the Presidential Task Force on nonrubber footwear concluded that "from the consumer point of view, imports have opened up important new options. The extremely low-priced imports, priced often far below any comparable domestic footwear except canvas-upper, rubber soled footwear, have provided entire new lines of basic foot coverings. At the other end, there can be little doubt that styles developed abroad in the higher price ranges have also provided new consumer choices."

The imposition of quotas on imports of footwear would be highly regressive, since it would be concentrated on imports of inexpensitive types. For example, in 1969, the unit value of imports (estimated at $5.32 retail) was about three-fifths the unit value of all domestic footwear consumed in that year ($8.77). In 1965, the price differential in favor of imports had been even greater, since the price of imported shoes rose much faster than the domestic product in the 1965-69 period.5/

5/ It has been estimated by the Tariff Commission that domestically produced nonrubber footwear is approximately twice as expensive as imported footwear. This is in the aggregate, covering all types. We have assumed, as indicated by the Tariff Commission study, that the retail markup is the same for both imported and domestic shoes, i.e., 50 per cent. This assumption is under heavy attack by the Tanners' Council which has charged that the markup on imported shoes is 75 per cent to 130 per cent compared with 50 per cent for shoes made in the U. S. Therefore, says the Council, the consumer is not really benefiting from the import of low-priced shoes. There may be some validity to this although the Tariff Commission has not been able to confirm it.

In the face of this experience with shoes -- as in the case of apparel -- it seemed reasonable to assume that consumers would continue to rely heavily on imports in the years ahead. In fact, if the rate of increase in the import/consumption ratio that prevailed in the 1965-69 period were to persist through 1975, imports could account for about 70 per cent of the domestic market for shoes in the latter year. The imposition of the quotas stipulated in the proposed legislation would hold the ratio to 24 per cent in 1975.

Thus, the public would have to meet the growth in demand from higher priced domestic sources. Without a quota, the unit value for total consumption of footwear was estimated at $6.72 in 1975 -- about 23 per cent below that for 1969. With a quota, the figure was estimated at $8.87 -- or 32 per cent higher than would be the case without a quota.

Using the estimates of the volume of consumption and unit values, the value of consumer outlays for footwear was determined. In 1969, this amounted to $6.9 billion. Without a quota, the level was estimated at $5.9 billion in 1975 -- despite an estimated increase of 12-1/2 per cent in the physical volume of consumption -- and reflecting the lower unit price of imports. However, with the quota imposed, domestic production would supply over 70 per cent of the total demand at unit prices almost one-third higher than the prices for imports.

Under these circumstances, the level of consumer expenditures is estimated at $7.8 billion in 1975. This is an extra cost of $1.9 billion -- or a premium of about 30 per cent -- that can be assigned as the burden of a quota on footwear.

Impact of Quotas on the Domestic Price Level

If quotas were applied to imports of apparel and footwear along the lines discussed above, they would add significantly to domestic inflationary pressures. This result stems from the fact that the domestically produced article -- shoes or apparel -- is more expensive than the equivalent imported article. In the absence of quotas, consumers are expected to increase the proportion of their total consumption devoted to cheaper imported shoes and apparel so that the average unit cost of these items would decline over the 1969-75 period. The proposed quotas, however, if imposed, would effectively freeze the import share of total consumption of footwear and apparel at about the present level, rather than allowing it to increase. Thus, the quotas would prevent the average unit cost to the consumer from declining as it would do if consumers were permitted to buy imports without restraint.

The higher unit prices resulting from the imposition of the quotas can be translated roughly into increases in the consumer price index (CPI). Using the same assumptions about the pattern of consumer demand and supply conditions discussed above -- along

with data on the relative importance of apparel and footwear in total consumer expenditures, the effects of quotas on the CPI were estimated. The calculations are shown in Table 2.[6/]

If imports of apparel and footwear are permitted to grow freely without quotas, and if the behavior of other components of the index are held constant, under the assumptions specified above, it is estimated that the total consumer price index would decline by 0.6 per cent, and the CPI excluding foods and services would decline by 1.4 per cent, between 1969 and 1975 (1969=100). On the other hand, the imposition of quotas on imports of apparel and footwear is estimated to result in a small increase from 1969 to 1975 of approximately 0.1 per cent in the total CPI and of around 0.2 per cent in the CPI excluding foods and services (1969=100). Thus, on an index base of 1969=100, the total CPI would be 0.7 percentage points higher, and the CPI excluding foods and services would be 1.6 percentage points higher, in 1975, with a quota than without a quota, assuming no change in other items of the CPI.

Thus, it appears that the adoption of quotas, aside from their other adverse effects, would aggravate inflationary pressures as well. This general conclusion seems evident -- although again it is necessary to interpret the above estimates of the effects on the CPI with considerable caution.

6/ In making these estimates, the data on consumption and unit values presented in Table 1 were used along with information showing the approximate weights for footwear and apparel in the total CPI and in the CPI excluding foods and services. The percentage changes in the CPI, which would occur from 1969 to 1975 with and without the quotas, were thus estimated.

Looking beyond the apparel and footwear industries, there can be no doubt that protectionist devices hurt our efforts to fight inflation and undermine our efforts to raise exports. In fact, many countries have used trade policy to induce greater imports as an effective way to combat rising domestic prices, and to induce their industries to operate more efficiently. Our own experience has been that the greatest increase in our overall imports has come since 1965 -- and has coincided with our failure to control inflation. Excess demand with rising prices is the basic cause of our trade problem, and we cannot expect to get relief from measures that will keep prices high.

Moreover, in their concern with rising imports, proponents of quotas forget that we are still a great and effective exporting country. We have succeeded in raising exports to an annual rate of $42 billion -- double the 1960-65 rate. At this rate, exports are greater than total domestic expenditures on residential structures or on automobiles and parts. When exports are so important to many sectors of our economy, especially agriculture, it would be a tragic mistake to start a round of retaliatory trade restrictions such as darkened the depression years. And if we are to make genuine progress in export expansion, we will need to achieve -- and maintain -- a much greater degree of domestic price stability than we have attained in recent years.

If we can achieve this objective, I would hope that at some point, perhaps before 1975, our competitive position for shoes and textiles -- and certainly overall -- would improve so that the sharp uptrend in imports would be moderated.

I do not believe the threat of imposing quotas would be effective in getting other countries to lower their barriers to U. S. exports. In my view, the only policy that will achieve this in the long run is a policy that encourages greater trade flows under free competitive conditions.

An Alternative Course for Public Policy

In commenting on the adverse effects of quotas on consumers, I am not suggesting that the textile and shoe industries face no problems. Quite the contrary, as indicated above, they are confronted with serious structural problems, and the sharp rise in imports in recent years has added to these. Both workers and businesses (especially the smaller firms) are being affected adversely.

For example, in the case of footwear (which must be considered a low-wage industry in the United States), foreign producers enjoy a sizable cost advantage. In mid-1969, the average wage of shoe production workers in the United States was about $2.29 per hour. In Italy, their counterparts received about $1.04 per hour, and the corresponding figures were $0.58 and $0.56, respectively, in Japan and Spain. The low foreign wages more than offset the higher output per manhour of the U. S. workers. Consequently, foreign producers of footwear could land shoes in the United States at prices well below U. S. production costs.

A similar story can be told for textiles. So, the competitive impact of imports in both industries is severe. Those employed in the industry -- both workers and business enterprises -- do need help. However, in my judgment, quotas are simply the wrong way to help them. Instead of pursuing that course, I think it is far preferable to adopt more effective programs to provide retraining and transitional benefits or financial assistance for those who are displaced by competitive forces over which they have no control -- whether the forces originate at home or abroad.

In this connection, the provisions for adjustment assistance in the proposed quota bill point in the right direction, but they could be improved considerably. The criteria to be met in granting assistance to industries, firms, or workers hurt by increased imports are liberalized by the bill. In general, the increase in imports would no longer have to be the "major factor" causing or threatening to cause serious injury; it would only have to "contribute substantially" to the injury. In determining whether serious injury to an industry has occurred, moreover, fairly rigid rules would be established: the imported article must constitute over 15 per cent of apparent U. S. consumption, and the ratio of imports to consumption must have increased by at least 3 percentage points in the year immediately prior to the investigation and by at least 5 percentage points in the year before that; or domestic production, jobs, man-hours worked, or wages must be declining substantially; and the imported articles are sold at prices substantially below those of comparable domestic products, and foreign unit labor costs are substantially below U. S. unit labor costs.

Under these rules, many industries -- which previously could not obtain relief -- might qualify for assistance. While some liberalization of the criteria for assistance would be helpful, there is a real danger that the grant of protection might go too far. Under the umbrella of adjustment assistance, even some of the strongest or least efficient industries might find shelter. Moreover, it would also be preferable to consider the need for adjustment assistance apart from any proposal to impose quotas.

Concluding Observations

In addressing myself to the question of the effects of quotas on shoes and textiles, I have attempted to show the adverse impact on consumers. The direction and rough magnitude of that impact have been indicated at several points in this discussion. But before concluding this presentation, it might be well to remind ourselves of the bad experience we have already had with quotas.

There are several items on which mandatory import quotas have been in effect for an extended period -- principally petroleum and sugar -- and these provide some clues to the cost of import quotas. The situation on oil imports has been intensively studied by a Cabinet Task Force on Oil Import Control, whose report was released early this year. The Task Force found that, "In 1969 consumers paid $5 billion more for oil products than they would have paid in the absence of import restrictions. By 1980 the annual cost to consumers would approximate $8.4 billion. Without import

controls the domestic wellhead price would fall from $3.30 per barrel to about $2.00, which would correspond to the world price. Although we cannot exclude the possibility, we do not predict a substantial price rise in world oil markets over the coming decade." A majority of the Task Force recommended that the present quotas be replaced by a system of tariffs involving a lesser degree of protection. It seems to me that this would move us some distance in the right direction.

In the case of sugar, the policy of controlling supplies goes back to the mid-1930's, and is intended to maintain stable prices and support the domestic sugar industry. The sugar control program has many complexities, but one clear result is that the U.S. sugar price averages considerably higher than the world price. One of the reasons that the quoted world price is so low -- currently about 4 cents per pound compared with a domestic equivalent price of about 8 cents per pound -- is that foreign producers, after supplying their U. S. quota amount at very favorable prices, can afford to sell their residual supplies on world markets at very low prices and realize a reasonable overall profit margin. If the United States were to remove its controls on sugar imports, the price to U. S. consumers would tend to fall, the world price would rise, and a single effective price would be established at some level between the two.

In the meantime, however, quotas on oil are in effect, and consumers are paying the cost. And, sadly, the new quota proposals would prohibit the abolition of the oil import quota and its replacement with a tariff, which at least would have the virtue of allowing the total supply to rise -- although at higher prices.

So, although we may have to live with the existing quotas for some time, I wonder how many of us -- as consumers -- would like to add others?

Table 1. Demand and Supply of Apparel and Footwear, 1965-1975

Commodity	1965	1969	Average Rate of Growth 1965 - 69 (per cent)	Projected 1975 Without Quota	Projected 1975 With Quota
Apparel					
Domestic Demand					
Value of consumption ($ million)	30,505	42,302	8.5	52,725	54,528
Volume of consumption (mil. of lbs.)	3,568	4,226	4.3	5,412	5,412
Unit Value ($ per lb.)	8.55	10.01	4.0	9.74	10.08
Per capita consumption (lbs.)	18.34	20.80	3.2		
Cost of Quota ($ million)	-	-		-	1,803
Sources of Supply (volume, mil. of lbs.)	3,568	4,226	4.3	5,412	5,412
Domestic production (mil. of lbs.)	3,382	3,898	3.6	4,647	5,077
Imports (mil. of lbs.)	186	328	15.2	765	335
Unit value of imports, retail ($ per lb.)	n.a.	6.14		6.14	6.14
Imports as per cent of total	5.21	7.76	10.5	14.13	6.18
Footwear					
Domestic Demand					
Value of consumption ($ million)	5,273	6,850	6.8	5,906	7,793
Volume of consumption (thous. of prs.)	719,729	780,741	2.1	878,697	878,697
Unit value ($ per pr.)	7.33	8.77	4.6	6.72	8.87
Per capita consumption (prs.)	3.70	3.84	1.0		
Cost of quota ($ million)		-		-	1,887
Sources of Supply (thousands of pairs)	719,729	780,741	2.1	878,697	878,697
Domestic production (thous. of prs.)	623,738	578,533	-1.9	264,312	669,301
Imports (thous. of prs.)	95,991	202,208	20.5	614,385	209,396
Unit value of imports, retail ($ per pr.)	3.08	5.32	14.7	5.32	5.32
Imports as per cent of total	13.34	25.90	18.0	69.92	23.83

Table 2. The Effect on the Consumer Price Index in 1975 of Imposing Import Quotas on Footwear and Apparel

	1969	1975 Without Quota	1975 With Quota
Apparel			
Value of consumption (millions of $)[1/]	42,302	52,725	54,528
Volume of consumption (millions of lbs.)	4,226	5,412	5,412
Unit value ($ per lb.)	$10.01	$9.74	$10.08
Change in unit value from 1969 (per cent)	0	-2.70	+0.70
Weight in consumer price index (per cent)			
Total	7.03	7.03	7.03
Excluding food and services	17.10	17.10	17.10
Change in CPI from 1969 to 1975 (1969=100 per cent)[2/]			
Total	0	-0.19	+0.05
Excluding food and services	0	-0.46	+0.12
Footwear			
Value of consumption (millions of $)[1/]	6,850	5,906	7,793
Volume of consumption (thous. of prs.)	780,741	878,697	878,697
Unit value ($ per pr.)	$8.77	$6.72	$8.87
Change in unit value from 1969 (per cent)	0	-23.38	+1.14
Weight in consumer price index (per cent)			
Total	1.60	1.60	1.60
Excluding food and services	3.89	3.89	3.89
Change in CPI from 1969 to 1975 (1969=100 per cent)[2/]			
Total	0	-.37	+.02
Excluding food and services	0	-.91	+.04

1/ Assumes prices of both domestically produced goods and imports are same in 1975 as in 1969. Changes in unit value thus reflect changes in the quantity of imports or domestically produced goods consumed.

2/ Assuming that the behavior of all other components of the CPI are held constant between 1969 and 1975.