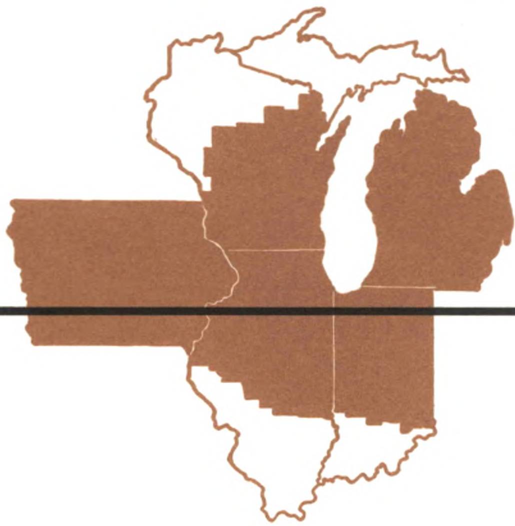
A review by the **Federal Reserve Bank of Chicago**

Business Conditions

1961 April



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THE Trend OF BUSINESS

The indicators of business activity are interpreted by many analysts in both business and Government as suggesting that the downturn has reached, or soon will reach, bottom. If they are right attention then turns to the questions: how rapidly will activity rise and will the economy soon approach full utilization of labor force and plant?

Industrial production appears to have stabilized in recent months. Since the start of the year rising output in steel, copper, electrical machinery and farm machinery has about balanced a substantial cutback in automobiles and small declines in a variety of industries. Unemployment has been fairly stable at a seasonally adjusted rate of over 6½ per cent of the labor force. Retail sales, after sagging in January, improved in February and perhaps in March as well.

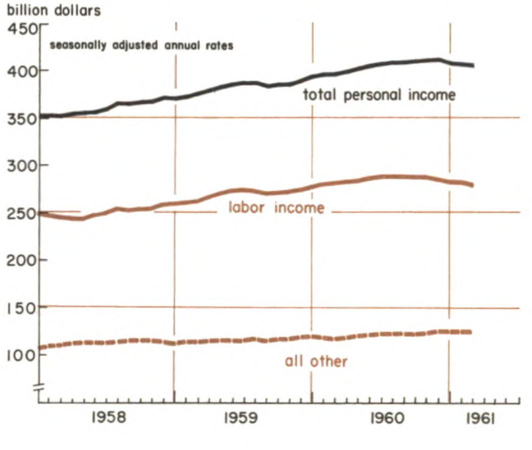
Government spending has been increasing at Federal, state and local levels and this trend is expected to continue. Construction activity may rise substantially as weather improves seasonally; construction contracts have been at a record in recent months. Farm income is at the highest rate in more than two years. Sales of farm machinery are rising from the reduced level in 1960.

Consumer income has been well maintained and personal saving, in the form of liquid assets, has risen to a high level. In January, at least, repayment of consumer debt exceeded new consumer loans made. Throughout the recession, consumer spending on soft goods, principally food and apparel, has held close to the reeord rate in the second quarter of 1960.

It is the hard goods sector, including automobiles, appliances and furniture, which has declined. In February sales of nondurable goods stores were 3 per cent above last year while sales of durable goods stores were 10 per cent *less* than last year. Recent surveys of consumer buying intentions suggest a stronger trend in hard goods sales may be developing.

If the current appraisals prove to be correct, the 1960-61 recession will have been both shallower and less prolonged than most of its predecessors. In 1948-49 industrial production declined for eight months to a

Wages and salaries have declined but other personal income has been maintained



point 9 per cent below the preceding peak. It took nine months to regain the previous high. In the 1953-54 movement the decline totaled 11 per cent in a period of eight months. It took thirteen months to get back to the starting point. In 1957-58 the decline totaled 15 per cent and lasted eight months. It took ten months to regain the peak. If industrial production touched bottom in February, the recent decline will have totaled only 7 per cent and will have been under way only seven months.

What lies ahead? After reaching the low point, will production rise slowly as in 1954 or rapidly as in 1958? At present the preponderant opinion is that the gain may be fairly slow. However, this view was widely held in each of the preceding recessions also. It is typical that potential sources of rising demand are not foreseen clearly.

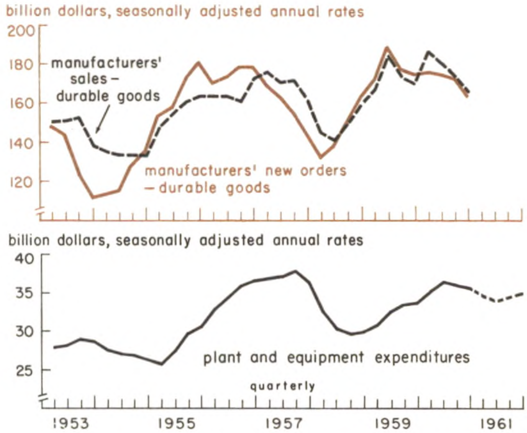
Capital spending to rise

Throughout the recession most businessmen have remained confident that the economy would not enter a severe or protracted decline. Recent evidence of this fact is found in the survey of business capital expenditure plans released in March by the Department of Commerce and Securities Exchange Commission.

The survey indicates that business firms will spend only 3 per cent less on new plant and equipment in the United States in 1961 than in 1960—34.6 billion dollars as compared with 35.7 billion. The rate of spending for this purpose has been declining since the second quarter of last year and is expected to continue downward through the first half of 1961. However, the results of the recent survey suggest that a moderate *rise* in capital spending will occur beginning in the second half of the current year.

Industries which are indicated to cut capital expenditures the most in 1961 are iron and steel, communications and railroads. The latter expect to reduce outlays 40 per cent, to the lowest level since 1946.

Capital outlays expected to rise in midyear after moderate decline from 1960 peak



A number of important industries plan to increase capital outlays for 1961 as a whole. These include gas and electric utilities, motor vehicles, machinery producers, and in the nondurable goods lines, food processing, chemicals and petroleum products.

The moderate decline now projected for capital expenditures in 1961 is the same as the McGraw-Hill survey had indicated last November. This is an encouraging sign. In the 1957-58 recession, capital spending plans were reduced further during the comparable interval.

From the peak in the third quarter of 1957 to the trough in the third quarter of 1958, capital expenditures declined by 22 per cent. If these outlays reach bottom in the second quarter of 1961, as now indicated, the decline from the high of the previous year will have been only 7 per cent.

Clearly, the capital expenditure uptrend of the 1958-60 period was neither so long nor so vigorous as in 1954-57. Outlays rose 23 per cent from the low point as compared with 53 per cent. Total activity reached a new high by a substantial margin in 1960, but capital expenditures did not exceed the 1957 record.

The capital expenditure boom which reached its peak in 1957 was dominated by huge projects to expand basic capacity in such industries as steel, iron ore, aluminum, copper refining and cement. In the 1954 and 1955 period the managers of most firms in these industries decided that the postwar prosperity was not a temporary phenomenon and that more "elbow room" was needed. Influenced in part by the desire to maintain position in their industry, expansion plans were formulated and put into effect almost simultaneously by many firms. As a result, substantial capacity to produce basic materials was added. The amount of unused capacity in important raw materials industries indicates that a similar movement of comparable scope is not likely to develop in the next capital expenditures upswing.

In the period since 1957 business managers have placed emphasis upon modernization, cost cutting and the provision of more capacity to produce finished products. These projects typically do not bulk as large in dollar volume of capital outlays as do expansions in basic materials. This explains in part the relatively small rise in expenditures between 1958 and 1960 and the relatively small decline projected for the current year. For this reason plant and equipment spending, traditionally a highly volatile sector of activity, has not fluctuated so widely during the recent cyclical movement as earlier.

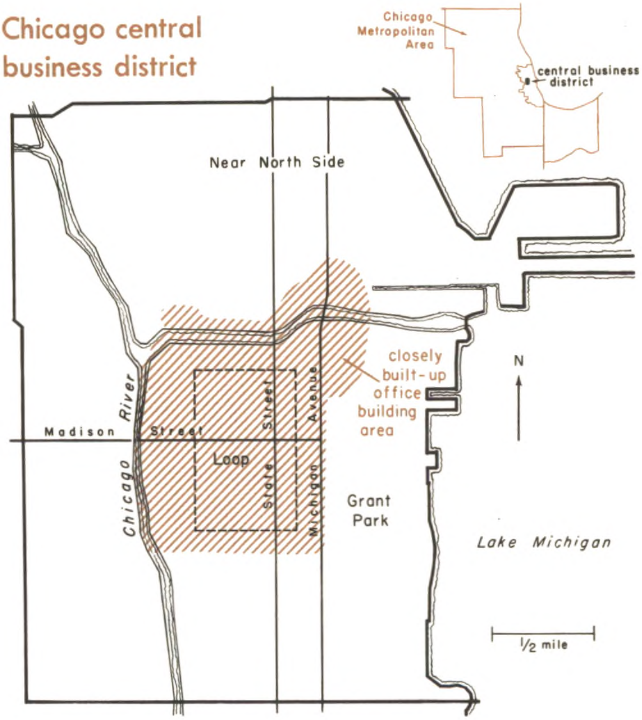
Downtown office space in Chicago —supply up, rising further

Since the end of World War II, the physical make-up of the nation's cities has undergone profound change. This has been most apparent in the "urban sprawl" which has pushed out the built-up areas around virtually every large city. Somewhat less apparent has been the rebuilding in the cities themselves. While the renewal of badly deteriorated residential areas in the older portions has been widespread, in only a few cities has the face of the central business district (CBD) been noticeably transformed.

In any large city the downtown area has long been the prime location for business offices, retail and wholesale establishments, hotels and theaters and other entertainment and cultural attractions. While this remains the case today, a number of factors have worked to reduce the CBD's *relative* importance. In almost every major city retailing has decentralized, following the customers to the suburbs. In Chicago, for example, one of the big State Street department stores closed its doors in 1948, releasing a substantial building for conversion into office space. Wholesale firms also have spread out, often to one-story plants on extensive tracts at the edge of the city. Television, "do-it-yourself" home modernization and maintenance work, larger families and the growing inconvenience of travel between remote residential sections and the heart of the city have cut deeply into the entertainment business in the central district.

The downtown area has for the greater part, however, retained its primacy as a location for offices. Although moves to outlying sites have occurred, there has been no general exodus.

Chicago central business district



The best example of a central area which has not only maintained but greatly enhanced its position as a location for business offices is Manhattan Island. The postwar boom in construction of new office buildings in New York has increased the office space available in that city about 50 per cent since 1947.

In downtown Chicago, the amount of office space has grown since the war by about 20 per cent.[1] At the end of 1960 the supply stood at 47.6 million square feet.

Most of the added space has come from conversions of area previously used for retailing, wholesaling, storage and other non-office purposes. This source has provided about 5.4 million square feet. New construction has contributed 3.9 million. Meanwhile, the demolition of old buildings has subtracted 0.8 million, for a net increase of 8.5 million square feet.

Construction activity gains sharply

Construction now "under way" will provide almost 4.7 million square feet of additional area for office use. Some will become available later this year, but the bulk is not due for occupancy until 1962 or later. Two of the ten projects in progress are only at the stage of site clearance.

Most of the postwar construction of new offices has taken place since 1950; only 250,000 feet or so were built in the earlier postwar years. Furthermore, the work in progress at present considerably exceeds the total volume completed in the fifteen years since 1945. However, all the construction since the war (including that now under way and the conversions) add up to only about

[1]Data are drawn largely from a recent report, *Central Area Office Space Study: Chicago, Illinois,* prepared for the City Planning Department by the Real Estate Research Corporation (1960).

half the 17.8 million square feet added during the boom of the Twenties.

Construction carried on between 1920 and 1930 raised the office space in the CBD from 5.9 to 7.8 square feet per resident of the Chicago metropolitan area. By 1940 the average had increased still further, to 8.2 square feet, mainly because of the completion after 1930 of several structures begun in 1929 or before. Largely reflecting building demolitions and population growth, the supply per capita dropped to 7.1 feet by the end of 1960, despite the new construction and conversion of existing buildings. Thus, the supply today is smaller in relation to the area's population than it was thirty years ago. But with the completion of work now in progress, space per capita will roughly equal the supply available in 1930.

A conspicuous feature of postwar office construction in Chicago has been the comparatively small amount done "speculatively." All but two of the dozen major new buildings (250,000 square feet or larger) have been erected by or on behalf of firms expecting to occupy most of the space.

Insurance companies have been especially prominent as sponsors of new office buildings. Their share of construction completed since the war amounts to 30 per cent, as measured by floor area, and these companies are responsible for more than 40 per cent of the work under way.

Central area remains concentrated

The Chicago area has witnessed some decentralization of offices to the suburbs. This has had little impact, however, upon the role of the central business district as the community's major office location. Much of the new office space in outlying sections has simply supplanted space adjacent to manufacturing and other facilities at sites inside the city but beyond the central area.

Within the downtown section, the small area in which most of the city's office space is located gives little appearance of having spread out appreciably even though several of the structures built since the war, and five of the major conversions, have been at sites on the outer edge of this area. Comparatively little has been added farther out. Of the office space to be provided by current construction, at least three-fourths lies in the central district.

Automation versus expansion?

Will the demand for office space in the CBD continue to grow? The answer depends, of course, on the over-all demand and the competitive position of the downtown area in relation to outlying areas and other cities in providing this "service."

Office-type employment has been growing rapidly. Since World War I, the number of official, managerial, professional, technical and clerical workers in the United States has grown threefold and now accounts for 36 per cent of total employment, compared with 20 per cent at the beginning of the period. During the past decade alone, the number of office workers has increased 30 per cent, rising from 18.6 million in 1950 to 24.1 million last year.

The mechanization of accounting and other data handling and improvement in communications are regarded in some quarters as likely in time to halt the growth of, or possibly even reduce, *total* employment in office work. The downward drift of employment in manufacturing is cited as an example of what may be achieved by mechanization of office work. It often is true that a single piece of modern equipment will do the work of a sizable number of bookkeepers or clerks. Many users of the new machines, though, have found that their data and record-keeping needs have expanded so rapidly that mechanization has merely slowed the growth in office employment.

In any event, the recent spurt in the construction of new office space appears to have been associated with the postwar rise in the proportion of the labor force engaged in office-type activities. The possibility that automation in data handling and entirely new techniques for performing such work will lead to a reduction in labor and space requirements apparently has yet to be established. Meantime the plans of business for office expansion continue to reflect current trends in white collar employment.

Economic integration in Europe— its significance for U.S. exports

In 1960, United States merchandise exports totaled 19.6 billion dollars or 20 per cent higher than in 1959. Our imports, on the other hand, tapered off slightly to about 14.7 billion dollars. This dramatic improvement in our export trade picture was an important source of strength for the economy during a period when domestic demand began to slacken noticeably. In the international area the export surplus helped materially to cushion the impact of a substantial increase in the outflow of private capital on the United States balance of payments.

Several factors have contributed to the surge in exports. There have been substantial worldwide reductions in import controls —including quotas, licensing requirements and bilateral trade agreements—which discriminated against exports from the dollar area. As international economic conditions improved and the gold and dollar reserves of major trading nations increased, the need and justification for maintaining restrictions on dollar imports disappeared. U. S. Government sources have estimated that "possibly twenty-five per cent" of the improvement in our exports during 1960 can be attributed to increased sales of goods made possible by the loosening of restrictions on trade.

A high level of business activity in Western Europe and Japan boosted demand for American raw materials, capital equipment and consumer goods. The presence of spare capacity in our economy, moreover, facilitated prompt delivery of many of these items.

American industry introduced many new products, including some that were more competitive with foreign goods in terms of design and price (the compact cars, for example) and others that possessed substantial technological advantages over foreign merchandise (commercial jet aircraft, electronic computers, etc.).

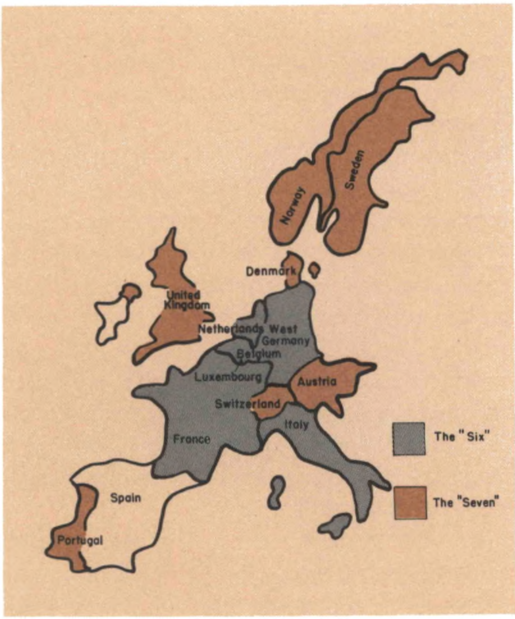
Foreign trade experts are predicting that United States exports in 1961 may approximate last year's total. The long-range outlook, however, will be heavily influenced by an entirely new set of conditions—the emergence of regional economic groups in Europe.

The "Six" and the "Seven"

The European integration movement, which sprang from the common desire for greater economic and political unity following World War II, is producing rapid and far-reaching changes in the European economic structure. Since 1957, two regional economic groups embracing a total of 13 countries have emerged—the European Economic Community, or Common Market, in 1957 and the European Free Trade Association in 1959. They have come to be known as the inner "Six" and the outer "Seven."

Following the formation of the Common Market intensive efforts were made to find a way in which the other European countries might become associated with the "Six" in a European free trade area. The negotiations broke down in the latter part of 1958, however, when the nonmember countries refused to go along with the Common Market countries' demands for a common external tariff, harmonization of economic policies and establishment of a common agricultural policy. Ultimately seven of the countries, led by Great Britain, formed the European Free Trade Association.

Western European trade areas



Within each group, tariffs and other trade barriers are being dismantled to stimulate increased trade and mutual economic growth. By broadening markets and enhancing competition, the move toward freer trade within these two groups of countries should facilitate a more efficient utilization of resources. Each country will be able to concentrate on producing the goods it can make most economically. This would permit the strongest firms to grow in size and obtain the benefits of producing for larger markets.

So far the Common Market countries, in three steps, have slashed their internal tariffs on industrial goods by 30 per cent from "basic rates" in effect January 1, 1957, and will decide soon whether to execute a further cut of 10-20 per cent during 1961. If plans go according to schedule, internal tariffs will be reduced to zero by 1966. Internal quotas have been liberalized 20 per cent and are scheduled to be eliminated entirely by the end of the current year.

The "Six" do not contemplate free trade in agriculture. Instead, they intend to establish a uniform agricultural market with a "basically common level of prices" which will probably be generally higher than the world price level. They have cut internal tariffs on most farm commodities by 20-25 per cent and have raised quotas slightly. Fur-

Salient features of the . . .

	European Common Market—the "Six"	European Free Trade Association—the "Seven"
Basic treaty	Treaty of Rome, March 25, 1957	Stockholm Convention, November 20, 1959
Membership	Belgium, France, Italy, Luxembourg, Netherlands, West Germany	Austria, Denmark, Norway, Portugal, Sweden, Switzerland, United Kingdom
Objectives	Expansion of trade and mutual economic growth through formation of a closely knit customs union, involving broad integration of the members' economies into one large common market and erection of a common external tariff.	Expansion of trade and mutual economic growth through formation of a flexible customs union or free trade area in which each member will retain control over its own economic policies. Also, strengthen bargaining position of "Seven," in their negotiations with the "Six."
Economic policies	Complete abolition of all tariffs and quotas on *all* trade between the member countries. Harmonization of social, commercial, financial and economic policies. Removal of restrictions on the movement of capital and labor. Erection of a common external tariff. Establishment of a common agricultural policy.	Trade liberalization measures pertain to manufactured goods *only*. There is no provision for common agricultural policy or a common external tariff. Each member will be free to maintain and adjust its own tariff against imports from outside countries.
Time table	Transition to unified common market is expected to be completed by 1970. Internal quotas on industrial goods will be eliminated by the end of 1961, and internal tariffs are tentatively scheduled to be reduced to zero by 1966. Progress with respect to agriculture may be slower because of difficulties encountered in formulating common agricultural policy.	Internal tariffs and quotas are scheduled to be eliminated by 1970, but this date may be advanced to match rapid progress of the "Six."
Escape clauses	Member countries can temporarily suspend or delay trade liberalization measures because of balance of payments difficulties or hardships attributable to increased competition.	Escape clause provisions are essentially similar to those of the "Six."
Principal governing agencies	Council of Ministers, supreme policy-making body, coordinates economic policies of the member countries and decides on basic issues arising out of establishment of Common Market. Commission administers provisions of Rome Treaty and formulates policies which are subject to review by Council of Ministers. Court of Justice decides on legal disputes arising under the treaty.	Council of Ministers has sole authority for making decisions and implementing objectives of the Stockholm Convention. Administrative matters are handled by small secretariat.

ther steps will depend upon the common agricultural policy that is finally adopted.

On January 1, 1961, the "Six" took the first of a series of steps designed to erect a common tariff against industrial goods from nonmember countries. It was originally intended that the common external tariff would represent the average of the members' tariffs in effect January 1, 1957.[1] But to make the move more acceptable to other countries, the "Six" decided to reduce their proposed external tariff by 20 per cent. This reduction was conditional, however, on an offer of reciprocal concessions from other countries during the 1960-61 GATT tariff negotiations in Geneva, Switzerland.[2]

As the first step, the Common Market countries adjusted their individual commodity rates 30 per cent of the way toward the new common tariff (reduced 20 per cent). This meant that Germany, Belgium, Netherlands and Luxembourg (the latter three known as the Benelux nations), the low-tariff members of the "Six," on balance raised the general level of their tariffs while France and Italy, the high-tariff members, lowered theirs.

Trade liberalization moves taken by the "Seven" have been less far-reaching. The "Seven" have cut their internal industrial tariffs 20 per cent from "basic rates" in effect January 1, 1960, and raised internal quotas 20 per cent. To match the rapid pace of the Common Market, the "Seven" recently agreed to advance the date of the next 10 per cent reduction in their internal tariffs from January 1, 1962, to July 1 of this year. Seven additional tariff cuts of 10 per cent annually are scheduled, beginning January 1, 1963, but this program may well be accelerated. The "Seven" have excluded most agricultural products from their trade liberalization moves and do not contemplate the erection of a common external tariff.

A united Europe?

The rapid pace of developments during the past year has brought home to many parties the urgency of strengthening bridges between the "Six" and the "Seven" to avert the possibility of Europe being divided into two permanent trade blocks. Britain, the leading member of the "Seven," has held separate talks with the German, French and Italian Governments on the subject, and studies have been launched to find ways of reconciling the special economic interests of each group, an undertaking that will not be achieved easily.

Britain, for example, is particularly concerned with preserving its long-standing preferential trade relationships with the Commonwealth countries. The low-tariff Scandinavian countries, on the other hand, feel that the principle of a common external tariff as envisaged by the "Six" would conflict with their traditional liberal trade policies. Countries like Austria, Sweden and Switzerland are reluctant to associate with any trade group that might clash with their long-standing political neutrality. Several countries in both groups are determined to shield their agriculture from outside competition.

[1]Tariffs on some 70 items considered "sensitive" by the members were negotiated separately. A number of these products, including lead and zinc ores, synthetic rubber and latex and aluminum scrap and magnesium scrap, will be admitted duty-free. A number of others such as auto engines will be subject to duties ranging from 19-22 per cent, aircraft engines 10-12 per cent and large aircraft 12 per cent.

[2]Organized January 1, 1948, GATT—General Agreement on Tariffs and Trade—is the chief international forum for the negotiation of tariff concessions and the settlement of trade disputes. The United States and 37 other major trading countries are contracting parties to GATT. These countries account for roughly 80 per cent of the world's international trade.

A union of the "Six" and the "Seven" would create a vast market with a total area of nearly 800,000 square miles, a combined population of approximately 260 million people and a gross national product equal to roughly 265 billion dollars in 1959. In comparison, the United States, which encompasses an area of 3.6 million square miles, reported a population of 178 million and a gross national product of 482 billion dollars in 1959. The "Six" and the "Seven," moreover, would be a substantial factor in world trade. In 1959 their combined exports and imports amounted to nearly 86 billion dollars or 42 per cent of total world trade.

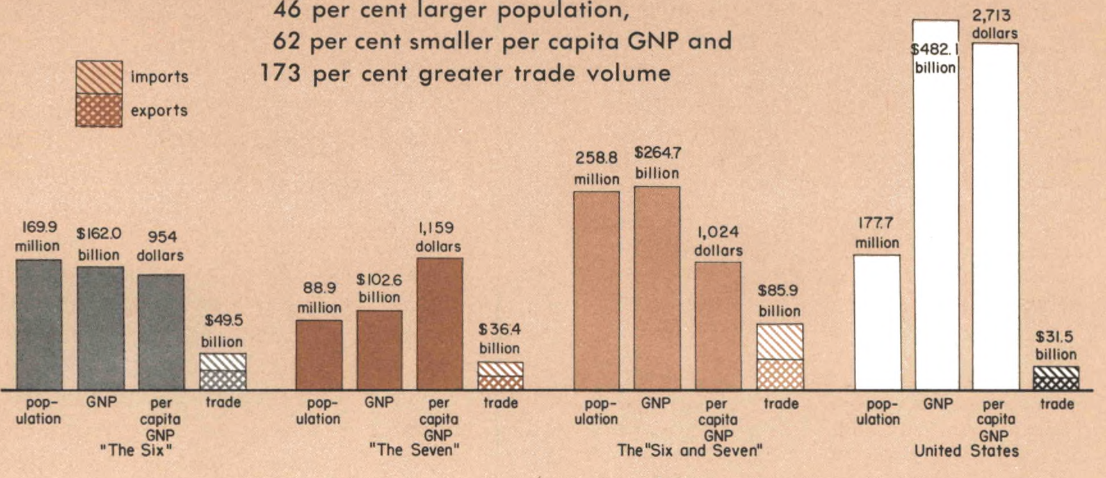
Discrimination against U. S. exports

The lowering of intra-European tariffs associated with the economic integration movement will handicap some kinds of American exports. As tariffs come down inside the Common Market (as noted above, they have already been reduced 30 per cent), German and Benelux manufacturers of electrical machinery, heavy engineering equipment, tractors and machine tools stand to make substantial gains at the expense of American and other outside suppliers in the formerly high-tariff French and Italian markets. French chemical, glass and textile firms engaged in supplying the German and Benelux markets will derive similar benefits.

In the case of the "Seven," where internal tariffs will soon be reduced 30 per cent, British-made automobiles, electrical machinery and engineering equipment may displace some American exports to the Scandinavian and Swiss markets.

Upward tariff adjustments made by Germany and the Benelux countries on January 1, to bring their tariffs into line with the proposed Common Market external tariff, will undoubtedly create additional problems for American exporters. It has been esti-

Compared with the U. S., the "Six" and the "Seven" in 1959 had a 46 per cent larger population, 62 per cent smaller per capita GNP and 173 per cent greater trade volume



mated that the external tariffs of the Benelux countries will be increased by an average of about 6 per cent from present levels, and the German tariffs by 22 per cent, to conform with the proposed final outer tariff. For some items, important to American exporters, the increases would be substantially greater (see table below).

The expansion in volume, and the commensurate gains in the efficiency of European industries that are likely to accrue from the lowering of intra-European tariffs, will also enable European suppliers to compete more effectively in such important overseas markets as Canada, Latin America and Africa. European competition has already had a noticeable impact on our exports of generating equipment, electrical machinery and farm equipment to those areas.

The outlook for American agricultural exports to Europe is rather difficult to assess. Although the "Seven" have decided to leave agriculture alone, present indications are that the common agricultural policy being formulated by the "Six" will assume a decidedly protectionist tone, reflecting the political strength of agricultural interests in the member countries. The high-cost members are reluctant to take any steps toward a unified agricultural market that would involve substantial adjustments for their agricultural economies.

Unable to agree on a common external agricultural tariff, the "Six" have proposed a series of "variable import duties" on a wide range of agricultural products. These "variable import duties" would enable the "Six" to equalize price differentials between home production and imports from outside countries, thereby assuring a high degree of protection for their domestic producers. Any attempt on the part of an outsider to sell his agricultural products in the Common Market could be thwarted by simply raising the "variable import duties." The flow of imports will be further controlled by quotas and licensing arrangements.

It is believed that actual implementation

First step toward Common Market external tariff necessitates increases in some German and Benelux tariffs

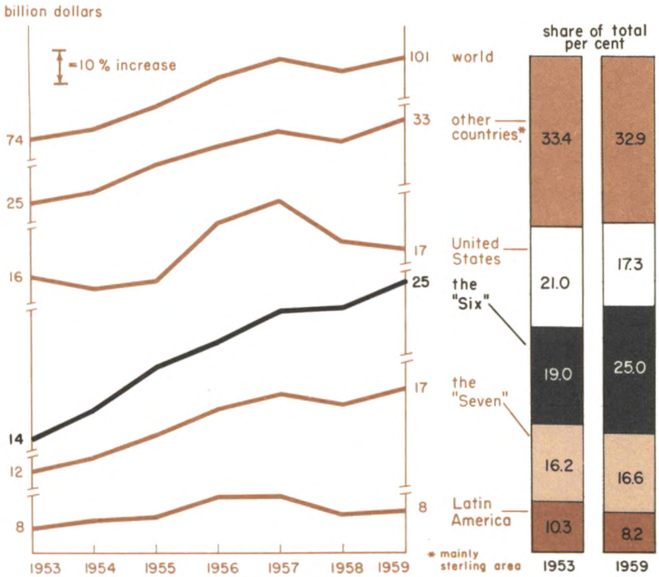
	Sample tariffs (per cent, ad valorem)					
	Benelux		Germany		Common Market	
Product	Jan. 1, 1957	Jan. 1, 1961	Jan. 1, 1957	Jan. 1, 1961	Originally proposed	Reduced 20 per cent
Textile machinery	6	7.1	5	6.4	12	9.6
Mining machinery	8	9	0	3.4	14	11.2
Lifting and handling machinery	8	8.9	6	7.5	13-14	11
Mowers and harvesters	6	7.1	5	6.4	12	9.6
Steam boilers	6	7.6	8	9	14	11.2
Agricultural tractors, under 5,000 kg	6	7.8	11	11	15	12

Note: Jan. 1, 1957, country tariff schedules and Common Market proposed external tariff from *Tariffs and Trade in Western Europe* (Political and Economic Planning, London, December 1959). Changes are estimated.

of these proposals will afford the greatest protection to such commodities as wheat, fruits and vegetables, poultry and certain dairy products which the "Six" are capable of producing in sufficient quantity to meet the overall needs of the community, albeit at higher cost than imports from outside countries. Imports of these commodities in the future may depend increasingly on the marginal requirements of the "Six."

In the circumstances, it is not surprising that the United States and other important agricultural countries, such as Canada, Australia and New Zealand, have been vigorously attacking the Common Market's stand on agriculture since the opening of the 1960-61 GATT tariff conference. These countries are not happy about the prospect of being relegated to the role of marginal suppliers of the European market.

Exports of Common Market countries have increased more rapidly than others since 1953



Note: Compiled from United Nations trade statistics. Exports are f.o.b.

If no compromise is forthcoming, United States exports of wheat, fruits and vegetables to the "Six" could decline substantially in the years ahead. American exports of cotton, tobacco and certain fats and oils, on the other hand, will probably continue in large volume. These items are in short supply among the "Six" and cannot be readily obtained in sufficient quantity or quality from their African territories (see table on page 15).

U. S. exports to Europe at high level

American business firms face the difficult task of retaining competitive positions in the rapidly growing European markets. They have the option of cutting prices and offering more liberal credit terms or expanding manufacturing and distribution facilities inside the "Six" and the "Seven." The recent revaluation of the German mark and the Dutch guilder (the value of each in terms of the dollar was raised 5 per cent) may also help somewhat by making United States exports more competitive in European markets.

American business firms are investing a substantial amount of capital in Western Europe. According to the Department of Commerce, capital expenditures of United States manufacturing companies in Western Europe during 1958-60 averaged nearly one-half billion dollars per year. By the end of 1960 the value of their direct investments in Europe totaled roughly 3.5 billion. In 1959 these facilities generated total sales of 6.3 billion dollars, of which 5.0 billion represented sales in European markets and 1.3 billion exports to other areas including the United States. Recent capital expenditure surveys, moreover, indicate that United States companies plan to accelerate their expansion in Europe (see *Business Conditions,* October 1960).

This has caused many to ponder whether the European integration movement might ultimately lead to a permanent erosion of American exports. So far, this has not happened; in fact, the opposite has been the case. Since the end of 1958 our merchandise exports to Western Europe have scored substantial gains. During the first nine months of 1960 such shipments totaled 4.9 billion dollars compared with 3.4 billion in the like period of 1959—an increase of nearly 45 per cent. As can be seen in the accompanying table this gain reflected, in large part, a brisk demand for American capital equipment and raw materials associated with the European economic boom.

Airplanes, metals and cotton pace rise in U. S. exports to Western Europe during 1960

	January-September*		
	1959	1960	Increase
	(million dollars)		
Cotton	95	336	241
Iron and steel scrap and products	59	202	143
Nonferrous metals	139	381	242
Industrial machinery	284	417	133
Civilian aircraft	16	307	291
Chemicals	314	416	102

* Military and "special category" exports excluded throughout. Also excludes exports to Greece and Turkey.

The future

In the long run the lowering of intra-European tariffs and other trade barriers will undoubtedly divert some demand from American to European producers. For certain manufactured goods the shift may be substantial. A tentative list of these items would include chemicals, textiles, glass products, optical and photographic equipment, certain types of electronic equipment and electrical machinery, heavy engineering equipment and general-purpose machine tools.

Yet, the impact of any such diversion on our over-all export picture may be slight inasmuch as shipments of finished manufactured goods to Western Europe have accounted for no more than 7 per cent of total United States merchandise exports in recent years. Moreover, there is a good possibility that any reductions in this category will be more than offset by increased exports of such raw materials as cotton, coal, aluminum and copper alloys and iron and steel scrap, all essential to expanding European industries. Many of these are in short supply in the "Six" and the "Seven" and are admitted duty-free or at low rates.

Competition from European suppliers may have its greatest impact on our exports to Canada, Latin America and Africa—markets in which finished manufactured goods constitute a substantial part of our total exports. As noted above, European suppliers have already made noticeable inroads on our exports of capital goods to these areas. Such competition is bound to become more intense as European industries gain in size and efficiency.

Is multilateral trading possible?

This European integration movement, which has brought about a lowering of intra-European tariffs and a provisional 20 per cent reduction in the Common Market external tariff, reflects a desire to achieve the benefits of broader markets and sharpened competition. In this respect the European integration movement could make a significant contribution toward establishment of a really meaningful multilateral trading system among all Western nations based on comparative economic advantage. The United States, which produces vast quantities of strategic industrial raw materials and important agricultural commodities and maintains a substantial lead in industrial technology, could derive substantial benefits under such a system.

Cotton, fats and oils dominate U. S. agricultural exports to Common Market countries—

	1956	1957	1958	1959	Share of U.S. total 1956-59
		(million dollars)			(per cent)
Wheat	184	99	63	53	13
Corn and sorghum	92	78	85	150	33
Fruits and vegetables	67	68	69	58	18
Cotton	224	366	200	108	31
Tobacco	86	95	106	98	23
Fats and oils	232	241	137	229	47
Other	164	92	120	200	13
Total	1,049	1,039	780	896	23

The give and take of the first session of the 1960-61 GATT tariff conference has revealed again, however, that any further substantial progress toward freer trade will not be achieved easily. The difficulties encountered in renegotiating compensatory tariff concessions to offset the increases in rates associated with the erection of the Common Market's external tariff are proving to be much more complicated than originally anticipated. Many of the GATT participants feel that the concessions offered by the "Six" are inadequate. As a result the second phase of the GATT conference, in which the participants will begin bargaining for new tariff concessions, has been postponed to an indeterminate date. (The second phase was originally scheduled to begin in January of this year.)

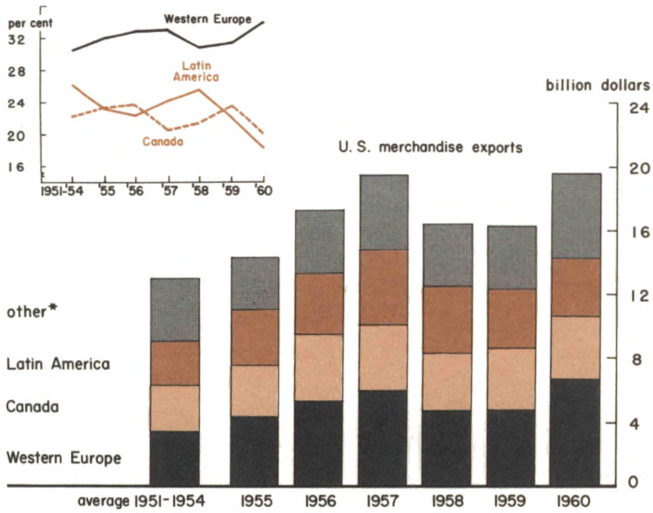
Agriculture is another stumbling block. The United States and other important agricultural countries, as noted above, have challenged the Common Market's proposal for a series of "variable import duties" on a wide range of agricultural products. Their principal objection is that it involves too much uncertainty.

Tariff schedules adopted by nations within the framework of GATT are ordinarily "fixed" or "bound" against increases in the future. The Common Market's "variable import duty" proposal does not provide for such "binding." This could mean, as the United States delegation has argued, that the GATT participants in negotiating with the "Six" would be trading fixed tariff concessions for those subject to considerable fluctuation.

The hassle over agriculture

emphasizes the extraordinary sensitivity that most Western nations have toward this industry regardless of their state of economic development. In many industrial countries, including the United States, domestic agricultural prices are maintained substantially above world price levels by Government support programs, and internal markets are insulated from outside competition by a complex maze of tariffs, quotas, licensing arrangements and other controls. Subsidies are often utilized to promote exports so as to moderate the accumulation of surpluses, but such action tends to elicit charges of dumping by other producer countries and may invite retaliatory action. The results are an expensive misallocation of world resources, a fostering of ill will among nations and a further proliferation of the web of government controls on agriculture.

U. S. exports to Western Europe have risen in importance while those to Canada and Latin America have declined



*Includes Africa, Asia and Oceania.

Agricultural commodities are important in world trade and for many low-income countries agricultural exports constitute the primary source of foreign exchange earnings. Thus, no matter how much progress is made in lowering of industrial tariffs between nations, the full realization of the benefits of free trade still depends upon a satisfactory solution of the problems associated with agricultural commodities.

The GATT negotiations are also complicated by uncertainty regarding the bargaining position of the United States and its posture toward free trade. The 1958 Trade Agreements Extension Act, which authorizes the President to reduce United States duties up to 20 per cent from rates in effect July 1, 1958, expires next year. Hence, the fear has arisen among Europeans that any concessions offered by the United States may be abrogated by new trade legislation. Protectionist demands, accentuated recently by economic recession, have not passed unnoticed.

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